Clerk's Stamp

COURT FILE NUMBER	2401-09688
COURT	COURT OF KING'S BENCH OF ALBERTA
JUDICIAL CENTRE	CALGARY
	IN THE MATTER OF THE *COMPANIES' CREDITORS ARRANGEMENT ACT*, RSC 1985, c C-36, AS AMENDED AND IN THE MATTER OF A PLAN OF COMPROMISE OR ARRANGEMENT OF DELTA 9 CANNABIS INC., DELTA 9 LOGISTICS INC., DELTA 9 BIO-TECH INC., DELTA 9 LIFESTYLE CANNABIS CLINIC INC. and DELTA 9 CANNABIS STORE INC.
APPLICANTS	DELTA 9 CANNABIS INC., DELTA 9 LOGISTICS INC., DELTA 9 BIO-TECH INC., DELTA 9 LIFESTYLE CANNABIS CLINIC INC. and DELTA 9 CANNABIS STORE INC.
DOCUMENT	**BOOK OF AUTHORITIES FOR THE BENCH BRIEF OF SNDL INC. TO BE HEARD ON JANUARY 10, 2024 AT 10:00 A.M.**
ADDRESS FOR SERVICE AND CONTACT INFORMATION OF PARTY FILING THIS DOCUMENT	McCarthy Tétrault LLP 4000, 421 – 7th Avenue SW Calgary, AB T2P 4K9 Attention: Sean Collins, KC / Lance Williams / Ashley Bowron Tel: 403-260-3531 / 604-643-7100 Fax: 403-260-3501 / 604-643-7900 Email: scollins@mccarthy.ca / lwilliams@mccarthy.ca / abowron@mccarthy.ca

LIST OF AUTHORITIES

Case Law

1. *Canadian General Electric Co. v Canadian Rubber Co. of Montreal*, 1915 CanLII 45 (SCC);
2. *Capital Steel Inc v Chandos Construction Ltd*, 2019 ABCA 32;
3. *Chandos Construction Ltd. v. Deloitte Restructuring Inc.*, 2020 SCC 25;
4. *Elsley v J.G. Collins Ins. Agencies*, 1978 CanLII 7 (SCC);
5. *Frenchmen's Creek Estates Inc. v Tuckernuck Mortgage Administration Inc.*, 2007 CanLII 7404 (ON SC);
6. *Frenchmen's Creek Estates Inc. v. Tuckernuck Mortgage Administration Inc.*, 2008 ONCA 107;
7. *Goodfellow v CUMIS General Insurance Company*, 2021 ONSC 3604;
8. *Group Eight Investments Ltd. v Taddei*, 2005 BCCA 489;
9. *HF Clarke Ltd. v Thermidaire Corp. Ltd.*, 1974 CanLII 30 (SCC);
10. *Hnatiuk et al. v Court et al.*, 2010 MBCA 20;
11. *Infinite Maintenance Systems Ltd. v ORC Management Ltd.*, 2001 CanLII 24082 (ON CA);
12. *Jinnah v Alberta Dental Association and College*, 2022 ABCA 336;
13. *Kentucky Fried Chicken Canada v Scott's Food Services Inc.*, 1998 CanLII 4427 (ON CA);
14. *Mimi's Parlour Ltd v 1816112 Alberta Ltd*, 2021 ABQB 254;
15. *MTK Auto West Ltd. v Allen*, 2003 BCSC 1613;
16. *Pioneer Hi-Bred International Inc. v Richardson International Ltd.*, 2010 MBQB 161;
17. *Prudential Insurance Co. of America v Cedar Hills Properties Ltd.* (1994), 1994 CanLII 1960 (BC CA);
18. *Resolute FP Canada Inc. v Ontario (Attorney General)*, 2019 SCC 60;
19. *Royal Bank of Canada v Swartout*, 2011 ABCA 362;
20. *Sattva Capital Corp. v Creston Moly Corp.*, 2014 SCC 53;
21. *Tercon Contractors Ltd. v British Columbia (Transportation and Highways)*, 2010 SCC 4;

Secondary Sources

22. Geoff R. Hall, *Canadian Contractual Interpretation Law* 3rd ed. (Toronto: LexisNexis, 2016);

23. Geoff R. Hall, *Canadian Contractual Interpretation Law*, 4th ed (Toronto: LexisNexis Canada, 2020); and,

24. Paul-Erik Veel, "Penalty Clauses in Canadian Contract Law" (2008) 66:2 UT Fac L Rev 229.

TAB 1

THE CANADIAN GENERAL ELECTRIC COMPANY (PLAINTIFFS) ... } APPELLANTS;

AND

THE CANADIAN RUBBER COMPANY OF MONTREAL (DEFENDANTS) ..... } RESPONDENTS.

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*Nov. 18, 19.
*Dec. 29.

ON APPEAL FROM THE SUPERIOR COURT, SITTING IN REVIEW, AT MONTREAL.

Contract—Delivery—Specified time—Default—Liquidated damages—Pre-estimate—Penalty—Inexecution — Compensation — Cross-demand—Practice—Arts 1013, 1076, 1131 *et seq., C.C.—Art.* 217, *C.P.Q.*

A contract (in the form usual in the Province of Ontario) for the manufacture, in Ontario, of electrical machinery to be delivered within a specified time at Montreal, provided that in case of failure to deliver various parts of the machinery as provided therein the sum of $25 should "be deducted from the contract price as liquidated damages and not as a forfeit for every day's delay in the delivery of the apparatus as specified, etc." The contractor brought action in the Province of Quebec to recover an unpaid balance of the price and the defendants contended that they were entitled to have the claim reduced by a sum equal to the amount so stipulated for default in prompt delivery.

Held, that, on the proper construction of the contract, the intention of the parties was to pre-estimate a reasonable indemnity as liquidated damages for delay in the execution of the contract; that effect should be given to their intention by allowing the deduction of the amount so estimated from the contract price, and that there was no necessity for a cross-demand therefor by the defendants nor that they should allege or prove that they had sustained actual damages in consequence of the delay in delivery. *Dunlop Pneumatic Tyre Co.* v. *New Garage and Motor Co.* ([1915] A.C. 79); *Wallis* v. *Smith* (21 Ch. D. 243); *Web-*

*PRESENT:—Sir Charles Fitzpatrick C.J. and Davies, Idington, Anglin and Brodeur JJ.

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ster v. *Bosanquet* ([1912] A.C. 394); *Clydebank Engineering and Shipbuilding Co.* v. *Yzquierda y Castaneda*, ([1915] A.C. 6); *Hamlyn* v. *Talisker Distillery Co.* ([1894] A.C. 202); *The "Industrie"* ((1894) P. 58); and *Ottawa Northern and Western Railway Co.* (36 Can. S.C.R. 347), referred to.

Judgment appealed from (Q.R. 47 S.C. 24) affirmed.

APPEAL from the judgment of the Superior Court, sitting in review(1), affirming the judgment of Charbonneau J., in the Superior Court, District of Montreal, by which the action of the plaintiffs was dismissed with costs.

The material circumstances of the case are stated in the head-note. The defendants contended that, on account of delay in the delivery of the machinery in question, they were entitled to deduct from the amount of the purchase price the sum of $14,550, either as pre-estimated liquidated damages or as a reduction in price stipulated in the contract, but, being willing to effect an amicable settlement of the plaintiffs' contention that in some measure the delay was to be attributed to the defendants themselves, they had tendered to the plaintiffs, before action, $3,000 in full settlement of their claim, and they renewed the tender with their plea. In the trial court, Mr. Justice Charbonneau gave effect to the contentions of the defence and dismissed the plaintiffs' action with costs. This decision was affirmed by the judgment now appealed from.

F. W. Hibbard K.C. and *G. H. Montgomery K.C.* for the appellants.

A. Chase-Casgrain K.C. and *Errol M. McDougall* for respondents.

(1) Q.R. 47 S.C. 24.

THE CHIEF JUSTICE.—I am of opinion that the judgment in this case is right. It is unnecessary for me to go into the facts of the case; the only point that was pressed upon us at the hearing of the appeal was the legal effect of the provision in the contract that

> the sum of $25 per day for each motor, each generator and a complete switchboard shall be deducted from the contract price as liquidated damages and not as a forfeit for every day's delay in the delivery of the apparatus as specified in the delivery clause.

The contract is in English, relates to a purely business transaction and uses terms well recognized in English law. The words "liquidated damages" and "forfeit or penalty" are commonly to be found in similar contracts and, as judicially interpreted by the courts, have a perfectly well understood meaning in English and French law.

A penalty is the payment of a stipulated sum on breach of the contract, irrespective of the damage sustained. The essence of liquidated damages is a genuine covenanted pre-estimate of damage.

I think any difficulty the case may present has arisen from the fact that similar terms have not perhaps quite the same meaning in English and in French law. In the latter the word "peine" does not correspond to the word "penalty" as construed by the English courts. Whilst the exact amount of the former may be recovered irrespective of damage, it is only so much of the latter as represents the actual damage sustained that the party in default can be made liable for. To some extent, therefore, the word "peine" corresponds more nearly to "liquidated damages" than to a penalty. See Planiol (6 ed.), vol. II., pp. 90 and 91. I think it must be some confusion of these terms which caused Mr. Justice Tellier to dissent from the

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judgment of all the other judges before whom the case has come. He seems to think that as the contract provides that the agreed sum payable in lieu of damages is declared not to be a forfeit, the respondent can only recover the damages which he is able to prove he has sustained.

Mais il n'y a pas lieu de rechercher si le créancier souffre ou non un dommage par suite de l'inexécution de l'obligation. La convention faite à forfait a justement pour but de supprimer tout examen de ce genre. La clause pénale est due (et c'est là un de ses grands avantages) dès que le débitur est responsable de l'inexécution. Planiol, *loc. cit.*

The first paragraph of article 1229, C.N., is not reproduced in the Quebec Civil Code.

There are innumerable cases in which it has been necessary, in particular cases, to decide whether the parties intended that the payment provided for by the contract should be in the nature of a penalty or liquidated damages. The principles on which such cases are determined are well established. It is only necessary for me to refer to the recent case in the House of Lords of *Dunlop Pneumatic Tire Co.* v. *New Garage and Motor Co.*(1), in which they are very clearly laid down. The English rule seems to be in accord with that laid down by Pothier, Obligations No. 345:—

Where the payment of a smaller sum is secured by a larger, the stipulation will be relieved against as penal, but where the agreement is for an act other than the payment of money and the injury that may result from a breach is not ascertainable with exactness, depending upon extrinsic circumstances, a stipulation for damages, not on the face of the contract out of proportion to the probable loss, may be upheld, the difficult cases turning mainly upon the interpretation of the language of the particular contract. Harvard Law Review, vol. 29, p. 129, and cases there cited.

(1) [1915] A.C. 79.

In the contract in the present case there is a clear agreement for the deduction from the contract price for delay in delivery; there is no objection to such an agreement being entered into and no reason why effect should not be given to the agreement by the courts. As Sir George Jessel puts it:—

> Courts should not overrule any clearly expressed intention on the ground that judges know the business of the people better than the people know it themselves.

Wallis v. *Smith* (1882) (1), at page 266.

Article 1076, C.C.:—

> When it is stipulated that a certain sum shall be paid for damages for the inexecution of an obligation, such sum and no other, either greater or less, is allowed to the creditor for such damages.

As far back as 1849 it was said by Cresswell J., in the case of *Sainter* v. *Ferguson* (2):—

> If there be only one event upon which the money was to become payable and there is no adequate means of ascertaining the precise damage that may result to the plaintiff from a breach of the contract, it is perfectly competent to the parties to fix a given amount of compensation, in order to avoid the difficulty.

This ruling has been approved in many cases ever since. Halsbury, vol. 10, Damages Nos. 604 *et seq.* It appears to me that it entirely covers the stipulation in the present contract. It could not have been possible to ascertain the damage in advance; the amount fixed is not alleged to have been an extravagant one; and the provision was in every respect a reasonable and proper one which both parties may perfectly well be supposed to have intended.

I may add that the contract is for delivery of an apparatus consisting of the things therein specified, for which apparatus the purchaser agrees to pay

(1) 21 Ch. D. 243.

(2) 7 C.B. 716, at p. 730.

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$33,000. The delivery clause provides for the delivery of the apparatus not later than May 1st, 1911, and the contract provided that

> the sum of $25 per day for each motor, each generator, and a complete switchboard shall be deducted from the contract price (1) for every day's delay in the delivery of the apparatus.

It might perhaps be contended that until the whole apparatus was delivered, $25 per day should be deducted for each motor, etc., whether delivered or not. The contract does not say for each motor undelivered. It is not necessary, however, to decide this as the respondents advanced no claim on such a construction of the contract. I mention it because the appellant has certainly suffered no hardship in the deduction made from the contract price and perhaps is fortunate in not having to submit to a larger deduction. But one cannot entirely overlook that possible construction of the contract because of the second paragraph of article 1076 C.C. However, the parties are presumed to be the best judges of the object they had in view when this provision was inserted in the agreement and neither has chosen to raise the question as to whether the obligation to deliver was performed in part.

It may possibly be useful to observe that article 1076 C.C. is new law. See Report of Codifiers for the reasons why they reject the rule as laid down in Pothier, "Obligations," No. 345.

The appeal is dismissed with costs.

DAVIES J.—This is an appeal from the Court of Review of the Province of Quebec affirming a judgment of the Superior Court as to the proper construction of a contract made between the parties for the

manufacture and delivery by the electric company to the rubber company of certain apparatus comprising direct and alternating current motors and a large switchboard in the wiring.

The controversy turned upon the proper construction of a clause in the contract providing for the damages to be paid by the electric company to the rubber company in case default was made in the delivery of the apparatus within the time contracted for.

The clause reads as follows:—

> The sum of twenty-five dollars ($25) per day for each motor, each generator and a complete switchboard shall be deducted from the contract price as liquidated damages and not as a forfeit for every day's delay in the delivery of the apparatus as specified in the delivery clause herein, and this sum shall be over and above the cost of any extra inspection.

The rubber company, on being sued for the price of the apparatus manufactured and supplied, claimed the right under this clause to deduct from the contract price as genuine pre-estimated liquidated damages $25 per day for 582 days the plaintiff electric company was in default in delivering the motors and generators less 122 days which it conceded should not be charged because they were or might be attributable to the defendant company's own fault, thus reducing the number of days for which damages were chargeable to 460, and fixing the damages at $11,500.

Both courts below maintained the defendants' contentions alike as to its legal rights under the above clause of the contract and as to the actual number of days for which it was entitled to deduct the $25 per diem as genuine pre-estimated liquidated damages.

On the question of fact as to the actual number of days chargeable owing to fault in the delivery of the apparatus, after listening to the lengthy argument of

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counsel for the respective parties, I felt myself quite unable to say that the findings of the trial judge concurred in by the Court of Review should be disturbed.

As to the legal question, the principal objection raised was that it was not competent for the defendants, respondents, to plead in answer to an action for the recovery of the stipulated price of these motors and generators the liquidated damages agreed upon in the contract for delays in the delivery of the articles, unless and until damages of some kind and amount had at least been first alleged and proved.

I have not been able to understand on what principle such a contention can be maintained.

Once it is established that the damages are genuine pre-estimated liquidated damages, and are not unconscionable, I cannot see why they should not be pleaded in answer to a plaintiff's demand for the price of the article sold.

But in the case at bar the parties expressly provided that these damages should "be deducted from the contract price" and so the courts below properly held that the defendant was entitled to deduct them for the number of days he established the vendors' default.

It has been suggested as a possible construction of the contract that a failure to deliver even a fractional part of the "apparatus" might make the vendor liable for the $25 per diem even on the motors and generators he had delivered until the entire apparatus was delivered.

I think, however, this is not the true construction of the clause which only makes the vendor liable for the per diem damages pre-estimated for each motor

and each generator undelivered on time and for the days only there was default in the delivery of each such motor and generator.

If the suggested possible construction was the true one there would certainly be strong ground for holding the $25 per diem for each motor and generator not a genuine pre-estimated damage, but an unconscionable amount which was really a penalty.

On the whole, I would dismiss the appeal with costs.

IDINGTON J.—The appellant seeks to recover from the respondent the balance due for certain machines to be made at the factory of appellant in Peterborough, in Ontario, and delivered to respondent in Montreal for the contract price of $33,000 and for some other supplies and work incidental to the contract.

The differences between the parties are confined to a claim made by the respondent, and so far sustained by the courts below, to deduct $25 a day from the contract price in the event of a failure to comply with certain alleged terms of the contract.

The frame of the contract is in some regards ambiguous, and as the claim to these reductions must rest upon the correct interpretation and construction of the contract which is somewhat complicated, I purpose analyzing it.

It consists of three parts. The first is briefly the operative part and therein contains the respective obligations of each party as follows:—

> The contractor will manufacture, deliver and erect and operate the apparatus contracted for herein, consisting of four direct current motors—two motor generator sets—four alternating current motors, and a large switchboard with wiring, etc., all as herein specified.

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The purchaser agrees to accept and pay for the apparatus the sum of thirty-three thousand dollars ($33,000) under the terms and conditions set forth herein, provided that the apparatus complies in every respect with the general conditions and the specifications herein contained.

The next part consists of the conditions referred to in the foregoing. In one of these conditions is the following somewhat ambiguous expression:—

The contractor will begin work immediately upon signing the contract and complete the same as per the delivery clause, free of all liens and charges within the time specified herein, etc.

Another condition provides as follows:—

The sum of twenty-five dollars ($25) per day for each motor, each generator and a complete switchboard shall be deducted from the contract price as liquidated damages and not as a forfeit for every day's delay in the delivery of the apparatus as specified in the delivery clause herein, and this sum shall be over and above the cost of any extra inspection.

It is upon this clause coupled with the delivery clause thus referred to and what that delivery clause contains that the claim of respondent to reductions must rest.

This condition is immediately followed by another which says:—

In the event of the purchaser ordering the work in connection with this contract to be discontinued, or in any manner whatsoever delays the work, it is hereby agreed that such delay caused by purchaser shall be added to the delivery date, mentioned herein, and such delivery date extended by the number of days that will be equal to the delay caused by the purchaser.

Upon this condition the appellant rests a number of claims to reduction from what respondent might otherwise be entitled to. With these I shall deal presently in detail.

The respondent, however, alleges it has made due allowance for all such counterclaims as well founded.

These delays it estimated at one hundred and

twenty-two days in all and tendered a sum to cover same which the learned trial judge has found sufficient and in that has been sustained by the court of appeal.

The "delivery clause" above referred to I find under the heading "Delivery and Erection" and under that appear the following provisions:—

> The apparatus shall be delivered on purchaser's foundations, free of cost to the purchaser in his power house in the City of Montreal, Province of Quebec, not later than May 1st, 1911.
>
> In case the contractor should fail to deliver the apparatus by May 1st, 1911, the sum of twenty-five dollars ($25) per day for damages as provided for herein shall apply.
>
> * * * * *
>
> The purchaser agrees to have the power house foundations, etc., ready for the apparatus. If the purchaser causes any delay to the contractor thereby preventing the installation of the apparatus, or the delivery of the same, the damages of $25 per day provided for herein shall not apply for the number of days delay caused by the purchaser.

It is herein I find the ambiguity I first mentioned. Clearly there is in this latter clause a confusion between delivery and installation.

True, there are between these just quoted, two provisions I omit, of which one provides appellant shall provide men to erect without delay and have same complete and ready for service not later than May 20th, 1911. But as there is no reduction of price or provision for liquidated damages or anything specifically bearing thereon I find none can by any possibility be claimed in that regard. Indeed, respondent in argument renounced any such claim save in respect of failure to deliver within the time agreed upon.

Notwithstanding that, can appellant, by virtue of the clause lastly quoted, exonerating the appellant for delays caused by respondent, take any benefit therefrom in way of reduction of respondent's claim, by reason of the peculiar expression therein which reads:

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Thereby preventing the installation of the apparatus, or the delivery of the same,

followed by the words:—

The damages of $25 per day provided for herein shall not apply for the number of days' delay caused by the purchaser?

I am of opinion it cannot. It is restricted to the damages provided therein, and they are only provided for in respect of default in delivery. And that default must be computed from the date, after the 1st of May, when the delays caused by the purchaser have been duly credited, and thus appellant given a later day for delivery.

Now let us consider the bearing of these clauses, thus interpreted and construed, upon the respective claims of respondent to make the reductions allowed, and the appellant to be relieved therefrom by virtue of what the purchaser has thus agreed to excuse.

Beginning with the latter which is chiefly in question herein, I shall take them in the order presented.

The first claim so set up is a delay alleged by the respondent's failure, for nearly a month, to execute the contract, after the appellant had duly signed same and sent it to respondent to be executed. I cannot understand how it can be claimed that such a delay can be held as one of those which was caused by the purchaser within the meaning of the contract. It is clearly a hindering the progress of the work which is aimed at and nothing else.

The appellant had the remedy in its own hands by refusing, if it could justify such a course under the attendant circumstances, to go on, unless and until a modification of the terms had been made, but the contract cannot permit of such a mode of construction. Indeed, the appellant in fact did go on meanwhile with

the work. It was, as I read the contract in the expression I quote above, clearly contemplated by the parties that it should do so as soon as it had signed it; and everything must be treated as if the contract, which has no date, became operative from the date when the appellant signed it.

I have no doubt that, not only was that the purpose of the peculiar expression used, but also that it was the understanding of the parties.

The next item of claim is a change in three of the 175 h.-p. motors.

Inasmuch as the specifications forming part of the contract provided for terminals as follows:—

> The motors shall be provided with terminals located suitably for connecting to the switchboard leads; the terminals will be provided with approved insulating couplings. The switchboard location and wiring may call for the terminals to be on top of the motor,

it does not appear to me as self-evident that the respondent was to blame for asking that they should be placed as at first asked.

It was competent for the engineer to have insisted, as some stubborn, self-sufficient men might have done, that what he had written must stand. If he had I cannot see anything appellant could have done but submit.

Because the engineer was gracious enough to try and meet the appellant's urgent petition to save it expense I do not think his company can be bound to bear the burden thereof. Moreover, I suspect there was ample work for appellant's men, working on these machines, to keep going steadily on.

The next is in respect of the test on those 175 h.-p. motors. The evidence bearing upon this item illustrates, by the slip-shod methods of those in the appel-

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lant's employment, in charge of its business, how very provoking they could be.

The appellant had been warned by a letter of the 5th May, in the nature of a personal appeal to its vice-president, and by a formal letter of 9th May to the company, that full deductions for delays for non-delivery would be insisted upon. Yet in face of these appeals neither business energy nor ordinary despatch, much less the urgency that a possible loss of a hundred dollars a day should have evoked, was used. And there is no proof which can excuse them at the expense of the respondent.

The next item is in regard to three 175 h.-p. motors and one 20 h.-p. motor. The fault in part admittedly was on the part of appellant, and the requirements of the engineer in way of change were within the contract and no proof is adduced that the entire work was held up by any such cause as assigned.

The next cause of delay by respondent, if any, rests upon what transpired relative to some sub-bases which formed no part of the contract in question, yet were to be so used in connection with the work done under the contract that it might reasonably have been considered by the appellant as due to the respondent that the work done or to be done in Peterborough, pursuant to the contract, should be so fitted there as to be ready when erected to operate upon the sub-bases.

With every desire to give effect to this reasonable suggestion I am unable to discover wherein the parties concerned provided in the contract for the due execution thereof.

Whatever relief appellant is entitled to herein must rest within the terms of the contract as expressed in that condition above quoted providing for

the extension of the date of delivery by reason of the purchaser causing delay to the contractor.

The reasonableness of the suggestion made in the letter of 1st April, upon which and what followed appellant's claim rests, cannot be gainsaid. But how far does that carry us in relation to the business in hand ?

It, when coupled with what preceded and followed it, seems to disclose only this, that some one had blundered.

The contract itself does not seem to have provided for the contingencies involved in anything relating to the sub-bases. If the appellant's men had paid careful attention to the matter they should have seen to it earlier than this letter of 1st April to Sheldon's Ltd., indicates.

The fact is the fitting of the machines to be made by the appellant to serve sub-bases must have been patent to all concerned if heed paid to the business in hand and the means of doing so or anticipating same, ought to have been provided for in the contract. So far as I can discover this was not done.

In such a situation, what, within the contract, should have been done ?

Clearly the only alternative in law was to have gone on with the completion of the work according to contract so far as it reached, and shipment of the machines so that the terms regarding delivery might have been fulfilled. If shipped in that condition a new difficulty would have been presented no doubt. The installation would have been delayed but for that no damages per diem for delays could have been claimed. Another difficulty would have arisen relative to the extra expense of having the work of fitting

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done in Montreal instead of in Peterborough for which due compensation no doubt would have had to be made by respondent.

Indeed, the parts which needed fitting to the sub-bases might have had to be shipped to Peterborough. But for any such event the respondent would only have itself to blame. It need not have concerned appellant.

It is impossible now for us to re-mould the contract and provide for all this. It is, I repeat, within the lines of the contract as framed that we must determine the rights of the parties and not by something we can presume to have been inserted and assume to have been contemplated as within same when it is clearly not so provided.

A letter of 13th February from respondent to the appellant made clear what was wanted. And therein appellant is asked for a tender for these sub-bases and it ought to have dawned upon some one in appellant's employment that unless this unprovided for feature of the contract was duly provided for, there was trouble ahead.

It may be excusable to overlook the need of this provision in a contract which covers twenty-eight printed pages of the case before us, but doing so furnishes no basis for us to allot the shares to be borne of the burden of a joint blunder.

It was possibly a case for an application within the terms of the contract for an extension of time or for a direct appeal to respondent.

Instead of adopting either such course there was correspondence between appellant and the sub-contractors—Ross & Greig and Sheldons—and needless waste of time at that, without a direct communication

(and probable understanding) with respondent. The only direct thing appellant has from respondent to shew, and rely upon, is the ambiguous letter of the 4th May. It passes my understanding why that should be relied upon, for nothing preceding that letter had been done in any way approaching business methods so far as these sub-bases were concerned. Standing alone as it does, the letter is worthless for appellant's present purpose.

There certainly is fair ground for an appeal in regard to this item to the sense of justice respondent should have. It may or may not have taken that into consideration in arriving at the total of the hundred and twenty-two days it allows for.

But I can see no ground in law upon which to rest the claim made by the appellant in this regard.

I think it might have been possible for the appellant in a contract of this magnitude to have made the templets as requested in the letter of respondent of 13th February at, say, a couple of hundred dollars expense, even without an appropriation.

The next claim is one arising out of the admitted error made by the engineer in connection with the starters for the synchronous and induction motors. It seems well founded, but its consequences, in my opinion, are grossly exaggerated, and amply covered by allowances made.

The last claim relative to the motor generator sets may be disposed of by the like considerations.

I confess, notwithstanding the argument presented, I was disposed at its close to think the claims made by respondent were somewhat harsh and possibly unfounded in law, but the examination I have made

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leads to the conclusion that appellant has only itself to blame for the result.

There remains only the question of law striking at respondent's entire claim as presented for consideration.

In the first place it is to be observed that the terms of the contract raise a most formidable obstacle in the way of the appellant. It sues upon a contract for a price agreed upon which it is stipulated, in certain contingencies which have taken place, shall be reduced to another price. What can it matter in such a case that the reduction of price is called "liquidated damages"?

It is not for the law, unless such stipulation is against law, to act upon the name given or name assigned the amount of reduction, but to give effect to the contract.

Of course, if the law clearly expressed such a stipulation to be null, or subject to modication, then the contract could be of no avail.

I do not think the article 1076 of the Civil Code governing the parties' rights in the premises does so interfere with the efficacy of what the parties have contracted for.

The case of *Ottawa Northern and Western Railway Co.* v. *Dominion Bridge Co.*(1), does not help the appellant. It would be very difficult to extract from the decision in that case anything to help any one. For there was such a difference of opinion in the court as to render its decision unlikely to be ever applicable to another case unless that other should happen to be, as this is not, exactly the same.

(1) 36 Can. S.C.R. 347.

I had the misfortune, in common with my then brother, Mr. Justice Nesbitt, to differ from the result reached by the majority. But each member of that majority took different grounds for the conclusion reached.

There were two contracts involved therein; and in no way could one, by construction of the contract fixing the price, as may be held herein, be able to say that as the result of an application of the damages then and there in question, the price was thereby determined. The case chiefly turned, so far as the majority of those expressing opinions held, upon the point of whether there could be held to be an application of article 217 of the Code of Civil Procedure. The question of whether or not the party seeking there compensation or set-off based in liquidated damages or, as here, such a reduction of price as claimed herein must shew actual damages could only arise in a very incidental manner therein. And as I viewed it then my opinion would be against the appellant. If this court had by the majority clearly expressed a view in conflict therewith upon the exact point involved, I should cheerfully bow thereto, but unfortunately it did not.

The neat point raised herein, that, of necessity, in law the party claiming the reduction of price must allege and prove damages before he can apply the estimate fixed by the contract, does not seem to me tenable in this case.

In the first place the contract does not permit of such a holding. And in the next place the fact is that such proof as was adduced seems to answer the contention.

I can conceive of such a case arising as might give

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place to such a contention as raised herein, but not in this case, or in the way it is presented.

I find in respondent's factum, article 1076 C.C., quoted as follows:—

> 1076. When it is stipulated that a certain sum shall be paid for damages for the inexecution of an obligation, such sum and no other, either greater or less, is allowed to the creditor for such damages.

This is not the whole of that article. The part quoted is followed by this:—

> But if the obligation have been performed in part, to the benefit of the creditor and the time for its complete performance be not material, the stipulated sum may be reduced unless there be a special agreement to the contrary.

This gives an entirely different aspect to the article as a whole and provides for such cases as I have just indicated may possibly arise. In such a case this second part of the article should be availed of by pleading the facts applicable thereunder, which was not done or pretended to be claimed herein.

In concluding I may say that the parties are both agreed that the Quebec law must govern their rights. But there are many features in the case arising from the execution of the contract by appellant in Ontario, and the form of contract, which not only contemplated the work of constructing the machines in Ontario but also the right given respondent incidentally thereto to interfere with the expedition of the work there and the shipment thence and only a delivery at Montreal being provided for, before the clauses in question should become operative, which might suggest the law of Ontario was intended to govern. For the later work of installation, in respect of which nothing arises herein, different considerations might apply.

I express no opinion. I merely suggest there is

room for argument and should not feel bound in that regard by this decision in any case presenting the like features and any different submission as to the law of the place by which the contract should be interpreted.

I think the appeal should be dismissed with costs.

ANGLIN J.—The appellant submits three distinct grounds of appeal:—

(1) That the contract in question must be interpreted and effect given to it according to the civil law of Quebec and not according to English law; and that, under the former, the provision fixing the amount of damages to be paid by the vendors for delay in delivery, installation, etc., is not "a penal clause" within articles 1131 *et seq.*, of the Civil Code, but a pre-determination of the amount of damages under article 1076, and that the purchasers, therefore, cannot recover under it without alleging and proving that the delay complained of had actually caused them some damage, the appellants conceding, however, that upon proof of any damage, more than merely nominal, regardless of its extent, the purchasers would be entitled to recover the full sum stipulated for in the contract.

(2) That damages under the clause in question are not a proper subject of compensation or set-off, but recovery of them can be had only in a cross-action.

(3) That the number of days' delay charged to the vendor is excessive.

Before considering the character and legal effect of the clause in the contract upon which this litigation has arisen, a word should be said as to its scope. It has been suggested that it might render the vendors liable for the sum of $25 per day in respect of each of

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the eleven distinct articles which they undertook to supply so long as any one of them should remain undelivered, because until all had been delivered there was delay in the delivery of the "apparatus" contracted for. But both the parties, by their conduct before action and by their attitude in the litigation itself, have made it clear that they understood that the right to recover the stipulated sum for delay in respect of each of the eleven specified articles should be limited to delay in its delivery. That this is the real purview of the agreement seems to be at least equally probable. As the parties have acted upon this view of its scope and have suggested no other, it would appear to be contrary to sound construction to give to the clause in question an effect different from what they seem to have contemplated (art. 1013, C.C.) more onerous, and possibly calculated to render its enforceability doubtful.

The first point made by the appellants is based upon the words "as liquidated damages and not as a forfeit." Only a very cursory examination of the clause in question is required to make it practically certain that it was prepared from the point of view of the English jurist. It is in a form familiar to every English lawyer who knows anything of commercial contracts. It was no doubt taken from some similar contract framed for use in one of the provinces where English law prevails. The obvious purpose of the parties was to prevent the application of the equity rule, under which courts administering English law relieve from penalties and forfeitures, by inserting a provision that it would be difficult to regard as anything else than "a genuine covenanted pre-estimate of damages" (*Dunlop Pneumatic Tire Co.* v. *New Gar-*

age and Motor Co.(1), at p. 86), in a case in which "it was impossible to foresee the extent of the injury which might be sustained" by the purchasers should the vendors make default. *Webster* v. *Bosanquet*(2), at p. 398. The circumstances are such that it cannot be said that the sum agreed upon is extravagant or unconscionable; it is made to depend upon the number of articles undelivered and the duration of the delay in the delivery of each; and a precise estimate of actual damage either before or after the default would have been so difficult to arrive at as to be impracticable. *Clydebank Engineering and Shipbuilding Co.* v. *Yzquierdo y Castaneda*(3), at pp. 16, 19.

The apparent intention of the parties, therefore, was to provide for the payment by the vendors, on default, of a sum agreed upon as pre-estimated damages in such a manner that the courts would not relieve from or modify the stipulation and to dispense with what would possibly be very expensive proof of the actual loss to which the delay had subjected the purchasers. Such an intention is conformable to the policy of the civil law of Quebec quite as much as it is to that of English law. Under both systems alike their contract is the law of the parties. It is the duty of the courts to ascertain as best they can from what the parties have expressed, read in the light of the surrounding circumstances proper to be considered, the nature and extent of the engagements to which they intended to commit themselves, and to give effect to them. In English law the term "penalty" may bear a meaning and may import incidents which differ somewhat from

(1) [1915] A.C. 79. (2) [1912] A.C. 394.
(3) [1905] A.C. 6.

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those attached to it by the Civil Code of Quebec. Yet where it is clear, as it seems to be in the present case, that it was the intention of the parties to contract according to English law, although their agreement was partly made and was partly to be carried out in the Province of Quebec, the courts of that province, giving effect to such intention, will put upon its language the interpretation which it would receive in an English court rather than defeat the real purpose of the parties by giving to the terms they have used the significance which they ordinarily bear in contracts governed by the civil law of Quebec when there is no sufficient indication that they should receive any other interpretation. The present contract was partly made in Ontario, where one of the contracting parties had its chief place of business. That fact may account for its having taken the English form. But, however that may be, effect must be given to the manifest intention of the parties that their contract should be construed according to the rules of English law. *Hamlyn & Co.* v. *Talisker Distillery*(1); *The "Industrie"*(2), at pp. 72, 73. In doing so we are but carrying out the provisions of article 8 of the Civil Code.

In this view it is unnecessary that I should consider the points suggested by the appellants as to the differences between the cases provided for by article 1076 C.C., and those dealt with under articles 1131, etc., or whether, if the present case falls under the first mentioned article, it would be necessary for the respondents to allege and to prove that they had sustained some actual damages. I may, however, observe that I would have difficulty in placing a con-

(1) [1894] A.C. 202. (2) [1894] P. 58.

struction on the clause in question which would require the purchasers to prove some actual damage, more than merely nominal, but would upon any such actual damage being shewn, regardless of its extent, entitle them to recover the entire amount stipulated for. I think the first ground of appeal fails.

The term of the contract that the purchasers shall deduct from the contract price any sum payable by the vendors for damages for delay in delivery is an express provision for set-off or compensation which must prevail, the contract being the law of the parties. The effect of this clause must have escaped the notice of Mr. Justice Tellier. But for it I should be prepared to accept his conclusion that, in view of the provisions of article 1188 C.C., and article 217 C.P.Q., there could not be compensation in such a case as this. *Ottawa Northern and Western Railway Co.* v. *Dominion Bridge Co.*(1).

A study of the record has satisfied me that there has been no overcharge against the vendors for the several periods of delay in delivery and that they have had the full advantage of any reduction in damages to which defaults of the purchasers entitled them. In every case where there was any room for doubt they have not been charged with delay. Only in a very clear case could we interfere on this branch of appeal with the concurrent judgments of the Quebec courts.

BRODEUR J.—Les appelants sont manufacturiers de pouvoirs moteurs électriques et ils s'étaient engagés envers l'intimée de lui livrer certaines machines le 1er mai, 1911, avec obligation de leur part de payer $25

(1) 36 Can. S.C.R. 347.

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par jour de dommages pour livraison tardive. La convention portait que ces dommages seraient déduits du prix du contrat

as liquidated damages and not as a forfeit for every day's delay in the delivery.

Il s'agit de savoir si la compagnie intimée était obligée d'alléguer et de prouver qu'elle avait souffert des dommages.

En principe général, le débiteur est tenu de payer des dommages quand il n'exécute pas son obligation (article 1065 C.C.) et le créancier est alors tenu de justifier de la perte qu'il a éprouvée et du gain dont il a été privé et il doit aussi établir le *quantum* des dommages. (Article 1073 C.C.) Cette preuve est parfois extrêmement difficile à faire et donne lieu à des frais d'enquête considérables et alors les parties conviennent d'une certaine somme pour tenir lieu des dommages-intérêts. (Article 1076 C.C.) C'est la loi qu'elles se font et qu'elles doivent, par conséquent, observer.

Il y a eu évidemment dans la cause actuelle inexécution de son obligation de la part de l'appelante. Elle n'a pas livré les machines dans le délai stipulé au contrat. Alors, comme la convention portait que le prix de vente serait reduit dans la proportion de $25 par jour de retard dans la livraison de chacune des machines, la defenderesse avait le droit par sa defense d'invoquer cette réduction (article 196(3) C. P.Q.).

Mais l'appelante dit que l'intimée aurait dû tout de même, malgré cette stipulation, prouver qu'elle avait subi des dommages.

Je suis d'opinion que la convention dispense le

créancier de faire aucune preuve du préjudice qui lui a été causé.

Marcadé et Pont, art. 1153, p. 421; Larombière Obligations, vol. 4, p. 32, art. 1231; 26 Demolombe, No. 663; 17 Laurent, No. 451, p. 448; *McDonald* v. *Hutchins* (1)..

Les parties avaient en vue évidemment qu'il était essentiel pour l'intimée d'avoir ses machineries à une date fixe et, à raison, je suppose, de certains contrats qu'elle aurait eu elle-même à remplir, il était absolument nécessaire pour elle qu'elles fussent livrées à cette date-là, afin de pouvoir à son tour remplir les obligations qu'elle avait contractées envers d'autres personnes. Comme ces dommages auraient été extrêmement difficiles à établir, il a été jugé à propos par les parties de déterminer immédiatement par convention le *quantum* de ces dommages et dans quelles conditions ils deviendraient dûs. Le *quantum* a été fixé à $25 par jour et la condition est que si la marchandise n'est pas livrée le 1er mai cette somme de $25 par jour pourra être déduite du prix de vente.

Si nous interprétons même littéralement la convention nous pouvons dire qu'une certaine somme avait été stipulée pour le prix des marchandises si elles étaient livrées le 1er mai mais que cette marchandise commanderait un prix moindre si elle était livrée plus tard.

Je ne vois pas comment l'intimée aurait été obligée, dans les circonstances, de prouver qu'elle a souffert des dommages.

L'appelante cependant aurait pu établir que si le temps pour l'entière exécution avait été de peu d'im-

(1) Q.R. 12 K.B. 499.

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portance la somme stipulée aurait pu être réduite (articles 1076, 1135); mais le fardeau de la preuve retombait sur elle; et, comme elle n'a pas rempli cet *onus,* nous ne pouvons pas faire autrement que d'appliquer la convention des parties et dire que l'appelante est tenue de subir une reduction de prix.

Une preuve volumineuse cependant a été faite sur la question de savoir si l'inexécution de la convention n'était pas due à la négligence de l'intimée. Une clause de la convention comportait que si l'acheteur causait quelque délai au vendeur, qui aurait pour effet d'empêcher l'installation des machineries ou leur livraison, la reduction de prix ne pourrait pas être réclamée pour le nombre de jours de délai qui auraient été causés par l'acheteur.

L'intimée elle-même admet dans ses plaidoiries qu'un certain nombre de jours de délai devaient lui être imputés et elle donne crédit à l'appelante de ce chef pour une somme d'environ $3,000.

Il s'agissait de savoir si les autres délais n'étaient pas également dûs à la faute ou à la négligence de l'intimée.

L'un des premiers chefs imputés à la *Canadian Rubber Company* était que le contrat n'avait été signé par elle qu'un mois environ après que l'appelante elle-même eût signé.

Il aurait fallu dans ce cas-là pour la demanderesse établir qu'elle avait au moins protesté l'intimée; mais elle n'a pas jugé à propos de faire cette procédure. Elle a reçu le contrat dûment signé par l'intimée et d'ailleurs il est en preuve que les parties s'étaient entendues longtemps auparavant sur la nature des travaux à faire et que même la demanderesse avait commencé à exécuter son contrat. Le contrat formel

qui a été signé n'a été fait que dans le but de coucher dans un document formel leurs conventions qui étaient déjà bien arrêtées et bien connues.

Il résulte de la preuve que la demanderesse a signé cette convention d'une manière bien imprévoyante. En effet, nous avons au dossier une lettre du surintendant de sa manufacture lui disant, peu de jours après la signature du contrat, qu'il était absolument impossible de fabriquer les machines dans le temps stipulé. Il me semble alors qu'avant de s'obliger formellement, comme elle l'a fait, la demanderesse aurait dû s'enquérir du surintendant de la manufacture s'il était en position de fabriquer ces machines dans le temps stipulé. Elle me paraît n'en avoir rien fait et alors elle n'a pas raison d'imputer ce delai à l'intimée, lorsqu'il est bien évident que c'est elle qui est en faute.

Elle se plaint également d'autres délais, concernant, par exemple, les bases sur lesquelles les machines devaient être assises.

Ces bases devaient être faites par la Canadian Rubber Company. Elle les a fait faire par un fabricant à Montréal; mais comme les machines avaient à être fixées sur ces bases-là, il était très important qu'elles fussent essayées à l'avance pour que ces machines qui demandent à être installées avec beaucoup de soin fissent les travaux qu'on attendait d'elles. L'appelante a fait transporter ces bases à sa manufacture à Peterboro pour faire ces essais.

Il y a divergence d'opinion dans la preuve à ce sujet. Quelques témoins disent que ces essais étaient nécessaires; d'autres disent que c'était inutile.

La Cour Supérieure et la Cour de Revision, sur ce

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point aussi bien que sur les autres, qu'il est inutile de discuter, sont arrivés à la conclusion que sur ces faits l'intimée devait réussir.

Il est bien difficile pour nous de mettre de côté ces décisions concurrentes des deux cours inférieures. Il s'agit, comme on le voit, d'une question de faits; et, suivant la jurisprudence bien établie de cette cour, nous ne devons intervenir que lorsqu'il y a une injustice bien flagrante et bien évidente.

Dans ces circonstances, je suis d'opinion que le jugement de la Cour de Revision doit être confirmé avec dépens.

On a dit que le contrat en question en cette cause-ci, étant un contrat commercial, devrait être interprété suivant la loi anglaise.

Je ne puis pas accepter ce principe. Nos lois dans Québec sur la clause pénale sont différentes de la loi anglaise. Glasson, dans son ouvrage sur l'Histoire du Droit et des Institutions de l'Angleterre, déclare expressément, au vol. 6, p. 375, que les lois françaises et les lois anglaises posent des règles différentes quant aux obligations avec clause pénale.

Appeal dismissed with costs.

Solicitors for the appellants: *Hibbard, Gosselin & Moyse.*

Solicitors for the respondents: *Casgrain, Mitchell, McDougall & Creelman.*

TAB 2

In the Court of Appeal of Alberta

Citation: Capital Steel Inc v Chandos Construction Ltd, 2019 ABCA 32

Date: 20190129
Docket: 1703-0085-AC
Registry: Edmonton

Between:

Deloitte Restructuring Inc. in its Capacity as Trustee in Bankruptcy of Capital Steel Inc., a Bankrupt

Appellant
(Plaintiff/Applicant)

- and -

Chandos Construction Ltd.

Respondent
(Defendant/Respondent)

The Court:

The Honourable Madam Justice Patricia Rowbotham
The Honourable Madam Justice Barbara Lea Veldhuis
The Honourable Mr. Justice Thomas W. Wakeling

Reasons for Judgment Reserved of The Honourable Madam Justice Rowbotham
Concurred in by The Honourable Madam Justice Veldhuis

Dissenting Reasons for Judgment Reserved of The Honourable Mr. Justice Wakeling

Appeal from the Order by
The Honourable Mr. Justice K.G. Nielsen
Dated the 17th day of March, 2017
Filed on the 27th day of March, 2017
(Docket: BK03 2169632)

Reasons for Judgment Reserved of
The Honourable Madam Justice Rowbotham

I. Introduction

[1] A construction contract between Capital Steel Inc. (Capital Steel) and Chandos Construction Ltd. (Chandos) contained a provision that imposed a monetary consequence on Capital Steel's insolvency. When Capital Steel filed an assignment in bankruptcy, Deloitte Restructuring Inc. (Deloitte) was appointed as the trustee in bankruptcy for Capital Steel's estate. A chambers judge allowed Chandos to rely on the provision with the result that there were less assets in Capital Steel's estate for distribution to creditors. At issue on appeal is whether the provision conflicts with the common law anti-deprivation rule, which prevents parties from contracting out of bankruptcy laws.

[2] This case is not fundamentally one of contract law but of bankruptcy law. It is insolvency law that determines the outcome. The *Bankruptcy and Insolvency Act*, RSC 1985, c B-3 (*BIA*) provides the mechanism for the orderly liquidation of a bankrupt's estate and the distribution of the value of the estate in accordance with the statutory provisions, including the priorities established therein. Its purpose is to codify, for all debtors and creditors, what will transpire in the event of a bankruptcy. This certainty is critical to the operation of commercial entities throughout Canada.

[3] One of the purposes of the *BIA* is to prevent a premature race to the debtor's assets. The Act is premised on collective action intended to maximize the return to all creditors *pari passu*. The Act specifically gives trustees the power to set aside preferences and other fraudulent transactions whose underlying objective is to circumvent the Act.

[4] A trustee in bankruptcy has an obligation to take possession of all property of the bankrupt. Section 67(1) of the *BIA* defines property of the bankrupt that is divisible among the creditors. Accounts receivable clearly fall within that definition. In addition, a right of set off that existed at the date of bankruptcy (not as a result of the bankruptcy) is not affected.

[5] A contractual provision triggered only in the event of insolvency or bankruptcy which would deprive creditors of value otherwise available to them and effectively directs the value to an unsecured creditor is void: *Aircell Communications Inc v Bell Mobility Cellular Inc*, 2013 ONCA 95 at paras 10-12, 14 CBR (6th) 276.

[6] The contractual provision at issue in this appeal is such a provision and offends the common law anti-deprivation rule. The rule forms part of the common law of Canada and has not been ousted by amendments to the *BIA*. The chambers judge acknowledged the rule but, in my view, applied the wrong test for determining whether the provision offended the anti-deprivation rule. I allow the appeal.

II. Facts

[7] Chandos was hired as the general contractor for a condominium project in St. Albert, Alberta. It subcontracted steel-related work on the project to Capital Steel for a price of $1,373,300.47. Capital Steel completed the majority of the work required under the subcontract, and Chandos made payments to Capital Steel totalling $1,223,682.08. This left an outstanding balance of $149,618.39.

[8] On September 26, 2016, Capital Steel filed an assignment in bankruptcy. Deloitte was appointed as the trustee. Capital Steel had not completed everything required under the subcontract prior to filing the assignment, causing Chandos to incur costs estimated at $22,800.00 to complete Capital Steel's work on the project.

[9] Offsetting the $22,800.00 in completion costs against the outstanding balance of $149,618.39, Chandos owed a total of $126,818.39 to Capital Steel. Chandos took the position that it was entitled to further offset this amount against 10 percent of the total contract price, or $137,330.05, which it alleged Capital Steel had agreed to forfeit in the event of insolvency. This would effectively eliminate the debt owing from Chandos to Capital Steel and give Chandos a $10,511.66 claim provable in the bankruptcy proceedings. Clause VII Q of the subcontract reads, in part:

> In the event the Subcontractor commits any act of insolvency, bankruptcy, winding up or other distribution of assets, or permits a receiver of the Subcontractor's business to be appointed, or ceases to carry on business or closes down its operations, then in any such events:
>
> …
>
> (d) the Subcontractor shall forfeit 10 [percent] of the within Subcontract Agreement price to the Contractor as a fee for the inconvenience of completing the work using alternate means and/or for monitoring the work during the warranty period.

[10] On March 6, 2017, Deloitte applied to the Court of Queen's Bench seeking advice and directions on whether Chandos was entitled to rely on clause VII Q(d).

III. Decision Below

[11] Before the chambers judge, Deloitte argued that clause VII Q(d) had the effect of withdrawing value from Capital Steel's estate that would otherwise flow to creditors. As the clause was triggered by Capital Steel's insolvency, Deloitte argued that it violated the common law anti-deprivation rule. It also argued that clause VII Q(d) was an unenforceable penalty, rather than a liquidated damages provision.

[12] The chambers judge recognized that the common law anti-deprivation rule prevents parties from contracting out of bankruptcy laws. He stated that if clause VII Q(d) were a liquidated damages provision rather than a penalty, it would not violate the rule.

[13] The chambers judge ultimately found that the clause was a genuine pre-estimate of damages, which imposed liquidated damages and not a penalty. He also held that clause VII Q(d) represented a *bona fide* commercial transaction that did not have as its predominant purpose the deprivation of Capital Steel's property. Consequently, the chambers judge concluded that Chandos could enforce clause VII Q(d) against Deloitte.

IV. Grounds of Appeal and Standard of Review

[14] Deloitte's appeal raises two issues:

1. Does clause VII Q(d) violate the common law anti-deprivation rule?

2. Does clause VII Q(d) impose liquidated damages or a penalty?

[15] The content of the common law anti-deprivation rule and the proper test for invalidating penalty provisions are pure questions of law reviewable for correctness: *Housen v Nikolaisen*, 2002 SCC 33 at para 8, [2002] 2 SCR 235. Absent an extricable legal error, the chambers judge's application of the proper tests is reviewable on a standard of palpable and overriding error: *Housen* at para 36.

V. Analysis

[16] The common law anti-deprivation rule and the rule against penalties are two distinct concepts that must be assessed separately. Clause VII Q(d) may be found unenforceable under either of the two rules. I conclude that clause VII Q(d) conflicts with the anti-deprivation rule, and it is therefore unnecessary for me to consider whether clause VII Q(d) imposes liquidated damages or a penalty.

A. The Common Law Anti-Deprivation Rule

[17] The anti-deprivation rule forms a part of what is referred to as the "fraud on the bankruptcy law" principle. The essence of the fraud on the bankruptcy principle is that parties cannot arrange their affairs through contract in a way that conflicts with the operation of bankruptcy laws: Roderick J Wood, "Direct Payment Clauses and the Fraud Upon the Bankruptcy Law Principle: Re Horizon Earthworks Ltd. (Bankrupt)" (2014) 52:1 Alta LR 171 [Wood, "Fraud Upon the Bankruptcy"]; Anthony Duggan et al, *Canadian Bankruptcy and Insolvency Law*, 3rd ed (Toronto: Emond, 2015) at 297.

[18] The chambers judge commented that there was some debate about whether the anti-deprivation rule applied in Canada and the extent of its application. He ultimately concluded

that it was clear that there was a common law rule, based on public policy, that prevented parties from contracting out of bankruptcy law and that given the rule, he would determine whether clause VII (Q)(d) was an attempt to contract out of bankruptcy law. Deloitte submits that Canadian jurisprudence recognizes the common law anti-deprivation rule. Chandos does not deny the existence of the rule, but contends it has not enjoyed significant application in Canada. My colleague, Wakeling JA, goes further and concludes that the common law anti-deprivation rule is not part of Canadian law. I disagree with his conclusion.

[19] The fraud on the bankruptcy law principle traces its origins from England; by the 19th century, the principle's adoption was certain enough to warrant commentary that "the law is too clearly settled to admit of a shadow of doubt" about its application: *Whitmore v Mason* (1861), 70 ER 1031 at 1034, 2 J & H 204.

[20] The fraud on the bankruptcy law principle can be divided into two distinct sub-rules: Roderick J Wood, *Bankruptcy and Insolvency Law*, 2nd ed (Toronto: Irwin, 2015) at 88 [Wood, "Bankruptcy and Insolvency"]. The first is the *pari passu* rule. This rule invalidates contractual provisions that, if enforced during bankruptcy proceedings, would alter the bankruptcy scheme of distribution. Provisions that offend the *pari passu* rule do not affect the size of the total pot of assets available to creditors but allow certain creditors to receive more than their fair share: Duggan et al at 444; Wood, "Fraud Upon the Bankruptcy" at 177. Under the *pari passu* rule, it is irrelevant whether the contractual provision is triggered by insolvency; arrangements that would have been enforceable against the debtor outside of bankruptcy proceedings, but would alter the scheme of distribution after proceedings begin, are unenforceable against the trustee: Wood, "Fraud Upon the Bankruptcy" at 177.

[21] The second rule of the fraud on the bankruptcy law principle is the anti-deprivation rule. The anti-deprivation rule prevents parties from agreeing to remove property from a bankrupt's estate in the event of insolvency that would have otherwise vested in the trustee: Duggan et al at 297; Wood, "Fraud Upon the Bankruptcy" at 176. Provisions that offend the anti-deprivation rule reduce the total pot of assets available to the bankrupt's creditors. As stated in *Whitmore* at 1034:

> [N]o person possessed of property can reserve that property to himself until he shall become bankrupt, and then provide that, in the event of his becoming bankrupt, it shall pass to another and not to his creditors.

[22] In my view, the fraud on the bankruptcy law principle, including the anti-deprivation rule, has a clear jurisprudential and policy basis that supports its application. The anti-deprivation rule was adopted from England and continues to apply in Canada.

[23] There is no doubt that the *pari passu* rule applies in Canada. In *AN Bail Co v Gingras et al*, [1982] 2 SCR 475, 54 NR 280, the Supreme Court dealt with a direct payment clause in a construction contract. The clause allowed the property owner to pay any amounts owing to the general contractor directly to subcontractors to satisfy the general contractor's obligations. When

the general contractor entered bankruptcy, the trustee argued that this provision was no longer effective. While the provision would not reduce the total amount available to creditors, the subcontractors receiving a direct payment would have received more than what they would have under the applicable legislative scheme. The Supreme Court stated at 487 that:

> It would be to disregard the *Bankruptcy Act* and deprive it of all meaning if the debtor of a bankrupt, instead of paying the trustee, were authorized, by contract or some other means, to pay one or other of the creditors of the bankrupt as he saw fit.

[24] Notably, the contractual arrangement in *Bail* would have been enforceable against the debtor outside of bankruptcy proceedings. And even though, as a general rule, the trustee in bankruptcy enjoys no greater rights than the debtor, it would have been inequitable to enforce the provision against the trustee to alter the legislated scheme of distribution.

[25] This Court applied *Bail* to invalidate a similar provision in *Greenview (Municipal District No 16) v Bank of Nova Scotia*, 2013 ABCA 302, 556 AR 34, as offending the *pari passu* rule.

[26] Canadian courts have also adopted the anti-deprivation rule: *In re Hoskins and Hawkey*, [1877] OJ No 16, 1 OAR 379 (CA); *Re Wetmore*, [1924] NBJ No 6, [1924] 4 DLR 66 (SC (AD)); *Westerman (Re) (Trustee of)*, 1998 ABQB 946, 234 AR 371, rev'd on other grounds 1999 ABQB 708, 275 AR 114; *Knechtel Furniture Ltd (Re)*, [1985] OJ No 1265, 56 CBR (NS) 258 (SC); *Frechette (Re*) (1982), 138 DLR (3d) 61, 42 CBR (NS) 50 (Que SC). *Canadian Imperial Bank of Commerce v Bramalea Inc* (1995), 33 OR (3d) 692, [1995] OJ No 4884 (Ct J (Gen Div)), is often cited as the leading authority. The provision at issue in *Bramalea* would have allowed one party to purchase their insolvent partner's partnership interest at the lesser of book value or fair market value. Blair J accepted the respondent's argument, at 694, that:

> A provision in an agreement which provides that upon an insolvency, value is removed from the reach of the insolvent person's creditors to which would otherwise have been available to them, and places that value in the hands of others ... is void on the basis that it violates the public policy of equitable and fair distribution amongst unsecured creditors in insolvency situations.

[27] The Ontario Court of Appeal recently adopted Blair J's formulation of the rule: *Aircell* at paras 10-12. The rule was again recently recognized by the Ontario Superior Court: *HGC v IESO*, 2019 ONSC 259 at para 100.

[28] A judge of this Court has also recognized the anti-deprivation rule. At issue in *1183882 Alberta Ltd (Sok's Contracting) v Valin Industrial Mill Installations Ltd*, 2012 ABCA 62, 522 AR 285, leave to appeal to SCC refused, [2012] SCCA No 180, was a contractual provision that conveyed an option that had the effect of depriving creditors of one of the debtor's assets. McDonald JA concluded that the provision offended the common law anti-deprivation rule and

was therefore invalid. While McDonald JA was in dissent, the majority did not comment on the provision or the anti-deprivation rule.

[29] There does not appear to be any decision that expressly rejects the anti-deprivation rule's application in Canada. Chandos argues, however, that the Supreme Court of Canada's decision in *Coopérants, Mutual Life Insurance Society (Liquidator of) v Dubois*, [1996] 1 SCR 900, 133 DLR (4th) 643 implicitly abandons the rule. This argument is premised on the basis that the reasoning in *Bramalea* relied, in part, on the Quebec Court of Appeal decision that was overturned by the Supreme Court of Canada in *Coopérants*. In my view, *Coopérants* does not reject the anti-deprivation rule's application in Canada. The outcome in *Coopérants* turned on the fact that there was no evidence the contractual provision at issue prejudiced creditors: Adrienne Ho, "The Treatment of Ipso Facto Clauses in Canada" (2015) 61:1 McGill LJ 139 at 169.

[30] The provision at issue in *Coopérants* allowed the debtor's co-owners, in the event of the debtor's insolvency, to purchase the debtor's interest in certain immovable property at 75 percent of the property's fair market value. Though this type of provision could potentially prejudice creditors, the Supreme Court determined that no prejudicial effect was apparent in the circumstances. The property's fair market value was calculated without considering ownership restrictions that would affect the price obtained through liquidation: *Coopérants* at para 42. The evidentiary record also lacked information about the property's appraisal value, which prevented the Court from identifying any prejudice: *Coopérants* at para 44. The Supreme Court stated at para 40 that:

> The assets available for distribution to the other creditors are not diminished. Even if this may mean that the appellant's claim is satisfied while unsecured monetary claims are not, the other unsecured creditors cannot complain because they will not be suffering any harm.

[31] The Supreme Court's reasoning in *Coopérants* is consistent with the anti-deprivation rule described in *Bramalea*. The anti-deprivation rule is concerned with provisions that have a prejudicial impact on creditors. The rule has no application where the prejudicial effect is not immediately apparent and the party seeking to have the contractual arrangement deemed unenforceable has not established any prejudice.

[32] In summary, the principle that parties cannot contract out of bankruptcy laws has a lengthy common law history, dating back at least to the 18th century in England: Wood, "Fraud Upon the Bankruptcy" at 171. The anti-deprivation rule in particular has received positive treatment from Canadian courts. Contracting parties cannot rely on provisions that are engaged by a debtor's insolvency and remove value from the debtor's estate to the prejudice of creditors. Much like the *pari passu* rule, I accept that it would disregard the *BIA* and deprive it of all meaning if a bankrupt could agree that assets would be diverted out of its estate in the event of insolvency: *Bail* at 487.

B. Effect of the Statutory *Ipso Facto* Provisions

[33] The *BIA* includes provisions invalidating certain types of contract clauses that take effect upon the occurrence of a debtor's insolvency. However, the statutory provisions apply only to corporate restructuring, consumer proposals, and consumer bankruptcies. None of the *BIA* provisions applies to corporate bankruptcies, meaning that they do not apply in this case. Chandos contends and my colleague concludes that the *BIA* provisions codify and, in the present context, supplant the common law anti-deprivation rule. In my view, a more appropriate conclusion is that the statutory provisions were intended to expand the common law to provide protection to debtors in situations where the anti-deprivation rule would not have protected them.

[34] Provisions that offend the anti-deprivation rule are also referred to as *ipso facto* clauses, a term which encompasses any provision that sets out the consequences of a debtor's insolvency: *Black's Law Dictionary*, 10th ed, *sub verbo* "*ipso facto* clause"; Duggan et al at 296. However, not all *ipso facto* clauses offend the anti-deprivation rule. For example, some *ipso facto* clauses operate to terminate executory agreements between an insolvent debtor and another contracting party: Duggan et al at 296; Wood, "Bankruptcy and Insolvency" at 178. Eliminating a debtor's opportunity to perform a contract does not necessarily result in a deprivation of value that would prejudice creditors.

[35] The United States Code expressly prohibits *ipso facto* provisions regardless of whether they offend the anti-deprivation rule: 11 USC § 365(e); 11 USC § 541(c). The provisions read, in part:

> 365(e)(1) Notwithstanding a provision in an executory contract or unexpired lease, or in applicable law, an executory contract or unexpired lease of the debtor may not be terminated or modified, and any right or obligation under such contract or lease may not be terminated or modified, at any time after the commencement of the case solely because of a provision in such contract or lease that is conditioned on—
>
> > (A) the insolvency or financial condition of the debtor at any time before the closing of the case;
> >
> > (B) the commencement of a case under this title; or
> >
> > (C) the appointment of or taking possession by a trustee in a case under this title or a custodian before such commencement.
>
> …
>
> 541(c)(1) … an interest of the debtor in property becomes property of the estate … notwithstanding any provision in an agreement, transfer instrument, or applicable nonbankruptcy law—

> …
>
> (B) that is conditioned on the insolvency or financial condition of the debtor, on the commencement of a case under this title, or on the appointment of or taking possession by a trustee in a case under this title or a custodian before such commencement, and that effects or gives an option to effect a forfeiture, modification, or termination of the debtor's interest in property.

[36] In contrast, section 65.1 of the *BIA*, which applies when a commercial debtor has filed a notice of intention or proposal, is representative of the *BIA*'s *ipso facto* provisions. The provision reads, in part:

> 65.1 (1) If a notice of intention or a proposal has been filed in respect of an insolvent person, no person may terminate or amend any agreement, including a security agreement, with the insolvent person, or claim an accelerated payment, or a forfeiture of the term, under any agreement, including a security agreement, with the insolvent person, by reason only that
>
> (a) the insolvent person is insolvent; or
>
> (b) a notice of intention or a proposal has been filed in respect of the insolvent person.

[37] Sections 66.34 and 84.2 of the *BIA* are similarly worded and invalidate *ipso facto* clauses in the context of consumer proposals and consumer bankruptcies, respectively. Notably, all of these sections mirror 11 USC § 365(e) but make no mention of the property deprivation targeted by 11 USC § 541(c). In my view, this is because the *BIA* provisions were primarily intended to prohibit *ipso facto* clauses that terminate or modify executory agreements.

[38] The prohibition on *ipso facto* clauses initially applied only to commercial restructuring and consumer proposals, as sections 65.1 and 66.34 of the *BIA* were enacted prior to section 84.2. In other words, Parliament first saw fit to prohibit the use of certain *ipso facto* provisions in contexts where debtors are attempting to reach a compromise with their creditors. In those contexts, it is important to maintain the *status quo* by allowing debtors to continue to rely on existing contractual relationships: Ho at 146. Preserving such relationships helps provide debtors with the opportunity to successfully restructure their liabilities: *Crystalline Investments Ltd v Domgroup Ltd* (2002), 58 OR (3d) 549 at paras 6-8, 210 DLR (4th) 659 (CA), aff'd 2004 SCC 3, [2004] 1 SCR 60. The same concern is not as pressing with respect to a corporate bankruptcy, as the corporate entity is destined for liquidation: Ho at 182.

[39] For consumers, the *ipso facto* provisions provide further protection, preventing creditors from terminating basic services even where the debtor has failed to make required payments: *BIA*, ss 66.34(3), 84.2(3).

[40] For example, section 66.34(3) provides:

> 66.34 (3) Where a consumer proposal has been filed in respect of a consumer debtor, no public utility may discontinue service to that consumer debtor by reason only that
>
> (a) the consumer debtor is insolvent,
>
> (b) a consumer proposal has been filed in respect of the consumer debtor, or
>
> (c) the consumer debtor has not paid for services rendered, or material provided, before the filing of the consumer proposal
>
> until the consumer proposal has been withdrawn, refused by the creditors or the court, annulled or deemed annulled.

[41] In the 2009 amendments to the *BIA*, the *ipso facto* prohibitions were extended to consumer bankruptcies. This was motivated by the "fresh start" principle that stems from the discharge available to consumer bankrupts. Prohibiting *ipso facto* termination clauses ensures that a debtor seeking a fresh start cannot be "unreasonably evicted from their home, denied basic and essential services or denied other benefits to which they would otherwise be entitled": Duggan et al at 296, citing Industry Canada, *Bill C-55 Clause-by-Clause Analysis* (6 September 2011). The Senate Standing Committee on Banking, Trade and Commerce, which recommended the reform, similarly stated that *ipso facto* clauses "should be unenforceable in order to ensure that debtors continue to have access to the basic services that they and their families need": Senate, Standing Committee on Banking, Trade and Commerce, *Debtors and Creditors Sharing the Burden*: *A Review of the Bankruptcy and Insolvency Act and the Companies' Creditors Arrangement Act* (November 2003) at 75 (Chair: Hon Richard H. Kroft). This concern has no bearing on corporate bankruptcies.

[42] The statutory provisions exhibit a debtor-protection purpose with two facets. First, they ensure that consumer and corporate debtors seeking to restructure their affairs have the time and resources to do so by maintaining the *status quo*. Second, the provisions extend protection to all consumer debtors to prevent the termination of basic services and executory agreements. This protection recognizes the impact such terminations would have on individuals and their families. These purposes are either less pressing or completely inapplicable to corporate bankruptcies, which may explain why the statutory provisions were not extended to those situations. Moreover, the *debtor*-protection purpose of the statutory provisions stands in contrast to the anti-deprivation rule, which protects *creditors* by ensuring a fair and equitable distribution of the debtor's estate:

Bramalea at 694. In my view, this difference in purpose suggests that the statutory provisions expanded the common law. It does not lead to the inference that the common law rule was replaced.

[43] Furthermore, the *BIA* provisions represent only a partial codification of the anti-deprivation rule: Wood, "Bankruptcy and Insolvency" at 90. None of the statutory provisions mentions a deprivation of assets from the debtor's estate – the sole concern of the anti-deprivation rule. In my view, there are at least some deprivations of property that would not be considered a termination, amendment, acceleration, or forfeiture of a term caught by the language of the statutory provisions. Professor Wood also notes that "there may be instances where the transaction arises out of a grant rather than an agreement or involves a transfer of an asset to a third party so as to take it outside the ambit of the statutory provision[s]": Wood, "Bankruptcy and Insolvency" at 90.

[44] Even if the *BIA* provisions do fully capture the common law rule, their scope is certainly much broader. The anti-deprivation rule is not generally concerned with the termination of agreements unless value is removed from the debtor's estate. The anti-deprivation rule also differentiates between the defeasance of an absolute interest and grants that create limited interests from the outset, holding that the latter are enforceable: *Belmont Park Investments Pty Ltd v BNY Corporate Trustee Services Ltd*, [2011] UKSC 38 at paras 84-87, [2012] 1 All ER 505; *Knechtel*. The *BIA* provisions do not have the same limitation, extending their application to interests such as leases and licenses: Wood, "Bankruptcy and Insolvency" at 90. I conclude that expansion of the common law in the restructuring and consumer bankruptcy contexts does not mean that the anti-deprivation rule was eliminated for corporate bankruptcies.

[45] In my view, the distinctions between the statutory provisions and the common law anti-deprivation rule prohibit the inference that the statutory provisions have occupied the field with respect to *ipso facto* clauses. As the *BIA* provisions and the anti-deprivation rule serve different purposes, and the overlap between them is not extensive, Parliament's legislative prohibition of one type of clause does not invite the inference that it condones the other. The statutory provisions expand the common law, ***protecting debtors*** by prohibiting *ipso facto* clauses that would not have been caught by the anti-deprivation rule. The anti-deprivation rule continues to apply, ***protecting creditors*** by ensuring that a bankrupt's property is distributed in accordance with the *BIA*'s scheme of distribution.

C. The Test for Applying the Anti-Deprivation Rule

[46] Even if the anti-deprivation rule applies in Canada, Chandos contends that it does not invalidate good faith commercial transactions and urges this Court to adopt the test enunciated by the United Kingdom Supreme Court in *Belmont*. The court concluded that the anti-deprivation rule does not apply to "bona fide commercial transactions which do not have as their predominant purpose, or one of their main purposes, the deprivation of the property of one of the parties on bankruptcy": *Belmont* at para 104. This test looks at the purpose of the provision rather than its

effect. I decline to adopt *Belmont.* The purpose-based test articulated in *Belmont* is inconsistent with Canadian cases applying the anti-deprivation rule and would eliminate virtually all of the rule's utility.

[47] Canadian cases applying the anti-deprivation rule adopt an effects-based approach to determining the validity of a contractual provision: Wood, "Bankruptcy and Insolvency" at 89-90. Blair J in *Bramalea*, stated that the fraud on the bankruptcy law principle targets "not necessarily 'fraud' in the sense of dishonesty or impropriety, but fraud in the effect": *Bramalea* at 694. And while the Supreme Court of Canada did not address the issue directly in *Coopérants*, an effects-based approach is implicit in the court's determination that no prejudicial effect was evident in the circumstances: *Coopérants* at para 44.

[48] Cases dealing with the *pari passu* rule similarly apply an effects-based approach. *Bail* and *Greenview* both dealt with contractual provisions allowing payments to be made directly to subcontractors to satisfy the obligations of a general contractor. Such provisions are generally motivated by the inability of subcontractors to acquire liens over public lands: *Greenview* at para 31; *Bail* at 483-484. The provisions clearly served a legitimate commercial purpose. Nevertheless, applying them after the general contractor had entered bankruptcy proceedings would have operated to disrupt the bankruptcy scheme of distribution. Both this Court and the Supreme Court of Canada refused to allow such a result.

[49] In *Belmont* at paras 78-79, the court distinguished between the anti-deprivation rule and the *pari passu* rule, holding that a purpose-based approach applies only to the former. However, both rules stem from the basis that it would be inequitable to creditors if parties could contract out of the bankruptcy scheme. I see no principled basis to adopt differing standards for the two rules.

[50] Furthermore, adoption of a purpose-based approach in the United Kingdom has received criticism for defeating the purpose of the anti-deprivation rule. Professor Worthington notes that "insisting that breach of the [anti-deprivation] rule depends on a deliberate intention to evade the insolvency law effectively emasculates this limb of the [fraud on the bankruptcy principle]": Sarah Worthington, "Good Faith, Flawed Assets and the Emasculation of the UK Anti-Deprivation Rule" (2012) 75:1 Mod L Rev 112 at 117. Professor Wood similarly concludes that Canadian courts should not adopt a purpose-based test: Wood, "Fraud Upon the Bankruptcy" at 184. The purpose of the anti-deprivation rule is to ensure that contracting parties cannot opt out of the distribution of assets mandated by the *BIA*. This purpose is best served by invalidating provisions that operate in the event of insolvency and have the effect of prejudicing creditors.

[51] Finally, I do not accept that an effects-based approach would inappropriately undermine the values of freedom of contract and party autonomy, given the creditor-protection purpose of the fraud on the bankruptcy principle. The Supreme Court recognized this in *Coopérants* at para 41, stating that contracts signed in good faith should be respected, "*unless* the obligations contained therein are prejudicial to the other creditors and give rise to an unjust preference in light of all the circumstances" [emphasis added]. Freedom of contract is a much more central consideration when

enforcing provisions that have been negotiated by the parties they affect. A party who might become insolvent has no motivation to negotiate a clause that directs property out of its estate upon insolvency. At the moment the clause becomes operative, the insolvent party is set to lose the property regardless of the contractual provision. The creditors who are impacted by the clause do not have a seat at the negotiating table.

[52] For all of these reasons, I decline to adopt the purpose-based approach espoused in *Belmont*. Canadian authorities on the anti-deprivation rule support an effects-based approach to determining whether a provision is enforceable against the trustee in bankruptcy. Moreover, I agree with the conclusion that considering the purpose of a contractual provision would all but sterilize the anti-deprivation rule. The anti-deprivation rule applies to provisions that operate in the event of insolvency and, in effect, remove value from a bankrupt's estate to the prejudice of the bankrupt's creditors. It follows that I do not endorse the new test proposed by my colleague.

VI. Application

[53] The chambers judge correctly identified the existence and application of the fraud on the bankruptcy principle in Canada. In outlining the scope of the anti-deprivation rule, however, the chambers judge erred. The chambers judge adopted the purpose-based approach set out by the Supreme Court of the United Kingdom in *Belmont*. He stated that if the clause were a genuine pre-estimate of damages, or a *bona fide* commercial transaction not premised on the avoidance of bankruptcy laws, it would have to be upheld.

[54] As I have indicated, the proper approach is to look at the effect of clause VII Q(d), rather than its purpose. Whether the provision is a liquidated damages or penalty clause is a separate analysis.

[55] Looking at the effect of clause VII Q(d), this case is not comparable to *Coopérants*, where there was no established prejudice to creditors. Clause VII Q(d) effectively redirects $126,818.39 to Chandos that would have otherwise formed part of Capital Steel's estate and gives Chandos a further claim for $10,511.66. Other provisions of Clause Q address the ability of Chandos to complete the work, to recover the cost to complete the work, and to withhold a percentage of the contract price until all warranties have expired. It is only Clause VII Q(d) which is at issue. While Chandos undoubtedly has legitimate commercial interests it was seeking to protect, it would conflict with the *BIA*'s scheme of distribution if Chandos could elevate itself to a preferred status through such a contractual arrangement. The common law anti-deprivation rule invalidates clause VII Q(d) and Chandos cannot rely on the provision in defence of a claim for payment by the trustee.

[56] Given that clause VII Q(d) contravenes the common law anti-deprivation rule, it is unnecessary to address whether it also would constitute an unenforceable penalty.

VII. Conclusion

[57] The appeal is allowed. Chandos is not entitled to rely on clause VII Q(d) of the subcontract against Deloitte, the trustee in bankruptcy.

Appeal heard on November 28, 2017

Reasons filed at Edmonton, Alberta
this 29th day of January, 2019

Rowbotham J.A.

I concur: Veldhuis J.A.

Dissenting Reasons for Judgment Reserved of
The Honourable Mr. Justice Wakeling

I. Introduction

[58] This case presents challenging contract and bankruptcy law issues of national importance.

[59] At issue is the enforceability of a construction-contract term providing that the subcontractor forfeits ten percent of its total fee if the subcontractor commits an act of bankruptcy.

[60] I agree with the chambers judge that it is enforceable and dismiss the trustee in bankruptcy's appeal.

A. The Penalty Rule Issue

[61] For over 200 years courts in England[1] and the United States[2] and, for shorter periods of time in Canada,[3] Australia,[4] New Zealand[5] and Hong Kong,[6] have declined to enforce contractual

[1] *Holles v. Wyse*, 23 Eng. Rep. 787 (Ch. 1693)(the Court refused to enforce a default-interest-uplift term because it was a penalty); *Sloman v. Walter*, 28 Eng. Rep. 1213 (Ch. 1783)(the Court refused to enforce a promise a coffee-house partner made to pay £500 to another partner if the promisor refused to make available a particular room in the coffee-house whenever the promisee demanded it: "where a penalty is inserted merely to secure the enjoyment of a collateral object [access to the coffee-house room], the enjoyment of the object is considered as the principal intent of the deed, and the penalty only as accessional, and therefore, only to secure the damage really incurred"); *Hardy v. Martin*, 29 Eng. Rep. 1046 (Ch. 1783)(the Court enjoined by injunction a promissee who secured a common law judgment on a bond from enforcing it because the promisor breached his obligation not to operate a competitive brandy-merchant business within a defined area and time); *Astley v. Weldon*, 126 Eng. Rep. 1318 (Common Pleas 1801)(the Court characterized an actress' promise to pay 200£ if she failed to discharge her obligations to the theatre owner as a penalty and unenforceable because the parties did not intend her to pay £200 for any breach regardless of its nature); *Kemble v. Farren*, 130 Eng. Rep. 1234 (Common Pleas 1829)(the Court characterized a comedian's promise to pay £1000 if he failed to discharge his obligations to the theatre owner as an unenforceable penalty because the parties could not have intended this to be the consequence of minor and major breaches alike); *Betts v. Burch*, 157 Eng. Rep. 938 (Ex. 1859) (the Court upheld a jury verdict that the purchaser of stock-in-trade was not obliged to pay the vendor £50 for breach of the purchase-and-sale agreement as it was an unenforceable penalty); *Commissioner of Public Works v. Hills*, [1906] A.C. 368 (P.C.) (Cape of Good Hope) (the Court held that a ten per cent forfeit of retained moneys was unenforceable because it did not reflect the promisee's actual loss); *Pearl Assurance Co. v. South Africa*, [1934] A.C. 570 (P.C.) (S. Africa); (the Privy Council declared that a term in a commercial agreement acknowledging that a £10,000 deposit be forfeited on the occurrence of certain conditions and described as liquidated damages was an unenforceable penalty); *United Dominions Trust (Commercial) v. Ennis*, [1967] 2 All E.R. 345 (C.A.) (the Court refused to enforce a term in a consumer hire-purchase contract that obliged the hirer to pay a minimum of two-thirds of the hire-purchase price on early termination of the hire-purchase agreement); *Gilbert Ash (Northern) Ltd*. v. *Modern Engineering (Bristol) Ltd.*, [1974] A.C. 689, 703 (H.L. 1973) per Lord Morris of Borth-y-Gest ("Such a heavily penalising provision ought not to be accorded any validity"); *Jobson v. Johnson*, [1989] 1 All E.R. 621 (C.A.

1988) (the Court characterized a term in a share-purchase agreement that required the purchaser of shares in a football club to deliver the shares to the vendor upon default for one-quarter of the instalment amounts paid before default as an unenforceable penalty); *Workers Trust Bank Ltd. v. Dojap Ltd.*, [1993] A.C. 573 (P.C.)(Jamaica)(the Privy Council allowed a land purchaser's appeal and held that the forfeiture of a twenty-five percent deposit was an unenforceable penalty); *Jeancharm Ltd. v. Barnet Football Club Ltd.*, [2003] EWCA Civ 58 (the Court allowed an appeal on the ground that a 260 percent annual interest on late payments was an unenforceable penalty) & *CMC Group Plc & Ors v. Zhang* [2006] EWCA Civ 408 (the Court allowed the appeal on the ground that the key term in the settlement agreement was primarily a deterrent and not a genuine preestimate of damages).

[2] *Perkins v. Lyman*, 11 Mass. 76 (Sup. Ct. 1814)(the Court held that a ship vendor's promise not to do business in the northwest coast of America and pay $8000 if he did to be an unenforceable penalty); *Robeson v. Whitesides*, 16 Serge & Rawle 320; 1827 Pa. Lexis 88 (Sup. Ct.) (the Court held that a $1000 defeasible bond made void upon the obligor's extinguishment of encumbrances on sold property within a nine month period was an unenforceable penalty); *Van Buren v. Digges*, 52 U.S. 461, 477 (1851)("The clause of the contract providing for the forfeiture of ten per centum on the amount of the[building] contract price, upon a failure to complete the work by a given day, cannot properly be regarded as an agreement or settlement of liquidated damages. … [I]t has no necessary or natural connection with the measure or degree of injury which may result from a breach of contract, or from an imperfect performance. It implies an absolute infliction, regardless of the nature and extent of the causes by which it is superinduced"); *Greenblatt v. McCall*, 67 Fla. 165, 169 (Sup. Ct. 1914)(the Court concluded that a retailer's promise to pay a sum equal to two-thirds of the charges for the duration of the supply contract following breach was an unenforceable penalty); *Advance Amusement Corp. v. Franke*, 109 N.E. 471 (Ill. Sup. Ct. 1915) (the Court upheld lower court determinations that a theatre-rental deposit of $2500 was not liquidated damages and on breach of the rental agreement the theatre owner was not entitled to keep it); *Priebe & Sons, Inc. v. United States*, 332 U.S. 407, 418 (1947) per Frankfurter, J. ("exactions for a breach of contract not giving rise to damages and merely serving as added pressure to carry out punctiliously the terms of a contract, are not enforced by courts. In familiar language, penal provisions in a contract ... are not enforceable"); *Wilmington Housing Authority v. Pan Builders, Inc.*, 665 F. Supp. 351, 354 (D. Del. 1987)("If the provision fails to meet one of these criteria, the damages stemming from a breach being easily ascertainable or the amount fixed excessive, the provision is void as a penalty"); *City of Rye v. Public Service Mutual Insurance Co.*, 315 N.E. 2d 458 (N.Y. Ct. App. 1974) (the Court refused to enforce against a surety a construction bond for late completion of a large residential complex on the ground that it provided for a penalty) & American Law Institute, The Restatement (Second) of Contracts (1981) §356(1) ("Damages for breach by either party may be liquidated in the agreement but only at an amount that is reasonable in light of the anticipated or actual loss caused by the breach and the difficulties of proof of loss. A term fixing unreasonably large liquidated damages is unenforceable on grounds of public policy as a penalty").

[3] *Empire Loan and Savings Co. v. McRae*, 5 O.L.R. 710 (H. Ct. 1903) (the Court upheld a Master's decision refusing to give force to a term it characterized as a penalty); *Townsend v. Rumball*, 19 O.L.R. 433 (Div. Ct. 1909)(the Court set aside a County Court judgment on the ground that a noncompetition term in a business-sale contract was a penalty and not liquidated damages); *St. Catherines Improvement Co. v. Rutherford*, 26 O.W.R. 76 (K.B. 1914)(the Court refused to enforce a stipulated-payment-on-breach term characterizing it as a penalty); *Shatilla v. Feinstein*, [1923] 3 D.L.R. 1035 (Sask. C.A.) (the Court characterized a promise by a wholesale dry-goods merchant to pay the purchaser of the business $10,000 if the vendor engaged in a competitive business as an unenforceable penalty); *MacDonald v. N.W. Biscuit Co.*, [1924] 1 D.L.R. 987, 998-99 (Alta. Sup. Ct. App. Div.)(the Court declared a provision in a construction contract that deprived the contractor of an amount over and above the cost of repairing deficient work to be an unenforceable penalty); *Waugh v. Pioneer Logging Co.*, [1949] S.C.R. 299 (the Court characterized a provision in a commercial logging contract that entitled the vendor of the timber rights to claim a portion of the proceeds of the sale of timber held in trust as an unenforceable penalty); *Charterhouse Leasing Corp. v. Sanmac Holdings Ltd.*, 57 W.W.R. 615 (Alta. Sup. Ct. 1966) (the Court held that a term obliging the lessee of equipment on default to pay immediately the whole balance due under the lease was an unenforceable penalty); *Canadian Acceptance Corp. v. Regent Park Butcher Shop Ltd.*, 3 D.L.R. 3d 304 (Man. C.A. 1969)(the Court held that an acceleration-payment term in an

equipment-lease agreement was an unenforceable penalty); *H.F. Clarke Ltd. v. Thermidaire Corp*, [1976] 1 S.C.R. 319, 339 (1974)("I would characterize the exaction of gross trading profits for a three-year period as a penalty [and unenforceable] ... The respondent is, however, entitled to recover its provable damages for the breach of covenant"); *Unilease Inc. v. York Steel Construction Ltd.*, 83 D.L.R. 3d 275 (Ont. C.A. 1978) (the Court allowed the appeal on the ground that the accelerated-lease-payment-on-default term was an unenforceable penalty); *Dial Mortgage Corp. v. Baines*, 15 Alta. L.R. 2d 211 (Q.B. 1980)(the Court declined to enforce a stipulated-payment-on-breach term in a mortgage application because it was a penalty); *Prince Albert Credit Union v. Johnson*, 131 D.L.R. 3d 710 (Sask. Q.B. 1982)(the Court held that a term requiring the defaulting borrower to pay a designated sum to cover the lender's resulting expenses on default was an unenforceable penalty); *Dezcam Industries Ltd. v. Kwak*, [1983] 5 W.W.R. 32 (B.C.C.A.)(the Court reversed the original court and held that the licencee's obligation to pay $85,000 was an unenforceable penalty); *B.L.T. Holdings Ltd. v. Excelsior Life Insurance Co.*, 52 A.R. 1 (Q.B. 1984)(the Court characterized a mortgage standby fee of $61,500 as an unenforceable penalty), rev'd, [1986] 6 W.W.R. 534 (C.A.); *Federal Business Development Bank v. Eldridge*, 76 N.B.R. (2d) 399 (C.A. 1986) (the Court upheld the trial judgment declaring a commitment fee of three percent an unenforceable penalty); *Newman, Hill, Duncan & Lacoursiere v. Murray*, [1987] B.C.J. No. 2326 (C.A.)(the Court held that a provision in an employment agreement obliging the employee who breached a noncompetition term to pay 150 % of the fees the plaintiff charged the client that the defendant serviced contrary to the employment agreement as an unenforceable penalty); *Deer Valley Shopping Centre Ltd. v. Sniderman Radio Sales and Services Ltd.*, 67 Alta. L.R. 2d 203 (Q.B. 1989)(the Court declined to enforce an interest-escalation-on-overdue rent term because it was an unenforceable penalty); *Ashland Scurlock Permian Canada Ltd. v. NESI Energy Marketing Canada Ltd. (Bankrupt)*, [1999] 1 W.W.R. 364, 371 (Alta. Q.B. 1998) (the Court declared a provision in a natural gas sales contract as an unenforceable penalty because "the amount of the multiple used in the formula creates an extravagant amount which cannot be regarded as having any real relation to any loss which Ashland could possibly sustain"); *Cracknell v. Jeffrey*, 284 A.R. 372, (Prov. Ct. 2001) (the Court refused to enforce a property-lease term that obliged the tenant to pay a $5 assessment for every day rent is outstanding); *Place Concorde East Limited Partnership v. Shelter Corp. of Canada*, [2003] O.J. No. 5437; 43 B.L.R. 3d 54 (Super. Ct.)(the Court declined to enforce an interest-escalation term on a promissory note default); *MTK Auto West Ltd. v. Allen*, 2003 BCSC 1613 (the Court declared a provision in a vehicle-purchase agreement that obliged the purchaser to pay the car dealer $5000 if the purchaser sold the vehicle in the United States contrary to the terms of the vehicle-purchase agreement to be an unenforceable penalty) & *Dundas v. Schafer*, 2014 MBCA 92; 377 D.L.R. 4th 485 (the Court refused to enforce a term in a prenuptial agreement that obliged the wife to pay the husband $20,000 if she challenged the prenuptial agreement on the ground that it was a penalty).

[4] *O'Dea v. Allstates Leasing System (W.A.) Pty. Ltd.*, [1983] HCA 3, ¶15; 152 C.L.R. 359, 374 (the High Court held that a stipulated-payment-on-breach term in a truck-lease contract was an unenforceable penalty); *Paciocco v. Australia and New Zealand Banking Group*, [2016] HCA 28,¶74; 258 C.L.R. 525, 558 per Gageler, J. ("The ultimate question ... is whether the contractual stipulation for the late payment fee was unenforceable as a penalty at common law").

[5] *T.K. (Hong Kong) Ltd. v. Diamond Milk Formulas Ltd.*, [2016] NZHC 2642, ¶39 ("before there can be any question of disallowance of penalties, it must involve the contract imposing a penalty in circumstances where it provides for a sanction to be paid by a party breaking the contract which exceeds the likely loss that will flow from the breach").

[6] *Leatra Co. v. Wing*, [1978] HKDC 32 (the Court refused to enforce a termination term in an employment contract because it was not a pre-estimate of damages; it was a penalty); *Arnold & Co. v. Attorney General*, [1989] HKCFI 275 (the Court declared a fee-reduction-for-delay term in a construction contract as an unenforceable penalty); *Polyset Ltd. v. Panhandat Ltd.*, [2002] HKCFA 15 (the Court held that a term in a commercial land agreement allowing the vendor to keep $40.25 million in deposits in a $115 million transaction on the failure of the purchaser to close was an unenforceable penalty); *Savino Del Bene China Ltd. v. Convac Technologies Ltd.*, [2002] HKDC 106 (the Court refused to enforce a term in a freight contract relieving the shipper of the obligation to pay the freight forwarder because part of the shipment was not delivered on time); *Ricoh Hong Kong Ltd. v. Maxwin Digital Printing Ltd.*, 2008

stipulated-consequence-on-breach terms[7] that they characterized as penalties and contrary to public policy. As a consequence, in spite of the promisor's express agreement to the contrary, the disappointed promisee has had to prove the damages caused by the promisor's contract breach, just as the promisee would have had to do if there had been no stipulated-consequence-on-breach term.[8] These and related propositions are known as the common law penalty rule.[9]

HKDC 146 (the Court characterized an acceleration-payment in an equipment hire-purchase agreement as an unenforceable penalty); *Canning International Ltd. v. Freenet Asia Ltd.*, [2011] HKDC 1595 (the Court characterized a delay-charge-reduction term in a clothing manufacture contract as an unenforceable penalty) & *Sun Champ Investment Ltd. v. Green Leaves Trade Investment Ltd.*, [2013] HKDC 1461 (the Court refused to enforce a term in a property sale agreement obliging the vendor to pay a stipulated sum on its failure to convey good title, characterizing the term as an unenforceable penalty).

[7] This is a contractual term that imposes an obligation on a promisor to pay a sum of money to the promisee or do some other thing for the promisee's benefit, or accept some other detriment for the promisee's benefit if the promisor fails to discharge a specified obligation in the agreement. Scottish Law Commission, Discussion Paper on Penalty Clauses (No. 162) 11 (November 2016) ("[The Scottish Law Commission] recommended that judicial control over contractual penalties should apply whether the penalty was expressed in monetary terms or in some other way. The basis of our recommendation was that there was no apparent reason why a provision should escape control simply because it is in the form of a penalty other than the payment of money"). E.g., *Jobson v. Johnson*, [1989] 1 All E.R. 621, 628 (C.A. 1988) (the Court characterized a term in a football-club share-sale contract that obliged the purchaser to transfer ownership of the shares back to the vendor for a fraction of the price the purchaser had paid before the purchaser defaulted on an instalment payment as a penalty) & *Cavendish Square Holding BV v. El Makdessi*, [2015] UKSC 67, ¶16; [2016] A.C. 1172, 1197 (S.C.) per Lord Neuberger & Lord Sumption ("there is no reason why an obligation to transfer assets (either for nothing or at an undervalue) should not be capable of constituting a penalty"), ¶170 & [2016] A.C. at 1253-54 per Lord Mance ("the doctrine should [not] be confined to cases of payment of money. It would be absurd to draw a rigid distinction between a requirement to transfer money and property. It would also be absurd to draw such a distinction between them and the withholding of moneys due. Such uncertainties as may exist regarding the doctrine's applicability to deposits or to clauses forfeiting pre-payments must await decision in due course") & ¶226 & [2016] A.C. at 1270 per Lord Hodge ("I see no principled reason why the law on penalties should be confined to clauses that require the contract-breaker to pay money in the event of breach and not extend to clauses that in the same circumstances allow the innocent party to withhold moneys which are otherwise due").

[8] *Cavendish Square Holding BV v. El Makdessi*, [2015] UKSC 67, ¶9; [2016] A.C. 1172, 1195 per Lord Neuberger & Lord Sumption ("Deprived of the benefit of the provision, the innocent party is left to his remedy in damages under the general law"); *Scandinavian Trading Tanker Co. v. Flota Petrolera Ecuatoriana (Scaptrade)*, [1983] 2 A.C. 694, 702 per Lord Diplock ("The classic form of relief against ... a penalty clause has been to refuse to give effect to it, but to award the common law measure of damages for the breach of the primary obligation instead"); *Dunlop Pneumatic Tyre Co. v. New Garage and Motor Co.*, [1915] A.C. 79, 100 (H.L. 1914) per Lord Parmoor ("If the Court ... comes to the conclusion that the parties have made a mistake in calling the agreed sum liquidated damages, and that such sum is not really a pactional pre-estimate of loss within the contemplation of the parties at the time when the arrangement was made, but a penal sum inserted as punishment on the defaulter irrespective of the amount of any loss which could at the time have been in contemplation of the parties, then such sum is a penalty, and the defaulter is only liable in respect of damages which can be proved against him") & *United States v. Bethlehem Steel Co.*, 205 U.S. 105, 119 (1907) ("[the courts] tendency was to construe language as a penalty, so that nothing but the actual damages sustained by the party aggrieved could be received").

[62] The classic penalty rule – a stipulated-consequence-on-breach term that is a penalty and not a genuine pre-estimate of damage is unenforceable – is confusing and complex[10] and produces inconsistent results. Its value has been questioned for almost as long as it has existed.

[63] In 2015 Lord Neuberger and Lord Sumption, of the United Kingdom Supreme Court, described the penalty rule in unflattering language:[11] "The penalty rule in England is an ancient, haphazardly constructed edifice, which has not weathered well, and which in the opinion of some should simply be demolished ...".

[64] These judges were not the penalty rule's first detractors.

[65] There were a number of high profile nineteenth century critics. Lord Eldon railed against the penalty rule in 1811,[12] observing that the rule was "utterly without foundation". Justice Ruggles of New York's highest court acknowledged in an 1854 opinion that "[t]he ablest of judges have declared that they felt themselves embarrassed in ascertaining the principle on which the decisions [refusing to enforce stipulated-consequence-on-breach terms] were founded".[13] In 1859,

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[9] The penalty rule is not an alien concept in the civil law. See generally Scottish Law Commission, Review of Contract Law: Discussion Paper on Penalty Clauses 15-18 (Discussion paper No. 162 November 2016) for a discussion of the law of France, Germany and the Netherlands.

[10] *Mortgage Makers Inc. v. McKeen*, 2009 NBCA 61, ¶39; 312 D.L.R. 4th 82, 100 ("The above summary attests to the complexity of the common law surrounding the enforcement of clauses that pre-determine damages for breach of contract").

[11] *Cavendish Square Holding BV v. El Makdessi*, [2015] UKSC 67, ¶3; [2016] A.C. 1172, 1192. Lord Carnwath agreed with his colleagues.

[12] *Hill v. Barclay*, 34 Eng. Rep. 238, 239 (Ch. 1811). See also *Astley v. Weldon*, 126 Eng. Rep. 1318, 1321 (Common Pleas 1801) per Lord Eldon ("when their case came before me ..., I felt as I have often done before in considering the various cases on this head, much embarrassed in ascertaining the principle upon which those cases were founded") & *Robophone Facilities Ltd. v. Blank*, [1966] 3 All E.R. 128, 142 (C.A.) per Diplock, C.J. ("I make no attempt, where so many others have failed, to rationalize this common law rule").

[13] *Cotheal v. Talmadge*, 9 N.Y. 551, 553 (Ct. App. 1854). Other American judges have subsequently expressed similar sentiments. E.g., *Brecher v. Laikin*, 430 F. Supp. 103, 106 (S.D.NY. 1977) ("Liquidated damages provisions have a checkered history"); *Callanan Road Improvement Co. v. Colonial Sand & Stone Co.*, 72 N.Y.S. 2d 194, 196 (Sup. Ct. App. Div. 1947) ("Many more complex and intrinsically less tractable subjects have been reduced to order; this one, from the struggles of the English judges with it before the Revolution to the present time, remains oddly elusive"); *Evans v. Moseley*, 114 P. 374, 377 (Kan. Sup. Ct. 1911) ("There is no branch of law on which unanimity of decision is more difficult to find or on which more illogical and inconsistent holdings may be found"); *Wilson v. Mayor of Baltimore*, 34 A. 774, 775 (Md. Ct. App. 1896) ("Whether a sum named in a contract to be paid by a party in default on its breach is to be considered liquidated damages or merely a penalty, is one of the most difficult and perplexing inquiries encountered in the construction of written agreements. The solution of that question ... [is] to some extent controlled by artificial general rules which are not wholly in harmony with the ordinary canons of construction); *Gobble v. Linder*, 76 Ill. 157, 158 (Sup. Ct. 1875) (" No branch of the law is involved in more obscurity, by contradictory decisions, than whether the sum named in an agreement to secure performance will be treated as liquidated damages or as penalty") & *Jaquith v. Hudson*, 5 Mich. 123, 133 (Sup. Ct. 1858)("It is not to be denied that

Baron Martin[14] of the English Court of Exchequer expressed his frustration with the penalty rule. He complained that binding precedent precluded him from declaring that "parties are at liberty to enter into any bargain they please" and must live with "improvident" bargains. In 1882 Sir George Jessel decried it as an "absurdity"[15] and lamented that he did not know "[t]he ground of that doctrine".[16]

[66] Opposition to the penalty rule in India was so profound in the nineteenth century that it was statutorily revoked by s. 74 of the *Indian Contract Act, 1872*. [17] Speaking almost 100 years after this legislative intervention, the Indian Supreme Court observed that "[s.74] is clearly an attempt to eliminate the somewhat elaborate refinements made under the English common law in distinguishing between stipulations providing for payment of liquidated damages and stipulations in the nature of penalty".[18]

[67] Complaints about the theoretical underpinnings of the penalty rule continued in the twentieth century. For example, Lord Parmoor, in 1914, used more restrained language to flag the rule's shortcomings:[19] "It is too late to question whether such interferences with the language of a contract can be justified on any rational principle."

[68] The Supreme Court of the United Kingdom, in *Cavendish Square Holding BV v. El Makdessi,*[20] the High Court of Australia in *Paciocco v. Australia and New Zealand Banking Group Ltd.*[21] and the Scottish Law Commission[22] have all recently extensively reviewed the merits of the penalty rule and provided valuable fresh insights on its utility. This is a task that the Supreme

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there is some conflict, and *more* confusion, in the cases; judges have been long and constantly complaining of the confusion and want of harmony in the decisions upon this subject") (emphasis in the original).

[14] *Betts v. Burch*, 157 Eng. Rep. 938, 940 (Ex. 1859).

[15] *Wallis v. Smith*, 21 Ch. D. 243, 257 (1882). See also 21 Ch. D. 243, 277 per Lord Justice Lindley ("The decisions on penalty and liquidated damages ... are perplexing").

[16] Id. 256.

[17] C. 6, as amended ("When a contract has been broken, if a sum is named in the contract as the amount to be paid in case of such breach, or if the contract contains any other stipulation by way of penalty, the party complaining of the breach is entitled, whether or not actual damage or loss is proved to have been caused thereby, to receive from the party who has broken the contract reasonable compensation not exceeding the amount so named or, as the case may be, the penalty stipulated for").

[18] *Fateh Chand v. Balkishan Das*, [1964] 1 S.C.R. 515, 526 (1963).

[19] *Dunlop Pneumatic Tyre Co. v. New Garage and Motor Co.*, [1915] A.C. 79, 101 (H.L. 1914).

[20] [2015] UKSC 67; [2016] A.C. 1172.

[21] [2016] HCA 28; 258 C.L.R.525.

[22] Review of Contract Law: Discussion Paper on Penalty Clauses (No. 162) (November 2016).

Court of Canada has not yet undertaken. Indeed, it has not had an opportunity to do so since its 1978 judgment in *Elsley v. J.G. Collins Insurance Agencies Ltd.*[23]

B. The Fraud-on-the-Bankruptcy-Law Issue

[69] England enacted its first bankruptcy statute in 1542.[24] It[25]

> displayed two central features of bankruptcy law that have persisted to the present day. First, it created a summary and collective procedure that operated for the benefit of all the creditors, and not simply for the creditor who initiated the process. Second, it adopted a *pro rata* sharing principle in respect of the distribution of the debtor's assets among the creditors.

[70] It is not clear when English judges first thought it prudent to construct a rule that parties could not order their affairs so as to minimize the adverse effect the fundamental tenets of the bankruptcy laws would have on their legitimate interests. But it is obvious that by 1812 such a principle had been in place for a considerable period of time.[26] Lord Eldon, in *Higinbotham v. Holme*,[27] described a trust term the validity of which had been challenged as a "direct fraud upon the Bankrupt Laws" and refused to enforce it against the interests of a bankrupt's creditors. No doubt, the strategies that ingenious English solicitors had adopted to diminish the harm the application of the bankruptcy laws had on their clients' interests prompted this judicial response.

[71] Bankruptcy practitioners usually refer to contract terms that impose adverse consequences on the insolvent party and the insolvent party's creditors on the occurrence of an act of insolvency as *ipso facto* clauses.[28]

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[23] [1978] 2 S.C.R. 916.

[24] *An Acte against such persons as doo make Bankrupte*, 34 & 35 Hen. 8, c. 4. In 1571 Parliament passed a second bankruptcy act, *An Acte touching Orders for Bankruptes*, 13 Eliz. 1, c. 7. It introduced more acts of bankruptcy and only applied to merchant or trader debtors. R. Wood, Bankruptcy and Insolvency Law 30 (2d ed. 2015) & C. Tabb, The Law of Bankruptcy 40 (2d ed. 2009). A third amendment in 1705, *An Act to prevent Frauds frequently committed by Bankrupts*, 4 & 5 Anne, c. 4 introduced "the concept of the discharge of a bankrupt. Prior to this, a bankrupt remained liable for all amounts remaining unpaid to the creditors following the bankruptcy". R. Wood, Bankruptcy and Insolvency Law 31 (2d ed. 2015). See also C. Tabb, The Law of Bankruptcy 40 (2d ed. 2009).

[25] R. Wood, Bankruptcy and Insolvency Law 30 (2d ed. 2015).

[26] E.g., *Re Murphy*, 1 Sch. & Lef. 44, 49 (Ch. 1803) (Ire.) ("All the cases in England have held this to be a fraud upon the bankrupt laws which cannot be supported").

[27] 34 Eng. Rep. 451, 453 (Ch. 1812). Writing in 2012, Lord Collins observed that "[t]he [fraud-on-the-bankruptcy-law] rule has existed for nearly 200 years". *Belmont Park Investments Pty Ltd. v. BNY Corporate Trustee Services Ltd.*, [2011] UKSC 38, ¶59; [2012] 1 A.C. 383, 409.

[28] R. Wood, Bankruptcy and Insolvency Law 178 (2d ed. 2015)("these [contractual] provisions – often referred to as *ipso facto* clauses – stipulate that the commencement of bankruptcy or other insolvency proceedings is of itself an event of default that permits the party to terminate the contract"); Ho, "The Treatment of *Ipso Facto* Clauses in

[72] One wonders why, if the harm *ipso facto* clauses caused was so pressing, Parliament did not declare them unenforceable.[29] This, after all, was an era when "English Law had a distinctly pro-creditor orientation … Imprisonment for debt was the order of the day, from the time of the Statute of Merchant in 1285, until Dicken's time in the mid-nineteenth century".[30]

[73] I suspect that at least 150 years following 1542 passed before a judge introduced the fraud-on-the-bankruptcy-law principle. In this gap period courts gave *ipso facto* terms in contracts, wills and trusts their plain and ordinary meaning.

[74] By 1861 the existence of this rule was not in doubt. Sir W. Page Wood, V.C., in *Whitmore v. Mason*,[31] proclaimed that "the law is too clearly settled to admit of a shadow of a doubt that no person possessed of property can reserve that property to himself until he shall become bankrupt, and then provide that … it shall pass to another and not to his creditors".

[75] The same observation cannot be made about the Canadian law. The Supreme Court of Canada has never acknowledged that a fraud-on-the-bankruptcy law principle is a component of the Canadian common law. Only a few Canadian courts have ever considered it.[32] If there is such a principle in Canada, its content is certainly debatable.

[76] In 2009 important changes were made to the *Bankruptcy and Insolvency Act*[33] and the *Companies' Creditors Arrangement Act*.[34] These amendments declared unenforceable *ipso facto*

Canada", 61 McGill L.J. 139, 141 (2015) ("Many parties preserve contractual rights, through what are commonly known as *ipso facto* clauses, to terminate and amend contracts or to demand an accelerated payment in the event that a counterparty to the contract becomes insolvent") & Black's Law Dictionary 905 (10th ed. B. Garner ed. in chief 2014)("A contract clause that specifies the consequences of a party's bankruptcy").

[29] Professor Atiyah notes that at the dawn of the nineteenth century Parliament and the executive were not assisted by a large complement of skilled civil servants and that "there was good reason to assume that in general the Courts would make a better job of law-making than Parliament'. P. Atiyah, The Rise and Fall of Freedom of Contract 96 (1979). While this may be true, Parliament had amended the bankruptcy statute on several occasions before this judicial foray into law making. C. Tabb, The Law of Bankruptcy 40 (2d ed. 2009)("The first comprehensive bankruptcy law was passed in 1570 during the reign of Queen Elizabeth I. Over the next two centuries, Parliament periodically amended the bankruptcy laws, in each instance enhancing the power of the bankruptcy commissioner to reach more of the debtor's assets and increasing the penalties against debtors").

[30] C. Tabb, The Law of Bankruptcy 39 (2d ed. 2009).

[31] 70 Eng. Rep. 1031, 1034 (Ch. 1861).

[32] Ho, "The Treatment of *Ipso Facto* Clauses in Canada", 61 McGill L.J. 139, 170 (2015) ("the anti-deprivation rule … has not been widely used in Canadian jurisprudence").

[33] The *Economic Recovery Act (stimulus)*, S.C. 2009, c. 31, s. 64 introduced s. 84.2 of the *Bankruptcy and Insolvency Act.* It came into force December 15, 2009. Section 65.1 of the *Bankruptcy and Insolvency Act* came into force on August 1, 1992. *An Act to amend the Bankruptcy Act and to amend the Income Tax Act in consequence thereof,* S.C. 1992, c. 27, s. 30 & S.I./92-135. This section declared unenforceable an *ipso facto* term affecting an insolvent debtor – a natural person or a corporation – upon the debtor filing a notice of intention or proposal.

terms that imposed adverse consequences on natural person bankrupts and corporations pursuing restructuring and their creditors.

[77] The 2009 amendments said nothing about corporate bankruptcy *ipso facto* terms. Section VII Q(d), the term under review in this appeal, is a corporate bankruptcy *ipso facto* term.

II. Questions Presented

A. Contract Law

[78] On what principled basis may a court decline to enforce a stipulated-consequence-on-breach term in a commercial contract between two or more parties that have the resources necessary to obtain legal advice and that are perfectly capable of protecting their own interests?

[79] What is the common law in Canada on the enforceability of stipulated-consequence-on-breach provisions in commercial contracts?

[80] Does the classic penalty rule apply?

[81] Or is a stipulated-consequence-on-breach term only unenforceable if it is oppressive?

[82] If so, what are the features of an oppressive term?

[83] How does the law apply to the term in dispute in this appeal?

[84] Is s. VII Q(d), the provision in the agreement between Chandos Construction Ltd. and Capital Steel Inc. in which Capital Steel agreed that "[i]n the event [it] ... commits any act of ... bankruptcy [it would] forfeit ten percent of the [$1,373,000] ... subcontract agreement price to ... [Chandos Construction] as a fee for the inconvenience of completing the work using alternate means ... [or] for monitoring the work during the warranty period [or both]", a stipulated-consequence-on-breach term?

[85] If so, is it enforceable?

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[34] R.S.C. 1985, c. C-36. *An Act to establish the Wage Earner Protection Program Act, to amend the Bankruptcy and Insolvency Act and the Companies' Creditors Arrangement Act and to make consequential amendments to other Acts*, S.C. 2005, c. 47, s. 131 introduced s. 34 of *the Companies' Creditors Arrangement Act*. This provision came into force on September 18, 2009. S.I./2009-68.

[86] Justice Nielsen concluded that s.VII Q(d) was an enforceable liquidated-damages term, in part, because the sum – $137,300 – was not "extravagant and unconscionable" and that it would be "impossible to calculate the cost of [Capital Steel's] ongoing obligations with any precision".[35]

B. Bankruptcy Law

1. Introduction

[87] There are two sets of questions here. The first set focuses on the common law. The second set puts the *Bankruptcy and Insolvency Act*[36] under the microscope.

2. Common Law

[88] In 2011 the United Kingdom Supreme Court substantially rewrote the English common law on *ipso facto* terms.[37] It directed courts to enforce an *ipso facto* clause unless it has as its "predominant purpose, or one of ... [its] main purposes, the deprivation of the property of one of the parties on bankruptcy".[38] *Ipso facto* terms that constitute "a blatant attempt to deprive a party of property in the event of liquidation"[39] contravene public policy and are of no force.

[89] Is a similar principle part of the common law of Canada?

[90] If so, what are its distinguishing features?

3. *Bankruptcy and Insolvency Act*

[91] The *Bankruptcy and Insolvency Act*[40] is a sophisticated and comprehensive statute. It has close to 300 sections. It applies to both natural persons and corporations, and, as its title reveals, to both bankruptcies and insolvencies.[41]

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[35] Appeal Record F11.

[36] R.S.C. 1985, c. B-3.

[37] *Belmont Park Investments Pty Ltd. v. BNY Corporate Trustee Services Ltd.*, [2011] UKSC 38; [2012] 1 A.C. 383.

[38] Id. at ¶104; [2012] 1 A.C. at 421.

[39] Id.

[40] R.S.C. 1985, c. B-3.

[41] The American *Bankruptcy Code*, 11 U.S.C. also applies to both natural persons and corporations. "In England, Australia, and New Zealand, there is a basic division between insolvency of individuals and insolvency of corporations. Bankruptcy law governs the former, while corporate insolvency legislation governs the latter". R. Wood, Bankruptcy and Insolvency Law 35 (2d ed. 2015).

[92] Section 84.2 of the *Bankruptcy and Insolvency Act*, introduced by the 2009 amendments,[42] and in force as of December 15, 2009, declares a category of *ipso facto* terms unenforceable if the bankrupt is a natural person.[43]

[93] But no provision in the *Bankruptcy and Insolvency Act* declares corporate *ispo facto* terms of any type of no force or effect.

[94] Also noteworthy is the fact that on September 18, 2009 s. 34 of the *Companies' Creditors Arrangement Act* came into force.[44] This provision expressly deprived a corporate restructuring *ipso facto* term of any force.

[95] Is it reasonable to assume that if Parliament had intended to accord the same treatment to corporate bankruptcy *ipso facto* terms as it attached to natural bankruptcy person *ipso facto* terms and corporate restructuring *ipso facto* terms that it would have incorporated unambiguous statutory text to that effect?

[96] Has Parliament, with the passage of s. 84.2 of the *Bankruptcy and Insolvency Act*, occupied the field relating to the regulation of *ipso facto* clauses tied to an act of bankruptcy?

[97] If so, does that mean that s. VII Q(d), a corporate bankruptcy *ipso facto* term, must be enforceable?

[98] If Parliament has not occupied the field and the common law on *ipso facto* terms applies, is s. VII Q(d) enforceable?

[99] Does the bankrupt's property include the accounts receivable for work performed for Chandos Construction but unpaid or does it exclude the ten percent forfeiture fee triggered when Capital Steel became bankrupt?

III. Brief Answers

A. Contract Law

[100] The classic penalty rule provides no principled basis for assessing the enforceability of stipulated-consequence-on-breach provisions in commercial contracts between parties with sufficient resources to protect their own interests. It should not be used anymore.

[101] The Supreme Court said so in *Elsley v. J.G. Collins Insurance Agencies Ltd.*[45] It stated that only oppressive stipulated-consequence-on-breach terms were unenforceable.

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[42] *Economic Recovery Act (stimulus)*, S.C. 2009, c. 31, s. 64.

[43] *Bankruptcy and Insolvency Act*, R.S.C. 1985, c. B-3.

[44] S.I. /2009-68.

[102] The Supreme Court of Canada has not recorded the benchmarks of an oppressive stipulated-consequence-on-breach term in the context of ascertaining the enforceability of such a term.

[103] Because freedom of contract is of paramount importance in Canada, oppression should be given a limited meaning.[46]

[104] It should only apply in extraordinary circumstances to a commercial contract between parties that have the resources necessary to retain legal counsel to advise them on the nature of their responsibilities and benefits under a proposed contract. It makes no sense whatsoever to ask a court to assess the enforceability of a term that commercial entities with the resources required to secure legal advice have agreed upon. It is presumptuous in the extreme to believe that judges have a better grasp of what obligations and benefits should be in a commercial contract than those who negotiated it and are expected to understand the implications of their bargain.

[105] The United Kingdom Supreme Court case – *Cavendish Square Holdings BV v. El Makdessi*[47] – illustrates this point. One contracting party was part of the world's leading marketing communications group.[48] The other contracting parties, Messrs. Makdessi and Ghossoub, were the co-founders and co-owners of the Middle East's largest advertising and marketing communications group.[49] Messrs. Makdessi and Ghossoub had agreed to sell sufficient shares in

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[45] [1978] 2 S.C.R. 916, 937.

[46] See *Philips Hong Kong Ltd. v. Hong Kong*, [1993] UKPC 3a, ¶22; [1993] 1 H.K.L.R. 269, 280 ("the court has to be careful not to set too stringent a standard and bear in mind that what the parties have agreed should normally be upheld. Any other approach will lead to undesirable uncertainty especially in commercial contracts").

[47] [2015] UKSC 67; [2016] A.C. 1172. See also *Clydebank Engineering and Shipbuilding Co. v. Castaneda*, [1905] A.C. 6 (H.L. 1904) (why should judges be asked to review a contract between the Spanish government and a shipbuilder in order to determine whether an important term should be enforced?) & *Polyset Ltd. v. Panhandat Ltd.*, [2002] HKCFA 15, ¶158 (why should judges be asked to review a $115 million land sale contract to determine whether the purchaser's agreement to forego a $40.25 million deposit in the volatile Hong Kong real estate market if it failed to close? per Litton, N.P.J.: "Over the past half-century there have been many cycles of dramatic rise and fall. Upon entering into the contract, in May 1997, the purchaser had the possibility of almost immediate profit upon sub-division and re-sale. With the contract in hand, in an inflationary environment, the purchaser would have had little difficulty in raising money from the market. The vendor was, of course, locked into the contract for over 9 months, and exposed to uncertainties over a long period. It was therefore entirely reasonable for the vendor to seek reassurance that if the market should fall and the purchaser should default, it would be compensated: And that the compensation should be certain : that is to say, not dependent upon a court assessing the amount of compensation years after the event : Few vendors would welcome the prospect of expensive litigation to claim compensation, when the outcome would depend upon the resolution of conflicting evidence based upon valuation exercises by opposing experts, whose opinions could vary widely (as occurred in this case). The size of the deposit was a matter of bargain for the parties, as was every other term. They were contracting at arm's length, each independently advised, with each looking to its own advantage").

[48] [2015] UKSC 67, ¶116; [2016] A.C. 1172, 1232.

[49] Id.

their advertising and marketing business to give Cavendish Square Holdings majority control of it. The purchase price was over US $100 million. Mr. Makdessi had violated a term in the share-sale agreement and the purchaser sought a declaration that the agreed-upon consequences for that breach were now in force and that the amount the purchaser had to pay Mr. Makdessi for this shares had drastically declined. No court should have to spend much time assessing the enforceability of a term in this contract.

[106] An extraordinary circumstance exists if the stipulated-consequence-on-breach term is oppressive. A term in a commercial contract is oppressive if it is so manifestly grossly one-sided that its enforcement would bring the administration of justice into disrepute. The focus is on the contested term and not the relative bargaining strengths of the contracting parties.[50]

[107] This is a bright-line test.

[108] Stipulated-consequence-on-breach terms in commercial contracts will seldom breach this marker.

[109] The oppression concept may be engaged more frequently in consumer contracts. A less demanding standard for oppression in consumer contracts – rental-car, parking, credit-card and utility adhesion contracts and perhaps also increasingly online contracts of adhesion, such as Facebook's "terms of use" – may be appropriate. In these situations a dominant party provides a service or a product to a large number of consumers who are not in a position to extract any concessions from the service or product provider. If the consumer wishes to acquire the services or the product provided by the dominant party, it will be only on the terms stipulated by the dominant party.

[110] A promisor that asks to be relieved of a burden that it promised to discharge bears the legal burden of establishing the facts it relies on to support its oppression claim.[51]

[111] In this appeal, there can be no reason to doubt that both Chandos Construction and Capital Steel had the resources necessary to retain legal counsel and secure competent advice as to the burdens and benefits that each party would have under their steel-construction contract. They were able to protect their own interests.

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[50] *Imperial Tobacco Co. v. Parsley*, [1936] 2 All E.R. 515, 522 (C.A.) (the Court thought it important that the tobacconist who entered into a price-maintenance agreement was "of full age and understanding" and that it was irrelevant that the tobacco supplier was a large commercial enterprise). Some courts have held that inequality of bargaining power is a relevant consideration. E.g., *Birch v. Union of Taxation Employees Local 70030*, 2008 ONCA 809, ¶45; 305 D.L.R. 4th 64, 78 & *Bankers Mortgage Corp v. Plaza 500 Hotels Ltd.*, 2016 BCSC 722, ¶71; 35 C.B.R. 6th 263, 278.

[51] *Mortgage Makers Inc. v. McKeen*, 2009 NBCA 61, ¶47; 312 D.L.R. 4th 82, 104 & *Robophone Facilities Ltd. v. Blank*, [1966] 3 All E.R. 128, 142 (C.A.). Contra, *Law Reform Act*, S.N.B. 1993, c. L-1.2, s. 5(1).

[112] The term in this commercial contract is a stipulated-consequence-on-breach term and is undoubtedly enforceable. The breach is the subcontractor's failure to carry on business and discharge the promise that it made and its acquisition of the status of a bankrupt.

[113] Section VII Q(d) is part of a binding contract between commercial actors. It clearly is not so manifestly grossly one-sided that its enforcement would bring the administration of justice into disrepute. This term is not one-sided in any way at all. A judgment giving effect to s. VII Q(d) will not diminish the reputation of the judicial branch of government.

[114] The result would be the same if the standard applied was that fashioned by the House of Lords and the Privy Council at the start of the twentieth century in *Clydebank Engineering and Shipbuilding Co. v. Castaneda,*[52] *Dunlop Pneumatic Tyre Co. v. New Garage and Motor Co.*[53] and *Webster v. Bosanquet*[54] and adopted by many Canadian courts.

[115] Section VII Q(d) is not a penalty provision. It is fair and balanced. It serves a justifiable business purpose. It is not unreasonable, extravagant, or unconscionable. It may fairly be characterized as a liquidated damages term.

B. Bankruptcy Law

1. Common Law

[116] The fraud-on-the-bankruptcy-law principle is not now and likely never has been part of the common law of Canada.

[117] The Supreme Court of Canada has never expressly acknowledged the existence of this principle and has implicitly denied its status as part of Canadian law.[55]

[118] Only one provincial appellate court has applied the concept.[56] It did so in a 2013 appeal in a very brief judgment that assumed the fraud-on-the-bankruptcy-law was an element of Canadian common law. No consideration was given to the effect that the 2009 amendments to the *Bankruptcy and Insolvency Act* and the *Companies' Creditors Arrangement Act* had on the common law.

[119] If the fraud-on-the-bankruptcy-law principle was ever a feature of the Canadian common law, the aspect that dealt with *ipso facto* clauses ceased to exist no later than 2009.

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[52] [1905] A.C. 6.

[53] [1915] A.C. 79 (H.L. 1914).

[54] [1912] A.C. 394 (P.C.) (Ceylon).

[55] *Les Coopérants Société mutuelle d'assurance-vie (Liquidateur) v. Dubois*, [1996] 1 S.C.R. 900.

[56] *Trustee of Aircell Communications Inc. v. Bell Mobility Cellular Inc.,* 2013 ONCA 95; 14 C.B.R. 6th 276.

[120] The amendments to the *Bankruptcy and Insolvency Act* and the *Companies' Creditors Arrangement Act* that came into force in 2009 relating to *ipso facto* terms now constitute the code governing the enforceability of *ipso facto* clauses. There was no room for any common law norms after 2009.

[121] If, contrary to my conclusion, the 2009 amendments do not occupy the field and there is still some room for the common law, does it have the bite that the Ontario Court of Appeal attributed to it – an *ipso facto* term is unenforceable if its effect is the diminution of the bankrupt's estate?[57] Or should the benchmark of an enforceable corporate *ipso facto* term be less demanding and easier to meet? Should the common law test not accord more weight to the values of party autonomy and freedom of contract?

[122] I agree with the approach that the United Kingdom Supreme Court set out in *Belmont Park Investments Pty Ltd. v. BNY Corporate Trustee Services Ltd.*.[58] The common law should attach more weight to the value of party autonomy and freedom of contract than the collective interests of creditors favoured by the effects-based test given that bankruptcy is a statutory construct and judicial intervention is only interstitial in nature. Parliament has already identified the circumstances when collective interests trump party autonomy and freedom of contract.[59]

[123] This rebalance leads to a new Canadian common law test.

[124] A corporate bankruptcy *ipso facto* term is enforceable if its most important feature is the advancement of a reasonable and defensible commercial purpose and its enforcement provides a benefit for the nonbankrupt party that is not significantly greater than is necessary to promote the nonbankrupt party's legitimate commercial interests.

[125] Section VII Q(d) meets this new common law standard.

[126] Its only purpose is to declare the amount to which Chandos Construction is entitled if Capital Steel goes out of business and Chandos Construction must find other suppliers to provide the material and services that Capital Steel had promised to provide. Objectively assessed, this is a reasonable and defensible commercial purpose.

[127] The benefit Chandos Construction derives from the enforcement of the *ipso facto* clause is not greater, let alone significantly greater, than is necessary to promote Chandos Construction's legitimate commercial interests.

[128] Section VII Q(d) is not a blatant and egregious attempt to hijack Capital Steel's property and attack the interests of its creditors.

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[57] Id.

[58] [2011] UKSC 38; [2012] 1 A.C. 383.

[59] *Bankruptcy and Insolvency Act*, R.S.C. 1985, c. B-3, ss. 65.1, 66.34 & 84.2.

2. *Bankruptcy and Insolvency Act*

[129] Parliament's decision in 2009[60] not to follow the American[61] and Australian[62] legislative models and accord the same treatment to natural person bankruptcy and corporate bankruptcy *ipso facto* terms is strong evidence that Canada's legislators were not convinced that corporate bankruptcy *ipso facto* clauses are inimical to the welfare of the Canadian bankruptcy regime.

[130] I am satisfied that Parliament has occupied the field and that corporate bankruptcy *ipso facto* terms are enforceable.

[131] If Parliament had intended to deny enforceability to corporate *ipso facto* clauses it would have said so in unambiguous language.

[132] There is no compelling reason that would justify the contrary conclusion. Parliament cannot have left this subject matter unregulated satisfied that the common law had introduced norms that are generally recognized and applied across the country. There is little judge-made law on this topic.

[133] Because the *Bankruptcy and Insolvency Act* does not deprive a corporate bankruptcy term of its force and s. VII Q(d) is a corporate bankruptcy term, s. VII Q(d) is enforceable.

3. Conclusion

[134] To summarize, s. VII Q(d) is enforceable for two independent reasons. First, the *Bankruptcy and Insolvency Act* does not proscribe corporate bankruptcy *ipso facto* terms. Section VII Q(d) is a corporate bankruptcy *ipso facto* term. Second, if the *Bankruptcy and Insolvency Act* does not extinguish the common law on corporate bankruptcy *ipso facto* clauses, s. VII Q(d) meets the new party-autonomy-inspired common law test and is valid.

IV. Statement of Facts

A. The Construction Contracts

[135] On March 2, 2015 Boudreau Developments Ltd., the developer, and Chandos Construction, the general contractor, entered into a stipulated-price contract for the construction of

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[60] *Economic Recovery Act (stimulus)*, S.C. 2009, c. 31, s. 64.

[61] *Bankruptcy Code*, 11 U.S.C. §365(e).

[62] *Bankruptcy Act 1966*, No. 33 s. 301 (Cth) & *Treasury Laws Amendment (2017 Enterprise Incentives No. 2) Act 2017*, No. 112, s. 7 (introduced s. 415 D of the *Corporations Act 2001*, No. 50). See Australia House of Representatives, Treasury Laws Amendment (2017 Enterprise Incentives No. 2) Bill 2017 Explanatory Memorandum.

phase one of "The Botanica" condominium project in St. Albert.[63] The developer agreed to pay the general contractor $55 million to construct phase one.

[136] In order to discharge its obligation to the developer, Chandos Construction entered into a number of agreements with other construction businesses to perform and provide some of the necessary tasks and materials.

[137] Capital Steel was one of these construction enterprises. It agreed to supply and install the structural and miscellaneous steel components of the project.[64] The agreed price was $1,373,300.47.

[138] Capital Steel did not do what it promised. It did not complete its work.

[139] Chandos Construction paid Capital Steel $1,223,682.08 for the work performed and material supplied. The outstanding balance is $149,618.39.

[140] The completion costs are estimated to be $22,800.

[141] Capital Steel is responsible for warranty work that arises in a twelve-month period following substantial completion of the project. The start date has tolled. The extent of this obligation cannot be catalogued until the warranty period has expired.

B. Capital Steel Is a Bankrupt

[142] On September 26, 2016 Capital Steel filed an assignment in bankruptcy.

[143] The court subsequently appointed Deloitte Restructuring Inc. as the trustee of the estate of the bankrupt Capital Steel.

C. Deloitte Restructuring Seeks Advice and Directions

[144] On March 6, 2017 Deloitte Restructuring filed an application in the Court of Queen's Bench asking the court to determine "whether Chandos [Construction] is entitled to rely on s. VII Q(d) of the Subcontract between it and Capital Steel and, if not, for a direction that the balance of $126,818.39 is payable to ... [Deloitte Restructuring"].[65]

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[63] This is a standard form contract prepared by the Canadian Construction Documents Committee. This committee is a national joint committee made up of representatives of public and private sector owners, The Association of Consulting Engineering Companies, The Canadian Construction Association, Construction Specifications Canada and The Royal Architecture Institute of Canada.

[64] Counsel informed us during oral argument that this is a contract Chandos Construction uses. It is not prepared by the Canadian Construction Documents Committee.

[65] This is the difference between the outstanding balance of $149,618.39 and estimated completion costs of 22,800.

D. Justice Nielsen's Decision

[145] Justice Nielsen concluded that s. VII Q(d) is valid and that the $126,818.39 is Chandos Construction's property.

[146] The key parts of Justice Nielsen's March 17, 2017 decision are as follows:

> Section 97 of the *Bankruptcy and Insolvency Act* ... provides that the law of set off ... applies to all claims made against the estate of the bankrupt, except in cases involving frauds or fraudulent preferences. …
>
> In this case, there is no suggestion by … [the bankruptcy trustee] of fraud or a fraudulent preference in relation to … [s. VII Q(d)].
>
> The issue … is whether … [s. VII Q(d)] was such as to provide that all funds due from Chandos to Capital Steel would be the property of Capital Steel unless it became insolvent, in which case the property would pass to Chandos, as opposed to … [s. VII Q(d)] being a genuine covenanted pre-estimate of damages.
>
> To answer this question, it is necessary to have regard to the whole … [of the two contracts between Chandos Construction and Capital Steel, and Boudreau Developments and Chandos]. Chandos … is fully responsible for the acts and work of its subcontractors. Further, it has undertaken to indemnify… [Boudreau Developments] in respect of the involvement of Chandos … . Chandos has undertaken to warrant the work under the [contract with Boudreau Developments], which includes the work of Capital Steel, for a period of one year from the date of substantial performances of the work, which has not yet occurred.
>
> …
>
> … [Section VII Q(d)] provides for the payment of a fee to Chandos of 10 percent of the subcontract price. … [T]he total amount of the subcontract was $1,373,300. A 10 percent fee is … $137,330.
>
> I do not find that such a sum is "extravagant and unconscionable in amount in comparison with the greatest loss that could conceivably be proved to have flowed from the breach", nor is it "a grossly and punitive response to the problem to which it was addressed", all as referred to by the Supreme Court of Canada in the *H.F. Clarke Ltd.* case.
>
> Clearly, Chandos has ongoing obligations which flow from the work of Capital Steel … . It would be impossible to calculate the cost of such ongoing obligations with any precision. It is, therefore, fair and reasonable for such risk to be calculated on the basis of a percentage of the value of … [the contract between Chandos

> Construction and Capital Steel]. … [T]he value of the … [contract between Chandos Construction and Capital Steel] is $1,373,300. The value of the [contract between Boudreau Developments and Chandos Construction] was $56,852,453. In my view, a payment of 10 percent of … [$1,373,300] or 0.24 percent of the value of the [contract between Boudreau Developments and Chandos Construction], could not be considered to be gross and punitive given the ongoing obligations of Chandos and its potential risk with respect to the work of Capital Steel.
>
> I acknowledge that ... [s. VII Q(d)] uses the term "forfeit". This is an unfortunate choice of words as it could connote that the 10 percent amount is being lost or surrendered as a penalty. In my view, this single word cannot be determinative of the issue. ... [Section VII Q(d)] must be considered in the context of the [two contracts] and the position that Chandos is in as a result of the insolvency of Capital Steel. Clearly, it would incur administration and management costs as a result of the insolvency of Capital Steel, and is at risk for future liabilities of Capital Steel. [Chandos Construction and Capital Steel] must be taken to have had these considerations in mind at the time of execution of ... [their contract].

E. Deloitte Restructuring Appeals

[147] Deloitte Restructuring appeals. It argues that Justice Nielson committed several reversible errors.

V. Relevant Contract and Statutory Provisions

[148] The relevant provisions of the contract between Chandos Construction and Capital Steel are set out below:

> III. Guarantee
>
> [Capital Steel] agrees to immediately, or in accordance with a schedule acceptable to … [Chandos Construction], repair and make good any defect in its work and all resulting damages that may appear as the result of any improper work or defective materials furnished by … [Capital Steel]. This provision shall apply for the entire guarantee period specified in the prime contract, but shall not be less than one year from completion of the project.
>
> VII. Conditions
>
> …
>
> Q. Subcontractor Ceases Operations

> In the event …[Capital Steel] commits any act of insolvency, bankruptcy, winding up or other distribution of assets, or permits a receiver of the Subcontractor's business to be appointed, or ceases to carry on business or closes down its operations, then in any of such events:
>
> (a) this Subcontract Agreement shall be suspended but may be reinstated and continued if … [Chandos Construction], the Liquidator, or Trustee of … [Capital Steel] and the surety, if any, so agree. If no agreement is reached, … [Capital Steel] shall be considered to be in default and … [Chandos Construction] may give written notice of default to … [Capital Steel] and immediately proceed to complete the work by other means as deemed appropriate by … [Chandos Construction], and
>
> (b) any cost to … [Chandos Construction] arising from the suspension of this Subcontract Agreement or the competition of the work by … [Chandos Construction] plus a reasonable allowance for overhead and profit, will be payable by … [Capital Steel] and or his sureties, and
>
> (c) [Chandos Construction] … is entitled to withhold up to 20% of the within Subcontract Agreement price until such time as all warranty and or guarantee periods which are the responsibility of … [Capital Steel] have expired, and
>
> (d) [Capital Steel] shall forfeit 10 percent of the … Subcontract Agreement price to [Chandos Construction] as a fee for the inconvenience of completing the work using alternate means [or] monitoring the work during the warranty period [or both].

[149] The important parts of the "General Conditions" of the stipulated price contract between Boudreau Developments Ltd., the owner of the condominium project, and Chandos Construction, follow:[66]

> GC 3.7 Subcontractors and Suppliers
>
> 3.7.1 The *Contractor* shall preserve and protect the rights of the parties under the *Contract* with respect to work to be performed under subcontract, and shall:
>
> …
>
> .3 be as fully responsible to the *Owner* for acts and omissions of *Subcontractors* … as for acts or omissions of persons directly employed by the *Contractor*.

[66] Emphasis in original.

Part 12 Indemnification, Waiver of Claims and Warranty

GC 12.3 Warranty

12.3.1 Except for extended warranties, as described in paragraph 12.3.6, the warranty period under the *Contrac*t is one year from the date of *Substantial Performance of the Work.*

12.3.4 Subject to paragraph 12.3.2, the *Contractor* shall correct promptly, at the Contractor's expense, defect or deficiencies in the *Work* which appear prior to and during the one year warranty period.

[150] Sections 2, 65.1,[67] 66.34,[68] 71, 84.2,[69] 95(1) and (2), and 97(3) of the *Bankruptcy and Insolvency Act*[70] are as follows:

2 In this Act,

…

property means any type of property, whether situated in Canada or elsewhere, and includes money, goods, things in action, land and every description of property, whether real or personal, legal or equitable, as well as obligations, easements and every description of estate, interest and profit, present or future, vested or contingent, in, arising out of or incident to property ... .

65.1(1) If a notice of intention or a proposal has been filed in respect of an insolvent person, no person may terminate or amend any agreement, including a security agreement, with the insolvent person, or claim an accelerated payment, or a forfeiture of the term, under any agreement, including a security agreement, with the insolvent person, by reason only that

(a) the insolvent person is insolvent; or

(b) a notice of intention or a proposal has been filed in respect of the insolvent person.

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[67] *An Act to amend the Bankruptcy Act and to amend the Income Tax Act in consequence thereof,* S.C. 1992, c. 27, s. 30 (in force November 30, 1992 S.I./92-194).

[68] *An Act to amend the Bankruptcy Act and to amend the Income Tax Act in consequence thereof,* S.C. 1992, c. 27, s. 32 (in force November 30, 1992 S.I./92-194).

[69] *Economic Recovery Act (stimulus),* S.C. 2009, c. 31, s. 64 (in force December 15, 2009 S.I./2009-68).

[70] R.S.C. 1985, c. B-3.

…

66.34(1) If a consumer proposal has been filed in respect of a consumer debtor, no person may terminate or amend any agreement, including a security agreement, with the consumer debtor, or claim an accelerated payment, or the forfeiture of the term, under any agreement, including a security agreement, with the consumer debtor, by reason only that

(a) the consumer debtor is insolvent, or

(b) a consumer proposal has been filed in respect of the consumer debtor

until the consumer proposal has been withdrawn, refused by the creditors or the court, annulled or deemed annulled.

…

(5) Any provision in an agreement that has the effect of providing for, or permitting, anything that, in substance, is contrary to subsections (1) to (3) is of no force or effect.

...

71 On a bankruptcy order being made ... , a bankrupt ceases to have any capacity to dispose of or otherwise deal with their property, which shall, subject to this Act and to the rights of secured creditors, immediately pass to and vest in the trustee named in the bankruptcy order ... .

…

84.2(1) No person may terminate or amend – or claim an accelerated payment or forfeiture of the term under – any agreement, including a security agreement, with a bankrupt individual by reason only of the individual's bankruptcy or insolvency.

(2) If the agreement referred to in subsection (1) is a lease, the lessor may not terminate or amend, or claim an accelerated payment or forfeiture of the term under, the lease by reason only of the bankruptcy or insolvency or of the fact that the bankrupt has not paid rent in respect of any period before the time of the bankruptcy.

(3) No public utility may discontinue service to a bankrupt individual by reason only of the individual's bankruptcy or insolvency or of the fact that the bankrupt individual has not paid for services rendered or material provided before the time of the bankruptcy.

(4) Nothing in this section is to be construed as

(a) prohibiting a person from requiring payments to be made in cash for goods, services, use of leased property or other valuable consideration provided after the time of the bankruptcy; or

(b) requiring the further advance of money or credit.

(5) Any provision in an agreement that has the effect of providing for, or permitting, anything that, in substance, is contrary to this section is of no force or effect.

…

95(1) A transfer of property made, a provision of services made, a charge on property made, a payment made, an obligation incurred or a judicial proceeding taken or suffered by an insolvent person

(a) in favour of a creditor who is dealing at arm's length with the insolvent person, or a person in trust for that creditor, with a view to giving that creditor a preference over another creditor is void as against — or, in Quebec, may not be set up against — the trustee if it is made, incurred, taken or suffered, as the case may be, during the period beginning on the day that is three months before the date of the initial bankruptcy event and ending on the date of the bankruptcy; and

(b) in favour of a creditor who is not dealing at arm's length with the insolvent person, or a person in trust for that creditor, that has the effect of giving that creditor a preference over another creditor is void as against — or, in Quebec, may not be set up against — the trustee if it is made, incurred, taken or suffered, as the case may be, during the period beginning on the day that is 12 months before the date of the initial bankruptcy event and ending on the date of the bankruptcy.

(2) If the transfer, charge, payment, obligation or judicial proceeding referred to in paragraph (1)(a) has the effect of giving the creditor a preference, it is, in the absence of evidence to the contrary, presumed to have been made, incurred, taken or suffered with a view to giving the creditor the preference — even if it was made, incurred, taken or suffered, as the case may be, under pressure — and evidence of pressure is not admissible to support the transaction.

…

97(3) The law of set-off or compensation applies to all claims made against the estate of the bankrupt and also to all actions instituted by the trustee for the

> recovery of debts due to the bankrupt in the same manner and to the same extent as if the bankrupt were plaintiff or defendant, as the case may be, except in so far as any claim for set-off or compensation is affected by the provisions of this Act respecting frauds or fraudulent preferences.

[151] Section 3(1) and part of s. 34[71] of the *Companies' Creditors Arrangement Act*[72] read as follows:

> 3(1) This Act applies in respect of a debtor company or affiliated debtor companies if the total of claims against the debtor company or affiliated debtor companies ... is more than $5,000,000 or any other amount that is prescribed.
>
> …
>
> 34(1) No person may terminate or amend, or claim an accelerated payment or forfeiture of the term under, any agreement, including a security agreement, with a debtor company by reason only that proceedings commenced under this Act or that the company is insolvent.
>
> (2) If the agreement referred to in subsection (1) is a lease, the lessor may not terminate or amend the lease by reason only that proceedings commenced under this Act, that the company is insolvent or that the company has not paid rent in respect of any period before the commencement of those proceedings.
>
> …
>
> (5) Any provision in an agreement that has the effect of providing for, or permitting, anything that, in substance, is contrary to this section is of no force or effect.

VI. Analysis

A. Introduction

[152] The first part of this segment of the judgment records the deficiencies that strip the classic penalty rule of any utility and explains why a stipulated-consequence-on-breach term in a

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[71] *An Act to establish the Wage Earner Protection Program Act, to amend the Bankruptcy and Insolvency Act and the Companies' Creditors Arrangement Act and to make consequential amendments to other Acts*, S.C. 2005, c. 47, s. 131 (in force September 18, 2009 S.I./2009-68).

[72] R.S.C. 1985, c. C-36.

commercial contract should be enforced unless it is oppressive, a position staked out by the Supreme Court of Canada in 1978.[73] The next part applies the oppressive test to s. VII Q(d).

[153] The second part explains why corporate bankruptcy *ipso facto* terms are lawful in Canada. It also constructs a new common law test for the identification of unenforceable corporate bankruptcy *ipso facto* terms, in the event the *Bankruptcy and Insolvency Act*[74] does not preclude common law intervention. The final segment applies the new common law test to s. VII Q(d) and concludes that it is enforceable against the bankruptcy trustee.

B. Section VII Q(d) Is Neither Oppressive Nor a Penalty and Is Enforceable

1. The Classic Penalty Rule Is Without Merit and Should Be Abandoned

[154] The penalty rule was suspect when common law courts first applied it and it has not shed this limiting characteristic in the intervening centuries.[75] It is unsound and should not be used any more. Justice Dickson, as he then was, speaking for the Supreme Court in *Elsley v. J.G. Collins Insurance Agencies Ltd*.,[76] said so roughly forty years ago. But many Canadian courts have not paid heed to his unequivocal message.[77]

[155] A stipulated-consequence-on-breach term should be enforced unless doing so would bring the administration of justice into disrepute.[78] With regard to a commercial contract, this would happen only if a stipulated-consequence-on-breach term is manifestly grossly one-sided. A less onerous standard may be suitable for consumer contracts.

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[73] *Elsley v. J.G. Collins Insurance Agencies Ltd.*, [1978] 2 S.C.R. 916, 937.

[74] R.S.C 1985, c. B-3.

[75] *Cavendish Square Holdings BV v. El Makdessi*, [2015] UKSC 67,¶36; [2016] A.C. 1172, 1206 ("[The penalty rule] is the creation of the judges, and, she argued, the judges should now take the opportunity to abolish it. There is a case to be made for taking this course. ...We rather doubt that the courts would have invented the rule today if their predecessors had not done so three centuries ago").

[76] [1978] 2 S.C.R. 916, 937.

[77] E.g., *B.L.T. Holdings Ltd. v. Excelsior Life Insurance Co.*, [1986] 6 W.W.R. 534 (Alta. C.A. 1986); *Dial Mortgage Corp. v. Baines*, 15 Alta. L.R. 2d 211 (Q.B. 1980); *Dezcam Industries Ltd. v. Kwak*, [1983] 5 W.W.R. 32 (B.C.C.A.); *Colliers Macaulay Nicolls Inc. v. Park Georgia Properties Ltd.*, 2003 BCSC 1785; 15 R.P.R. 4th 132; *Schindler Elevator Corp. of Canada v. New Vista Society*, [1998] B.C.J. No. 2327 (Sup. Ct.); *Place Concorde East Ltd. Partnership v. Shelter Corp. of Canada*, [2003] O.J. No. 5437; 43 B.L.R. 3d 54 (Sup. Ct.).

[78] See Principles, Definitions and Model Rules of European Private Law, Draft Common Frame of Reference (C. von Bar & E. Clive eds. 2009)(a penalty clause may be modified and a different obligation imposed only if it is "grossly excessive"); Scottish Law Commission, Report on Penalty Clauses (No. 171) ¶3.10 (May 1999) (the Commission recommended that a penalty term be unenforceable only if it is "manifestly excessive") & Davis, Penalty Clauses Through the Lens of Unconscionability Doctrine: *Birch v. Union of Taxation Employees*, 55 McGill L.J. 151, 164 (2010) ("Employing the unconscionability doctrine instead of the traditional penalty doctrine was a bold and valuable step. But the potential benefits of that innovation will not be realized so long as courts' vision continues to be occluded by the remnants of the penalty doctrine").

a. The Purpose of the Penalty Rule Is Unclear

[156] The purpose of the penalty rule is unclear.[79] The few courts that have addressed this issue have presented a variety of opinions. This is troublesome.[80] If there is no consensus as to the purpose a concept serves, how can it be implemented in a consistent and rational manner?

[157] Chief Justice Laskin, in *H.F. Clarke Ltd. v. Thermidaire Corp.*,[81] asserted that the rule "is simply a manifestation of a concern for fairness and reasonableness ... whenever the parties seek to remove from the courts their ordinary authority to determine ... what damages may be recovered as a result [of contractual breach]". Is this focus on the fairness and reasonableness of a contractual term misplaced? Courts have historically disavowed any jurisdiction to review bargains for their fairness or reasonableness.[82] Why should a stipulated-consequence-on-breach term be singled out for special treatment?

[158] Lord Roskill, in *Export Credits Guarantee Department v. Universal Oil Products Co.*,[83] a 1983 case, suggested that the "main purpose [of the penalty rule] ... is to prevent a plaintiff

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[79] *Robophone Facilities Ltd. v. Blank*, [1966] 3 All E.R. 128, 142 (C.A.) per Lord Diplock ("I make no attempt ... to rationalize this common law rule"); *Hill v. Barclay*, 34 Eng. Rep. 238, 239 (Ch. 1811) per Lord Eldon ("[the penalty rule was] utterly without foundation") & *Astley v. Weldon*, 126 Eng. Rep. 1318, 1321 (Common Pleas 1801) per Lord Eldon ("I felt ... much embarrassed in ascertaining the principle upon which [the penalty rule cases were founded").

[80] Holmes, "The Path of the Law", 10 Harv. L. Rev. 457, 469 (1897)("a body of law is more rational ... when every rule it contains is referred articulately and definitely to an end which it subserves, and when the grounds for desiring that end are stated ... in words") & Coke, The First Part of the Institutes of the Lawes of England or a Commentarie upon Littleton 395 (1628) ("knowing for certaine that the Lawe is unknowne to him that knoweth not the reason thereof"). See *The Queen v. Big M Drug Mart Ltd.*, [1985] 1 S.C.R. 295, 331 ("All legislation is animated by an object the legislation intends to achieve"); *City of Montreal v. 2952-1366 Quebec Inc.*, 2005 SCC 62, ¶23; [2005] 3 S.C.R. 141, 156 ("Identifying the purpose of a regulation can be helpful in determining the meaning of a given word or expression"); *Hirsch v. Protestant Board of School Commissioners*, [1926] S.C.R. 246, 267 (a court must always consider the object of the statute) & *Alberta v. Cardinal*, 2013 ABQB 407, ¶51; 565 A.R. 271, 286 ("a court forced to interpret legislation and apply it to a fact pattern without an understanding of the underlying purpose of the enactment functions with a severe handicap").

[81] [1976] 1 S.C.R. 319, 331 (1974).

[82] *Cavendish Square Holding BV v. El Makdessi*, [2015] UKSC 67, ¶13; [2016] A.C. 1172, 1196 (H.L) per Lord Neuberger & Lord Sumption ("Leaving aside challenges going to the reality of consent, such as those based on fraud, duress or undue influence, the courts do not review the fairness of men's bargains either at law or in equity") & ¶73, [2016] A.C. at 1216 per Lord Neuberger & Lord Sumption ("It is not a proper function of the penalty rule to empower the courts to review the fairness of the parties' primary obligations, such as the consideration promised for a given standard of performance"); *Export Credits Guarantee Department v. Universal Oil Products Co.* [1983] 1 W.L.R. 399, 403 (H.L.) per Lord Roskill ("it is not and never has been for the courts to relieve a party from the consequences of what may ... prove to be an onerous or possibly even a commercially imprudent bargain"); *Bridge v. Campbell Discount Co.*, [1962] A.C. 600, 626 (H.L.) per Lord Radcliffe ("the courts of equity never undertook to serve as a general adjuster of men's bargains") & *Jobson v. Johnson*, [1989], 1 All E.R. 621, 626 (C.A. 1988) ("This is of course not saying that the courts claim a general power not to enforce any agreement which the courts regard as unconscionable and extravagant".)

[83] [1983] 1 W.L.R. 399, 403 (H.L.). The other judges agreed with Lord Roskill.

recovering a sum of money ... which bears little or no relationship to the loss actually suffered by the plaintiff as a result of the breach by the defendant". The unstated assumption is that an innocent promisee deprived of a bargained benefit is only entitled to an award in accordance with governing common law damage principles and that this principle is more important than the benefits society derives from the enforcement of bargained contracts. It is not obvious to me that this is a defensible proposition.

[159] Justice Frankfurter, dissenting in *Priebe & Sons, Inc. v. United States*,[84] had a different understanding: "I assume that the basic reason for this doctrine is that the infliction of punishment through courts is a function of society and should not inure to the benefit of individuals". He cites no authority for this opinion.[85] The underpinning for this norm is the assumption that a promisor has agreed to suffer punishment if the promisor fails to discharge a contractual promise. This strikes me as an unsupportable assumption. The promisor makes a commitment necessary to secure the agreement of the other side. From my perspective, the punishment concept has nothing to do with whether a stipulated-consequence-on-breach-term is enforceable.

b. There Are Fundamental Problems with the Classic Penalty Rule

[160] There are six fundamental problems with the classic penalty rule – and one unrelated and unwelcome consequence.

[161] First, it is not clear what constitutes a penalty. "The test for distinguishing penal from other principles is unclear".[86] This is a significant drawback.[87] If an adjudicator does not know what the core element of a principle is, it is impossible to apply it rationally and consistently.[88]

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[84] 332 U.S. 407, 418 (1947).

[85] Justice Frankfurter was not the first to present this idea. See *Craig and Son v. M'Beath*, 1 M. 1016, 1018 (Scot. Ct. Sess. 1863) per Inglis, L.J.-Clerk ("Parties cannot lawfully enter into an agreement that the one party shall be punished at the suit of the other"). Other jurists have subsequently agreed with Justice Frankfurter. See *Paciocco v. Australia and New Zealand Banking Group Ltd.*, [2016] HCA 28, ¶253; 258 C.L.R. 525, 605-06 per Keane, J. ("the real objection, as a matter of public policy, to a penalty clause which operates upon breach of contract is that it is no part of the law of contract to allow one party to punish the other for non-performance") & *Legione v. Hateley*, [1983] HCA 11, ¶32; 152 C.L.R. 406, 445 per Mason & Deane JJ. ("A penalty ... is the nature of a punishment for non-observance of a contractual stipulation; it consists of the imposition of an additional or different liability upon breach of the contractual stipulation").

[86] *Cavendish Square Holding BV v. El Makdessi*, [2015] UKSC 67, ¶3; [2016] A.C. 1172, 1192 per Lord Neuberger & Lord Sumption.

[87] See Clarkson, Miller & Muris, "Liquidated Damages v. Penalties: Sense or Nonsense?" 1978 Wis. L. Rev. 351 & *Hunter Engineering Co. v. Syncrude Canada Ltd.*, [1989] 1 S.C.R. 426, 460 (the Court favoured abandoning the fundamental breach doctrine because the proper characterization of a breach is fraught with difficulties and tended to camouflage the important issue – did the parties intend the limitation-of-liability term to capture this breach?).

[162] Some courts adopt an objective test and employ a variety of inconsistent criteria.[89]

[163] Some courts scrutinize the contract text[90] to determine if the parties agreed that the stipulated-consequence-on-breach term is liquidated damages[91] or a penalty.[92] Does the text mean

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[88] *International Association of Firefighters, Local 2461 v. County of Strathcona* 22 (Wakeling 1982)("Neither the shooters nor the officials know what the target is when the match begins") & *Woodlands Enterprises Ltd. v. International Woodworkers of America Local 1-184*, at 4 (Wakeling 1978) ("Should both sides discharge their howitzers against different targets, an observer will never know which one is the better shot").

[89] Canada: Chief Justice Fitzpatrick, in *Canadian General Electric Co. v. Canadian Rubber Co.*, 52 S.C.R. 349, 351 (1915), stated that "[a] penalty is the payment of a stipulated sum on breach of the contract, irrespective of the damage sustained". This is not helpful. Under this test, all stipulated-payment-on-breach terms are penalties. United Kingdom: Lord Neuberger and Lord Sumption, with Lord Carnwath's concurrence, in *Cavendish Square Holding BV v. EI Makdessi*, [2015] UKSC 67, ¶32; [2016] A.C. 1172, 1204, concluded that "[t]he true test is whether the impugned provision is a secondary obligation which imposes a detriment on the contract-breaker out of all proportion to any legitimate interest of the innocent party in the enforcement of the primary obligation". This obviously introduces an objective yardstick – what is "out of all proportion"? Lord Diplock presented a definition in *Scandinavian Trading Tanker Co. v. Flota Petrolera Ecuatoriana ("The Scaptrade")*, [1983] 2 A.C. 694, 702 (H.L.) that adopted an element with historical precedents: "The classic form of penalty clause is one which provides that upon breach of a primary obligation under the contract a secondary obligation shall arise on the part of the party in breach to pay to the other party a sum of money, which does not represent a genuine pre-estimate of any loss likely to be sustained by him as a result of the breach of primary obligation but is substantially in excess of that sum". Lord Dunedin, in *Dunlop Pneumatic Tyre Co. v. New Garage & Motor Co.*, [1915] A.C. 79, 86 (H.L. 1914) opined that "[t]he essence of a penalty is a payment of money stipulated as in terrorem of the offending party". This is an objective feature, but is it helpful? Could a term not be a penalty even if it does not terrorize the promisor? This distinction strikes me as highly artificial. See also *Lordsvale Finance PLC v. Bank of Zambia*, [1996] Q.B. 752, 762 ("whether a provision is to be treated as a penalty is a matter of construction to be resolved by asking whether at the time the contract was entered into the predominant contractual function of the provision was to deter a party from breaking the contract or to compensate the innocent party for breach"). Australia: In *AMEV – UDC Finance Ltd. v. Austin*, 162 C.L.R. 170, 190 (1986), Justices Mason and Wilson of the Australian High Court constructed a definition with a strong objective component: "[T]here is much to be said for the view that the courts should [allow] ... parties to a contract greater latitude in determining what their rights and liabilities will be, so that an agreed sum is only characterised as a penalty if it is out of all proportion to damages likely to be suffered as a result of breach". Justices Mason and Deane, in *Legione v. Hateley*, [1983] HCA 11, ¶32; 152 C.L.R. 406, 445, gave the term this meaning: "A penalty ... is in the nature of a punishment for non-observance of a contractual stipulation; it consists of the imposition of an additional or different liability upon breach of the contractual stipulation". United States: *Interstate Industrial Uniform Rental Service, Inc. v. Couri Pontiac, Inc.*, 355 A. 2d 913, 921 (Me. Sup. Jud. Ct. 1976)("This Court has often said that an agreement made in advance of breach, fixing the damages thereon, is not enforceable unless the damages caused by the breach are very difficult to estimate accurately and the amount so fixed is a reasonable forecast of the amount necessary to justly compensate one party for the loss occasioned by the breach") Has the Maine Supreme Judicial Court not fashioned contradictory markers? How can both coexist? How can one reasonably forecast damages if it is very difficult to forecast damages?

[90] *Rickman v. Carstairs*, 110 Eng. Rep. 931, 935 (K.B. 1833) ("in ... cases of construction of written instruments [the question] is, not what was the intention of the parties, but what is the meaning of the words they have used").

[91] *Wallis v. Smith*, 21 Ch. D. 243, 267 (C.A. 1882) per Cotton L.J. ("liquidated damages ... means ... the sum which the parties have by the contract assessed as the damages to be paid, whatever may be the actual damage") & T. Sedgwick, A Treatise on the Measure of Damages, or, an Inquiry into the Principles Which Govern the Amount of Pecuniary

that the contract-breaker must pay the stipulated sum? Or does the text support the conclusion that its purpose was only to incentivize the promisor to keep its commitment and the parties never contemplated that the contract-breaker would pay the stipulated sum?

[164] The intention school of thought is without merit. The proposition that the parties intended that the contract-breaker would be relieved of the obligation under a stipulated-consequence-on-breach term strikes me as impractical and artificial. Why would a party agree to an important term inserted for its benefit that it knows is unenforceable? This does not accord with commercial standards with which I am familiar.

Compensation Awarded by Courts of Justice 411 (3d rev. ed.1858) ("[liquidated damages:] where the contracting parties fix or liquidate the amount that shall furnish the measure of compensation in case of non-fulfillment of the agreement").

[92] Canada: *Canadian General Electric Co. v. Canadian Rubber Co. of Montreal*, 52 S.C.R. 349, 352 (1915)("There are innumerable cases in which it has been necessary, in particular cases, to decide whether the parties *intended* that the payment provided for by the contract should be in the nature of a penalty or liquidated damages") (emphasis added); United Kingdom: *Peachy v. Duke of Somerset*, 93 Eng. Rep. 626, 630 (Ch. 1720) ("The true ground of relief against penalties is from the original intent of the case, where the penalty is designed only to secure money, and the Court gives him all that he expected or desired"); *Reynolds v. Bridge*, 119 Eng. Rep. 961, 966 (Q.B. 1856)("[a]ll that the Courts have done has been only to lay down a canon for establishing the intention of the parties") 967 per Crompton, J ("[N]o decision ever went so far as to say that the Courts would not follow what they considered to be the meaning of the parties"); *Clydebank Engineering and Shipbuilding Co. v. Castaneda*, [1905] A.C. 6, 16 (H.L. 1904) per Lord Davey ("if you find a sum of money made payable for the breach, not of an agreement generally which might result in either a trifling or a serious breach, but a breach of one particular stipulation in an agreement, and when you find that the sum payable is proportioned to the amount ... or the rate of non-performance of the agreement ... then you infer that primâ facie the parties intended the amount to be liquidate damages and not penalty. 1 say 'primâ facie' because it is always open to the parties to show that the amount ... is so exorbitant and extravagant that it could not possibly have been regarded as damages for any possible breach which was in the contemplation of the parties") & *Photo Production Ltd. v. Securicor Transport Ltd.*, [1980] UKHL 2, ¶9; [1980] A.C. 827, 850 per Lord Diplock ("[a term] must not offend against the equitable rule against penalties; that is to say, it must not impose upon the breaker of a primary obligation a general secondary obligation to pay to the other party a sum of money that is manifestly intended to be in excess of the amount which would fully compensate the other party for the loss sustained by him in consequence of the breach of the primary obligation"); Australia: *O'Dea v. Allstates Leasing System (W.A.) Pty. Ltd.*, [1983] HCA 3, ¶5; 152 C.L.R. 359, 378 per Wilson, J. (" In essence the task of a court in such a case is to discern the true intention of the parties: is the clause under challenge a genuine pre-estimate of damage, or is it a penal sanction imposed on the observance of the agreement by the lessee?") & *Lamson Store Service Co. v. Russell Wilsons & Sons Ltd.*, [1906] HCA 87; 4 C.L.R. 672, 686 per Griffith, C.J. ("On the whole, to use the words of Jessel M.R. in *Wallis v. Smith*, 'I am glad to find that I do not feel myself compelled to decide contrary to what is the plain meaning of the terms by any of the decisions'"); United States: *Sun Printing and Publishing Assoc. v. Moore*, 183 U.S. 642, 662 (1902)("this court has consistently maintained the principle that the intention of the parties is to be arrived at by a proper construction of the agreement ... and that whether a particular stipulation to pay a sum of money is to be treated as a penalty, or as an agreed ascertainment of damages, is to be determined by the contract, fairly construed").

[165] Courts decline to enforce stipulated-consequence-on-breach terms in spite of the obvious fact that the parties intended them to be enforced.[93]

[166] Many modern courts have held that the term the parties use to describe the stipulated-consequence-on-breach provision – "penalty", "forfeiture" or "liquidated damages" – is not determinative.[94] Does this orientation not completely undermine the validity of the intention

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[93] *Wilmington Housing Authority v. Pan Builders, Inc.*, 665 F. Supp. 351, 354 (D. Del 1987)("Courts adopting this intention criterion have been criticized by numerous commentators for merely paying lip service to the intention of the parties while deciding the cases based on ... the certainty of damages and the reasonableness of the stipulated amount. ... [T]his Court declines to adopt the intention criterion") *& Interstate Industrial Uniform Rental Service, Inc. v. Couri Pontiac, Inc.*, 355 A. 2d 913, 921 (Me. Sup. Jud. Ct. 1976) ("This Court has held that the question of whether a stipulated amount is liquidated damages or a penalty shall be resolved by finding the intent of the parties. ... Clearly that ... does not mean that the Court must follow the intent as it appears on the face of the contract, for so doing would require the Court to uphold any provision designated 'liquidated damages' since the parties have clearly stated that they intend to pay that amount in the event of breach").

[94] Canada: *Waugh v. Pioneer Logging Co.*, [1949] S.C.R. 299, 311 per Estey J. ("the mere use of the words 'liquidated damages' or 'penalty' is not conclusive. In this case the language used is not particularly helpful as both the words 'forfeited' and 'liquidated damages' appear in the text"); *Canadian General Electric Co. v. Canadian Rubber Co.*, 52 S C.R. 349, 366 (1915) per ldington, J. ("It is not for the law ... to act upon the name given or name assigned the amount of reduction"); J. McCamus, The Law of Contracts 965 (2012)("The fact that the parties may describe the stipulated sum as 'liquidated damages' or, as is often stipulated, 'as liquidated damages and not as a penalty' is not dispositive"); United Kingdom: *Cavendish Square Holding BV v. EI Makdessi*, [2015] UKSC 67, ¶15; [2016] A.C. 1172, 1197 ("the classification of terms for the purpose of the penalty rule depends on the substance of the term and not on its form or on the label which the parties have chosen to attach to it"); *Jeancharm Ltd. v. Barnet Football Club Ltd.*, [2003] EWCA Civ 58, ¶ 27 per Peter Gibson L.J. ("the court looks at the substance of the matter, rather than the form of words, to determine what was the real intention of the parties"); *Dunlop Pneumatic Tyre Co. v. New Garage and Motor Co*, [1915] A.C. 79, 86 (H.L. 1914) ("Though the parties to a contract who use the words 'penalty' or 'liquidated damages' may prima facie be supposed to mean what they say, yet the expression used is not conclusive. The Court must find out whether the payment stipulated is in truth a penalty or liquidated damages"); *Commissioner of Public Works v. Hills*, [1906] A.C. 368, 375 (P.C.) (Cape of Good Hope) ("it is well settled law that the mere form of expression 'penalty' or 'liquidated damages' does not conclude the matter"); *Clydebank Engineering and Shipbuilding Co. v. Castaneda*, [1905] A.C. 6, 9 (H.L. 1904) per Earl of Halsbury, L.C.) ("Both in England and Scotland it has been pointed out that the Court must proceed according to what is the real nature of the transaction, and that the mere use of the word 'penalty' ... or 'damages' ... would not be conclusive as to the right of the parties"); *Thompson v. Hudson*, L.R.4 H.L.1, 30 (1869)("if the sum described as liquidated damages be a very large sum, and the title to that sum is to arise upon some very trifling consideration, then it follows plainly that the large sum never could have been meant to be the real measure of damages"); *Forrest and Barr v. Henderson, Coulborn & Co.*, 7 Scot. L. Rptr. 112, 115 (Ct. Sess. 1869)("even where parties stipulate that a sum of this kind shall not be regarded as a penalty, but shall be taken as an estimate and ascertainment of the amount of damage to be sustained in a certain event, equity will interfere to prevent the claim being maintained to an exorbitant and unconscionable amount)"; *Astley v. Weldon*, 126 Eng. Rep. 1318, 1321 (Common Pleas 1801) per Lord Eldon ("A principle has been said to have been stated in several cases, the adoption of which one cannot but lament, namely, that if the sum would be very enormous and excessive considered as liquidated damages, it shall be taken to be a penalty though agreed to be paid in the form of contract"); Australia: *Paciocco v. Australia and New Zealand Banking Group Ltd.*, [2016] HCA 28, ¶46 per Kiefel, J. ("The fact that the sum was called a penalty was not, of course, conclusive"); Hong Kong: *Polyset Ltd. v. Panhandat Ltd.*, [2002] HKCFA 15, ¶8 ("Even if the sum so specified is described as liquidated damages, it may be seen upon examination to have been fixed as a threat to be held over a party's head with a view to compelling him to perform. If so, the specified sum will be regarded as a penalty and therefore not recoverable") & United States: *United States v*

test? How can an adjudicator assert that the parties' intention is important and then proclaim that the text unequivocally proclaiming that intention is not determinative? One must assume that the ordinary and plain meaning of the text conveys what the parties intended.

[167] Second, because the penalty rule is confusing, it produces inconsistent results that cannot be rationally explained.[95] This is not a trait of a useful norm. It is the mark of a misleading and suspect measure.

[168] Third, even if the benchmarks of a penalty term were universally acknowledged, it is not readily apparent that the penalty concept captures the essence of judicial reluctance to enforce some contract terms and provides much assistance in deciding whether a contested term should be enforced or not. A determination that a provision is a penalty provides little assistance to an adjudicator who must decide whether it is appropriate to relieve a promisor of a contractual obligation. How does the knowledge that a term is a penalty assist a court to decide whether it should be enforced? Characterizing a stipulated-consequence-on-breach term as a penalty is no more helpful than describing it as a remedial term or written in English. Suppose that a Casablanca

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Bethlehem Steel Co., 205 U.S. 105, 120 (1907)("Either expression [penalty or liquidated damages] is not always conclusive as to the meaning of the parties"); *Truck Rent-A-Center, Inc., v. Puritan Farms 2nd, Inc.*, 361 N.E. 2d 1015, 1018 (N.Y. Ct. App. 1977) ("it is not material whether the parties themselves have chosen to call the provision one for 'liquidated damages,' or have styled it as a penalty.. ... Such an approach would put too much faith in form and too little substance"); *Caesar v. Robinson*, 67 N.E. 58, 59 (N.Y. Ct. App. 1903) ("The circumstance that the deposit is described in the lease as liquidated damages ... is not at all conclusive"); *Willson v. Mayor of Baltimore*, 34 A. 774, 775 (Md. Ct. App. 1896)("the intention of the parties at the time the contract was entered into is often, though not always, given weight; and whilst the language they have used in the instrument, if they declare that the damages shall be liquidated, is a circumstance that may have its influence ... yet even their explicit words will be sometimes disregarded"); *Jaquith v. Hudson*, 5 Mich. 123, 138 (Sup. Ct. 1858)("Thus, though the word 'penalty' be used ... or 'forfeit' ... or 'forfeit and pay' ... it will still be held to be stipulated damages if, from the whole contract, the subject matter, and the situation of the parties, it can be gathered that such was their intention") & T. Sedgwick, A Treatise on the Measure of Damages, or, an Inquiry into the Principles Which Govern the Amount of Pecuniary Compensation Awarded by Courts of Justice 419 (3d rev. ed. 1858) ("The language of the contract is not controlling. If, indeed, the word 'Penalty' is used ... it will never be construed as a sum absolutely fixed. But the reverse is by no means the case; and the phrase *'liquidated damages'*, has often been made to read *'penalty'*"). Some contracts use both terms. E.g., *Commissioner of Public Works v. Hills*, [1906] A.C. 368, 375 (P.C.) (Cape of Good Hope) ("Indeed, the form of expression here, 'forfeited as and for liquidated damages', if literally taken, may be said to be self-contradictory, the word 'forfeited' being peculiarly appropriate to penalty, and not to liquidated damages").

[95] *Cavendish Square Holdings BV v. El Makdessi*, [2015] UKSC 67, ¶31; [2016] A.C. 1172, 1204 per Lord Neuberger & Lord Sumption ("the law relating to penalties has become the prisoner of artificial categorisation, itself the result of unsatisfactory distinctions: between a penalty and genuine pre-estimate of loss, and between a genuine pre-estimate of loss and a deterrent"); *Evans v. Moseley*, 114 P. 377 (Kan. 1911) ("There is no branch of the law on which a unanimity of decision is more difficult to find or on which more illogical and inconsistent holdings may be found"); *Gobble v. Linder*, 76 Ill. 157, 158 (Sup. Ct. 1875) ("No branch of the law is involved in more obscurity, by contradictory decisions, than whether the sum named in an agreement to secure performance will be treated as liquidated damages or as penalty") & *Jaquith v. Hudson*, 5 Mich. 123, 133 (Sup. Ct. 1858) ("It is not to be denied that there is some conflict, and *more* confusion, in the cases; judges have been long and constantly complaining of the confusion and want of harmony in the decisions upon this subject") (emphasis in original).

visitor gets lost in the Kasbah, the vast labyrinth of market lanes, and cannot remember the name or address of his or her hotel. A good Samaritan cannot help the tourist find his or her hotel when all the tourist can say is that he or she is lost. The knowledge that the tourist is lost does not contribute to the solution of the problem.

[169] Fourth, the distinction between a penalty and a pre-estimate of damages is of limited value. There are fact patterns which make it exceedingly difficult, if not impossible, to estimate damages.[96] This might mean that a stipulated-consequence-on-breach term is unenforceable even though it makes sound business sense.[97]

[170] Fifth, the penalty aspect of a provision can often be camouflaged by clever drafting. An onerous obligation can be transformed into a beneficial option, as Justice Heath explained more than 200 years ago in *Astley v. Weldon*:[98]

> It is a well-known rule in equity, that if a mortgage covenant be to pay £5 per cent., and if the interest be paid on certain days, then to be reduced to £4 per cent. The Court of Chancery will not relieve if the early day be suffered to pass without payment; but if the covenant be to pay £4 per cent, and if the party do not pay at a certain time it shall be raised to £5 per cent., there the Court of Chancery will relieve.

[171] Professor Farnsworth made the same point:[99]

> Although it is beyond the parties' power to provide for a penalty of, say, $1,000 for every day's delay in performance, up to a maximum of $10,000, they can shape their substantive rights and dates through a provision for a premium by setting the completion date ten days later and providing that the price shall be increased by $1,000 for each day the work is finished early, up to a maximum of $10,000.

[172] A doctrine that can so easily be manipulated must be carefully scrutinized. It is like a snow bridge – not as useful as it appears. In fact, it is downright dangerous.

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[96] *Cavendish Square Holdings BV v. El Makdessi*, [2015] UKSC 67, ¶31; [2016] A.C. 1172, 1204 per Lord Neuberger & Lord Sumption ("The real question ... is whether [a stipulated-consequence-on-breach term] ... is penal, not whether it is a pre-estimate of loss").

[97] Scottish Law Commission, Review of Contract Law: Discussion Paper on Penalty Clauses 6-7 (No. 162) (November 2016). Contra *Paciocco v. Australia and New Zealand Banking Group Ltd.*, [2016] HCA 28, ¶30; 258 C.L.R. 525, 547 per Kiefel, J. ("[a stipulated-payment-on-breach term may be enforceable even] if no pre-estimate is made at the time the contract is entered into").

[98] 126 Eng. Rep. 1318, 1322-23 (Common Pleas 1801). See also *Wallingford v Mutual Society*, 5 A.C. 685, 702 (H.L. 1880) per Lord Hatherley.

[99] E. Farnsworth, Contracts 818 (4th ed. 2004). See *Banta v. Stamford Motor Co.*, 92 A. 665 (Conn. Sup. Ct. 1914)(the yacht-construction contract featured a premium for advance delivery).

[173] Sixth, it is not obvious why a promisor's commitment in a commercial agreement to pay a sum for breach of another term of the agreement that may bear no relationship to the damages that a court would award for nonperformance is contrary to public policy. A stipulated-consequence-on-breach term in a commercial contract and the common law damages principle serve completely different purposes. The former is adopted to avoid the need to utilize the common law damages protocol to resolve the consequences of nonperformance of a contract promise. The latter is resorted to because the parties have been unable to resolve the obligation of the promisor to the promisee on the former's breach of a contractual obligation.

[174] Here is an example of a contract that is the product of careful negotiations that contain a stipulated-consequence-on-breach term that does not incorporate common law damage values. Suppose that A, a public undertaking responsible for the provision of healthcare services in E, a metropolitan area, enters into an agreement with B, a multi-national medical-testing services enterprise. B agrees to build in E a modern laboratory and provide medical-testing services for a twenty-five year period. A promises to pay B an annual minimum fee with escalating factors based on the number of test results produced for each of the twenty-five years of the contract. The price-per-test declines as the quantity of annual tests escalates.[100] A and B are satisfied that once the laboratory is up and running and meeting A's needs, C and D, public undertakings responsible for the provision of health care services in E's satellite communities, will want to do business with B and ultimately allow B to operate at maximum capacity. A expects that its needs will rise significantly over the contract term. If B operates at a maximum capacity A's per test costs drop. Both A and B appreciate that a change in government may affect A's willingness to do business with B. B insists that A undertake onerous commitments if A terminates the contract before the end date. A knows that B requires a guaranteed minimum income stream to justify B's upfront investment and that without A's business B could not attract other customers. A and B recognize that a change in service provider may leave B with a special-design facility that may have no market value; would leave B with an unprofitable business in E; would greatly inconvenience both sides; and consume large amounts of their leadership teams' time to secure a smooth transition. A accepts that B's concerns are reasonable and agrees to pay B three times the total minimum amount due over the unexpired portion of the contract. A understands that the likelihood a court would order A to pay a sum this large if A terminated the agreement prematurely is low. There is a change of government after five years and A terminates the agreement with B after year eight. B sues A for three times the minimum amount that A was obliged to pay B in the period covering years nine to twenty-five inclusive. A refuses to pay on the ground the stipulated-consequence-on-breach term is an unenforceable penalty.

[175] There is no good reason to relieve A of its obligation to pay the stipulated sum set out in the contract. A voluntarily made the agreement with B. It was the product of negotiations between parties with contracting capacity who fully understood their obligations and responsibilities under

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[100] Davis, "Penalty Clauses Through the Lens of the Unconscionability Doctrine", 55 McGill L.J. 151, 158 (2010)("[the penalty doctrine] ignores the possibility that the prejudicial impact of a penalty clause on a breaching party has been offset by a benefit such as a price reduction conferred by another term of the contract").

the contract. Each side had top-notch lawyers. Both believed the relationship was in their best interests.

[176] It would be a disservice to A, the promisor, to assume that it was unaware of this onerous obligation and that it did not extract from B, the beneficial promisee of this stipulated-consequence-on-breach term, compensating concessions that offset this detriment.[101] The correlation between B's fees and the volume of testing may fall in this category.

[177] I now mention the deleterious consequence of the penalty rule – the detriment the penalty rule does to contract-interpretation principles. It forces courts to make indefensible claims about the meaning of contract text and to give text implausible meanings that the text cannot bear.[102] Courts considering the enforceability of a stipulated-consequence-on-breach term frequently conclude that the parties did not intend a promisor to comply with a promise on breach when it is incontrovertible that they did.[103] Justice Christiancy of the Michigan Supreme Court adverted to the damages this charade causes to the principles of text interpretation:[104] "But, as a rule of construction, or interpretation of contracts, it is radically vicious, and tends to a confusion of ideas in the construction of contracts generally". This is undoubtedly true.

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[101] *L/3 Communications/ Spar Aerospace Ltd. v. International Association of Machinists and Aerospace Workers*, 127 L.A.C. 4th 225, 246 (Wakeling, Q.C. 2004) ("Or some issues may not be dealt with because a concession secured its absence from the agreement").

[102] *Composite Technologies Inc. v. Shawcor Ltd.*, 2017 ABCA 160, ¶107; [2017] 8 W.W.R. 427, 468 ("It is not the role of a court to inflict on the parties' contract text an implausible meaning. Courts that do so torture and destroy the text"); *Lenz v. Sculptoreanu*, 2016 ABCA 111, ¶4; 399 D.L.R. 4th 1, 6 ("A contrary interpretation would give the text an implausible meaning. A court may never do this"); *Valard Construction Ltd. v. Bird Construction Co.*, 2016 ABCA 249, ¶184; 57 C.L.R. 4th 171, 236 per Wakeling, J.A. ("This interpretation was not one that the words may bear. It is implausible"); *Lawson Store Service Co. v. Russell Wilkins & Sons Ltd.*, [1906] HCA 87; 4 C.L.R. 672, 685 & *Sun Printing and Publishing Assoc. v. Moore*, 183 U.S. 642, 673 (1902)(both courts approved the following statement in *Clement v. Cash*, 21 N.Y. 253, 257 (Ct. App 1860): "a court of law has no right to erroneously construe the intention of the parties, when clearly expressed, in the endeavour to make better contracts for them than they have made for themselves. In these, as in all other cases, the courts are bound to ascertain and carry into effect the true intent of the parties") & A. Scalia & B. Garner, Reading Law: The Interpretation of Legal Texts 31 (2012)("A fundamental rule of textual interpretation is that neither a word nor a sentence may be given a meaning that it cannot bear. Without the concept of permissible meanings, there is no such thing as a faithful interpretation of legal texts").

[103] *Interstate Industrial Uniform Restore Service, Inc. v. Couri Pontiac, Inc.* 355 A. 2d 913, 921 (Me. Sup. Jud. Ct. 1976)("this Court has held that the question of whether a stipulated amount is liquidated damages or a penalty shall be resolved by finding the intent of the parties. ... Clearly that ... does not mean that the Court must follow the intent as it appears on the face of the contract, for so doing would require the Court to uphold any provision designated 'liquidated damages' since the parties have clearly stated that they intend to pay that amount in the event of breach").

[104] *Jaquith v. Hudson*, 5 Mich. 123, 136 (Sup. Ct. 1858). See also *Willson v. Mayor of Baltimore*, 34 A. 774, 775 (Md. Ct. App. 1896)("Whether a sum named in a contract to be paid by a party in default on its breach is to be considered liquidated damages or merely a penalty, is one of the most difficult and perplexing inquiries encountered in the construction of written agreements. The solution of that question ... [is] to some extent controlled by artificial general rules which are not wholly in harmony with the ordinary canons of construction").

[178] The real explanation for nonenforcement is the manifest oppressiveness or unconscionability of the term.[105] Courts do not wish to lend their office to such a reprehensible task. Justice Christiancy of the Michigan Supreme Court recognized the diversionary nature of the intention model:[106] "[T]hough the parties actually intended the sum to be paid, as the damages agreed upon between them, yet it being clearly unconscionable, the court would disregard the intention and refuse to enforce the stipulation".

[179] In my opinion, the true explanation for the cases in which modern courts decline to give effect to a stipulated-consequence-on breach term in a commercial case is the courts' belief that the

[105] A. Swan & J. Adamski, Canadian Contract Law 950, 951 (3d ed. 2012) ("The more elaborate catalogue presented by Lord Dunedin [in *Dunlop Tyre*] was necessary only as long as the common law rejected the general power to police contracts for unconscionability").

[106] *Jaquith v. Hudson*, 5 Mich. 123, 136 (Sup. Ct. 1858). See Bildfell, "Exculpatory Clauses and Liquidated Damages Clauses: Two Sides of the Same Coin?", 78 Sask. L. Rev. 347, 357 (2015)("the test applied to penalties *prima facie* appears more focused on the reasonableness of the clause itself").

terms are so one-sided that the courts ought not to enforce them.[107] The wisdom of this standard should be directly confronted.[108]

[180] Courts do not decline to enforce bargained stipulated-consequence-on-breach terms in a commercial agreement to protect the interest of an improvident or incompetent promisor. The promisor is a fortunate beneficiary of a rule not crafted for the promisor's advantage.[109] Courts declare these

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[107] *Dunlop Pneumatic Tyre Co. v. New Garage and Motor Co.*, [1915] A.C. 79, 101 (H.L. 1914) per Lord Parmoor ("The agreed sum … is held to be a penalty if it is extravagant or unconscionable"); *Clydebank Engineering and Shipbuilding Co. v. Castaneda*, [1905] A.C. 6, 10 (H.L. 1904)("whether [this stipulated-payment-on-breach term] ... is ... unconscionable and extravagant, and one which no court ought to allow to be enforced"); *O'Dea v. Allstates Leasing System (W.A.) Pty. Ltd.*, [1983] HCA 3, ¶1; 152 C.L.R. 359, 374 per Murphy, J. ("These provisions permit the lessor to recover grossly in excess of any genuine pre-estimate of its loss. They are a trap for an unwary or unfortunate lessee. They are unenforceable because, by modern standards, they are unconscionably harsh"); *Truck Rent-A-Center, Inc., v. Puritan Farms 2nd, Inc.*, 361 N.E. 2d 1015, 1019-20 (N.Y. Ct. App. 1977) (the Court upheld an onerous stipulated-payment term, noting that "[t]he agreement was fully negotiated ... . There is no indication of any disparity of bargaining power"); *Hutchison v. Tompkins*, 259 So. 2d 129, 132 (Fla. Sup. Ct. 1972) ("The better result, ... is to allow the liquidated damage clause to stand if the damages are not readily ascertainable at the time the contract is drawn, but to permit equity to relieve against the forfeiture if it appears unconscionable in light of the circumstances existing at the time of breach"); *Jaquith v. Hudson*, 5 Mich. 123, 133 (Sup. Ct. 1858)("courts of justice will not recognize or enforce a contract, or any stipulation of a contract, clearly unjust and unconscionable; a principle of common sense and common honesty so obviously in accordance with the dictates of justice") & T. Sedgwick, A Treatise on the Measure of Damages, or, an Inquiry into the Principles Which Govern the Amount of Pecuniary Compensation Awarded by Courts of Justice 420 (1858) ("if ... the contract is such that the strict construction ... would work ... oppression, the use of the term liquidated damages will not prevent the courts from inquiring into the actual injury sustained and doing justice between the parties"). See also *Tercon Contractors Ltd. v. British Columbia*, 2010 SCC 4, ¶¶108 & 122; [2010] 1 S.C.R. 69, 116 ("The situations in which the doctrine [of fundamental breach] is invoked could be addressed more directly and effectively through the doctrine of "unconscionability", as assessed at the time the contract was made") & 122 ("What was demonstrated in *Plas-Tex* was that the defendant Dow was so contemptuous of its contractual obligations and reckless as to the consequences of the breach as to forfeit the assistance of the court"); *Hunter Engineering Co. v. Syncrude Canada Ltd.*, [1989] 1 S.C.R. 426, 455-56 per Dickson, C.J. ("the courts should not disturb the bargain the parties have struck, and I am inclined to replace the doctrine of fundamental breach with a rule that holds the parties to the terms of their agreement [liability-exclusion term], provided the agreement is not unconscionable").

[108] *Hunter Engineering Co. v. Syncrude Canada Ltd.*, [1989] 1 S.C.R. 426, 462 per Dickson, C.J ("there is much to be gained by addressing directly the protection of the weak from over-reaching by the strong, rather than relying on the artificial legal doctrine of "fundamental breach"); *Tercon Contractors Ltd. v. British Columbia*, 2010 SCC 4, ¶120; [2010] 1 S.C.R. 69, 122 ("a plaintiff who seeks to avoid the effect of an exclusion clause must identify the overriding public policy that it says outweighs the public interest in the enforcement of the contract") & *Wallis v. Smith*, 21 Ch. D. 243, 274 (C.A. 1882) per Lindley, L.J. ("Whether relief was given on the theory of oppression, or on the theory that the parties could not have meant what they said — that it was too absurd — or whether relief was given by reason of the usury laws, I do not know — it is an antiquarian research which I have not prosecuted").

[109] The recipient of punitive damages also derives a secondary benefit to which he or she would not ordinarily be entitled by the application of normal damage principles. *Hill v. Church of Scientology*, [1995] 2 S.C.R. 1130, 1208 ("Punitive damages may be awarded in situations where the defendant's misconduct is so malicious, oppressive and high-handed that it offends the court's sense of decency: Punitive damages bear no relation to what the plaintiff should receive by way of compensation").

terms invalid to protect the reputation of the administration of justice.[110] The reputation of the judiciary would be jeopardized if it gave its imprimatur to oppressive terms – terms that were manifestly one-sided and grossly unfair.[111] I agree with Justice Story of the United States Supreme Court when he declared extrajudicially[112]

> that the folly of one man cannot authorize gross oppression on the other side. And law, as a science, would be unworthy of the name, if it did not, to some extent, provide the means of preventing the mischiefs of improvidence, rashness, blind confidence, and credibility on one side: and of skill, avarice, cunning and gross violation of the principles of morals and conscience on the other.

2. In 1978 the Supreme Court of Canada Rejected the Penalty Rule and Adopted the Oppression Standard

[181] In 1978 the Supreme Court of Canada, in *Elsley v. J.G. Collins Insurance Agencies Ltd.*,[113] jettisoned[114] the classic penalty rule: "[T]he power to strike down a penalty clause is a blatant interference with freedom of contract and is designed for the sole purpose of providing relief

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[110] *Websters v. Bosanquet*, [1912] A.C. 394, 398 (P.C.) (Ceylon) ("the question must always be whether the construction contended for renders the agreement unconscionable and extravagant and one which no Court ought to allow to be enforced") & *Clydebank Engineering and Shipbuilding Co. v. Castaneda*, [1905] A.C. 6, 10 (H.L. 1904) per Earl of Halsbury ("whether it is ... unconscionable and extravagant and one which no Court ought to allow to be enforced").

[111] *Priebe & Sons, Inc. v. United States*, 332 U.S. 407, 418 (1947) per Frankfurter, J. ("But one man's default should not lead to another man's unjust enrichment").

[112] 2 J. Story, Commentaries on Equity Jurisprudence as Administered in England and America 743 (4th ed. 1846).

[113] [1978] 2 S.C.R. 916, 937.

[114] Some commentators have suggested that this portion of Justice Dickson's opinion is *obiter* and not binding on lower courts. I disagree. First, this statement is part of the *ratio decidendi* of the case. Second, even if the statement was *obiter*, there is a presumption that *obiter* statements supported by a majority of the Court are binding on lower courts. The presumption is at its strongest if the proposition in dispute plays a central role in the legal regime fashioned by the Supreme Court and is consistent with fundamental legal principles. The Supreme Court not only resolves the particular dispute that an appeal presents for resolution but creates a legal structure that accounts not only for the disposition of the appeal before it but all related matters as well. If Justice Dickson's opinion was *obiter*, the presumption kicks in. The presumption is at its weakest if the proposition plays only a minor role in the legal regime the Supreme Court has constructed and is inconsistent with fundamental legal principles. See generally *The Queen v. Henry*, 2005 SCC 76, ¶57; [2005] 3 S.C.R. 609, 642 ("The weight [of *obiter*] decreases as one moves from the dispositive *ratio decidendi* to a wider circle of analysis which is obviously intended for guidance and which should be accepted as authoritative. Beyond that, there will be commentary, examples or exposition that are intended to be helpful and may be found to be persuasive, but are certainly not 'binding'") & *The Queen v. Prokofiew*, 2010 ONCA 423, ¶20; 100 O.R. 3d 401 ("*Obiter dicta* will move along a continuum. A legal pronouncement that is integral to the result or the analysis that underlies the determination of the matter in any particular case will be binding. *Obiter* that is incidental or collateral to that analysis should not be regarded as binding, although it will obviously remain persuasive"). The presumption is nonexistent if an observation is nothing more than an off-hand or a "throw-away" remark. *Cavendish Square Holding BV v. El Makdessi*, [2015] UKSC 67, ¶42; [2016] A.C. 1172, 1209 per Lord Neuberger & Lord Sumption.

against oppression for the party having to pay the stipulated sum. It has no place where there is no oppression." A judgment declining to enforce a stipulated-consequence-on-breach term is an obvious abridgment of the autonomy of the parties and the freedom of contract.[115]

[182] *Elsley* clarified the law on the enforceability of a stipulated-consequence-on-breach term in a commercial contract between parties that had sufficient resources to retain legal counsel. It was enforceable unless oppressive. [116]

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[115] *Cavendish Square Holding BV v. El Makdessi*, [2015] UKSC 67, ¶33; [2016] A.C. 1172, 1205 per Lord Neuberger & Lord Sumption ("The penalty rule is an interference with freedom of contract. It undermines the certainty which parties are entitled to expect of the law") & S. Waddams, The Law of Contracts 313 (7th ed. 2017).

[116] Many Canadian courts have enforced stipulated-consequence-on-breach terms using the oppression standard. E.g., *32262 BC Ltd. v. See-Rite Optical Ltd.*, 1998 ABCA 89, ¶16; 39 B.L.R. 2d 102 (the Court enforced a stipulated-payment-on-breach default term because it was not oppressive); *Fern Investments Ltd. v. Golden Nugget Restaurant (1987) Ltd.*, 1994 ABCA 153; 149 A.R. 303 (the Court declared that a $100,000 security deposit was not refundable unless it was oppressive); *City of Calgary v. Northern Construction Co.*, 1985 ABCA 285; [1986] 2 W.W.R. 426 (the Court enforced a stipulated-payment-on-breach term because it was not oppressive); *RCAP Leasing Inc. v. Martin*, 2016 ABQB 542;62 B.L.R. 5th 336 (Masters chambers) (the Master refused to enforce an administrative fee payable on the lessee's default in an equipment lease agreement because it was unconscionable and oppressive); *Precision Drilling Canada Ltd. Partnership v. Yangarra Resources Ltd.*, 2015 ABQB 649; 46 B.L.R. 5th 327 (Master)(the Court enforced a promisor's obligation in a commercial contract to pay eighteen percent interest on unpaid accounts, having determined that the term was not extravagant or unconscionable); *Bucci Xenex Project Ltd. v. Ramasiuk*, 2010 ABQB 389 (the Court enforced a forfeiture term in a condominium purchase agreement because it was not oppressive); *Markdale Ltd., v. Ducharme*, 235 A.R. 283, 293 (Q.B. 1998) ("[*Elsley*] states that the rule that for a sum to be considered a penalty rather than liquidated damages, it must be oppressive"); *City of Edmonton v. Triple Five Corp.*, 158 A.R. 293 (Q.B. 1994)(the Court enforced a term allowing the City to draw on a letter of credit if the promisor did not complete a subdivision on time because the term was not oppressive); *Liu v. Coal Harbour Properties Partnership*, 2006 BCCA 385; 273 D.L.R. 4th 508 (the Court held that condominium deposits totalling $391,000 were forfeited as the term was not oppressive); *Prudential Insurance Co. of America v. Cedar Hills Properties Ltd.*, [1995] 3 W.W.R. 360, 369-70 (B.C.C.A. 1994)(the Court enforced a $100,000 interest-rate-standby fee in a $6.4 million commercial loan agreement because it was not unconscionable, extravagant or oppressive); *Bankers Mortgage Corp. v. Plaza 500 Hotels Ltd.*, 2016 BCSC 722; 65 R.P.R. 5th 120 (the Court enforced a $96,000 exit fee in a loan retainer agreement on the basis that it was not an unenforceable penalty); *GL&V Canada Inc. v. Deramore Construction Services Inc.*, 2015 BCSC 2534; 50 C.L.R. 4th 108 (the Court applied *Elsley* and enforced a stipulated-payment-on-breach term in a commercial contract); *Schindler Elevator Corp. v. New Vista Society*, [1998] B.C.J. No. 2327, ¶18 (Sup. Ct.)(the Court enforced a stipulated-payment-on-breach term in a commercial contract because it was not "excessive, extravagant or unconscionable"). *Volvo Truck Finance Canada Ltd. v. Premier Pacific Holdings Inc.*, 2002 BCSC 1137; 29 B.L.R. 3d 213 (the Court enforced an interest-escalation-on-default term in a commercial contract because the promisor had not demonstrated that it was oppressive); *Wolf Chevrolet Oldsmobile Ltd. v. 552234 B.C. Ltd.*, 2004 BCPC 154; 49 B.C.C.R. 3d 247 (the Court enforced a term in a vehicle-sale agreement that obliged the purchaser to pay the vendor $5000 if he resold the vehicle in the United States); *Canadian Wheat Board v. Pigeon Hill Elk Farm Ltd.*, 2009 SKQB 437; 345 Sask. R. 144 (the Court enforced a stipulated-payment-on-breach term in a commercial contract in the absence of oppression); *Carnoustie Holdings Ltd. v. Brennan Educational Supply Ltd.*, 2008 SKQB 257; 319 Sask. R. 53 (the Court enforced stipulated-payment-on-breach term in a commercial contract in the absence of oppression); *Lac- La Ronge Indian Band v. Dallas Contracting Ltd.*, 2001 SKQB 135; 206 Sask. R. 13 (the Court missed a stipulated-payment-on-breach term in a commercial contract - $1000/day the projected completion date was missed); *Peachtree II Associates - Dallas LP v. 857486 Ontario Ltd*, 256 D.L.R. 4th 490, 500 (Ont. C.A. 2005)("courts should, whenever possible,

[183] This was a surprising development.

[184] Just four years earlier, in *H.F. Clarke Ltd. v. Thermidiare Corp.*,[117] the Supreme Court, by a three-to-two majority,[118] refused to enforce an important term in an exclusive-distribution commercial contract between two businesses.[119] H.F. Clarke Ltd., in breach of the agreement, sold products manufactured by others than Thermidaire that served the same purpose as Thermidaire's products. The promisee invoked the stipulated-consequence-on-breach term and demanded that H.F. Clarke Ltd. pay the "gross trading profit" that it gained from the sale of the competition's products.

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favour analysis on the basis of equitable principles and unconscionability over the strict common law rule pertaining to penalty clauses"); *Birch v. Union of Taxation Employees*, 2008 ONCA 809, ¶39; 305 D.L.R. 4th 64, 77 ("I can discern nothing in the unique contractual relationship between a union member and his or her union which would suggest to the court that we should refuse to apply the doctrine of unconscionability in appropriate circumstances"); *Zander Sod Co. v. Solmar Development Corp.*, 2011 ONSC 7; 6 R.P.R. 5th 116 (the Court enforced a stipulated-payment-on-breach term in a commercial contract, noting the import of *Elsley*); *Nortel Networks Corp. v. Jervis*, 18 C.C.E.L. 3d 100 (Ont. Super. Ct. 2002)(the Court enforced a stipulated-payment-on-breach term because it was not unconscionable or vexatious); *Lee v. OCCO Developments Ltd*., 5 R.P.R. 3d 203 (N.B.C.A. 1996)(the Court enforced a default term in a large condominium purchase agreement because it was not unconscionable); *Beton Brunsuick Ltee v. Martin*, 176 N.B.R. 2d 81 (C.A. 1996)(the court opined that a noncompetition agreement would be unenforceable only if it was oppressive) & *Federal Business Development Bank v. Fredericton Motor Inn*, 32 N.B.R. 2d 108 (Q.B. 1980)(the Court enforced a $5000 commitment fee payable in the event the hotel decided not to conclude the loan transaction). See also Davis, "Penalty Clauses Through the Lens of Unconscionability Doctrine: *Birch v. Union of Taxation Employees, Local 70030*", 55 McGill L.J. 151, 164 (2010). So have Hong Kong courts. E.g., *Chow Kee James v. Transway Construction and Engineering Ltd.*, [2006] HKCFI 1433 (the Court enforced a late-completion change in a large public works contract, in part, because it was not unconscionable); *First Commercial Bank v. The Owners of "Liberty Container"*, [2004] HKCFI 7013, ¶13 ("the modern approach to penalty clauses is to look at whether in respect of a commercial contract, the disputed provision can be said to be unconscionable or oppressive by reason of its being extravagant, exorbitant or excessive and that the court should be slow to find terms agreed by the parties to be in terrorem rather than genuine agreement providing for fixed formula of loss") *& Vintech Co. v. Radio-Holland Hong Kong Co.*, [2001] HKDC 36 (the Court enforced a stipulated-payment-on-breach-term because it was not oppressive). Some post-1978 judgments determining the enforceability of stipulated-consequence-on-breach terms never refer to *Elsley*. E.g., *B.L.T. Holdings Ltd. v. Excelsior Life Insurance Co.*, [1986] 6 W.W.R. 534 (Alta. C.A. 1986); *Dial Mortgage Corp. v. Baines*, 15 Alta. L.R. 2d 211 (Q.B. 1980); *Dezcam Industries Ltd. v. Kwak*, [1983] 5 W.W.R. 32 (B.C.C.A.); *Colliers Macaulay Nicolls Inc. v. Park Georgia Properties Ltd.*, 2003 BCSC 1785; 15 R.P.R. 4th 132; *Dundas v. Schafer*, 2014 MBCA 92; 377 D.L.R. 4th 485; *Infinite Maintenance Systems Ltd. v. ORC Management Ltd.*, 139 O.A.C. 331 (C.A. 2001) & *Place Concorde East Ltd. Partnership v. Shelter Corp. of Canada*, [2003] O.J. No. 5437; 43 B.L.R. 3d 54 (Sup. Ct).

[117] [1976] 1 S.C.R. 319 (1974).

[118] Justices Martland and Dickson dissented. [1976] 1 S.C.R. 319, 339 (1974). They adopted the unanimous reasons of the Court of Appeal for Ontario. [1973] 2 O.R. 57, 70 ("The parties knew and appreciated these factors [the damage formula may exceed by a large margin the actual damages] and chose this method to establish compensation for a loss, the amount of which was difficult to determine and, no doubt, very costly to establish. I am convinced that they agreed upon a method which they both regarded as one which would lead to a fair and just determination of Thermidaire's damages and losses in the event of a breach of the covenant"). This position is hard to criticize.

[119] A. Swan & J. Adamski, Canadian Contract Law 952 (3d ed. 2012) ("Thermidaire Corporation ... was a small one-person corporation dealing with a much larger corporation").

[185] The trial court[120] and the Ontario Court of Appeal[121] granted Thermidaire what it bargained and paid for. The Supreme Court did not.[122] Chief Justice Laskin and two of his colleagues refused to enforce the stipulated-consequence-on-breach term because the "gross trading profit" was twice the amount the promisee would have received had the promisor promised to disgorge its net profits, the sum the Court believed was the loss it suffered as a result of H.F. Clarke Ltd.'s breach.

[186] Chief Justice Laskin substituted the Court's assessment of the fairness of the term for that of the contracting parties and ignored the fact that the stipulated-payment-on-breach term was a part of a bargain between two businesses:[123]

> The courts may be quite content to have the parties fix the damages in advance and relieve the courts of this burden in cases where the nature of the obligation upon the breach of which damages will arise, the losses that may reasonably be expected to flow from a breach and their unsusceptibility to ready determination upon the occurrence of a breach provide a base upon which a pre-estimation may be made. But this is only the lesser half of the problem. The interference of the courts does not follow because they conclude that no attempt should have been made to predetermine the damages or their measure. It is always open to the parties to make the predetermination, *but it must yield to judicial appraisal of its reasonableness in the circumstances.*

[187] Had it not been for the *H.F. Clarke Ltd. v. Thermidaire Corp.*[124] aberration, the decision in *Elsley* would have been consistent with a trend that started in England early in the twentieth century and was immediately followed in Canada.

3. Freedom of Contract Is a Fundamental Value in Societies Whose Welfare Depends on a Free-Market Economy

[188] Although Justice Dickson did not explain in *Elsley* why the Supreme Court rejected the much maligned penalty rule and endorsed an oppression principle that so unreservedly promoted freedom of contract values in commercial contracts, his reasoning is implied.

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[120] 5 C.P.R. 2d 108.

[121] [1973] 2 O.R. 57.

[122] A. Swan & J. Adamski, Canadian Contract Law 951 (3d ed. 2012) (the authors referred to *H.F. Clarke Ltd. v. Thermidaire Corp.* as a "bad detour").

[123] [1976] 1 S.C.R. 319, 331 (emphasis added).

[124] *H.F. Clarke Ltd. v. Thermidaire Corp*. now rests on the judicial sea floor. *Elsley* did it in. A. Swan & J. Adamski, Canadian Contract Law 952 (3d ed. 2012) ("The approach adopted by Laskin C.J. ... was implicitly rejected by the Court in *Elsley Estate v. J.G. Collins Insurance Agencies Ltd.*").

[189] There is no compelling reason to decline to enforce stipulated-consequence-on-breach terms in commercial contracts.[125]

[190] Freedom of contract is a fundamental value in Canada and any other society whose members' welfare is largely dependent on a thriving free-market economy.[126] Canadian,[127] English[128] Australian,[129] Hong Kong[130] and American[131] courts have frequently recognized the importance of freedom of contract.

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[125] *Harvest Operations Corp. v. Canada*, 2017 ABCA 393, ¶51; [2018] 3 W.W.R. 51, 65 ("Legal documents are important. They set out the rights and responsibilities of their signatories. They should be enforced as written unless there is a compelling reason to modify them").

[126] See P. Atiyah, The Rise and The Fall of Freedom of Contract (1979). Contracts are also important mechanisms in planned economies. But not freedom of contract. Grossfeld, "Money Sanctions for Breach of Contract in a Communist Economy", 72 Yale L.J. 1326, 1327 (1963) ("The function of the contract ... is to implement in detail the directives of governmental policy as expressed in the plan").

[127] E.g., *Tercon Contractors Ltd. v. British Columbia,* 2010 SCC 4, ¶¶82 & 123; [2010] 1 S.C.R. 69, 107 & 123 per Binnie J. ("the principle is that a court has no discretion to refuse to enforce a valid and applicable contractual exclusion clause unless the plaintiff ... can point to some paramount consideration of public policy sufficient to override the public interest in freedom of contact and defeat what would otherwise be the contractual rights of the parties") & ("[Canada recognizes] the very strong public interest in the enforcement of contracts"); *Elsley v. J.G. Collins Insurance Agencies Ltd.*, [1978] 2 S.C.R. 916, 937 ("the power to strike down a penalty clause is a blatant interference with freedom of contract"); *Hittinger v. Turgeon*, 2005 ABQB 257, ¶115; [2006] 3 W.W.R. 699, 716 ("The case law is replete with references to the need to maintain the integrity of contracts") & *Prudential Insurance Co. of America v. Cedar Hills Properties Ltd.*, [1995] 3 W.W.R. 360, 369 (B.C.C.A. 1994) ("To single out this provision in the absence of any circumstances suggesting oppression or overreaching is ... an unwarranted interference with freedom of contract"); *MTK Auto West Ltd. v. Allen*, 2003 BCSC 1613, ¶22 ("A court should not strike down a penalty clause as being unconscionable lightly because it is a significant intrusion on freedom of contract"); *869163 Ontario Ltd. v. Torrey Springs II Associates Ltd. Partnership,*256 D.L.R. 4th 490, 500 (Ont. C.A. 2005)("Judicial enthusiasm for the refusal to enforce penalty clauses has waned in the face of a rising recognition of the advantages of allowing parties to define for themselves the consequences of breach"); *Zander Sod Co. v. Solmar Development Corp.*, 2011 ONSC 7, ¶96; 6 R.P.R. 5th 116, 143 ("The common law has long recognized and respected private ordering. ... [P]arties generally enjoy the freedom to contract with one another as they see fit. That freedom includes the right to agree on a limit of damages or even a fixed sum to be paid in the event of breach") & S. Waddams, The Law of Contracts 320 (7th ed. 2017) ("It is often in the interests of both parties to make the cost of non-performance predictable in advance").

[128] *Cavendish Square Holding BV v. EI Makdessi*, [2015] UKSC 67, ¶257; [2016] A.C. 1172, 1278 per Lord Hodge ("The rule against penalties is an exception to the general approach of the common law that parties are free to contract as they please and that the courts will enforce their agreements"); *Belmont Park Investments Pty Ltd. v. BNY Corporate Trustee Services*, [2011] UKSC 38, ¶103; [2012] 1 A.C. 383, 421 per Lord Collins ("party autonomy is at the heart of English commercial law"); *Philips Hong Kong Ltd. v. Hong Kong*, [1993] UKPC 3a, ¶23;[1993] 1 H.K.L.R. 269, 280 ("bear in mind that what the parties have agreed should normally be upheld. Any other approach will lead to undesirable uncertainty, especially in commercial contracts"); *Scandinavian Trading Tanker Co. v. Flota Petrolera Ecuatoriana (Scaptrade)*, [1983] 2 A.C. 694, 703 (H.L.) per Lord Diplock ("Prima facie parties to a commercial contract bargaining on equal terms can make 'time to be of the essence' of the performance of any primary obligation under the contract that they please, whether the obligation be to pay a sum of money or to do something else"); *Scandinavian Trading Tanker Co. v. Flota Petrolera Ecuatoriana (Scaptrade)*, [1983] Q.B. 529, 540-41 (C.A. 1982)("It is of the utmost importance in commercial transactions that, if any particular event occurs which may affect

[191] Whenever parties with capacity and sufficient resources to retain legal counsel make commercial bargains the law is predisposed to enforce their bargains. This is so whether or not they actually retained counsel. There is a legal presumption that commercial parties know the burdens and benefits their bargain bestows on them and whether the terms are improvident or suspect for other reasons.[132]

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the parties' respective rights under a commercial contract, they should know where they stand. The court should so far as possible desist from placing obstacles in the way of either party ascertaining his legal position, if necessary with the aid of advice from a qualified lawyer, because it may be commercially desirable for action to be taken without delay, action which may be irrevocable and which may have far-reaching consequences"); *Dunlop Pneumatic Tyre Co. v. New Garage and Motor Co,* [1915] A.C. 79, 103 (H.L. 1914) per Lord Parmoor, ("I can see no reason why ... the law should interfere with freedom of contract"); *E. Underwood & Son Ltd. v. Barker*, [1899] 1 Ch. 300, 305 (C.A.) per Lindley, M.R. ("If there is one thing more than another which is essential to the trade and commerce of this country it is the inviolability of contracts deliberately entered into; and to allow a person of mature age, and not imposed upon, to enter into a contract, to obtain the benefit of it, and then to repudiate it and the obligations which he has undertaken is, prima facie at all events, contrary to the interests of any and every country") & *Wallis v. Smith*, 21 Ch. D. 243, 266 (C.A. 1882) per Jessel, M.R. ("it is of the utmost importance as regards contracts between adults – persons not under disability and at arm's length – that the Courts of Law should maintain the performance of the contracts according to the intention of the parties; that they should not overrule any clearly expressed intention on the ground that Judges know the business better than the people know it themselves").

[129] *Ringrow Pty. Ltd. v. BP Australia Pty. Ltd.*, [2005] HCA 71, ¶31; 224 C.L.R. 656, 669 ("there is much to be said for the view that the courts should [allow]… parties to a contract greater latitude in determining what their rights and liabilities will be, so that an agreed sum is only characterized as a penalty if it is out of all proportion to damage likely to be suffered as a result of breach").

[130] *Philips Hong Kong Ltd. v. Hong Kong*, [1993] UKPC 3a, ¶17;[1993] 1 H.K.L.R. 269, 277 ("courts have always avoided claiming that they have any general jurisdiction to rewrite the contracts that the parties have made"); *Polyset Ltd. v. Panhandat Ltd.*, [2002] HKCFA 15, ¶156 per Litton, J ("where business people are dealing with each other at arm's length, their freedom to contract as they please is something the courts respect and protect"); *Bank of East Asia Ltd. v. Yip Chi Wai*, [2011] HKCFI 844, ¶66 (High Ct.) ("At present, the public policy is to respect parties' freedom to contract, allow them to make the agreed compensation in specific circumstances and restrict judicial intervention to cases where the penalty is excessive, exorbitant and unreasonable") & *Luen Wai Crane Engineering Co. v. AJAX Pong Construction Equipment Ltd.,* [1994] HKCFI 22, ¶8 (High Ct.) ("the court should be disinclined to put asunder the bargain struck between ... contractual parties on a level playing field. Neither of the parties in this case was under oppression nor ... [did] either of them ... [suffer] from any disadvantage at the negotiation table).

[131] *Wise v. United States*, 249 U.S. 361, 365 (1919)("There is no sound reason why persons competent and free to contract may not agree upon this subject as fully as upon any other, or why their agreement ... should not be enforced"); *Lochner v New York*, 198 U.S. 45, 76 (1905) (the Court struck down a statute limiting the number of days a bakery employee could work in a day or week on the basis of freedom of contract) & *ABRY Partners v. F&W Acquisitions LLC*, 891 A. 2d 1032, 1036 (Del. Ch. 2006) (the Court expressly acknowledged that public policy promotes freedom of contract). See E. Farnsworth, Contracts 313 (4th ed. 2004) ("The principle of freedom of contract rests on the premise that it is in the public interest to accord individuals broad powers to order their affairs through legally enforceable agreements. In general, therefore, parties are free to make such agreements as they wish, and courts will enforce them without passing on their substance").

[132] *Dunlop Pneumatic Tyre Co. v. New Garage and Motor Co.*, [1915] A.C. 79 (H.C. 1914)(the Court upheld a stipulated-payment-on-breach provision to enforce a price-maintenance regime in a tire-distribution contract); *Webster v. Bosanquet*, [1912] A.C. 394 (P.C.) (Ceylon) (the Privy Council upheld a stipulated-payment-on-breach

[192] Sir George Jessel, M.R., a strong advocate of the merits of freedom of contract said this: "[M]en of full age and competent understanding [must] ... have the utmost liberty of contracting, and that their contracts when entered into freely and voluntarily shall be held sacred and shall be enforced by courts of justice".[133]

[193] This is a principle of fundamental importance.

[194] Moreover, judicial enforcement of stipulated-consequence-on-breach terms in commercial bargains has salutary effects.

[195] At a general level, it encourages contracting parties to discharge their obligations by introducing a sufficiently high degree of certainty that the other contracting party will honour its commitments. It also means that if the promisor does not act as promised the disappointed promisee may invoke the assistance of the court and secure a predictable remedy for contract breach.[134] This element of certainty and predictability promotes essential commercial activity. Commercial actors will be more inclined to do business with enterprises with whom they have no prior satisfactory working relationships. This is a positive development. Most commercial actors can accomplish more working together than they can on their own. The interaction would be at a minimal level if commercial actors could not proceed on the valid assumption that promises are a valuable commodity to the promisee.

[196] More specifically, there is no valid reason why commercial actors should not be able to agree on the consequences of nonperformance. Professor Farnsworth states that "[t]he advantages of stipulating in advance a sum payable as damages are manifold".[135] A promisor who agrees to accept substantially less if it fails to perform at a specified level may have a competitive advantage

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term in a commercial tea-purchase contract); *Clydebank Engineering and Shipbuilding Co. v. Castaneda*, [1905] A.C. 6 (H.C.) (the Court enforced the shipbuilder's promise to pay £500 per week for late delivery of torpedo boats to the Spanish navy even though the agreement described the payment as a penalty); *Lordsvale Finance PLC v. Bank of Zambia*, [1996] Q.B. 752 (the Court upheld a default-uplift interest term in a syndicated loan agreement because a valid business purpose accounted for its presence); *Sun Printing and Publishing Assoc. v. Moore*, 183 U.S. 642, 673 (1901) (the Court enforced the charter-party's promise to pay a stipulated amount if it failed to return the chartered yacht safe and sound) & *United States v. Bethlehem Steel Co.*, 205 U.S. 105, 121 (1907)(the Court upheld a late payment term for the delivery of gun carriages to the American military).

[133] *Printing and Numerical Registering Co. v. Sampson*, L.R. 19 Eq. 462, 465 (Ch. 1875). See also *E. Underwood & Son Ltd. v. Barker*, [1899] 1 Ch. 300, 305 (C.A.) per Lindley, M.R. ("If there is one thing more than another which is essential to the trade and commerce of this country it is the inviolability of contracts deliberately entered into").

[134] *Robophone Facilities, Ltd. v. Blank*, [1966] 2 All E.R. 128, 142 (C.A.) per Diplock L.J. ("It is good business sense that parties to a contract should know what will be the financial consequences to them of a breach on their part, for circumstances may arise when further performance of the contract may involve them in a loss. ... Not only does it enable the parties to know in advance what their position will be if a breach occurs and so avoid litigation at all, but, if litigation cannot be avoided, it eliminates what may be the very heavy legal costs of proving the loss actually sustained which would have to be paid by the unsuccessful party").

[135] E. Farnsworth, Contracts 811 (4th ed. 2004).

over other businesses that are unprepared to agree to such a stipulated-consequence-on-breach term.[136] In some cases, it will be exceedingly difficult to prove damages. What damages has the armed-forces promisee suffered if the ship-builder promisor failed to deliver torpedo boats on time?[137] Torpedo boats do not generate revenue for their naval owners. The promisor may insist on a stipulated-consequence-on-breach term to place a cap on the consequences of nonperformance.[138] Without this concession the promisor may have declined to do business with the promisee. It may have been unwilling to assume an unknown substantial risk. Provisions of this nature relieve the commercial actors and the state of the costs associated with litigation conducted to measure the common law damages to which the promisee is entitled.[139] Corporate executives much prefer to devote their energies to activities that will generate future wealth, as opposed to reconstructing past events that are critical to the assessment of damages. There are very few business leaders who are prepared to litigate only to enforce a principle.

[197] It goes without saying that a judicial disposition in favor of the enforcement of commercial bargains will serve as a significant stimulus to due diligence by the parties – they will carefully consider the merits and demerits of each and every term.

[198] Freedom of contract is a fundamental feature in a community whose widespread prosperity depends on an efficient and productive market economy.

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[136] *Graham v. Wagman*, 89 D.L.R. 3d 282, 285 (Ont. C.A. 1978)("And, finally, we think it is entirely possible that other considerations may have motivated the defendant in accepting the $5 [per parking space instead of $25], such as the continuation of good business relations with the plaintiff").

[137] *Clydebank Engineering and Shipbuilding Co. v. Castaneda*, [1905] A.C. 6, (H.L. 1904) (counsel for the ship builder argued that the Spanish navy could not prove any losses attributable to the defendant's late delivery of the torpedo-boat destroyers). See also *Brio Electronic Commerce Ltd. v. Tradelink Electronic Commerce Ltd.*, [2016] HKCA 164, ¶17 ("to require such a comparison to be made would remove one of the commercial advantages that a liquidated damages clause is recognised as achieving – the dispensation with the need to adduce evidence on damages and to calculate them, particularly in cases where proof of the amount of damages suffered may be difficult to achieve to any degree of precision").

[138] S. Waddams, The Law of Contracts 319 (7th ed. 2017) ("the power to [agree to a stipulated-consequence-on-breach term] ... gives flexibility to the process of negotiation by enabling the promisor to give an assurance of performance, while limiting liability for consequential damages and thereby making the cost of breach predictable"); Scottish Law Commission, Review of Contract Law: Discussion Paper on Penalty Clauses 6 (No. 162)(November 2016)("The advantage of [stipulated-consequence-on-breach-terms] for the contracting parties are the facilitation of contingency planning, the avoidance of disputes and litigation and the consequent reduction of uncertainty about the outcomes of breach") & E. Farnsworth, Contracts 811 (4th ed. 2004) ("For the party in breach, it may have the effect of limiting damages to the sum stipulated").

[139] *Mortgage Makers Inc. v. McKeen*, 2009 NBCA 61, ¶18; 312 D.L.R. 4th 82, 92; *Craig and Son v. M'Beath,* 1 M. 1016, 1019 (Scot. Ct. Sess. 1863) per Inglis, L.J.-Clerk; S. Waddams, The Law of Contracts 319-20 (7th ed. 2017); J. McCamus, The Law of Contracts 897 (2005) & E. Farnsworth, Contracts 811 (4th ed. 2004).

[199] While freedom of contract is a bedrock community value, it is not the only ideal our society cherishes and protects.[140]

[200] Some contract terms may promote objectives that are contrary to other important community interests of equal or transcendent importance[141] and so objectionable that courts will refuse to give effect to them. A court of justice must not be the vehicle to promote injustice.[142]

[201] The law will not enforce contracts that advance the interests of criminals[143] or other anti-social actors who blatantly disregard the interests of others with whom they have a contractual relationship.[144]

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[140] *Shafron v. KRG Insurance Brokers (Western) Inc.*, 2009 SCC 6, ¶16; [2009] 1 S.C.R. 157, 166 ("Restrictive covenants give rise to a tension in the common law between the concept of freedom to contract and public policy considerations against restraint of trade") *& Sternaman v. Metropolitan Life Insurance Co.*, 62 N.E. 763, 764 (N.Y. Ct. App. 1902)("The power to contract is not unlimited. While as a general rule there is the utmost freedom of action in this regard, some restrictions are placed upon the right by legislation, by public policy and by the nature of things. Parties cannot make a binding contract in violation of law or of public policy").

[141] *Tercon Contractors Ltd. v. British Columbia*, 2010 SCC 4, ¶117; [2010] 1 S.C.R. 69, 121 ("freedom of contract will often, but not always, trump other societal values. The residual power of a court to decline enforcement exists but, in the interest of certainty and stability of contractual relations, it will rarely be exercised") *& Re Millar Estate*, [1938] S.C.R. 1, 4 per Duff, C.J. ("It is the duty of the courts to give effect to contracts ... according to the settled rules and principles of law ...; but there are cases in which rules of law cannot have their normal operation because the law itself recognizes some paramount consideration of public policy which over-rides the interest and what otherwise would be the rights and powers of the individual").

[142] J. Côté, An Introduction to the Law of Contract 107 (1971) ("no rational system of law could enforce contracts which call for cheating or the commission of crimes or other serious infractions of the rules of that very legal system") & *Bank of the United States v. Owens*, 27 U.S. 527, 538-39 (1829) ("no court of justice can ... be ... the handmaid of iniquity. Courts are instituted to carry into effect the laws of a country, how can they then become auxiliary to the consummation of violations of law?").

[143] Suppose that C promises A and B that he will drive the getaway car in a bank robbery A and B plan to perpetrate on a designated date in return for payment of a $25,000 fee. If C subsequently informs A and B a week before the planned bank heist that he will not be available to drive the getaway car and A and B have to pay D $30,000 to provide this service, a court will not enforce the bargain between A and B and C. A court will not order C to pay A and B $5000 in damages. The law recognizes that criminal activity is inimical to the welfare of the community and will do nothing to promote it. *Printing and Numerical Registering Co. v. Sampson*, L.R. 19 Eq. 462, 465 (Ch. 1875)("there is no doubt public policy may say that a contract to commit a crime, or a contract to give a reward to another to commit a crime, is necessarily void"); S. Waddams, The Law of Contracts 389 (7th ed. 2017) ("Even though an agreement does not actually require... the commission of an illegal act, it may be struck down if it tends to facilitate an illegality"); G. Fridman, The Law of Contract in Canada 338 (6th ed. 2011)("A contract for an illegal purpose, *i.e.,* a purpose regarded by the law as improper, though it conforms to all other requirements of a valid transaction, will... be void") & A. Swan & J. Adamski, Canadian Contract Law 985 (3d ed. 2012) ("Canadian courts have an inherent power to prevent an abuse of their process and may refuse to give effect to contracts that are illegal"). Enforcement of this bank-robbery term would adversely affect the interests of others besides the contracting parties. *Tercon Contractors Ltd. v. British Columbia,* 2010 SCC 4, ¶120; [2010] 1 S.C.R. 69, 122 per Binnie, J. ("Conduct approaching serious criminality or egregious fraud are ... examples of well-accepted and 'substantially incontestable' considerations of public policy that may override the countervailing public policy that favours freedom of contract"). See also *Irwin v.*

[202] Vice-Chancellor Stine of the Delaware Chancery Court refused to enforce a contractual term that rewarded fraudsters:[145]

> The public policy against fraud is a strong and venerable one that is largely founded on the societal consensus that lying is wrong. Not only that, it is difficult to identify an economically-sound rationale for permitting a seller to deny the remedy of rescission to a buyer when the seller is proven to have induced the contract's formation or closing by lying about a contractually-represented fact.
>
> For these reasons, when a seller intentionally misrepresents a fact embodied in a contract – that is when a seller lies – public policy will not permit a contractual provision to limit the remedy of the buyer to a capped damage claim. Rather, the buyer is free to press a claim for rescission or for full compensatory damages. By this balance, I attempt to give fair and efficient recognition to the competing public policies served by contractual freedom and by the law of fraud.

[203] The Delware Chancery Court understandably concluded that lying is harmful in commerce and other spheres and that it ought not to receive judicial approbation.

[204] Sometimes courts refuse to enforce a term that is inimical to fundamental economic values of the community.[146]

[205] Most employers will be unable to enforce a noncompetition covenant that is part of an employment agreement and is not an integral component of a sale of business agreement.[147]

Williar, 110 U.S. 499, 510 (1884)("In England, it is held that the contracts, although wagers, were not void at common law, ... while generally, in this country, all wagering contracts are held to be illegal and void as against public policy").

[144] *Plas-Tex Canada Ltd. v. Dow Chemical of Canada Ltd.*, 2004 ABCA 309, ¶49; 245 D.L.R. 4th 650, 665 ("Alberta Courts have generally held that contracts should be enforced regardless of the stringency of their terms limiting liability because parties require certainty that negotiated provisions in a contract will be legally enforceable... . However, this principle is subject to an important caveat: the court will intervene when the party desiring to enforce a liability limiting clause has engaged in unconscionable conduct").

[145] *ABRY Partners v. F&W Acquisitions LLC*, 891 A. 2d 1032, 1035-36 (2006).

[146] E.g., *Shafron v. KRG Insurance Brokers (Western) Inc.*, 2009 SCC 6, ¶16; [2009] 1 S.C.R. 157, 166 ("At common law, restraints of trade are contrary to public policy because they interfere with individual liberty of action and because the exercise of trade should be encouraged and should be free"); *Elsley v. J.G. Collins Insurance Agencies Ltd.*, [1978] 2 S.C.R. 916, 923 ("There is an important public interest in discouraging restraints on trade, and maintaining free and open competition unencumbered by the fetters of restrictive covenants") *& Nordenfelt v. Maxim Nordenfelt Guns and Ammunition Co.*, [1894] A.C. 535, 592 (H.L.) per Lord Watson ("the general policy of the law is opposed to all restraints upon liberty of individual action which are injurious to the interests of the State or community").

[147] *Elsley v. J.G. Collins Insurance Agencies Ltd.*, [1978] 2 S.C.R. 916, 925 ("In a conventional employer/employee situation [the court will enforce a nonsolicitation covenant, but not a noncompetition covenant]") & *T. Lucas & Co. v.*

[206] These examples[148] are exceptions to the general rule that a court will enforce a bargain between parties with capacity to contract. The reasons for these three special cases are clear and cogent. They constitute compelling reasons for abridging the freedom of contract principle.[149]

[207] A compelling case cannot be made for the penalty rule.

[208] Professor Waddams, one of Canada's leading academic contract lawyers, favours its destruction:[150]

> [T]here can be no doubt that in relieving against penalty clauses, the courts are limiting the freedom of contract.
>
> It appears that the underlying criterion of enforceability in this area is, and must eventually be recognized to be the fairness of the provision sought to be enforced. The courts, however, here as elsewhere, retreated from the recognition of so vague a test, and have resorted instead to a supposed distinction between penal clauses held "in terrorem" over the obligor (which are unenforceable) and "genuine pre-estimates" liquidating damages for breach (which are enforceable).
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> …
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> …It is not suggested that a rule of universal enforceability should be adopted – only that, first, a test of unfairness or unconscionability is the only workable and just test, and, secondly, that in applying the test, the considerations that weigh in favour of enforcement should not be underestimated.

[209] Party autonomy should not be abridged on account of public policy[151] in the absence of a compelling reason.[152]

Mitchell, [1974] 1 Ch. 129, 135 (C.A.)(the Court declared a noncompetition provision in an employment agreement unenforceable because a nonsolicitation agreement would have adequately protected the promisee's interests).

[148] See generally E. Farnsworth, Contracts 313-343 (4th ed. 2004).

[149] *Ringrow Pty. Ltd. v. BP Australia Pty. Ltd.*, [2005] HCA 71, ¶12; 224 C.L.R. 656, 663 ("Exceptions from ... freedom of contract require good reason to attract judicial intervention to set aside the bargains upon which parties of full capacity have agreed").

[150] S. Waddams, The Law of Contracts 313 & 320 (7th ed. 2017).

[151] See *Richardson v. Mellish*, 130 Eng. Rep. 294, 299 per Best, C.J. (Ex. 1824)("I am not much disposed to yield to arguments of public policy ... the courts of Westminster-hall ... have gone much further than they were warranted in going in questions of policy: ... courts of law look only at the particular case and have not the means of bringing before them all those considerations which ought to enter into the judgment of those who decide on questions of policy") & 303 per Burroughs, J. ("public policy ... is a very unruly horse, and when once you get astride it you never know where it will carry you. It may lead you from the sound law").

[210] A compelling reason exists if a court is asked to enforce an oppressive [153] stipulated-consequence-on-breach term, the standard *Elsley* adopted.

[211] An oppressive term in a commercial contract is one that is so manifestly grossly one-sided that its enforcement would bring the administration of justice into disrepute.

[212] Judges should not use the authority of their office to enforce stipulated-consequence-on-breach terms of this nature.

[213] This is a theme that can be traced to the extrajudicial writings of Justice Story of the United States Supreme Court[154] and the opinions of the Earl of Halsbury in *Clydebank Engineering and Shipbuilding Co. v. Castandea*[155] and the Privy Council in *Webster v. Bosanquet*.[156]

[214] This is a very onerous test, as it should be.[157] It will seldom be met.

[215] Parties to commercial contracts have the means to look after their own interests. The public knows this and there is no danger that their confidence in the ability of the courts to administer justice will be eroded if courts decline to enforce contract terms only if they are oppressive.

4. This Disposition Continues the Trend Established in the Previous Centuries

a. Canadian Jurisprudence

[216] The Supreme Court of Canada decided *Canadian General Electric Co. v. Canadian Rubber Co. of Montreal*[158] on December 29, 1915, roughly eighteen months after the House of

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[152] *Hunter Engineering Co. v. Syncrude Canada Ltd.*, [1989] 1 S.C.R. 426, 462 ("Only where the [limitation-of-liability term in the] contract is unconscionable, as might arise from situations of unequal bargaining power between the parties, should the courts interfere with agreements the parties have freely concluded.").

[153] According to Webster's Third New International Dictionary of the English Language Unabridged (2002), "oppressive" may mean "unjustly severe, rigorous or harsh: constituting oppression: < ~ legislation> < ~ taxes> <~ exactions>".

[154] 2 J. Story, Commentaries on Equity Jurisprudence as Administered in England and America 743 (4th ed. 1846).

[155] [1905] A.C. 6, 10 (H.L. 1904).

[156] [1912] A.C. 394, 398 (P.C.) (Ceylon).

[157] See Bildfell, "Exculpatory Clauses and Liquidated Damages Clauses: Two Sides of the Same Coin". 78 Sask. L. Rev. 347, 354 (2015)("courts are highly reluctant – and rightly so, in my opinion – to interfere with freedom of contract in cases involving exclusions").

[158] 52 S.C.R. 349.

Lords released its well-known *Dunlop Pneumatic Tyre Co. v. New Garage and Motor Co.*[159] judgment.

[217] At issue in the Canadian case was the enforceability of a stipulated-consequence-on-breach term that reduced the $33,000 purchase price of electrical equipment that Canadian General Electric had agreed to manufacture for the Canadian Rubber Company.

[218] Canadian General Electric commenced an action seeking judgment for the sum Canadian Rubber withheld under the stipulated-consequence-on-breach term.

[219] Both the trial and the appeal courts upheld the defendant's position.[160] The stipulated-consequence-on-breach term was enforceable.

[220] So did the Supreme Court. Any other result would have been indefensible. On what basis could a court have declared of no force an essential term in a commercial agreement between two very substantial corporations with access to first-class legal talent?

[221] Chief Justice Fitzpatrick, after noting that the "contract ... relates to a purely business transaction"[161] and quoting Sir George Jessel's famous admonition to judges about meddling in business contracts,[162] said this:[163]

> In the contract in the present case there is a clear agreement for the deduction from the contract price for delay in delivery; there is no objection to such an agreement being entered into and no reason why effect should not be given to the agreement by the courts. …
>
> …
>
> … [T]he amount fixed is not alleged to have been an *extravagant* one; and the provision was in every respect a reasonable and proper one which both parties may perfectly well be supposed to have intended.

[222] Justice Davies thought it important to note that the stipulated-consequence-on-breach term was not "unconscionable".[164] So did Justice Anglin. "[I]t cannot be said that the sum agreed upon is extravagant or unconscionable".[165]

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[159] [1915] A.C. 79 (H.L. 1914).

[160] 52 S.C.R. 349, 354.

[161] Id. 351.

[162] Id. 353.

[163] Id. (emphasis added).

[223] Other Canadian courts have followed the *Dunlop Pneumatic Tyre* philosophy and accorded commercial contracting parties great latitude in ordering their own affairs.[166] They undoubtedly appreciated that there is no sound reason to characterize stipulated-consequence-on-breach terms as unenforceable penalties when the businesses that must live with the contracts regarded the terms as a central part of the transactions.

b. United Kingdom Jurisprudence

[224] Before reviewing the United Kingdom's post-1800 contribution to the law on this topic, it is helpful to record the significant events that preceded it.

i. The Ancient Equitable Origins of the Penalty Rule[167]

[225] By no later than the fourteenth century there existed a well-established commercial practice designed to avoid the canonical prohibition against usury[168] and at the same time provide the lender with a satisfactory form of security. This was the defeasible penal bond.[169]

[226] A penal bond had two principal characteristics.[170] The first obliged the borrower to pay the lender an amount larger than the amount that the lender advanced to the borrower and the borrower promised to repay in accordance with an agreed upon time schedule – the primary obligation. The second benchmark relieved the borrower of the obligation to pay this larger amount if the borrower

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[164] Id. 356.

[165] Id. 371.

[166] E.g., *Reimer v. Rosen*, 45 D.L.R. 1 (Man. C.A. 1919) & *Infinite Maintenance Systems Ltd. v. ORC Management Ltd.*, 139 O.A.C. 331 (C.A. 2001).

[167] See T. Sedgwick, A Treatise on the Measure of Damages, or, an Inquiry into the Principles Which Govern the Amount of Pecuniary Compensation Awarded by Courts of Justice 412-16 (3d rev. ed. 1858); Loyd, "Penalties and Forfeitures", 29 Harv. L. Rev. 117 (1915); Simpson, "The Penal Bond with Conditional Defeasance", 82 Law Q. Rev. 392 (1966); 5 W. Holdsworth, A History of English Law 330-32 (3d. ed. 1945) & Scott & Triantis, "Embedded Options and the Case Against Compensation in Contract Law", 104 Colum. L. Rev. 1428, 1440-42 (2004).

[168] The common law prohibited usury. *An Acte Against Usurye*, 37 Hen. 8, c. 9, s. 3 (1545) made it lawful.

[169] See also Biancalana, "Contractual Penalties in the King's Court 1260-1360", 64 Cambridge L.J. 212, 215 (2005) ("By 1348 the penal bond with conditional defeasance endorsed on the back of the bond had been invented") & Loyd, "Penalties and Forfeitures", 29 Harv. L. Rev. 117, 122 (1915)("the scrivener [avoided the word 'penalty']; the obligation will be for 'lawful money' and the conditions for the payment of a 'just sum' or 'full sum' ...; although court and counsel, long assured of the validity of the transaction, have not hesitated to call the instrument by its true name – a penal obligation").

[170] Loyd, "Penalties and Forfeitures", 29 Harv. L. Rev. 117, 121 (1915) & Simpson, "The Penal Bond with Conditional Defeasance", 82 Law Q. Rev. 392, 395 (1966) ("Suppose Hugo proposes to lend Robert £100. Robert will execute a bond in favour of Hugo for a larger sum, normally twice the sum lent, thus binding himself to pay Hugo £200 on a fixed day; the bond will be made subject to a condition of defeasance, which provides that if he pays £100 before the day the bond is to be void").

honoured his primary obligation and paid the lender the smaller amount in accordance with a separate promise to pay.

[227] The following passage provides an historical account of the larger forces at play when penal bonds were introduced into England: [171]

> So, when Britannia had grown sufficiently cosmopolitan to become a borrower, it was the mediaeval Italian banker who seems to have brought into common use in England the penal bond … .
>
> The rapid spread of this form of obligation is explained by the fact that it was well adopted to evade the canonical prohibition of interest on loans, regarded as usury and therefore unlawful for a Christian, and that by the time interest was made lawful it had become firmly established as a common form of conveyancing.
>
> …
>
> With medieval subtlety the careful conveyancer endeavors to avoid the perils of the defense of usury by unscrupulous debtors. A contingency is essential; the single bill under seal is… the most efficacious instrument of the day; so let the obligation be drawn for a round sum – say twice the amount of the loan – with a clause of defeasance… declaring the obligation void on payment of the loan on a particular day; then the condition or defeasance will be collateral to the bond… [C]ourt and counsel, long assured of the validity of the transaction, have not hesitated to call the instrument by its true name – a penal obligation.

[228] For centuries, courts ordered borrowers who failed to strictly comply with the defeasible term to pay the larger sum set out in the penal bond.[172] This outcome was consistent with other ancient legal practices. During this period courts "did not look with disfavour on the strict enforcement of forfeitures and interests in land for condition broken".[173]

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[171] Loyd, "Penalties and Forfeitures", 29 Harv. L. Rev. 117, 119 & 121-22 (1915).

[172] Id. 122 ("Contract and property law were swept along together, bound by ever tightening chains of precedent, in the development of doctrines, harsh and narrow perhaps, but capable of being understood and applied, a point not altogether to be despised in times of disorder and low credit. If the law bore heavily upon the individual, at least there was a known law, the certainty of which had become the 'safety of all'") & Simpson, "The Penal Bond with Conditional Defeasance", 82 Law Q. Rev. 392, 411 (1966) ("The law governing bonds is tough law, inspired by the general philosophy that it is not the business of the courts to remake private contracts; having made their bed the contracting parties must lie in it").

[173] Loyd, "Penalties and Forfeitures", 29 Harv. L. Rev. 117, 122 (1915).

[229] Over time equity smoothed these sharp common law edges.[174] Chancery gave attention to other interests besides the importance of contract enforcement. Equity was not insensitive to the plight of the defaulters and the disparity between the nature of the breach and the severity of the consequences attached to the breach for the defaulter.

[230] After 1660 equity introduced new regimes to soften the lot of defaulting mortgagors and penal bond obligors.[175] Equity invented a mortgagor's right of redemption and a defence for a penal bond obligor – payment of the amount due had the defeasance term been activated, along with interest and costs.[176] Chancery judges decided that these new solutions were fairer to the defaulting mortgagor[177] and penal bond obligor.[178] The interests of the mortgagee and obligee were not ignored. The new protocol ensured that the mortgagee and obligee were made whole. Equitable doctrines required the mortgagor and obligor to pay mortgagee and obligees the sum that they would have received had the primary obligations been honored and to cover mortgagee's and obligee's legal costs.

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[174] T. Sedgwick, A Treatise on the Measure of Damages, or, an Inquiry into the Principles Which Govern the Amount of Pecuniary Compensation Awarded by Courts of Justice 413 (3d rev. ed. 1858)("this severe rule of the common law was only mitigated by the practice of the courts of chancery, which interposed, and would not allow a man to take more than in conscience he ought"). See generally C. Rossiter, Penalties and Forfeitures: Judicial Review of Contractual Penalties and Relief Against Forfeiture of Property Interests (1992) & E. Farnsworth, Contracts 812 (4th ed. 2004).

[175] *Wyllie v. Wilkes*, 99 Eng. Rep. 331, 333 (K.B. 1780) ("Sir Thomas More ... in the reign of Henry VIII ... summoned [the common law judges] to a conference concerning the granting of relief at law, after the forfeiture of bonds upon payment of principal, interest and costs; and when they said they could not relieve against the penalty, he swore... he would grant an injunction") & *Friend v. Burgh*, 23 Eng. Rep. 238 (Ch. 1679)(the Court ordered the obligee under a penal bond to refund to the obligor an amount equal to the difference between the penalty less the principal, interest and costs). See Loyd, "Penalties and Forfeitures", 29 Harv. L. Rev. 117, 125 (1915)("Certainly by the time of the Restoration it could be said: 'it is a common case to give relief against the penalty of such bonds to perform covenants ... and to send it to a trial at law to ascertain the damages in a *quantum damnificatus*'") & Simpson, "The Penal Bond with Conditional Defeasance", 82 Law Q. Rev. 392, 417 (1966) ("After the Restoration it rapidly became established that the Chancery would grant relief against penalties due on money bonds on the payment of principal, interest and costs, and against penalties due for failure to perform covenants on payment of costs and damages").

[176] *Cavendish Square Holding BV v. Talal EI Makdessi*, [2015] UKSC 67, ¶4; [2016] A.C. 1172, 1192.

[177] 6 W. Holdsworth, A History of English Law 663-65 (2d ed. 1937)("The result had been to make the mortgagor's equity to redeem a right of property. He had an equitable estate in the land; and subject to the legal rights of the mortgagee, was, in equity, regarded as its owner. It was during [the seventeenth century] that the consequences of this new right of the mortgagor began to be worked out").

[178] 5 W. Holdsworth, A History of English Law 330-31 (3d. ed. 1945) ("the type of mortgage [that became prevalent in the latter half of the fifteenth century] gave the mortgagee the fee simple ... with a proviso that, if the debt was paid by a fixed-date, the land should be reconveyed. The strictness with which this proviso was construed made a recourse to equity very necessary").

[231] Two enactments codified the new penalty bond protocol.[179] As a result, common law courts alone heard penal bond cases; an obligor did not have to invoke the jurisdiction of Chancery to relieve against the harshness of the common law.[180] Chancery no longer had a platform from which it could influence the traits of the penalty law.

[232] The common law reshaped the law dealing with penalties when resolving the enforceability of a stipulated-consequence-on-breach term.[181] Lord Neuberger and Lord Sumption, in *Cavendish Square Holding BV v. EI Makdessi*,[182] describe its contribution:

> With the gradual decline of the use of penal defeasible bonds, the common law on penalties was developed almost entirely in the context of damages clauses – ie clauses which provided for payment of a specified sum in place of common law damages. … *If the agreed sum was a penalty, it was treated as unenforceable*. Starting with the decisions in *Astley v Weldon*… in 1801 and *Kemble v Farren*, … [in 1829], the common law courts introduced the now familiar distinction between a provision for the payment of a sum representing a genuine pre-estimate of damages and a penalty clause in which the sum was out of all proportion to any damages liable to be suffered. …
>
> The distinction between a clause providing for a genuine pre-estimate of damages and a penalty clause has remained fundamental to the modern law, as it is currently understood. The question whether a damages clause is a penalty falls to be decided as a matter of construction, therefore as at the time that it is agreed. … It is a species of agreement which the common law considers to be by its nature contrary to the policy of the law.

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[179] *An Act for the better preventing frivolous and vexatious Suit*, 8 & 9 Will. 3, c. 11, s. 8 (1696) & *An Act for the Amendment of the Law and better Advancement of Justice*, 4 & 5 Anne, c. 16, ss. 12 & 13 (1705). See T. Sedgwick, A Treatise on the Measure of Damages, or, an Inquiry into the Principles Which Govern the Amount of Pecuniary Compensation Awarded by Courts of Justice 414 (3d rev. ed. 1858)("this discretionary power was confirmed by statutory regulation, which provided that in actions on bonds with penalties, the defendant might bring in the principal debt, interest and costs, and be discharged").

[180] *Smith v. Bond*, 131 Eng. Rep. 853, 855 (Common Pleas 1833) ("The great object of the statute was to take away the necessity of applying for relief to a court of equity").

[181] See *Law v. Local Board*, [1892] 1 Q.B. 127, 134 per Kay, L.J. (C.A. 1891)("it became a settled rule in equity that, where a sum was agreed to be paid in respect of the performance or non-performance of a collateral matter, the actual damage for which could be estimated, the penalty would be cut down, and only the actual damages sustained would be allowed. It was for that very reason that the words "as and for liquidated damages" and similar words, came to be inserted in contracts. The contracting parties meant by the use of them to exclude this rule of equity ... . It was to avoid the interference of Courts of Equity that such words were introduced. But then the Courts of Law interfered, and, as it seems to me, went further than Courts of Equity had done originally").

[182] [2015] UKSC 67, ¶¶8 & 9; [2016] A.C. 1172, 1194 (emphasis added).

[233] The common law deprived the parties of the freedom to construct remedial provisions that served their needs.

[234] Not all the judges agreed that the diminution of the scope of freedom of contract was a positive development.

[235] As noted above, Lord Eldon, Lord Parmoor, Lord Neuberger, Lord Sumption, Lord Carnwath and Sir George Jessel recorded their opposition to the penalty rule.

ii. English Common Law Judges Refined the Penalty Rule

[236] In a 1907 judgment Justice Peckham of the United States Supreme Court offered this historical perspective:[183]

> The Courts at one time seemed to be quite strong in their views and would scarcely admit that there ever was a valid contract providing for liquidated damages. Their tendency was to construe the language as a penalty, so that nothing but the actual damages sustained by the party aggrieved could be recovered. Subsequently the courts became more tolerant of such provisions, and have now become strongly inclined to allow parties to make their own contracts, and to carry out their intentions, even when it would result in the recovery of an amount stated as liquidated damages, upon proof of the violation of the contract, and without proof of the damages actually sustained.

[237] I agree.

iii. The Penalty Rule in the Twenty-First Century

[238] In *Cavendish Square Holding BV v. El Makdessi*,[184] a 2015 judgment, the United Kingdom Supreme Court revisited the merits of the penalty rule. It rejected the appellant's argument to abandon the penalty rule completely, or at least in commercial cases. [185] But Lord Neuberger, Lord Sumption and Lord Carnwath acknowledged that a modern court would not assess the

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[183] *United States v. Bethlehem Steel Co.*, 205 U.S. 105, 119 (1907). See T. Sedgwick, A Treatise on the Measure of Damages, or, an Inquiry into the Principles Which Govern the Amount of Pecuniary Compensation Awarded by Courts of Justice 419 (1858)("the courts, especially in this country, have generally shown a marked desire to lean towards that construction which excludes the idea of liquidated damages, and permits the party to recover only the damages which he has actually sustained").

[184] [2015] UKSC 67; [2016] A.C. 1172.

[185] Id. at ¶162 (Lord Neuberger, Lord Sumption & Lord Carnwath), ¶168 (Lord Mance & Lord Toulson) & ¶261 (Lord Hodge); [2016] A.C. at 1251, 1253 & 1279.

enforceability of a stipulated-consequence-on-breach term using the same standard that courts constructed "three centuries ago".[186]

[239] I will review three of the five speeches delivered by the Supreme Court justices. Lord Neuberger and Lord Sumption gave an extensive joint opinion with which Lord Carnwath agreed. Lord Mance and Lord Hodge each wrote thorough separate judgments. Lord Clark and Lord Toulson gave short speeches adopting portions of their colleagues' views.

[240] Lord Neuberger and Lord Sumption were troubled by the assumption underlying the classic penalty rule that the concept of penalty and preestimate of damages were mutually exclusive concepts and that characterizing a term as a deterrent provided assistance in assessing the enforceability of a stipulated-consequence-on-breach term.[187] They were satisfied that these were not helpful analytical tools; that they provided useless information.[188] They concluded that the key query was this:[189] "[w]hether the means by which the contracting party's conduct is to be influenced are 'unconscionable' or (which will usually amount to the same thing) 'extravagant' by reference to some norm".

[241] And what are the benchmarks of these characteristics? Lord Neuberger and Lord Sumption provide this answer:[190] "The true test is whether the impugned provision ... imposes a detriment on the contract-breaker out of all proportion to any legitimate interest of the innocent party in the enforcement of the primary obligation".

[242] Lord Mance understood the penalty rule to make unenforceable terms that "attach exorbitant or unconscionable consequences following from breach".[191]

[243] Lord Hodge held that a stipulated-consequence-on-breach term is unenforceable if the

> consequence of a breach of contract is exorbitant or unconscionable when regard is had to the innocent party's interest in the performance of the contract. Where the test is to be applied to a clause fixing the level of damages to be paid on breach, an extravagant disproportion between the stipulated sum and the highest level of damages that could possibly arise from the breach would amount to a penalty, and thus be unenforceable. In other circumstances the contractual provision that applies on breach is measured against the interest of the innocent party which is protected

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[186] Id. at ¶36; [2016] A.C. at 1206.

[187] [2015] UKSC 67, ¶31; [2016] A.C. 1172, 1204.

[188] Id.

[189] Id.

[190] Id. at ¶32; [2016] A.C. at 1204.

[191] Id. at ¶¶162, 181 & 185; [2016] A.C. at 1251, 1257 & 1258.

> by the contract and the court asks whether the remedy is exorbitant or unconscionable.[192]

[244] It is fair to say that the Supreme Court all but abandoned the penalty rule. The only similarity between the modern penalty rule and the classic penalty rule is its name. Lord Hodge's speech amply illustrates this claim:[193] "[T]he rule against penalties [does not prevent] parties from reaching sensible arrangements to fix the consequences of a breach of contract and thus avoid expensive disputes. The criterion of exorbitance or unconscionableness should prevent the enforcement of only egregious contractual provisions".

iv. The Penalty Rule in the Twentieth Century

[245] The House of Lords and the Privy Council issued four important commercial judgments on the enforceability of stipulated-consequence-on-breach terms in the twentieth century that merit careful consideration.

[246] The House of Lords released *Dunlop Pneumatic Tyre Co. v. New Garage and Motor Co.*[194] and *Clydebank Engineering and Shipbuilding Co. v. Castaneda*[195] within ten years of each other early in the twentieth century. The Privy Council issued *Webster v. Bosanquet*[196] in 1912 and *Philips Hong Kong Ltd. v. Hong Kong*[197] in 1993.

[247] These four appeals upheld the enforceability of stipulated-consequence-on-breach terms. The law lords, in effect, declared the primacy of freedom of contract principles in commercial contracts between parties that had the resources to retain legal counsel.

- ***Dunlop Pneumatic Tyre Co. v. New Garage and Motor Co.***

[248] A 1914 judgment of the House of Lords, *Dunlop Pneumatic Tyre Co. v. New Garage and Motor Co.*[198], is one of the best-known Commonwealth penalty cases[199]. It has been cited with approval in Canada,[200] Australia,[201] New Zealand[202] and Hong Kong.[203]

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[192] Id. at ¶255; [2016] A.C. at 1278.

[193] Id. at ¶266; [2016] A.C. at 1280.

[194] [1915] A.C. 79 (H.L. 1914). English courts continued to rely on *Dunlop Pneumatic Tyre* in the twenty-first century. E.g., *Murray v. Leisureplay Plc*, [2005] EWCA Civ 963, ¶34 per Arden, L.J. ("The classic statement of the law on penalties [is] by Lord Dunedin in the *Dunlop* case") & ¶44 ("The judgments in the *Cine* case show the continued usefulness of the authoritative guidance given by Lord Dunedin in ... *Dunlop*").

[195] [1905] A.C. 6 (H.L. 1904).

[196] [1912] A.C. 394 (P.C.)(Ceylon).

[197] [1993] UKPC 3a; [1993] 1 H.K.L.R. 269.

[198] [1915] A.C. 79 (H.L. 1914).

[249] Dunlop manufactured tires and related products. It distributed them through a network of retailers who agreed not to sell Dunlop products to the public at a price below that set out in a schedule.[204] Retailers who breached the price-maintenance agreement "agree[d] to pay ... Dunlop ... the sum of 5£ for each and every tyre, cover or tube sold or offered [for sale] in breach of this agreement, as and by way of liquidated damages and not as a penalty ... ."[205]

[250] New Garage and Motor Co., the retailer, breached the price-maintenance provision.[206] Dunlop secured an injunction. The Master ordered the defendant to pay 250£ as damages, applying the stipulated-payment-on-breach term.[207] The Court of Appeal reversed. It held that the term was a penalty[208] and allowed only nominal damages.

[251] The House of Lords disagreed with the Court of Appeal.

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[199] *Mortgage Makers, Inc. v. McKeen*, 2009 NBCA 61, ¶18; 312 D.L.R. 4th 82, 92 ("Inevitably, everyone turns to the reasons of Lord Dunedin in *Dunlop Pneumatic Tyre Ltd. v. New Garage and Motor Co*."); *Prince Albert Credit Union Ltd. v. Johnson*, 131 D.L.R. 3d 710, 713 (Sask. Q.B. 1982)("the judgment in *Dunlop Pneumatic Tyre Co. v. New Garage and Motor Car Co. Ltd*. ... still stands as the definitive statement of the law"); *Jeancharm Ltd. v Barnet Football Club*, 2003 EWCA Civ. 58, ¶9 per Jacob, J. ("The classic statement of the law is to be found in the speech of Lord Dunedin in *Dunlop v. New Garage*"); S. Waddams, The Law of Contracts 314 (7th ed. 2017)("[*Dunlop Tyre* is] generally cited as the leading case"); A. Swan & J. Adamski, Canadian Contract Law 949 (3d ed. 2012)("The principles of the common law developed for dealing with penalties are generally based on the judgment of the House of Lords in *Dunlop Tyre Co. v. New Garage and Motor Co. Ltd.*"); Bildfell, "Exculpatory Clauses and Liquidated Damages Clauses: Two Sides of the Same Coin", 78 Sask. L. Rev. 347, 355 (2015) ("*Dunlop Pneumatic Tyre* ... is a leading authority on the penalty doctrine") & Veel, "Penalty Clauses in Canadian Contract Law", 66 U. Toronto L. Rev. 229, 233 (2008)("*Dunlop Pneumatic Tyre* ... represents the traditional starting point for Canadian courts' analyses of penalty clauses").

[200] E.g., *Waugh v. Pioneer Logging Co.*, [1949] S.C.R. 299; *Canadian General Electric Co. v. Canadian Rubber Co. of Montreal*, 52 S.C.R. 349, 352 (1915); *Newman, Hill, Duncan & Lacoursiere v. Murray*, [1987] B.C.J. No. 2326 (C.A.); *Shatilla v. Feinstein*, [1923] 3 D.L.R. 1035 (Sask. C.A.); *Reimer v. Rosen*, [1919] 1 W.W.R. 429 (Man. C.A.); *Canadian Acceptance Corp. v. Regent Park Butcher Shop Ltd.*, 3 D.L.R. 3d 304, (Man. C.A. 1969) & *Infinite Maintenance Systems Ltd. v. ORC Management Ltd.*, 139 O.A.C. 331 (C.A. 2001).

[201] E.g., *Paciocco v. Australia and New Zealand Banking Group Ltd.*, [2016] HCA 28; 258 C.L.R. 525; *Ringrow Pty. Ltd. v. BP Australia Pty. Ltd*., [2005] HCA 71, ¶ 12; 224 C.L.R. 656, 663.

[202] E.g., *T.K. (Hong Kong) Ltd. v. Diamond Milk Formulas Ltd.*, [2016] NZHC 2642, ¶47.

[203] E.g., *Polyset Ltd. v. Panhandat Ltd.*, [2002] HKCFA 15, ¶73; *Evergreen (FIC) Ltd. v. Golden Cup Industries Ltd.*, 2016 WL 1664247, ¶30 (H.K.C.F.I.); *First Commercial Bank v. "Liberty Container"*, [2004] HKCFI 1013, ¶7 & *Patrick Ho & Assoc. v. Fook Kong Trading Co.*, [1988] HKCFI 77, ¶29 (High Ct.).

[204] [1915] A.C. 79, 80 (H.L. 1914).

[205] Id. 81.

[206] Id.

[207] Id. 82.

[208] Id.

[252] Four law lords heard the appeal and delivered speeches that were sufficiently varied that it is difficult to identify much common ground.

[253] Lord Dunedin made several points. In assessing the significance of these, one must note that none of his three colleagues stated that they agreed with him.[209]

[254] First, "[t]he Court must find out whether the payment stipulated is in truth a penalty or liquidated damages".[210] This required an adjudicator to search for the most important or leading feature or aspect of the term. [211] If the leading feature of a term is its penalty aspect, the term is unenforceable. If it is in truth a liquidated damages term, it is enforceable.

[255] Second, "[t]he essence of a penalty is a payment of money stipulated as in terrorem of the offending party; the essence of liquidated damages is a genuine covenanted pre-estimate of damage".[212] The utility of the *"*in terrorem*"* concept[213] is hard to understand. In any event, it is not obvious to me why the law should disapprove of a term that serves to deter a party from breaching a contractual promise.[214]

[256] Third, in order to characterize the stipulated-consequence-on-breach term a court must study "the terms and inherent circumstances of each particular contract, judged of as at the time of the making of the contract, not as at the time of the breach".[215]

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[209] *Cavendish Square Holding BV v. El Makdessi*, [2015] UKSC 67, ¶22; [2016] A.C. 1172, 1199 per Lords Neuberger and Sumption ("none of the other three Law Lords expressly agreed with Lord Dunedin's reasoning").

[210] [1915] A.C. 79, 86 (H.L. 1914). See 5 S. Williston, A Treatise on the Law of Contracts 668 (3d ed. W. Jaeger 1961)("Liquidated damage ... is a sum fixed as an estimate made by the parties at the time when the contract is entered into, of the extent of the injury which a breach of the contract will cause").

[211] See *Lordsvale Finance Plc v. Bank of Zambia*, [1996] Q.B. 752, 762 ("whether a provision is to be treated as a penalty is a matter of construction to be resolved by asking whether at the time the contract was entered into the predominant contractual function of the provision was to deter a party from breaking the contract or to compensate the innocent party for breach").

[212] [1915] A.C. 79, 86 (H.L. 1914).

[213] Websters Third New International Dictionary of the English Language Unabridged 1182 (2002)("by way of threat or intimidation < if, after becoming aware of the other party's offence, the injured party could hold it in terrorem over his or her head >") & Black's Law Dictionary (10th ed. 2014 B. Garner ed. in chief) ["Latin 'in order to frighten'] (17c) (By way of threat; as a warning <the demand letter was sent *in terrorem*; the client has no intention of actually suing>"). See *Campbell Discount Co. v. Bridge*, [1962] A.C. 600, 622 (H.L.)("I do not find that that description adds anything of substance to the idea conveyed by the word 'penalty' itself, and it obscures the fact that penalties may quite readily be undertaken by parties who are not in the least terrorised by the prospect of having to pay them").

[214] *Mortgage Makers Inc. v. McKeen*, 2009 NBCA 61, ¶39; 312 D.L.R. 4th 82, 100 ("there is nothing inherently wrong in the parties agreeing to a penalty clause inserted for *in terrorem* purposes").

[215] [1915] A.C. 79, 87 (H.L. 1914).

[257] Fourth, there are three criteria that are either conclusive or presumptive indicia of a penalty. A stipulated-consequence-on-breach term must be adjudged to be a penalty "if the sum stipulated for is extravagant and unconscionable in amount in comparison with the greatest loss that could conceivably be proved to have followed from the breach".[216] The same result follows if the stipulated sum payable is triggered only by a failure to pay a sum of money and the stipulated sum is "greater than the sum which ought to have been paid".[217] A term that obliges a promisor to pay the same sum regardless of whether the contract breach imposes "serious [or] trifling damage"[218] is presumed to be a penalty. Lord Dunedin also believed that a term may be classified as liquidated damages if "the consequences of the breach are such as to make precise pre-estimation almost an impossibility".[219]

[258] This last observation accounts for Lord Dunedin's conclusion that the contested term was a pre-estimate of liquidated damage:[220]

> [T]he damage apprehended by … [Dunlop] owing to the breaking of the agreement was an indirect and not a direct damage. So long as [Dunlop] … got their price from the respondents for each article sold, it could not matter to them directly what the respondents did with it. Indirectly, it did. … But though damage as a whole from … [underselling] would be certain, yet damage from any one sale would be impossible to forecast. It is just, therefore, one of those cases where it seems quite reasonable for parties to contract that they should estimate that damage at a certain figure, and provided that figure is not extravagant there would seem no reason to suspect that it is not truly a bargain to assess damages, but rather a penalty to be held in terrorem.

[259] Dunlop's evidence proved that cost-cutting by some retailers in its retail distribution network may cause loyal retailers who honored their price-maintenance commitments to Dunlop and sold at the stipulated prices to cease to do business with Dunlop and start to sell competitor's

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[216] Id. This concept is frequently mentioned. E.g., *Lord Elphinstone v. Monkland Iron and Coal Co.*, 11 A.C. 332, 345 (H.L. 1886)("There is nothing whatever to shew that the compensation is exorbitant or extravagant"); *Forrest & Barr v. Henderson, Colbourne & Co.*, 8 M. 187, 193 (Scot. Ct. Sess. 1869)("equity will interfere to prevent the claim being maintained to an exorbitant or unconscionable amount"); *Charterhouse Leasing Corp. v. Sanmac Holdings Ltd.*, 57 W.W.R. 615, 621 (Alta. Sup. Ct. 1966)(the Court concluded that an accelerated lease obligation was extravagant and unconscionable) & *Cracknell v. Jeffrey*, 2001 ABPC 11, ¶16; 284 A.R. 372, 376 ("Payment of $5.00 per day [as a late payment fee] which results in a return over the course of 30 days of 46% on $325.00 in arrears ... is extravagant and unconscionable in comparison with the greatest loss that could possibly flow from the tenant's breach").

[217] [1915] A.C. 79, 87 (H.L. 1914).

[218] Id.

[219] Id. 87-88. The complete sentence reads as follows: "It is no obstacle to the sum stipulated being a genuine pre-estimate of damages, that the consequences of the breach are such as to make a precise pre-estimation almost an impossibility". How can a term be a pre-estimate of damages if it is impossible to pre-estimate damages?

[220] Id. 88.

products.[221] This contraction of the number of retail outlets selling Dunlop products would be inimical to the welfare of Dunlop's business.[222]

[260] Lord Atkinson held that the price-maintenance agreement was an enforceable pre-estimate of liquidated damages.[223] He did so for two principal reasons. First, Dunlop insisted that retailers adhere to a maintenance-price term to protect the integrity of Dunlop's distribution network. It made good business sense to adopt this strategy. Lord Atkinson concluded that Dunlop's "interest was … [commensurate] with the sum agreed to be paid".[224] This certainly provides a commercial explanation for Dunlop's bargaining position. Second, the stipulated-consequence-on-breach term was not "unreasonable, unconscionable, or extravagant".[225] This last criterion gives Lord Dunedin and Lord Atkinson some common ground.

[261] Lord Parker was convinced that any breach of the price-maintenance agreement harmed Dunlop's product-distribution system.[226] He saw "nothing to justify the Court in refusing to give effect to this bargain".[227] There was a sound business reason to justify the impugned term.

[262] Lord Parmoor, unlike his colleagues, started from this perspective:[228] "[W]hen competent parties by free contract are purporting to agree a sum as liquidated damages there is no reason for refusing a wide limit of discretion". A contraction of the freedom of contract principle is only justified if there is "an extravagant disproportion between the agreed sum and the amount of any damage capable of pre-estimate".[229] The disproportionality would have to be of such a magnitude as to be unconscionable, extortionate or extravagant.[230] Such disproportionality was not in evidence here.[231]

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[221] Id. 91.

[222] Id.

[223] Id. 96.

[224] Id. 92.

[225] Id. 97.

[226] Id. 99.

[227] Id.

[228] Id. 101.

[229] Id.

[230] Id.

[231] Id. 105.

[263] These speeches, with the exception of Lord Parker's, all emphasized the importance of the fact that the stipulated-consequence-on-breach term was not unconscionable, extravagant or extortionate.[232]

[264] *Dunlop Pneumatic Tyre Co.* reveals the law lords' sound understanding of Dunlop's business and the commercial realities that accounted for the price-maintenance agreement. The case's modern appeal is the ultimate disposition – enforce a commercial bargain that imposes a burden on a promisee if it is not unconscionable, extravagant or extortionate. The unspoken message is that freedom of contract must be respected in commercial transactions barring extraordinary circumstances.

- ***Clydebank Engineering and Shipbuilding Co. v. Castaneda***

[265] In *Clydebank Engineering and Shipbuilding Co. v. Castaneda*[233], a 1904 judgment, the House of Lords upheld a decision of Scotland's Second Division of the Court of Sessions ordering the shipbuilder to pay the Spanish government £500 per week for each torpedo-boat destroyer not delivered on time.

[266] The Earl of Halsbury, L.C. disposed of the appeal on a very narrow ground. He asked whether the stipulated-consequence-on-breach term was "unconscionable and extravagant" so that no court should enforce it.[234] The example he gave to illustrate this proposition reveals how unconscionability would be an extraordinary assessment:[235] "[I]f you agreed to build a house in a year, and agreed that if you did not build the house for 50£, you were to pay a million of money as a penalty, the extravagance of that would be at once apparent". I agree with the observation of Justice Kiefel of the High Court of Australia that this standard constitutes a "high hurdle".[236] No competent commercial contracting party would make a promise of this nature.

[267] The other law lords – Lord Davey[237] and Lord Robertson[238] – dismissed the appeal because the stipulated-consequence-on-breach term incorporated a proportionate payment schedule. The

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[232] Id. 87, 97 & 101. See *Cavendish Square Holding BV v. El Makdessi*, [2015] UKSC 67, ¶143; [2016] A.C. 1172, 1244 per Lord Mance ("The qualification and safeguard is that the agreed sum must not have been extravagant, unconscionable or incommensurate with any possible interest in the maintenance of the system").

[233] [1905] A.C. 6 (H.L. 1904).

[234] Id. 10.

[235] Id.

[236] *Paciocco v. Australia and New Zealand Banking Group Ltd.*, [2016] HCA 28, ¶53; 258 C.L.R. 525, 553.

[237] *Clydebank Engineering and Shipbuilding Co. v. Castaneda*, [1905] A.C. 6, 16 (H.L. 1904.

[238] Id. 19.

payments due for late delivery were a function of the length of the delay. But both of them acknowledged that exorbitant, extravagant or unconscionable consequences would be penalties.[239]

- ***Webster v. Bosanquet***

[268] *Webster v. Bosanquet*,[240] in my opinion, is the most important of the three pre-1915 judgments. Not only did the Privy Council uphold an essential term of a commercial contract, it clearly explained why:[241] "[W]hatever be the expression used in the contract in describing the payment, the question must always be whether the construction contended for renders the agreement unconscionable and extravagant and *one which no Court ought to allow to be enforced*." Lord Mersey, in a succinct judgment, approved an idea that the Earl of Halsbury championed in *Clydebank Engineering and Shipbuilding Co.*[242] No reference is made to penalties or liquidated damages in the quoted sentence. I place special emphasis on the clause "one which no court ought to allow to be enforced". This is a bold declaration that a commercial term should be given effect unless it is so one-sided that doing so would damage the reputation of the courts. In addition, the committee fully appreciated the business purpose that accounted for the contentious term:[243]

> When making the [tea partnership dissolution] contract it was impossible to foresee the extent of the injury which might be sustained by the plaintiff if sales of the tea were made to third parties without his consent. That such sales might seriously affect his business was obvious, and the very uncertainty of the loss likely to arise made it most reasonable for the parties to agree beforehand as to what the damages should be. And, furthermore, it is well known that damages of this kind, though very real, may be difficult of proof, and that the proof may entail considerable expense.

[269] Surprisingly, courts have seldom applied *Webster v. Bosanquet*. It is not very well known.[244]

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[239] Id. 16 per Lord Davey & 20 per Lord Robertson.

[240] [1912] A.C. 394 (P.C.) (Ceylon).

[241] Id. 398 (emphasis added).

[242] [1905] A.C. 6, 10 (H.L. 1904).

[243] [1912] A.C. 394, 398 (P.C.) (Ceylon).

[244] It has been cited sixteen times in the last 106 years. E.g., *Luen Yick Co. v. Tang Man Kee Machinery Workshop*, [1958] H.K.L.R. 405 (O.J). By comparison *Philips Hong Kong Ltd. v Hong Kong*, [1993] UKPC 3a; [1993] 1 H.K.L.R. 269 has been cited in forty-two judgments in the last twenty-five years.

- ***Philips Hong Kong Ltd. v. Hong Kong***

[270] In *Philips Hong Kong Ltd. v. Hong Kong*,[245] a 1993 opinion, the Privy Council upheld the decision of the Hong Kong Court of Appeal that a sophisticated stipulated-consequence-on-breach term in a contract part of a HK $649 million major highway construction project was enforceable. The Hong Kong Government entered into seven separate contracts with seven different construction companies, including Philips.[246] Each of these contracts contained key dates identifying certain milestones that had to be met so that the ability of the others to proceed with their distinct construction obligation would not be compromised, and a final completion date.[247] The per day financial consequences for failure to meet key dates varied depending on the number of other contractors that would be adversely affected by the failure of the contractor to meet its milestones – the amount ranged from a low daily rate of HK $60,655 to a high daily rate of HK $77,818.[248]

[271] Lord Woolf gave the committee's judgment. His opinion gave prominence to Lord Dunedin's speech in *Dunlop Pneumatic Tyre* and implicitly equated Lord Dunedin's opinion as the "Dunlop approach".[249] This is surprising given that the other law lords expressed positions different than that advanced by Lord Dunedin. While one may legitimately question this aspect of Lord Woolf's judgment, his dominant theme is appealing. He unequivocally upheld freedom of contract values when he pronounced that "the court has to be careful not to set too stringent a standard and bear in mind that what the parties have agreed should normally be upheld. Any other approach will lead to undesirable uncertainty especially in commercial contracts".[250]

[272] There are two important propositions that I derive from these four appeals.

[273] The first is that the House of Lords and Privy Council favoured the enforcement of commercial contracts between entities that had sufficient resources to retain counsel and advise them on their obligations under the contracts that they signed. [251]

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[245] [1993] UKPC 3a; [1993] 1 H.K.L.R. 269.

[246] Id. 273.

[247] Id.

[248] Id.

[249] Id. 279.

[250] Id. 280. He also quoted Lord Justice Diplock's statement in *Robophone Facilities Ltd. v. Blank*, [1966] 1 W.L.R. 1428, 1447 (C.A.) with approval: "[A] Court should not be astute to descry a 'penalty clause'". Id. 279.

[251] See *AMEV-UDC Finance Ltd. v. Austin*, [1986] HCA 63; 162 C.L.R. 170, 190 per Mason & Wilson, JJ. ("there is much to be said for the view that the courts should return to the *Clydebank* and *Dunlop* concept, thereby allowing parties to a contract greater latitude in determining what their rights and liabilities will be, so that an agreed sum is only characterized as a penalty if it is out of all proportion to damage likely to be suffered as a result of breach") & *Ringrow*

[274] Second, most of the law lords thought it improper for courts of justice to enforce one-sided bargains.

v. The Penalty Rule in the Nineteenth Century

[275] The receptiveness of twentieth-century judges to the freedom of contract principle did not distinguish them from their nineteenth-century colleagues.

[276] Many nineteenth-century judges vigorously proclaimed England's commitment to validate agreements voluntarily entered into by contracting parties with capacity.[252]

[277] The French *Code Civil* adopted in 1804 featured the primacy of contracting parties independence: "When the agreement provides that the party who fails to perform shall pay a certain sum on account of damages, no smaller or larger sum can be awarded to the other party".[253]

[278] *Reynolds v. Bridge*,[254] an 1856 appeal, is an excellent example.

[279] Two surgeons carried on the practice of surgery in partnership for roughly five years before they entered into an 1852 agreement whereby Dr. Reynolds agreed to employ Dr. Bridge for a three-year period. The agreement obliged each of the surgeons to undertake certain activities during the three year period in order to increase the likelihood that at the end of the three-year period Dr. Bridge's patients would become Dr. Reynold's patients. The agreement also prevented Dr. Bridge from practising surgery within a designated area after the expiration of the employment agreement. Dr. Bridge promised to pay as liquidated damages defined sums for breaches of specific contractual obligations.

[280] The Court, having found Dr. Bridge to be in contravention of the agreement, ordered Dr. Bridge to pay to Dr. Reynolds the sum he promised to pay if he breached specific obligations.

[281] Of particular interest is the opinion of Justice Erle. He strongly endorsed the principle that held promisors to account:[255]

Pty. Ltd. v. BP Australia Pty. Ltd., [2005] HCA 71, ¶31; 224 C.L.R. 656, 669 (the Court approved Justices Mason and Wilson's position in *AMEV*).

[252] *Astley v. Weldon*, 126 Eng. Rep. 1318, 1322 (Common Pleas 1801) per Lord Eldon, C.J. (" I do not understand why one brandy merchant who purchases the lease and goodwill of a shop from another may not make it matter of agreement, that if the vendor trade in brandy within a certain distance, he shall pay 600£; and why the party violating such agreement should not be bound to pay the sum agreed for").

[253] Art. 1152.

[254] 119 Eng. Rep. 961 (Q.B. 1856). See also *Atkyns v. Kinnier*, 154 E.R. 1429 (Ex 1850)(the Court enforced a surgeon's promise to pay £1000 as liquidated damages to his former partner if he left the partnership and commenced the practice of surgery within a defined area).

> [It is] an important principle of law … that parties are to assign such limits as they please to their own liability. If parties choose to lay down such a limit, I do not see why the Judges are to substitute another; and the tendency latterly has been very much to restrict the rule of construction. Certainly in some of the cases it was a very large exercise of the power of the Court, to say, we will see what we should have thought reasonable, and to construe the contract accordingly... .

[282] Chief Justice Tindal fervently believed in the importance of enforcing contractual bargains. In *Kemble v. Farren*[256] he stated that "we see nothing illegal or unreasonable in the parties, by their mutual agreement, settling the amount of damages, uncertain in their nature, at any sum upon which they may agree".

[283] In *Wallis v. Smith*[257] Sir George Jessel, M.R. and Lord Justice Cotton unequivocally expressed their support for a restrained judicial approach to penalties.

[284] Most nineteenth-century English judges focussed on the contract's text.[258] They asked if the key term demonstrated an intention to liquefy the damages that nonperformance would cause the innocent promisee, in which case the term would be accorded effect, or an intention to introduce a term that had no compensatory component but was designed to coerce contractual compliance, in which case the court would not enforce it, characterizing the term as a penalty.[259]

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[255] 119 Eng. Rep. 961, 967 (Q.B. 1856).

[256] 130 Eng. Rep. 1234, 1237 (Common Pleas 1829).

[257] 21 Ch. D. 243, 266 & 268 (C.A. 1882) ("I have always thought … that it is of the utmost importance as regards contracts between adults – persons not under disability, and at arm's length – that the Courts of Law should maintain the performance of the contracts according to the intention of the parties; that they should not overrule any clearly expressed intention on the ground that Judges know the business of the people better than the people know it themselves") & ("[T]he sounder view … is … to leave persons who are competent and under no disability to make their own contracts, and then to act on those contracts, whatever the true interpretation might be, without assuming on behalf of the Court, either of Law or Equity, to say, 'This is unreasonable and we will make another and different contract between the parties. They did not mean what they have said in their contracts'").

[258] *Rickman v. Carstairs*, 110 Eng. Rep. 931, 935 (K.B. 1833)("in ... cases of construction of written instruments [the question] is not what was the intention of the parties, but what is the meaning of the words they have used"). This is still the law. *Sattva Capital Corp. v. Creston Moly Corp.*, 2014 SCC 53, ¶47; [2014] 2 S.C.R. 633, 657 ("a decision-maker must read the contract as a whole, giving the words used their ordinary and grammatical meaning, consistent with the surrounding circumstances known to the parties at the time of formation of the contract") & *Re Lubberts Estate*, 2014 ABCA 216, n. 21; [2014] 10 W.W.R. 41, n. 21 per Wakeling, J.A. ("Multiparty documents cannot have multiple meanings which are a function of the subjective understanding of each party ... . There must be an enforceable meaning attached to the oral or written language which the parties acknowledge captures their consensus. It must be the product of an objective inquiry").

[259] *Law v. Local Board of Redditch*, [1892] 1 Q.B. 127, 130 per Lord Esher, M.R. ("where the sum agreed to be paid is ... so large as to make the idea that it was intended to be payable by way of liquidated damages so absurd that the Court would be compelled to arrive at the conclusion that it was to be paid, not as liquidated damages, but as a penalty") &

[285] Why judges of this era believed that this inquiry assisted them in any way in deciding whether there was a compelling reason to justify ignoring the clear meaning of a contract's text escapes me.

[286] Why would a contract party enter into an agreement that contained a term inserted for its benefit knowing that it would be unenforceable? This makes no sense.

c. The Penalty Rule in the United States

[287] Many twentieth-century decisions of the United States Supreme Court turned on the Court's response to a promisor's argument that the law relieved it of its obligation to honor a paid-for promise.

[288] This body of work fully justifies Justice Peckham's 1907 assertion that modern courts are predisposed to enforce stipulated-consequence-on-breach terms.

[289] I will refer to only four in detail. [260]

[290] The first two arose as a result of the Spanish-American War of 1898.

i. *Sun Printing and Publishing Association v. Moore*

[291] *Sun Printing and Publishing Association v. Moore*, [261] decided in 1902, dealt with a charterer's obligation after the yacht it chartered to cover the Spanish-American hostilities sank. The charter agreement contained a promise by the charterer to pay the yacht owner $75,000, the agreed value of the vessel, if it failed to return the yacht in good repair on the return date.

[292] The charterer failed to return the yacht and the yacht owner commenced an action against the charterer for $75,000. The trial and two appeal courts sided with the yacht owner. So did the Supreme Court.

[293] Justice White, after conducting a thorough review of the leading English and American cases, declared that the Court must examine the text of the charterparty and determine whether the

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132 per Lopes L.J. ("The distinction between penalties and liquidated damages depends on the intention of the parties to be gathered from the whole of the contract").

[260] *Priebe & Sons, Inc. v. United States*, 332 U.S. 407 (1947); *Wise v. United States*, 249 U.S. 361 (1919); *United States v. Bethlehem Steel Co.*, 205 U.S. 105 (1907) & *Sun Printing and Publishing Assoc. v. Moore*, 183 U.S. 642 (1902). See also *Robinson v. United States*, 261 U.S. 486 (1923) (the Court upheld a liquidated damages term to the detriment of the promisor-plaintiff); *J.E. Hathaway & Co. v. United States*, 249 U.S. 460, 464 (1919) ("there is no reason why parties competent to contract may not agree that certain elements of damage difficult to estimate shall be covered by a provision for liquidated damages ... . Provisions ... clearly expressed do not cease to be binding upon the parties, because they relate to the measure of damages").

[261] 183 U.S. 642 (1902).

parties intended "bona fide to fix the damages"[262] in which case the promisor must discharge its obligation or whether they intended "to stipulate the payment of an arbitrary sum as a penalty, by way of security",[263] in which case the promisor is relieved of the obligation to honor its commitment. Justice White quoted with approval Justice Wright's opinion in *Clement v. Cash*[264] to this effect:

> When [the contracting parties] declare, in distinct and unequivocal terms, that they have settled and ascertained the damages to be $500.00, or any other sum, to be paid by either failing to perform, it seems absurd for a court to tell them that it has looked into the contract and reached the conclusion that no such thing was intended; but that the intention was to name the sum as a penalty to cover any damages that might be proved to have been sustained by a breach of the agreement.

ii. *United States v. Bethlehem Steel Co.*

[294] *United States v. Bethlehem Steel Co.*[265] is the second case. It was a 1907 judgment.

[295] In 1898 Bethlehem Steel promised to construct six gun carriages for the United States armed forces for $216,000. The United States anticipated that it would soon be at war with Spain and was prepared to pay a premium for expedited delivery. A late-delivery provision reduced the purchase price by a sum equal to a daily amount multiplied by the period of late delivery measured in days. Bethlehem Steel delivered the gun carriages after the promised delivery date. For this reason, the United Stated paid Bethlehem Steel $195,000 instead of $216,000. Bethlehem Steel sued in the Court of Claims for the $21,000 shortfall. The Court of Claims found in favour of Bethlehem Steel. The United States Supreme Court reversed.

[296] Justice Peckham, for the Court, concluded that the parties intended the stipulated-consequence-on-breach term to liquidate the damages and not to serve as a penalty:[266]

> The acceptance of the proposal at the highest price for the delivery of the carriages in the shortest time is also evidence of the importance with which the Government officers regarded the element of speed. … In the light of this fact an examination of the language of the contract itself upon the question of deductions for delay in delivery renders its meaning quite plain.

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[262] Id. 673.

[263] Id.

[264] 21 N.Y. 253, 257 (Ct. App. 1860).

[265] 205 U.S. 105 (1907).

[266] Id. 119-20.

[297] In coming to this conclusion, the Court also recognized the fact that it would be very difficult to prove damages for late delivery of armaments.

iii. *Wise v. United States*

[298] *Wise v. United States*,[267] released in 1919, is the third case.

[299] In 1904 a builder promised to erect two laboratory buildings for the Department of Agriculture in Washington. The price tag was $1,171,000. There was a price-reduction term in the contract that the United States invoked to withhold $20,000 of the construction price. The builder claimed that the United States was not entitled to rely on the stipulated-consequence-on-breach term.

[300] The Supreme Court of the United States concluded that the contract unequivocally demonstrated an intention to fix the damages that the United States would endure if the two buildings were not constructed on time.[268] Justice Clarke, for a court that included Justice Oliver Wendell Holmes, provided this clear account of the law:[269]

> When that intention is clearly ascertainable from the writing, effect will be given to the provision as freely as to any other, where the damages are uncertain in nature or amount or are difficult of ascertainment or where the amount stipulated for is not so extravagant, or disproportionate to the amount of property loss, as to show that compensation was not the object aimed at or as to imply fraud, mistake, circumvention or oppression. There is no sound reason why persons competent and free to contract may not agree upon this subject as fully as upon any other, or why their agreement, when fairly and understandingly entered into with a view to just compensation for the anticipated loss, should not be enforced.

iv. *Priebe & Sons, Inc. v. United States*

[301] *Priebe & Sons, Inc. v. United States*[270] is the fourth case. It was decided in 1947.

[302] After Congress enacted the *Lend-Lease Act*[271] in 1941, the Department of Agriculture decided to ship dried eggs to England and Russia to ameliorate the wartime food shortage these countries were experiencing. Priebe & Sons, Inc. was one the suppliers. Priebe & Sons agreed to deliver a designated amount of dried eggs along with an inspection certificate within a specified

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[267] 249 U.S. 361 (1919).

[268] Id. 365.

[269] Id.

[270] 332 U.S. 407 (1947).

[271] 55 Stat. 31, 22 U.S.C. (Supp. V. 1946).

time. There was also a term that allowed the purchaser to pay ten cents less per pound of dried eggs if the supplier failed to meet designated milestones on time.[272] Priebe & Sons delivered the requested quantity of dried eggs on time but missed the deadline for the inspection certificate. The United States invoked the liquidated damages provision and paid the supplier ten cents less per pound. The supplier sued alleging that the term the United States relied on was an unenforceable penalty. The Court of Claims dismissed the action, holding that the contested term was not a penalty. The Supreme Court reversed, satisfied that the term was a penalty.

[303] Justice Douglas wrote for the five justices who constituted the majority. He opined that "The provision was included not to make a fair estimate of damages to be suffered but to serve only as an added spur to performance. ... [A]n exaction of punishment for a breach which could produce no possible damage has long been deemed oppressive and unjust".[273] While Justice Frankfurter disagreed with the majority because he was convinced that federal statutes compelled judicial validation of terms like the one under review, he agreed that the contested term was a penalty under common law.[274]

[304] Justices Black and Murphy parted company with their colleagues. They classified the stipulated-consequence-on-breach term as a liquidated damages provision.[275] They gave great weight to the fact that this was a commercial transaction and concluded that there was "no persuasive reason why [the promisor] should now be relieved of the obligation it advisedly assumed which was, in effect, to charge less for its goods if they were not ready for delivery on the date it promised".[276]

[305] Justice Frankfurter's statement that "one man's default should not lead to another man's unjust enrichment"[277] is perhaps the most significant contribution these four cases make to the development of the jurisprudence. This assertion clearly suggests that some stipulated-consequence-on-breach terms will be invalid because they are unconscionable and that no court should use its power in a way that would bring the administration of justice into disrepute.

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[272] It reads as follows: "Inasmuch as the failure of the vendor to deliver the quantity of the commodity ... specified in the contract in accordance with the terms of this announcement will, because of the urgent need for the commodity by the purchaser arising from the present emergent conditions, cause serious and substantial damages to the purchaser, and it will be difficult, if not impossible, to prove the amount of such damages, the vendor agrees to pay ... liquidated damages as stated in this paragraph. The sum is agreed upon as liquidated damages and not as a penalty and shall be in the amount set forth below for each pound of dried egg product undelivered in accordance with the terms of this announcement ... . The parties have computed, estimated, and agreed upon this sum as an attempt to make a reasonable forecast of probable actual loss because of the difficulty of estimating with exactness the damages which result".

[273] 332 U.S. 407, 413 (1947).

[274] Id. 419.

[275] Id. 417.

[276] Id.

[277] Id. 418.

[306] A general survey of state and federal jurisprudence [278] and academic literature [279] demonstrates that most American jurists recognize that commercial actors are the best judges of the merits and demerits of the burdens they incur and the benefits they enjoy by entering into a contract [280] and that in the absence of extraordinary terms – those that are unconscionable, manifestly and grossly unfair or will unjustly enrich the promissee – they should be allowed to agree upon stipulated-payment terms that they adjudge to be in their best interests.

5. The Contested Term Passes Both the *Elsley* and *Dunlop Pneumatic Tyre* Standards and Is Enforceable

[307] Regardless of which standard is applied – *Elsley* or *Dunlop Pneumatic Tyre* – s. VII Q(d) is enforceable.

a. *Elsley* Standard

[308] This is a commercial contract.

[309] There is no evidence that Capital Steel Inc. had insufficient resources to retain legal counsel before it signed the agreement with Chandos Construction.

[310] Nor is there any basis whatsoever to conclude that s. VII Q(d) is oppressive. A term is oppressive if it is so manifestly grossly one-sided that its enforcement would bring the administration of justice into disrepute. This is not such a term.

[311] Section VII Q(d) reflects the fact that Chandos Construction will incur administrative costs associated with completing the work that Capital Steel failed to do and monitoring the work during the warranty period. Chandos Construction will have to find another enterprise that is willing to accept a modest assignment and complete it on a time path acceptable to Chandos Construction. There is no evidence that suggests its enforcement will bestow a windfall on Chandos Construction.

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[278] *Lion Overall Co.*, 55 F. Supp. 789, 791 (S.D.N.Y 1943) ("The present rule is to look with candor, if not with favor, upon such provisions in contracts when deliberately entered into between parties who have equality of opportunity for understanding and insisting upon their rights, as promoting prompt performance, and because adjusting in advance, and amicably, matters the settlement of which through courts would involve difficulty, uncertainty, delay and expense").

[279] E. Farnsworth, Contracts 820 (4th ed. 2004).

[280] *Jewett, Bigelow & Brooks v. Detroit Edison Co.*, 274 F. 30, 37-38 (6th Cir. 1921) ("this court must not overlook the fact that the contracting parties were both familiar with the coal business in all its details ... Therefore no reason appears from the evidence in this case why this court should set aside and hold for naught a solemn contract, entered into between men of affairs, largely experienced and fully advised as to conditions and incidents of the business to which the contract relates and substitute its own judgment for the judgment of the contracting parties").

[312] The term also documents the parties' agreement that there is a correlation between Capital Steel's performance and its remuneration. "There is no reason in principle why a contract should not provide for a party to earn his remuneration, or part of it, by performing his obligations".[281]

[313] This is a compensatory provision that makes commercial sense.

b. *Dunlop Pneumatic Tyre* Standard

[314] *Dunlop Pneumatic Tyre Co. v. New Garage and Motor Co.*[282] stands for the proposition that a commercial bargain is unenforceable if it is unconscionable, extravagant or extortionate. Section VII Q(d) is none of these. The sum of money the ten percent fee represents will probably cover some or all of the administrative costs Chandos Construction will incur as a result of the administrative time that it must devote to finding others to complete the tasks Capital Steel had left undone, including monitoring the project for warranty purposes. There is no reason to believe that this fee is disproportionate to the actual costs Chandos Construction will actually incur because of Capital Steel's failure to complete the work. There is no evidence supporting such a conclusion.

C. Section VII Q(d) Is Not Contrary to Any Common Law Values Related to Bankruptcy or Any Provision of the *Bankruptcy and Insolvency Act* and Is Enforceable

1. Introduction

[315] Canada's *Bankruptcy and Insolvency Act*,[283] like the national insolvency enactments of the United Kingdom,[284] the United States,[285] Australia[286] and New Zealand,[287] catalogues most of the important principles and rules governing insolvency regimes.[288]

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[281] *Cavendish Square Holding BV v. El Makdessi*, [2015] UKSC 67, ¶73; [2016] A.C. 1172, 1216 per Lord Neuberger & Lord Sumption.

[282] [1915] A.C. 79 (H.L. 1914).

[283] R.S.C. 1985, c. B-3.

[284] *Insolvency Act 1986*, c. 45.

[285] *Bankruptcy Code*, 11 U.S.C.

[286] *Bankruptcy Act 1966*, No. 33 (Cth) & *Corporations Act 2001*, No. 50 (Cth).

[287] *Companies Act 1993*, No. 105 & *Insolvency Act 2006*, No. 55.

[288] R. Wood, Bankruptcy and Insolvency Law 11 (2d ed. 2015)("most of the insolvency regimes are overwhelmingly legislative in character"); Wood, "Direct Payment Clauses and the Fraud Upon the Bankruptcy Law Principle: *Re Horizon Earthworks Ltd. (Bankrupt)*", 52 Alta. L. Rev. 171, 171 (2014) ("Bankruptcy law is overwhelmingly statutory in character"); C. Tabb, The Law of Bankruptcy 2 (2d ed. 2009) ("The current Bankruptcy Code encompasses a wide spectrum of possible measures. These range from a straight liquidation bankruptcy (chapter 7), to the reorganization of businesses (chapter 11), to the adjustment of family farmer debts (chapter 12), to the adjustment

[316] The *Bankruptcy and Insolvency Act*, again, like most of its foreign counterparts,[289] displays three fundamental features.

[317] The first is the utilization of one procedural vehicle to advance the claims of the creditors against the bankrupt. Professor Wood explains the first benchmark this way: [290] "The creditors' remedies are collectivized in order to prevent the free-for-all that would otherwise prevail if creditors were permitted to exercise their remedies". This is accomplished by a statutory ban on the commencement of proceedings against a bankrupt. Section 69.3(1) of the *Bankruptcy and Insolvency Act*[291] provides that "on the bankruptcy of any debtor, no creditor has any remedy

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of the debts of individual consumers (chapter 13), and even to the adjustment of the debts of a municipality (chapter 9). Cross-border cases are dealt with in chapter 15") & *Re Potts*, [1893] 1 Q.B. 648, 657 (C.A.) per Lord Esher, M.R. ("the bankruptcy law is not the common law of England; it is an enacted law, and all the rights under it are determined by statute").

[289] While insolvency regimes frequently incorporate common critical components, they sometimes adapt different implementation solutions. E.g., *Century Services Inc. v. Canada*, 2010 SCC 60, ¶29; [2010] 3 S.C.R. 379, 400 ("Claims of priority by the state in insolvency situations receive different treatment across jurisdictions worldwide").

[290] R. Wood, Bankruptcy and Insolvency Law 3 (2d ed. 2015). See C. Tabb, The Law of Bankruptcy 4 (2d ed. 2009)("the core function of bankruptcy is as a *collective creditors' remedy* that furthers the goals of efficiency and of distributive justice") (emphasis in original); D. Epstein & S. Nickles, Principles of Bankruptcy Law 3 (2007) ("State law focuses on individual action by a particular creditor and puts a premium on prompt action by a creditor. ... Bankruptcy, on the other hand, compels collective creditor collection action and emphasizes equality of treatment, rather than a race of diligence") & *Allied Concrete Ltd. v. Meltzer*, [2015] NZSC 7, ¶96; [2016] 1 N.Z.L.R. 141, 174 ("As the material ... demonstrates, both the Government and Parliament understood that there was a conflict between the concept of collective realisation and individual justice in particular cases").

[291] R.S.C. 1985, c. B-3. See also s. 69(1)("[O]n the filing of a notice of intention under section 50.4 by an insolvent person, (a) no creditor has any remedy against the insolvent person's property, or shall commence or continue any action, execution, or other proceedings, for the recovery of a claim provable in bankruptcy"). See R. Wood, Bankruptcy and Insolvency Law 5 (2d ed. 2015)("The commencement of insolvency proceedings will typically prevent a claimant from pursuing a claim through an ordinary civil action before a court or enforcing it through the judgment enforcement system"). See also *Insolvency Act 1986*, c. 45, s. 126(1) (U.K.) ("At any time after the presentation of a winding-up petition, and before a winding-up order has been made, the company, or any creditor or contributory may... where any action or proceeding against the company is pending in the High Court or Court of Appeal ... apply to the court in which the action or proceeding is pending for a stay of proceedings therein ... and the court to which the application is so made may (as the case may be) stay, sist or restrain the proceedings accordingly on such terms as it thinks fit") & s. 130(2) ("When a winding-up order has been made ... , no action or proceeding shall be proceeded with or commenced against the company or its property, except by leave of the court and subject to such terms as the court may impose"); *Bankruptcy Act 1966*, No. 33, s. 60(1)(b)(Austl. Cth) ("The Court may, at any time after the presentation of a petition, upon such terms and conditions as it thinks fit … stay any legal process … against the person or property of the debtor"); *Corporations Act 2001*, No. 50, s. 471B (Austl. Cth) ("While a company is being wound up in insolvency or by the Court, or a provisional liquidator of a company is acting, a person cannot begin or proceed with … a proceeding in a Court against the company or in relation to property of the company; or … enforcement process in relation to such property; except with the leave of the Court and in accordance with such terms (if any) as the Court imposes"); *Insolvency Act 2006*, No. 55, s. 76(1)(N.Z.)("On adjudication [of bankruptcy], all proceedings to recover any debt provable in the bankruptcy are halted"); *Companies Act 1993*, No. 105, s. 239 ABE (N.Z.) ("During the administration of a company, a proceeding in a court against the company or in relation to any of its property must not be begun or continued, except ... (a) with the administrator's written consent; or (b) with the

against the debtor or the debtor's property, or shall commence or continue any action, execution or other proceedings, for the recovery of a claim provable in bankruptcy". "The automatic stay is one of the most important parts of any ... bankruptcy case".[292]

[318] A single-procedure-vehicle model probably maximizes the size of the bankrupt's property pool for the ultimate benefit of the creditors. It may reduce the risk that some of the bankrupt's property may not be tracked as effectively by debtors acting alone. Collective bargaining between the bankrupt's creditors and the bankrupt increases the likelihood that an acceptable remedial plan will be produced and reduces the need for the plaintiff creditors and the defendant bankrupt to complete duplicitous litigation steps.[293]

[319] The second benchmark is a provision that identifies the bankrupt's property as of a designated date and creates a mechanism that collects in the bankruptcy trustee's hands the bankrupt's property.[294] "'Property of the estate' is one of the most important, most basic

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permission of the court"); *Bankruptcy Code*, 11 U.S.C. §362(a)("Except as provided under subsection (b) of this section, a petition filed under section 301, 302 or 303 of this title ... operates as a stay, applicable to all entities of ... the commencement or continuation, including the issuance or employment of process, of a judicial, administrative, or other action or proceeding against the debtor that was or could have been commenced before the commencement of the case under this title") & C. Tabb, The Law of Bankruptcy 244 (2d ed. 2009)("An integral structural component of a bankruptcy case is the 'automatic stay' against creditor collection actions. ... It arises automatically upon the filing of a bankruptcy petition").

[292] D. Epstein & S. Nickles, Principles of Bankruptcy Law 15 (2007). See also *Newfoundland and Labrador v. AbitibiBowater Inc*., 2012 SCC 67, ¶21; [2012] 3 S.C.R. 443, 458 ("Under this [single proceeding] model, the court can stay the enforcement of most claims against the debtor's assets in order to maintain the *status quo* during negotiations with the creditors").

[293] *Century Services Inc. v. Canada*, 2010 SCC 60, ¶22; [2010] 3 S.C.R. 379, 397 ("The single proceeding model avoids the inefficiency and chaos that would attend insolvency if each creditor initiated proceedings to recover its debt. Grouping all possible actions against the debtor into a single proceeding controlled in a single forum facilitates negotiation with creditors because it places them all on an equal footing"); *Schreyer v. Schreyer*, 2011 SCC 35, ¶19; [2011] 2 S.C.R. 605, 615-16 ("Legislation that establishes an orderly liquidation process for situations in which reorganization is not possible, that averts races to execution and that gives debtors a chance for a new start is generally viewed as a wise policy choice"); R. Wood, Bankruptcy and Insolvency Law 3 (2d ed. 2015) ("The race to grab assets in the absence of a collective insolvency regime does not provide an environment within which an efficient and orderly liquidation can occur") & C. Tabb, The Law of Bankruptcy 4 (2d ed. 2009) ("the core function of bankruptcy is a *collective creditors' remedy* that furthers the goals of efficiency and of distributive justice") (emphasis in original).

[294] *Bankruptcy and Insolvency Act*, R.S.C. 1985, c. B-3, s. 2 ("*property* means any type of property, whether situated in Canada or elsewhere, and includes money, goods, things in action, land and every description of property, whether real or personal, legal or equitable, as well as obligations, easements and every description of estate, interest and profit, present or future, vested or contingent in, arising out of or incident to property") & *Bankruptcy Code*, 11 U.S.C. §541(a)(1) ("The commencement of a case ... creates an estate. Such estate is comprised of all the following property, wherever located and by whomever held: ... all legal or equitable interests of the debtor in property as of the commencement of the case"). This obviously sweeps in accounts receivables. See also *Re Barrington & Vokey Ltd.*, 48 C.B.R. 3d 270, 279 (N.S. Sup. Ct. 1996)("On the date of bankruptcy ... , all of the assets of B&V vested in the Trustee for the benefit of the general body of creditors ... . The Trustee became obligated and empowered to take possession of the property of the bankrupt ... , the intention being that all creditors would receive the distribution to which they were

bankruptcy concepts".[295] Section 71 of the *Bankruptcy and Insolvency Act*[296] is one provision that serves this purpose: "On a bankruptcy order being made ... a bankrupt ceases to have any capacity to dispose of or otherwise deal with their property, which shall, subject to this Act and to the rights of secured creditors, immediately pass to and vest in the trustee named in the bankruptcy order ... ."

[320] The third distinguishing feature is the equitable distribution of the bankrupt's property to the bankrupt's creditors. Section 141 of the *Bankruptcy and Insolvency Act*[297] declares that "[s]ubject to this Act, all claims proved in a bankruptcy shall be paid rateably."

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entitled") & C. Tabb, The Law of Bankruptcy 394 & 401 (2d ed. 2009) ("The bankruptcy 'estate' is a separate and distinct legal entity. It is comprised initially of all of the debtor's property at the time the case is commenced. ... [T]he instant of the bankruptcy filing is the magic moment at which the extent of the estate initially is determined. Section 541(a)(1) takes a snapshot of the debtor's assets at the moment of filing, bringing all of those assets into the estate").

[295] D. Epstein & S. Nickles, Principles of Bankruptcy Law 9 (2007).

[296] R.S.C. 1985, c. B-3. See *Bankruptcy Code*, 11 U.S.C. §323(a) ("The trustee in a case under this title is the representative of the estate"); *Insolvency Act 1986*, c. 45, s. 306(1) (U.K.) ("The bankrupt's estate shall vest in the trustee immediately on his appointment taking effect") & s. 145(1) ("When a company is being wound up by the court, the court may on the application of the liquidator by order direct that all or any part of the property of whatsoever description belonging to the company or held by trustees on its behalf shall vest in the liquidator by his official name; and thereupon the property to which the order relates vests accordingly"); *Corporations Act 2001*, No. 50, s. 474(1)(a) (Austl. Cth) ("If a company is being wound up in insolvency or by the Court, or a provisional liquidator of a company has been appointed … in a case in which a liquidator … has been appointed … the liquidator .. must take into his or her custody, or under his or her control, all the property which is, or which appears to be, property of the company"); *Bankruptcy Act 1966*, No. 33, s. 58(1)(a) (Austl. Cth) ("Subject to this Act, where a debtor becomes a bankrupt … the property of the bankrupt, not being after-acquired property, vests forthwith in the Official Trustee"); *Companies Act 1993*, No. 105, s. 239U (N.Z.) ("While a company is in administration, the administrator ... (a) has control of the company's business, property and affairs; and (b) may carry on that business and manage that property and those affairs; and (c) may terminate or dispose of all or part of that business, and may dispose of any of that property") & *Insolvency Act 2006*, No. 55, s. 101(1)(a) (N.Z.) (natural person: "On adjudication ... all property ... belonging to the bankrupt or vested in the bankrupt vests in the Assignee without the Assignee having to intervene or take any other step in relation to the property, and any rights of the bankrupt in the property are extinguished").

[297] R.S.C. 1985, c. B-3. See *Insolvency Act 1986*, c. 45, s. 107 (U.K.) ("Subject to the provisions of this Act as to preferential payments, the company's property in a voluntary winding up shall on the winding up be applied in satisfaction of the company's liabilities pari passu") & s. 328(3) ("Debts which are neither preferential debts nor debts to which the next section applies also rank equally between themselves and, after the preferential debts, shall be paid in full unless the bankrupt's estate is insufficient for meeting them, in which case they abate in equal proportion"); *Corporations Act 2001*, No. 50, s. 559 (Austl. Cth) ("The debts of a class referred to in each of the paragraphs of subsection 556(1) rank equally between themselves and must be paid in full, unless the property of the company is insufficient to meet them, in which case they must be paid proportionately"); *Bankruptcy Act 1966*, No. 33, s. 108 (Austl. Cth) ("Except as otherwise provided by this Act, all debts proved in a bankruptcy rank equally and, if the proceeds of the property of the bankrupt are insufficient to meet them in full, they shall be paid proportionately"); *Insolvency Act 2006*, No. 55, s. 280(2) (N.Z.) ("The [general creditors'] claims ... rank equally among themselves and must be paid in full, unless the money is insufficient to meet them, in which case they abate in equal proportions"); *Companies Act 1993*, No. 105, s. 313(2) (N.Z.) ("The [general creditors'] claims ... rank equally among themselves and must be paid in full, unless the assets are insufficient to meet them, in which case payment shall abate rateably among all claims"); *Bankruptcy Code*, 11 U.S.C. §726 (b) ("Payment on claims of a kind [described in numerous

[321] These three features serve as the foundation upon which a complete and sophisticated insolvency and bankruptcy structure rests.

[322] I will now use several hypotheticals to illustrate how these basic features affect some concrete fact patterns.

[323] Suppose that M, a municipality, enters into a contract with a highway construction company, HC Co., to build a road within the municipality. M agrees to pay HC Co. $5 million, payable in instalments on the completion of designated milestones. Before HC Co. completes the project and after M has paid HC Co. $3 million, HC Co. goes bankrupt. M owes HC Co. $750,000 for work that HC Co. has performed and billed. M is aware that HC Co. has not paid invoices submitted by subcontractors D, E and F for services and material. HC Co. owes each of the subcontractors $250,000 and other creditors $750,000. T, HC Co.'s bankruptcy trustee, has served M with a demand that M pay T the $750,000 due under the accounts rendered by HC Co.. M asks its lawyer if it can discharge its obligation to HC Co. by paying $250,000 to each of D, E and F. M is aware that if it pays T $750,000, D, E and F will likely receive less than $250,000 on any subsequent payout to HC Co.'s creditors. M wants to make D, E and F whole so that they will be willing in the future to work on M's infrastructure projects. M's lawyer advises M to pay T the $750,000 T demands. M's lawyer informs M that T owns all HC Co.'s property,[298] including the account receivable that HC Co.'s outstanding bill to M represents. M has a legal obligation to pay T[299] and cannot choose to ignore it without incurring adverse financial consequences.[300] This is so even though payments to D, E and F would not have had the effect of diminishing the size of the pool of assets available for distribution to HC Co.'s creditors. D, E and F are all creditors of HC Co. The real problem was the advantage these payments bestowed on D, E and F, compared to HC Co.'s other unsecured creditors.

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provisions] ... shall be made pro rata among claims of the kind specified in each such particular paragraph"). See also R. Wood, Bankruptcy and Insolvency Law 44-45 (2d ed. 2015) ("the proceeds of the liquidation of the debtor's assets are distributed to the proving creditors according to a statutory scheme of distribution. Although this scheme of distribution provides for *pari passu* sharing among ordinary creditors, certain kinds of claims are promoted and given more favourable treatment than the ordinary creditors (preferred creditors) while other kinds of claims are demoted and given less favourable treatment (postponed creditors)"); C. Tabb, The Law of Bankruptcy 674 (2d ed. 2009) ("For all of the general unsecured creditors, the controlling bankruptcy principle is *equality* of distribution") (emphasis in original) & D. Epstein & S. Nickles, Principles of Bankruptcy Law 3 (2007) ("While bankruptcy law does not require equal treatment for all creditors, all creditors within a single class are treated the same").

[298] The *Bankruptcy and Insolvency Act*, R.S.C. 1985, c. B-3, s. 2 defines "property" in very broad terms. See F. Bennett, Bennett on Bankruptcy 51-52 (19th ed. 2017) ("property in a business would include cash in the bank, receivables, inventory, equipment, real property, tax claims, refunds and tax losses, industrial property including patents, trademarks and copyright, customer lists, hedging contracts, options, equity in unexpired leases of premises and equipment, choses in action and third-party claims").

[299] *Bankruptcy and Insolvency Act*, R.S.C. 1985, c. B-3, s. 71.

[300] M would have to pay the same amount to T.

[324] The Supreme Court of Canada dealt with this issue in *A.N. Bail Co. v. Gingras*.[301] A general construction contractor, relying on a contract term binding the general contractor and the subcontractor, paid the bankrupt subcontractor's creditor the amount due the subcontractor and refused to pay the bankrupt subcontractor's trustee. "Property" was a broadly defined term under the *Bankruptcy Act*[302] and indisputably included the subcontractor's accounts receivable. Because the subcontractor had an interest in the accounts receivable, it was the subcontractor's property and the general contractor had an obligation to pay the bankruptcy trustee. The general contractor's payment to the bankrupt subcontractor's creditor did not discharge the general contractor's obligation under the statute:[303] "It would be to disregard the *Bankruptcy Act* and deprive it of all meaning if the debtor of a bankrupt, instead of paying the trustee, were authorized by contract or some other means, to pay one or other of the creditors of the bankrupt as he saw fit".

[325] There are other business structures that give an owner more control.[304]

[326] Suppose that M decided to revise the business model it used for the construction of its infrastructure projects. M retained a project manager to provide it with services on a fee-for-service basis. The project manager recommends service providers and suppliers and M enters into contracts with each enterprise that contributes to the infrastructure project. M follows this model for the construction of a community fitness center. M enters into twenty-five separate agreements with service providers and suppliers, as well as an agreement with FC Co., the project manager. FC Co. becomes bankrupt before the project is completed. M pays T, FC Co.'s bankruptcy trustee, the amount of FC Co.'s last bill, and continues to discharge its obligations under its other infrastructure project contracts. M is entitled to proceed in this manner because it has honored its obligations to T, as set out in the *Bankruptcy and Insolvency Act*.[305] It has paid to T FC Co.'s outstanding accounts receivable. This is FC Co.'s property, as defined in the *Bankruptcy and Insolvency Act*.[306]

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[301] [1982] 2 S.C.R. 475. See also *Municipal District of Greenview No. 16 v. Bank of Nova Scotia*, 2013 ABCA 302; 5 C.B.R. 6th 69 (the Court confirmed the chamber judge's conclusion that the municipality could not rely on a contract term that allowed it to pay directly an unpaid subcontractor to discharge its obligations to a bankrupt general contractor's trustee because the unpaid accounts receivable is the property of the bankrupt) & *International Air Transport Assoc. v. Ansett Australia Holdings Ltd.(Subject to Deed of Company Arrangement)*, [2008] HCA 3, ¶76; 234 C.L.R. 157 ("the critical point is that there was 'property' of British Eagle to which s. 302 applied and a contractual provision negating that outcome could not prevail against the terms of the statute").

[302] R.S.C. 1970, c. B-3, s. 2.

[303] [1982] 2 S.C.R. 475, 487.

[304] E.g., *Phillips Hong Kong Ltd. v. Hong Kong*, [1993] UKPC 3a; [1993] 1 H.K.L.R. 269 (Hong Kong entered into seven contracts with seven different contractors for the construction of a major highway project).

[305] R.S.C. 1985, c. B-3, s. 71.

[306] Id. s. 2.

[327] These hypotheticals highlight the obligations of a bankrupt's debtor under the *Bankruptcy and Insolvency Act*[307] to deliver the bankrupt's property to the bankrupt's trustee. They did not involve contract terms that had the effect of diminishing the size of the bankrupt's property pool.[308]

[328] The next example introduces this feature.

[329] Suppose that A Co. and B Co. are the sole shareholders of C Co. Each shareholder owns fifty shares of C. Co. C Co. owns a golf course with a fair market value of $4 million. The shareholders' agreement between A Co. and B Co. stipulates that in the event one of the shareholders becomes bankrupt, the nonbankrupt shareholder has the option to purchase the bankrupt's C Co. shares for eighty percent of the shares' fair market value. Their shareholder agreement documents the commercial reasons that account for this provision. First, A Co. and B Co. do not want to do business with a trustee in bankruptcy.[309] Involving a bankruptcy trustee in the day-to-day operations of an enterprise that has to routinely make difficult decisions quickly just to survive would be disastrous. A bankruptcy trustee would not be able to respond fast enough. Second, the nonbankrupt shareholder may have a difficult time securing the funds needed to pay the bankrupt shareholder fair market value for its shares. No financial institution would do business with them when they applied for a construction loan. Funds borrowed from family and friends allowed them to build the course. Lenders will be difficult to find and more difficult to deal with. They know that owners of golf courses often go bankrupt and are poor credit risks. A small reduction in the purchase price provides the nonbankrupt shareholder with some relief from the onerous burden of paying fair market value for the bankrupt company's shares in C Co. B Co. goes bankrupt. A Co. offers to purchase B Co.'s shares in C. Co. for $1.6 million. A Co. insists that T, B Co.'s bankruptcy trustee, honor the shareholders' agreement and transfer B Co.'s shares in C Co. to A Co. T, is willing to sell B Co.'s shares in C Co. for fair market value of $2 million. A Co.

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[307] R.S.C. 1985, c. B-3, s. 71.

[308] Niven, "The Anti-deprivation Rule and the Pari Passu Rule in Insolvency", 25 Insolvency L.J. 5, 16 (2017)("The anti-deprivation rule concerns attempts to remove assets from insolvency proceedings, which reduces the value of the bankrupt estate to the detriment of creditors. The pari passu rule concerns attempts to contract out of the statutory provisions for pro rata distribution, so that one creditor receives more than his or her proper share of the available assets").

[309] A prudent lawyer may wish to incorporate a term that provides the commercial validation for an *ipso facto* term. See *Les Coopérants Société mutuelle d'assurance-vie (Liquidateur) v. Dubois*, [1996] 1 S.C.R. 900, 911-12 ("The undivided co-owners recognize that they have thus waived an action in partition or for a sale by licitation for a number of reasons of common utility, including the possibility of obtaining hypothecary financing on the office tower and the desire to avoid the costs, delays, administrative difficulties and low realized prices that would result from an action in partition or for a sale by licitation"); *Brooks v. Bankson*, 445 S.E. 2d 473, 481 (Va. Sup. Ct. 1994)("And, although the Sellers seek to justify their insertion of the $24,500 claim based on their real estate agent's advice that they should receive this amount as compensation for the loss of less than four months of the 'best selling season,' no such justification is found in the contract") & Worthington, "Good Faith, Flawed Assets and the Emasculation of the UK Anti-Deprivation Rule", 75 Mod. L. Rev. 112, 121 (2012)("[After *Belmont*] [t]here will be a dramatic increase in defensive drafting as parties attempt to ensure their deprivation provisions are well justified as commercially sensible arrangements entered into in good faith").

cannot raise $2 million. T takes the position that the *ipso facto* clause on which A Co. relies is unenforceable. T seeks advice and direction from the court.

[330] The enforcement of this term does not adversely affect the proportionate interest of each of the bankrupt shareholder's creditors. It is not an equitable distribution problem. The enforcement of the *ipso facto* term reduces the size of the pie[310] – a fundamentally different complaint.

[331] This controversy arose in a 1995 Ontario case, *Canadian Imperial Bank of Commerce v. Bramalea Inc.*[311] The solvent shopping mall partner was entitled to purchase the bankrupt partner's interest for the lesser of book value or fair market value. The difference was several million dollars.

[332] In a very brief opinion, Justice Blair[312] held that the impugned partnership term violated the "fraud upon the bankruptcy law" principle and was unenforceable.

[333] Needless to say, Justice Blair decided this case roughly fourteen years before the 2009 amendments to the *Bankruptcy and Insolvency Act* and the *Companies' Creditors Arrangement Act*[313] came into force. There is good reason to believe, based on another bankruptcy judgment of Justice Blair, that had he heard this matter after the 2009 amendments were in force he may have come to a different conclusion.[314]

[334] Justice Blair did not assess the state of the Canadian common law on *ipso facto* clauses. He assumed that *ipso facto* terms were unenforceable if their effect was the diminution of the debtor's property pool. He referred to two English cases[315] and three Canadian cases,[316] one of which the

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[310] This example engages what English judges and lawyers call the "anti-deprivation rule". *Belmont Park Investments Pty v. BNY Corporate Trustee Services Ltd.*, [2011] UKSC 38, ¶1; [2012] 1 A.C. 383, 397 per Lord Collins of Mapesbury ("The anti-deprivation rule is aimed at attempts to withdraw an asset on bankruptcy or liquidation or administration, thereby reducing the value of the insolvent estate to the detriment of creditors"). I think of it as the "bankrupt's property pool preservation principle".

[311] 33 O.R. 3d 692 (Gen. Div. 1995). He relied on *Borland's Trustee v. Steel Bros. & Co.*, [1901] 1 Ch. 279, 291 (1900)(obiter: "If I came to the conclusion that there was any provision in these articles compelling persons to sell their shares in the event of bankruptcy at something less than the price that they would otherwise obtain, such a provision would be repugnant to the bankruptcy law").

[312] 33 O.R. 3d 692, 694 (Gen. Div. 1995).

[313] R.S.C. 1985, c. C-36.

[314] *Thibodeau v. Thibodeau*, 2011 ONCA 110, ¶37; 104 O.R. 3d 161, 172 (Justice Blair applied the negative-implication cannon and refused to treat a claim for a family equalization payment in the same manner as other family law claims expressly accorded preferential status under the *Bankruptcy and Insolvency Act).*

[315] *Re Harrison*, 14 Ch. D. 19 (C.A. 1880)(the Court declared unenforceable a term in an agreement between Ms. Meade, land owner, and Mr. Harrison, builder, that upon the latter's bankruptcy all improvements and materials on the land would vest in the former).

Supreme Court of Canada subsequently reversed. Had he the benefit of the Supreme Court's opinion he may have come to another conclusion.[317]

[335] Justice Blair concluded that it was dispositive that the partnership term devalued the bankrupt's interest solely because of the partner's status as a bankrupt and violated the "'fraud on the bankruptcy law' principle".[318] The diminished value of the bankrupt's partnership interest had a direct impact on the size of the pool representing the value of the bankrupt's property available for distribution to the bankrupt's creditors. It was not consequential that the term had no adverse impact on the percentage recovery of each debtor. This was not a *pari passu* problem. The percentage claim of each creditor remained the same, only the pool was reduced.

[336] As the bankrupt's creditors have a statutory interest in the bankrupt's property, it is of central importance to the creditors that the bankruptcy trustee properly identifies the bankrupt's property and asserts control over it. It is this pool from which the bankrupt's creditors will recover a portion or all of the bankrupt's obligation to them.[319]

[337] Capital Steel did not complete the work it promised Chandos Construction that it would perform. The estimated completion costs are $22,800. There is no suggestion that Capital Steel has any claim against Chandos Construction for this amount and that it constitutes part of the bankrupt's property.

[338] The controversy is whether the contract provision that allows Chandos Construction to set-off the forfeiture amount of $137,330 and that eliminates the $126,818.39 account receivable, is unenforceable.[320]

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[316] *Re Frechette*, 138 D.L.R. 3d 61 (Que. Super. Ct. 1982)(in obiter the Court concluded that an *ipso facto* term entitling solvent shareholders to purchase a bankrupt's shares at a twenty percent discount was contrary to public policy and unenforceable); *Les Cooperants Société mutuelle d'assurance-vie (Liquidateur) v. Dubois*, 37 C.B.R. 3d 207 (Que. C.A. 1993)(the Court, in a *Winding-Up Act* application, held that an *ipso facto* term allowing a solvent co-owner to purchase the insolvent co-owner's interest at a discount was contrary to public policy and unenforceable), rev'd [1996] 1 S.C.R. 900 & *Re Knechtell Furniture Ltd.*, 56 C.B.R. (N.S.) 258 (Ont. Super. Ct. 1985)(the Court refused to enforce a pension plan *ipso facto* term).

[317] Ho, "The Treatment of *Ipso Facto* Clauses in Canada", 61 McGill L.J. 139, 167 (2015)("One can only speculate whether the result in *Bramalea* might have been different had Justice Blair had the benefit of knowing the result in *Coopérants*").

[318] 33 O.R. 3d 692, 693 (Gen. Div. 1995).

[319] *Bankruptcy and Insolvency Act*, R.S.C. 1985, c. B-3, s. 71; *Insolvency Act 1986*, c. 45, s. 306(1)(U.K.); *Corporations Act 2001*, No. 50, s. 474(1)(a) (Austl. Cth); *Bankruptcy Act 1966*, No. 33, s. 58 (Austl. Cth); *Companies Act 1993*, No. 105, s. 239U (N.Z.); *Insolvency Act 2006*, No. 55, s. 101(1)(a) (N.Z.) & *Bankruptcy Code*, 11 U.S.C., §323(a).

[320] The respondent did not argue that Chandos Construction could not set-off the forfeiture amount. It did not allege that if Chandos Construction had a claim for the forfeiture amount that it could only advance it as a general creditor. I

2. The Common Law Does Not Provide a Principled Basis for Declaring Section VII Q(d) Unenforceable

a. There Is No Canadian Common Law Rule Precluding the Enforcement of *Ipso Facto* Terms

[339] There is not now and probably never has been a Canadian common law rule that precludes the enforcement of *ipso facto* terms.[321]

[340] When amendments made to the *Bankruptcy and Insolvency Act* and the *Companies' Creditors Arrangement Act* that denied any force or effect to the natural person bankruptcy and corporate restructuring *ipso facto* terms became law in 2009 they occupied the field and displaced any common law norms regarding *ipso facto* clauses.

[341] I am also satisfied that in the period preceding the date the 2009 amendments came into force that the English fraud-on-the-bankruptcy law principle had never been a generally accepted feature of the Canadian common law. [322]

[342] Why would it be necessary for Canadian judges to introduce norms that Parliament never considered necessary to protect the core features of the *Bankruptcy and Insolvency Act*? Most judge-made law that is inspired by public-policy considerations does not buttress statutory

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proceed on the assumption that Chandos Construction is entitled to set-off the forfeiture amount if s. VII Q(d) is enforceable. See *P.I.A. Investments Inc. v. Deerhurst Ltd. Partnership*, 20 C.B.R. 4th 116, 123-24 (Ont. C.A. 2000)(the Court allowed Canadian Pacific Hotels Corporation to claim an equitable set off to defeat a claim of the receiver) & *Re Brunswick Chrysler Plymouth Ltd.*, 2005 NBQB 83, ¶42; 11 C.B.R. 5th 10, 17 ("A valid set-off will inevitably affect and alter the priorities in a bankruptcy but that is what... [s. 97(3) of the] *BIA* contemplates").

[321] Professor Wood notes that "the 'fraud upon the bankruptcy law' principle … can be traced back to the eighteenth century in England but … has been applied [in Canada] in only a handful of cases over the past century". Wood, "Direct Payment Clauses and the Fraud Upon the Bankruptcy Law Principle: *Re Horizon Earthworks Ltd. (Bankrupt)*", 52 Alta. L. Rev. 171, 171 (2014). Ms. Ho made the same point in her excellent article "The Treatment of *Ipso Facto* Clauses in Canada", 61 McGill L.J. 139, 164 (2015): "Despite the principle's longstanding history in English jurisprudence, the rule has not been widely applied by Canadian courts. ... [There is] little Canadian law that applies the anti-deprivation rule". This condition no doubt prompted her observation that the "validity [of the anti-deprivation rule] in Canada ... is debatable". Id. 163.

[322] Judge-made law evolves to meet the modern needs of the community it serves. States separated by thousands of miles and developments reflecting unique social, economic and political patterns may have special needs that demand the emergence of features that distinguish their judge-made law from that in force in another common law country that has many shared values. See *Paciocco v. Australia and New Zealand Banking Group Ltd.*, [2016] HCA 28, ¶¶7 & 9; 258 C.L.R. 525, 539 per French, C.J. ("The countries of the common law world have a shared heritage which they owe to the unwritten law of the United Kingdom. That shared heritage offers the undoubted advantage, but does not import the necessity, of development proceeding on similar lines. ... The common law in Australia is the common law of Australia").

frameworks.[323] It modifies other judge-made laws. Judicial refusal to enforce contract terms that promote criminal conduct[324] or racist values[325] are examples of this condition.

[343] Perhaps the explanation for the English judges' decision to introduce the fraud-on-the-bankruptcy law principle several centuries ago[326] was the skeletal nature of early English bankruptcy statutes compared to their modern counterparts. "The anti-deprivation rule originally developed before the enactment of the modern statutory schemes governing bankruptcy, including in particular the wide statutory powers for the challenge of pre-bankruptcy transactions".[327] In addition, the early bankruptcy models were very decidedly pro-creditor in their orientation[328] and the judges of that time may have believed that the fraud-on-the-bankruptcy-law principle was consistent with the thrust of the statutory model.

[344] Regardless of the reasons why seventeenth and eighteenth century English judges thought public policy compelled them to act, it is undeniable that the conditions that exist in Canada today are fundamentally different from those that were present in England hundreds of years ago.[329]

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[323] E. Farnsworth, Contracts 318 (4th ed. 2004) ("These policies have many bases. Some are grounded on moral values, as are the policies against the impairment of family relationships and against gambling. Some are based on economic notions, as are the policies against restraint of trade and against restraints on alienation of property. Some arise from a desire to protect the institutions of government, as do the policies against encouraging litigation or otherwise interfering with the judicial process and those against improperly influencing legislators and other government officials").

[324] See J. Côté, An Introduction to the Law of Contract 107-26 (1974).

[325] *Re Drummond Wren*, [1945] 4 D.L.R. 674, 679 (Ont. H.C.) (the Court refused to enforce a restrictive covenant under which the land purchaser promised not to sell "to Jews or persons of objectionable nationality" on the basis that it was "void as against public policy").

[326] *Higinbotham v. Holme*, 34 Eng. Rep. 451 (Ex. Ct. 1812).

[327] Niven, "The Anti-deprivation Rule and the Pari Passu Rule in Insolvency", 25 Insolvency L.J. 5, 19 (2017).

[328] C. Tabb, The Law of Bankruptcy 40 (2d ed. 2009). Courts could sentence fraudulent bankrupts to death after the 1705 passage of *An Act to prevent Frauds frequently committed by Bankrupts*. 4 & 5 Anne, c. 4, s. 19. The *Capital Punishment Act 1820*, 1 Geo. 4, c. 115, s. 1 repealed the death penalty provisions. See generally B. Montagu, Thoughts upon the Abolition of the Punishment of Death, in Cases of Bankruptcy (1821).

[329] *Pope Manufacturing Co. v.Gormully*, 144 U.S. 224, 233-34 (1892) per Brown J. ("It is impossible to define with accuracy what is meant by that public policy for an interference and violation of which a contract may be declared invalid. It may be understood in general that contracts which are detrimental to the interests of the public as understood at the time fall within the ban. The standard of such policy is not absolutely invariable or fixed, since contracts which at one stage of our civilization may seem to conflict with public interests, at a more advanced stage are treated as legal and binding") *& Newfoundland and Labrador v. AbitibiBowater Inc.*, 2012 SCC 67, ¶47; [2012] 3 S.C.R. 443, 467 (the Court acknowledged that insolvency legislation often responds to evolving social conditions). See Reben, "Legislative and Judicial Confusion Concerning Executory Contracts in Bankruptcy", 89 Dick. L. Rev. 1029, 1034 (1985)("In ancient India and Nepal ... a creditor fasted at his debtor's door pending satisfaction of the debt, presuming that no debtor would allow his creditor to starve to death. Ancient Hindu law allowed a creditor to seize his debtor and force him to work off his debt. Alternatively, a creditor could maim or kill the debtor, confine his wife, sons, or cattle, or besiege him in his own home").

[345] In any event, the Supreme Court of Canada has never recognized and applied the fraud-on-the-bankruptcy-law principle.[330] Indeed, it has implicitly held that it does not exist.[331]

[346] My research reveals that only one provincial appeal court – the Court of Appeal of Ontario[332] – has applied this norm. It did so in a very short opinion without explaining why.

[347] There are only a few lower court decisions that have applied or acknowledged the existence of this principle.[333] "The anti-deprivation rule ... has not been widely used [in Canada]".[334]

[348] I will first examine the top court's jurisprudence.

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[330] In *Hobbs, Osborne & Hobbs v. Ontario Loan and Debenture Co.*, 18 S.C.R. 483, 504, an 1890 appeal, Justice Strong referred to the fraud-on-the-bankruptcy-law principle in English common law when there was no bankruptcy legislation in Canada. This was not an insolvency case. Professor Wood reports that "Canada had no bankruptcy law at all during the period from 1880 to 1919." R. Wood, Bankruptcy and Insolvency Law 34 (2d ed. 2015).

[331] *Les Coopérants Société mutuelle d'assurance-vie (Liquedateur) v. Dubois*, [1996] 1 S.C.R. 900.

[332] *Trustee of Aircell Communications Inc. v. Bell Mobility Cellular Inc.*, 2013 ONCA 95; 14 C.B.R. 6th 276. See also *P.I.A. Investments Inc. v. Deerhurst Ltd. Partnership*, 20 C.B.R. 4th 116, 127 (Ont. C.A. 2000)(the Court acknowledged that *Canadian Imperial Bank of Commerce v. Bramalea Inc.* discussed the fraud-on-the-bankruptcy law principle) & *Re Wetmore*, [1924] 4 D.L.R. 66, 76 (N.B. Sup. Ct. App. Div.) (the Court, in obiter, acknowledged the fraud-on-the-bankruptcy-law principle).

[333] See *National Bank of Canada v. Scollard Energy Ltd.*, 2018 ABQB 126, ¶55 (the Court, relying on *Canadian Imperial Bank of Commerce v. Bramalea Inc.*, assumed that the anti-deprivation principle was a feature of the current Canadian common law); *Re Westerman (Bankrupt)*, 1998 ABQB 946; 8 C.B.R. 4th 313 (Master Quinn held that a partnership term reducing a bankrupt partner's capital payout by fifty percent could not thwart a claim by the bankrupt's trustee for payout of the full capital account), rev'd on other grounds, 1999 ABQB 708; 275 A.R. 114 (the Court of Queen's Bench expressed its agreement with *Canadian Imperial Bank of Commerce v. Bramalea Inc*.); *1183882 Alberta Ltd. v. Valin Industrial Mill Installations Ltd.*, 2011 ABQB 440, ¶44; 521 A.R. 281, 289 (the Court did not recognize the "fraud upon the bankruptcy law" as a principle with broad effect: "In my view, it is inappropriate to paint all insolvency proceedings with the same broad brush without regard to the nature of the proceedings, the effects of the impugned covenant, and all other relevant circumstances"), aff'd, 2012 ABCA 62, ¶8; 64 Alta. L.R. 5th 163, 170 (the Court expressly declined to comment on any bankruptcy or insolvency issues); *Canadian Imperial Bank of Commerce v. Bramalea Inc.*, 33 O.R. 3d 692, 694 (Gen. Div. 1995) ("The principle is sometimes referred to as that of 'fraud upon the bankruptcy law', by which is meant not necessarily 'fraud' in the sense of dishonesty or impropriety, but fraud in the effect"); *Re Knechtel Furniture Ltd.*, 56 C.B.R. (N.S.) 258 (Ont. Super. Ct. 1985) (the Court held that a pension plan term allocating a surplus to the pension plan beneficiaries on the bankruptcy of the employer could not be invoked to deny the bankrupt's trustee claim to the portion of the surplus attributable to the bankrupt's contribution); *Re Frechette*, 42 C.B.R. (N.S.) 50 (Que. Super. Ct. 1982)(the Court held that a shareholders agreement term that obliged a bankrupt shareholder to sell his shares for eighty-percent of their fair market value could not be enforced against the bankrupt shareholder's bankruptcy trustee) *& Re Barrington & Vokey Ltd.*, 48 C.B.R. 3d 270 (N.S. Sup. Ct. 1996) (the Court refused to enforce a construction subcontract term that allowed a general contractor to use subcontractor property that was on the site when the subcontractor became bankrupt).

[334] Ho, "The Treatment of *Ipso Facto* Clauses in Canada", 61 McGill L.J. 139, 170 (2015). See also Niven, "The Anti-deprivation Rule and the Pari Passu Rule in Insolvency", 25 Insolvency L.J. 5, 6 (2017) ("There is little case law in New Zealand on the anti-deprivation rule").

[349] In *A.N. Bail Co. v. Gingras*,[335] the case referred to earlier, there was no dispute as to what amounts the general contractor owed the bankrupt subcontractor. The controversy turned on whether the general contractor could pay these undisputed amounts to the bankrupts' creditors as opposed to the bankruptcy trustee, notwithstanding the bankrupt's proprietary interest in the accounts receivable. There was a leap-frogging term in the contract that sanctioned this payment. Section 71 of the *Bankruptcy and Insolvency Act* expressly stipulates that the bankrupt's property immediately vests in the bankruptcy trustee and, without a doubt, prohibited this payment. There was no need to resort to the common law to resolve the question.[336] And the Court did not.

[350] The Supreme Court of Canada's opinion in *Les Coopérants Société mutuelle d'assurance-vie (Liquidateur) v. Dubois*[337] leads me to conclude that that Canadian common law does not incorporate the English fraud-on-the-bankruptcy law principle. Co-owners of Quebec real property agreed that there would be no partition of the properties for thirty-five years and that if one of the co-owners obtained a court liquidation order, the solvent co-owner could purchase the insolvent co-owner's interest for seventy-five percent of the market value. A co-owner, under the *Winding-Up Act*,[338] applied for the appointment of a liquidator, no doubt convinced that the *ipso facto* term was prejudicial to the bankrupt's creditors' interests.[339] The solvent co-owner invoked the sale provision. The liquidator applied to the Quebec Superior Court for a declaration that the mandatory-sale term was unenforceable against the liquidator.

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[335] [1982] 2 S.C.R. 475.

[336] See *International Air Transport Assoc. v. Ansett Australia Holdings Ltd. (subject to a Deed of Company Arrangement)*, [2008] HCA 3, ¶76; 234 C.L.R. 151, 181 ("the Clearing House arrangements ... operated as to give British Eagle an asset, the money claim against Air France, and that in the face of the mandatory operation of s. 302 of the *Companies Act 1948* (UK), this asset could not be captured for the netting-off system. ... No recourse to 'public policy' would be called for").

[337] [1996] 1 S.C.R. 900.

[338] R.S.C. 1985, c. W-11. "The *Winding Up Act* had been enacted in 1882 in order to deal with insolvent companies". R. Wood, Bankruptcy and Insolvency Law 35 (2d ed. 2015). The *Winding-Up Act* became the *Winding-Up and Restructuring Act* in 1996. *An Act to Amend, Enact and Repeal Certain Laws Relating to Financial Institutions*, S.C. 1996, c. 6, s. 133. "The *Winding-Up and Restructuring Act* ... is the only insolvency regime that can be used in connection with the insolvency of banks, insurance companies, trust companies, and loan companies". R. Wood, Bankruptcy and Insolvency Law 16 (2d ed. 2015).

[339] See *Perpetual Trustee Co. v. BNY Corporate Trustee Services Ltd.*, [2009] EWCA Civ 1160, ¶¶86 & 148; [2010] Ch. 347, 384-85 per Lord Neuberger, M.R. ("as BBCW must pay market value (indeed, at least market value) for the shares, the [anti-deprivation] rule cannot be engaged") & 401 per Patten L.J. ("An option to acquire shares in the event of bankruptcy is not objectionable on the grounds of public policy unless the price paid for the shares would constitute an undervalue").

[351] Justice Trudel declared that the mandatory-sale term was binding and enforceable against the insolvent co-owner and the liquidator. In effect, he concluded that the bankrupt co-owner did not have a property interest in the twenty-five percent discount. Part of his reasons follow:[340]

> [T]he undivided co-owners took care that disorder would not ensue and protected themselves from the difficulties that would result should one of them become insolvent. They … [protected] themselves from the coerciveness of a judicial sale and [avoided] having a new partner imposed on them. They limited or eliminated the right to assign their shares and included in the contracts a mechanism and conditions for terminating the indivision.
>
> There was no reason they could not provide … for the future resolution of the contract in the event that either of them failed to fulfil his or its obligations. *Bankruptcy* and winding-up are events upon which an obligation may validly be conditional and there was nothing to prevent the co-owners from providing in advance for the termination of indivision in such a case. …
>
> In addition, the clauses ... relating to default, mandatory or default sale and partition or sale by licitation are in no way contrary to public order or good morals.

[352] The likelihood that Justice Trudel would have referred to both bankruptcy and winding-up regimes when discussing an insolvency topic had he not assumed that they share fundamental feature is very low.

[353] The Quebec Court of Appeal allowed the liquidator's appeal.[341] Justice Beauregard, for the Court, opined that "[i]f this way of proceeding were allowed, security law would serve no purpose".[342] He stated that there must be an orderly distribution of a debtor's property under both the *Winding-Up Act* and the *Bankruptcy and Insolvency Act*.[343]

[354] Justice Beauregard must have concluded that the contested *ipso facto* term deprived the bankrupt co-owner of its interest in the full value of the property and that this term was unenforceable.

[355] Nothing in Justice Beauregard's opinion suggests that he disagreed with the proposition that the *Bankruptcy and Insolvency Act* and the *Winding-Up Act* have comparable foundational values.

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[340] [1992] R.J.Q. 2574, 2577-78 (emphasis added).

[341] [1994] R.J.Q. 55; 37 C.B.R. 3d 207.

[342] Id. 57.

[343] Id. 58.

[356] The Supreme Court agreed with Justice Trudel and reversed the Quebec Court of Appeal.[344]

[357] Justice Gonthier wrote for the Court.

[358] His judgment displays two themes.

[359] First, he emphasized at the outset the fact that the terms to which the liquidator objected were "the contractual will of the two parties, both of whom were knowledgeable about real estate investments".[345] Later, he again emphasized the underlying importance of freedom-of-contract values:[346]

> The principle that must guide the court in exercising its discretion in such a case is that of respect for contracts signed in good faith prior to the winding-up, unless the obligations contained therein are prejudicial to the other creditors and give rise to an unjust preference in light of all the circumstances, in which case equitable relief will be available.

[360] Second, Justice Gonthier confirmed that the purpose of the *Winding-Up Act* "is to arrange for the closing down of the company's business in an orderly and expeditious manner while minimizing, as far as possible, the losses and harm suffered by both the creditors and other interested parties and by distributing the assets in accordance with the Act".[347]

[361] Justice Gonthier adopted a common-sense approach to this problem. He asked whether "the harm caused to the other unsecured creditors would be disproportionate to the harm caused to the appellant, given the nature of his claim, by a failure to comply with the agreements and would create an unjust preference in his favour".[348]

[362] Satisfied that the enforcement of the contested terms would not impose on the unsecured creditors of the insolvent co-owner a measure of harm disproportionate to that the solvent co-owner would endure if deprived of the right to rely on the contested term, Justice Gonthier found in the solvent co-owner's favour.

[363] There is no direct or indirect reference to the fraud-on-the-bankruptcy principle or any of the case law on the topic, including the *Bramalea* case, in Justice Gonthier's opinion. It is hard to square this with the notion that the fraud on the bankruptcy principle plays an important role in Canada's insolvency law.

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[344] [1996] 1 S.C.R. 900.

[345] Id. 912.

[346] Id. 918.

[347] Id. 915-16.

[348] Id. 919.

[364] I will now refer to the one case out of the Ontario Court of Appeal that does acknowledge the fraud-on-the-bankruptcy principle.

[365] In *Trustee of Aircell Communications Inc. v. Bell Mobility Cellular Inc.*,[349] the Court, in a fourteen-paragraph opinion, declared that a term in a dealership contract relieving Bell Mobility of the obligation to pay Aircell Communications $188,981 for outstanding commissions upon the latter's bankruptcy was unenforceable against the bankrupt's trustee. The Court, relying on *Canadian Imperial Bank of Commerce v. Bramalea Inc.*,[350] assumed that there was a fraud-on-the-bankruptcy-law principle in force in Canada. But, as noted above, the 1995 judgment also assumed that the principle should be applied in Canada. The Court of Appeal gave no consideration to the effect s. 84.2 of the *Bankruptcy and Insolvency Act* or s. 34 of the *Companies' Creditors Arrangement Act* had on the enforceability of corporate *ipso facto* terms or the effect of *Les Coopérants Société mutuelle d'assurance-vie (Liquidateur) v. Dubois*[351] on the issue before it. Neither of these statutory provisions were in force when Justice Blair decided *Bramalea*.

[366] There is only one Alberta case the outcome of which turned on the application of the fraud-on-the-bankruptcy law principle.[352]

[367] It is *Re Westerman (Bankrupt)*, a 1998 case.[353] At issue was the enforceability of a law-partnership term that reduced a bankrupt partner's capital account by fifty percent. Master Quinn ordered the law firm to pay the bankrupt's trustee 100 percent of the former partner's capital account. He did so because "[t]o allow the partnership to take 50% of what is probably the bankrupt's largest available asset would be to grant an unjust preference to the partnership".[354] To have reached this conclusion the Master must have concluded that the *ipso facto* term did abridge the bankrupt's property interest in his capital account and that the term was unenforceable.

[368] The law firm successfully appealed to the Court of Queen's Bench.[355] While Justice Agrios sided with the law firm on another ground and disposed of the appeal on that basis, he made this

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[349] 2013 ONCA 95; 14 C.B.R. 6th 276.

[350] 33 O.R. 3d 692 (Gen. Div. 1995).

[351] [1996] 1 S.C.R. 900.

[352] Justice Topolniski adverted to the fraud-on-the-bankruptcy law principle in *1183882 Alberta Ltd. v. Valin Industrial Mill Installations Ltd.*, 2011 ABQB 440, ¶¶34-42; 521 A.R. 281, 288-89, but she did not apply it. Whether a lessee had a right to acquire the leased premises or not would have no impact on any creditors of the lessee. Justice Topolniski held that "the only persons affected by the Insolvency Clause are [the lessee] and ... [the lessor]. The creditors have not been prejudiced. Consequently, the higher principle of safeguarding the integrity of the insolvency system in these circumstances does not override the parties' freedom of contract". 2011 ABQB 440, ¶47; 521 A.R. 281, 290.

[353] 1998 ABQB 946; 8 C.B.R. 4th 313.

[354] Id. at ¶23; 8 C.B.R. 4th at 318.

[355] 1999 ABQB 708; 275 A.R. 114.

obiter observation:[356] "I accept the proposition that a provision in a partnership agreement which reduces value from creditors is void as it violates the public policy of equitable and fair distribution amongst unsecured creditors in insolvency situations". He cited the *Bramalea* case as authority for this proposition.

[369] Justice Agrios made this observation roughly ten years before s. 84.2 of the *Bankruptcy and Insolvency Act* and s. 34 of the *Companies' Creditors Arrangement Act* came into force.

[370] Enforcing the law partnership insolvency term would not in any way adversely affect the percentage payment the bankrupt's creditors would receive, assuming that the law partnership was not a creditor of the bankrupt. But its enforcement as against the bankruptcy trustee would reduce the size of the bankrupt's property pool. This must have been the concern that troubled Justice Agrios.

b. The English Common Law Has Changed

[371] There is no historical consensus as to the scope of the English fraud-on-the-bankruptcy law principle.[357]

[372] Some judges have held that it has sufficient vigor to deprive contract terms of their plain and ordinary meaning if the *effect* of the term is the diminution of the bankrupt's property pool to the detriment of the bankrupt's creditors.[358] For these judges there is a bankrupt's

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[356] Id. at ¶6; 275 A.R. at 115.

[357] *Money Markets Ltd. v. London Stock Exchange*, [2002] 1 W.L.R. 1150, 1182 (Ch. 2001) ("it is not possible to discuss a coherent rule, or even an entirely coherent set of rules, to enable one to assess in any particular case whether such a provision (a 'deprivation provision') falls afoul of the principle").

[358] *Re Johns*, [1928] 1 Ch. 737, 748 (Ch.) (the Court declared unenforceable a mortgage term that benefitted the mortgagee if the mortgagor declared bankruptcy: "[A mortgagee] cannot make a bargain with the mortgagor which secures to him, the mortgagee, a greater advantage if the mortgagor becomes bankrupt than he would get if he does not"); *Ex p. Barter*, 26 Ch. D. 510 (C.A. 1884) (the Court declared void and unenforceable a provision in a shipbuilding contract that allowed the buyer, on the bankruptcy of the ship builder, to claim control of the ship and ownership of any materials of the ship builder intended for use in constructing the ship); *Ex p. Jay*, 14 Ch. D. 19, 25 (C.A. 1880)(the Court declared unenforceable a term in the building agreement that transferred title to the owner to all building material on the property on the bankruptcy of the builder: "a simple stipulation that, upon a man's becoming bankrupt, that which was his property up to the date of the bankruptcy should go over to someone else and be taken away from his creditors, is void as being a violation of the policy of the bankrupt law"); *Ex p. Mackay*, L.R. 8 Ch. App. 643 , 647 (1873)(the Court declared unenforceable a term that allowed the bankrupt's creditor to maintain all royalties payable to the bankrupt until the bankrupt's debt to the creditor was extinguished: "a man is not allowed, by stipulation with a creditor, to provide for a different distribution of his effects in the event of bankruptcy from that which the law provides. ... [T]his is a clear attempt to evade the operation of the bankruptcy laws"); *Whitmore v. Mason*, 70 Eng. Rep. 1031, 1034 (Ch. 1861) (the Court declared unenforceable a mining partnership agreement that transferred a bankrupt partner's interest to the solvent partners for a discounted rate: "the law is too clearly settled to admit of a shadow of a doubt that no person possessed of property can reserve that property to himself until he shall become bankrupt, and then provide that, in the event of his coming bankrupt, it shall pass to another and not to his creditors") & *Higinbotham v. Holme*, 34 Eng. Rep. 451, 453 (Ch. 1811) (the Court declared unenforceable a trust provision that

property-pool-preservation rule that has teeth. A contract term that has the effect of reducing the bankrupt's property pool is unenforceable.

[373] On the other hand, there is a group of judges who gave the contested text its plain and ordinary meaning unless it is obvious that the parties set out to defeat the purpose of the bankruptcy status.[359] This cohort denies there is an *ipso facto* rule.

[374] The House of Lord's 1975 judgment in *British Eagle International Airlines Ltd. v. Compagnie Nationale Air France*[360] illustrates the nature of the judicial divide.

[375] British Eagle was an airline operator that held a membership in the International Air Transportation Association. IATA operated a clearing house that on a monthly basis tabulated whether each member was in a positive or negative position with another member airline. An airline that provided services of a greater value than the other member provided to it was in a positive position with respect to the other airline. That same airline might be in a negative position with other airlines. At the end of the month IATA would assess the overall position of all the member airlines. It would collect funds from members in a negative position and pay the members in a positive position.[361] By the term of the clearing house rules a member could not maintain a claim against another; the claim was against IATA. The clearing house rules functioned the same way without regard to whether a member was in liquidation.

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terminated the settlor's interest in the trust property on his becoming a bankrupt, in favour of his wife: "this is a direct fraud upon the Bankrupt Laws ... I cannot assimilate this to the case of the wife's property limited until the bankruptcy of her husband; or to the case of a lease made determinable by the bankruptcy of the lessee").

[359] *Money Markets International Stockbrokers Ltd. v. London Stock Exchange Ltd.*, [2002] 1 W.L.R. 1150 (Ch. D. 2001)(the Court declared enforceable a rule of the London Stock Exchange that cancelled the membership of a member that failed to fulfil its obligation to a fellow L.S.E. member and transferred the bankrupt's share to the L.S.E. for no consideration); *Re Apex Supply Co.*, [1942] Ch. 108, 114 (Ch. 1941) (the Court upheld a term in a hire-purchase agreement that obliged the hirer to pay an additional sum if the hirer went into liquidation and the owner retook possession of the goods: "[I]t would be extravagant, in my view, to suggest that the clause is aimed at defeating the bankruptcy laws or at providing for a distribution differing from that which the bankruptcy laws permit"); *Bombay Official Assignee v. Shroff*, 48 T.L.R. 443, 446 (P.C. 1932)(Bombay)(the Privy Council held that a stock broker whose membership in the stock exchange was terminated because he was unable to meet his obligations to his fellow members had no interest that could be passed on to an insolvency assignee); *Borland's Trustee v. Steel Bros. & Co.*, [1901] 1 Ch. 279 (Ch. 1900)(the Court enforced a term in a company's articles of incorporation compelling a bankrupt shareholder to sell its shares to a particular person at a fair price) & *Ex p. Newitt*, 16 Ch. D. 522, 531 (C.A. 1881)(the Court enforced a term in a lease agreement between the lessor/owner and the lessee/builder providing that the lessor/owner may terminate the lease on the bankruptcy of the lessee and claim ownership of all the builder/lessee's property left on the premises: "The broad general principle is that the trustee in bankruptcy takes all the bankrupt's property, but takes it subject to all the liabilities which affected it in the bankrupt's hands, unless the property which he takes as the legal personal representative of the bankrupt is added to by express provision of the bankruptcy law").

[360] [1975] 1 W.L.R. 758.

[361] Id. 762-63 per Lord Morris & 772 & 775 per Lord Cross.

[376] British Eagle went into liquidation in 1968. The liquidator of British Eagle commenced an action against Air France for the difference of the value of the services British Eagle rendered to Air France and the value of the services Air France rendered to British Eagle in an accounting period during which British Eagle was insolvent. It alleged that this amount was the property of British Eagle under s. 302 of the *Companies Act 1948*.[362] Air France denied that it owed British Eagle anything.

[377] Both the trial judge,[363] the Court of Appeal[364] and two law lords[365] were of the view that the IATA clearing house rules that deprived British Eagle of any property interests against member airlines were enforceable as against British Eagle's liquidator.

[378] Three law lords held the opposite view. They ignored the ordinary meaning of the clearing house rules, convinced that these provisions were contrary to public policy, and classified Air France's obligation to British Eagle as s. 302 property.[366] As a result, the creditors of British Eagle were declared to be entitled to the positive differential as between British Eagle and Air France. The *effect* of the clearing house rules on other creditors of British Eagle was the litmus test for invalidity.

[379] Lord Cross gave the judgment that reflected the majority's opinion. The key passage in his speech follows:[367]

> [T]he respondents are saying …that the parties to the "clearing house" arrangements by agreeing that simple contract debts are to be satisfied in a particular way have succeeded in "contracting out" of the provisions contained in section 302 [of the *Companies Act 1948*] for the payment of unsecured debts "pari passu". In such a context it is to my mind irrelevant that the parties to the "clearing house" arrangements had good business reasons for entering into them and did not direct their minds to the question how the arrangements might be affected by the insolvency of one or more of the parties. Such a "contracting out" must, to my mind, be contrary to public policy.

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[362] *Companies Act 1948*, c. 38, s. 302 ("Subject to the provision of this Act as to preferential payments, the property of a company shall, on the winding-up, be applied in satisfaction of its liabilities pari passu").

[363] [1973] 1 Lloyd's Rep. 414.

[364] [1974] 1 Lloyd's Rep. 429, 434 ("[Insolvency] laws require that the property of an insolvent company shall be distributed pro rata among its unsecured creditors: but the question here is whether the claim asserted against Air France is property of British Eagle. In our judgment it is not").

[365] Lord Morris & Lord Simon. The Australian High Court, in *International Air Transport Assoc. v. Ansett Australian Holdings Ltd.*, [2008] HCA 3; 234 C.L.R. 151, held that IATA was the creditor of an insolvent airline member, unlike the majority of the House of Lords.

[366] [1975] 1 W.L.R. 758, 781 per Lord Cross.

[367] Id. 780.

[380] Lord Morris followed a different path.[368] He was satisfied that "[t]here is no trace in the scheme of any plan to divert money in the event of a liquidation".[369] He gave effect to the ordinary meaning of the clearing house rule. Lord Morris held that Air France was not indebted to British Eagle and that British Eagle had no property interest that the liquidator could attach:[370]

> I see no reason to think that the contracts which were entered into by the members of the Clearing House offended against the principles of our insolvency laws. ... Services rendered during October and the first few days of November were in my view rendered under perfectly lawful contracts which were made in the same way as contracts had been made for years past. Because of the terms of the contracts which were made the Appellants had no claims against and no rights to sue other individual members of the Clearing House. It is a general rule that a trustee or liquidator takes no better title to property than that which was possessed by a bankrupt or a company. In my view the liquidator ... cannot remould contracts which were validly made.

[381] Lord Simon of Glaisdale expressed his "entire" agreement with Lord Morris and added this gloss:[371]

> Since this was a bona fide commercial transaction, and not a "deliberate device" to give a preference on liquidation, nor was that "the whole scope and object" of the interline agreement, nor its "dominant intention", nor was it "aimed at anything of that kind", the liquidator of British Eagle has no higher claim than the company had before liquidation.

[382] In 2011 the United Kingdom Supreme Court abandoned the ground the majority of the House of Lords occupied when deciding *British Eagle International Airlines Ltd. v. Compagnie Nationale Air France*.[372] Writing for six of the seven justices hearing *Belmont Park Investments Pty Ltd. v. BNY Corporate Services Ltd.*,[373] Lord Collins adopted a new test that increased the likelihood significantly that *ipso facto* terms would be enforced.[374] This new standard placed much

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[368] Id. 769.

[369] Id. 763.

[370] Id. 769.

[371] Id. 771.

[372] [1975] 1 W.L.R. 758.

[373] [2011] UKSC 38; [2012] 1 A.C. 383. For an excellent discussion of *Belmont* see Niven, "The Anti-deprivation Rule and the Pari Passu Rule in Insolvency", 25 Insolvency L.J. 5 (2017).

[374] Professor Worthington much prefers the American approach to *ipso facto* clauses. "The pivotal issue ... is defining when party autonomy must give way to the insolvency-triggered deprivation rule ... . The answer, surely, and as Lord Mance would have it, is that it must give way every time the parties' agreement avoids the normal operation of the

greater importance on the freedom of contract values and much less emphasis on the anti-deprivation or pool-protection rule that underlies bankruptcy legislation. Now a court must ask if the contract under review reveals an intention to evade the insolvency laws, as the following extract from Lord Collin's speech documents:[375]

> [C]ommercial sense and absence of intention to evade insolvency laws have been highly relevant factors in the application of the anti-deprivation rule. Despite statutory inroads, party autonomy is at the heart of English commercial law. Plainly there are limits to party autonomy … because the interests of third party creditors will be involved. But … it is desirable that, so far as possible, the courts give effect to contractual terms which parties have agreed. And there is a particularly strong case for autonomy in cases of complex financial instruments ... .
>
> No doubt that is why, except in the case of a blatant attempt to deprive a party of property in the event of liquidation ... the modern tendency has been to uphold commercially justifiable contractual provisions which have been said to offend the anti-deprivation rule ... . The policy behind the anti-deprivation rule is clear, that the parties cannot, on bankruptcy, deprive the bankrupt of property which would otherwise be available for creditors. It is possible to give that policy a common sense application which prevents its application to bona fide commercial transactions which do not have as their predominant purpose, or one of their main purposes, the deprivation of the property of one of the parties on bankruptcy.
>
> …
>
> The security was in commercial reality provided by the noteholders to secure what was in substance their own liability, but subject to terms, including the provisions for noteholder priority and swap counterparty priority, in a complex commercial transaction entered into in good faith. There has never been any suggestion that those provisions were deliberately intended to evade insolvency law.

[383] The Supreme Court was keenly aware that the law already enforced forfeiture-on-bankruptcy terms in land leases[376] and terms that identified the bankruptcy of the

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insolvency statute". Worthington, "Good Faith, Flawed Assets and the Emasculation of the UK anti-Deprivation Rule", 75 Mod. L. Rev. 112, 115-16 (2012).

[375] Id. at ¶¶103, 104 & 109; [2012] 1 A.C. at 421 & 422. See also id at ¶151; [2012] 1 A.C. at 434 per Lord Mance ("The more difficult question concerns the character of transaction and the state of mind which will attract the operation of the anti-deprivation principle. In my opinion, the court has to make an objective assessment of the purpose and effect of the relevant transaction or provision in bankruptcy").

[376] Id. at ¶85; [2012] 1 A.C. at 417 per Lord Collins ("The lease cases show that such a provision is regarded by the law as effective to bring the lease to an end whether the lease is expressed (a) to run "until bankruptcy" or (b) as a lease with "a proviso for forfeiture" in that event. The result has not depended upon linguistic differences of expression") &

grantee or beneficiary as the event terminating the grantee's or beneficiary's interest.[377] In other words, the new *Belmont Park Investment* test increases the likelihood that *ipso facto* terms would be enforced and complements specific rules that had been in force for centuries.[378]

[384] The English common law anti-deprivation rule did not apply to limited interests. This meant that *ipso facto* terms relating to leases and licenses could be enforced.[379]

c. The Common Law Should Enforce Corporate *Ipso Facto* Terms That Serve Reasonable and Defensible Commercial Purposes

[385] If I erred in concluding that the fraud-on-bankruptcy principle is not a part of the Canadian common law after 2009, I would adopt the essential components of the standard that Lord Collins introduced in *Belmont Park Investments Pty. Ltd. v. BNY Corporate Services Ltd.*[380] His formulation celebrates the primacy of party autonomy and freedom of contract values.

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id at ¶123; [2012] 1 A.C. at 425 per Lord Walker ("There are some reasonably well demarcated areas in which it is clear that the [anti-deprivation rule] principle does not apply. One is the grant of a lease, in which the reservation of a power of re-entry and forfeiture in the event of bankruptcy is standard practice, is unquestionably valid, and is recognised by statute").

[377] Id. at ¶86; [2012] 1 A.C. at 417 per Lord Collins ("licences of intellectual property expressed to determine (or to be determinable on notice) on bankruptcy of the licensee are valid; and interests under protective trusts granted by the settlor to a beneficiary until the beneficiary's bankruptcy") & id. at ¶124; [2012] 1 A.C. at 425 per Lord Walker ("a settlor can validly settle his own property so as to confer on another person an interest terminable on the bankruptcy of that other person"). See *Re Bailey*, 11 C.B.R. 399 (Ont. H. Ct. 1930), aff'd, 11 C.B.R. 444 (App Div. 1930)(the Court enforced a provision in a will that paid trust fund income to the testator's son so long as the son was not a bankrupt and the testator's grandson if the son became a bankrupt).

[378] Judge Peck of the Bankruptcy Court of the Southern District of New York came to the opposite conclusion on the same facts in *Lehman Brothers Holdings Inc. v. BNY Corporate Trustee Services Ltd.*, 422 B.R. 407 (S.D.N.Y 2010). The *Bankruptcy Code* compelled this result. 422 B.R. 407, 420 ("The Court finds that the provision in the Transaction Documents purporting to modify LBSF's right to a priority distribution solely as a result of a chapter 11 filing constitute unenforceable *ipso facto* clauses").

[379] Sections 65.1(2) and 84.2(2) of the *Bankruptcy and Insolvency Act* specifically state that *ipso facto* terms relating to leases are of no force or effect. While s. 65.1(2) also refers to licensing agreements, no mention is made of them in s. 84.2, the bankruptcy *ipso facto* provision. Ms. Ho suggests that the omission may be inconsequential "Although it is only section 65.1(2) of the *BIA* that mentions licenses, it is unlikely that *ipso facto* provisions would be enforceable under ... [s. 84.2(2) because it uses] the term "agreement" ... Licenses might fall under the term "agreement". Section 65.1 was enacted first, as part of the 1992 amendments, and so it may have been overly careful drafting". Ho, "The Treatment of *Ipso Facto* Clauses in Canada", 61 McGill L.J. 139, 180 (2015).

[380] [2011] UKSC 38; [2012] 1 A.C. 383. Professor Wood, one of Canada's leading insolvency scholars, favors the effects-based test. Professor Wood is of the view that the effects-based test is consistent with the "tide of legislative reform in Canada" and Justice Blair's 1995 *Bramalea* decision. R. Wood, Bankruptcy and Insolvency Law 89-90 (2d ed. 2015). But this argument cuts both way. While it is true that s. 84.2 of the *Bankruptcy and Insolvency Act* denies the force of natural person *ipso facto* clauses, because of their adverse effects on the bankrupt's estate, it is equally true that the *Bankruptcy and Insolvency Act* does not declare corporate *ipso facto* terms unenforceable. As I assert below, if

[386] Lord Collins' model denies enforceability only to *ipso facto* clauses that manifest a blatant attempt to hijack the bankrupt's property and defeat the legitimate interests of the bankrupt's creditors memorialized in the bankruptcy statute. It accords full force and effect to *ipso facto* terms that serve reasonable and defensible commercial purposes.

[387] There is no compelling reason to deny a corporate bankruptcy *ipso facto* term its full effect if its most important feature is the advancement of a reasonable and defensible commercial purpose and it bestows on the nonbankrupt party a benefit that is not significantly greater than is necessary to promote the nonbankrupt party's legitimate commercial interests.

[388] This formulation represents a modest infringement on party autonomy and freedom of contract values and it acknowledges the legislative primacy on a topic that is the subject of comprehensive statutory regulation both by the *Bankruptcy and Insolvency Act*[381] and the *Companies' Creditors Arrangement Act.*[382]

[389] Under these circumstances, an effects-based test is not very appealing.

[390] I return to the golf course example to illustrate the application of this norm. Both A Co. and B Co. agreed that the bankruptcy of one would trigger an option to purchase the bankrupt's shares in C Co. for eighty percent of fair market value - $1.6 million. This strikes me as an eminently defensible transaction that ought not to be set aside. There were reasonable and defensible commercial purposes that explained the term's value to A Co. and B Co. The enforcement of the corporate bankruptcy *ipso facto* term did not bestow on A Co. a benefit that was significantly greater than is necessary to promote A Co.'s legitimate commercial interests. Its presence was not a sign of a blatant attempt to undermine important interests of the bankrupt's creditors.

[391] But suppose that the corporate bankruptcy *ipso facto* term gave A Co. the option to purchase the bankrupt's shares for one-tenth of fair market value. In the absence of a cogent explanation in the shareholders agreement for this significant haircut, the likelihood that an adjudicator would conclude that the benefit this bestows on A Co. is significantly greater than is necessary to protect A Co.'s legitimate commercial interests increases significantly.

Parliament had intended to ban corporate *ipso facto* provisions, it would have said so. It is also important to remember that Justice Blair decided *Bramalea* fourteen years before the 2009 amendments came into force. There is a good reason to question whether Justice Blair would have come to a different conclusion had the case been resolved after 2009.

[381] R.S.C. 1985, c. B-3, s. 84.2.

[382] R.S.C. 1985, c. C-36, s. 34.

[392] If this standard were applied to the facts in *Canadian Imperial Bank of Commerce v. Bramalea Inc.*,[383] the *ipso facto* term relied on by the nonbankrupt partner may well be suspect.

[393] Commercial certainty is a neutral factor when assessing both the effects-based and commercial-purposes tests. Each of them contain features that make the result predictable. They are bright-line standards. The difference is that they rest at opposite ends of the likelihood-of-enforcement spectrum. Utilization of an effects-based test will deny most *ipso facto* terms of any force. Adoption of the commercial-purposes standard will have the opposite impact – most corporate *ipso facto* terms will be enforced.

d. Section VII Q(d) Serves a Reasonable and Defensible Commercial Purpose and Is Enforceable

[394] Section VII Q(d) is enforceable.

[395] Its only purpose is to promote the commercial interests of Chandos Construction. Capital Steel's bankruptcy will undoubtedly inconvenience Chandos Construction and cause it to divert management and administrative resources to deal with Capital Steel's unexpected absence from the condominium project.

[396] There is no basis whatsoever to support an allegation that this term is the embodiment of an intention to undermine the statutorily recognized interests of Capital Steel's creditors.

[397] I am satisfied that s. VII Q(d)'s most important feature is the advancement of a reasonable and defensible commercial purpose and that its enforcement does not bestow a benefit on Chandos Construction that is significantly greater than is necessary to protect Chandos Construction's legitimate commercial interests.

3. The *Bankruptcy and Insolvency Act* Does Not Provide a Statutory Basis for Declaring Section VII Q(d) Unenforceable

[398] If there is a Canadian common law relating to *ipso facto* terms and the Ontario Court of Appeal's judgment in *Trustee of Aircell Communications Inc.*[384] correctly states the common law, views I reject, it follows that s. VII Q(d) is inconsistent with this effects-based standard.

[399] Under this scenario, and only this scenario, is it necessary to consider whether the *Bankruptcy and Insolvency Act* provides a complete code for the regulation of bankruptcy *ipso*

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[383] 33 O.R. 3d 692 (Gen. Div. 1995).

[384] 2013 ONCA 95; 14 C.B.R. 6th 276. Contra *Perpetual Trustee Co. v. BNY Corporate Trustee Services Ltd.*, [2009] EWCA Civ 1160; [2010] Ch. 347 (the Court rejected the effects-based test) & *International Air Transport Assoc. v. Ansett Australia Holdings Ltd. (Subject to Deed of Company Arrangement)*, [2008] HCA 3, ¶¶27-29; 234 C.L.R. 151, 168-69 per Gleeson CJ (the Court rejected the effects-based test).

facto terms and deprives the common law relating to bankruptcy *ipso facto* clauses of any residual force.

[400] There is no express provision in the *Bankruptcy and Insolvency Act* that declares corporate bankruptcy *ipso facto* terms of no force.

[401] A fundamental principle of bankruptcy law is that it does not alter private law rights unless a specific provision in the *Bankruptcy and Insolvency Act* has this effect.[385]

[402] There are three important statutory interpretation principles that must be considered.

[403] The first is that legislators are presumed to know the law – statutory and judge made.[386] Legislation designed to ameliorate the effect of the common law cannot be effective unless the legislators have a sound understanding of its strengths and weaknesses. The common law is frequently the backdrop for legislative forays.[387]

[404] The first principle explains why I canvassed the Canadian jurisprudence to ascertain whether there was a generally recognized common law fraud-on-the-bankruptcy-law principle, and if so, its characteristics.[388] I concluded that there was no generally recognized Canadian common law on this topic.

[405] No more need be said about the first principle.

[406] The second sound principle is that a statute does not change the common law unless the text clearly reveals this purpose.[389]

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[385] R. Wood, Bankruptcy and Insolvency Law 6 (2d ed. 2015).

[386] *Frame v. Smith*, [1987] 2 S.C.R. 99, 112 per La Forest J. ("There is ... [a] presumption that the Legislature must be taken to have known the pre-existing law").

[387] *Cuthbertson v. Rasouli*, 2013 SCC 53, ¶18; [2013] 3 S.C.R. 341, 356 ("The Common Law Backdrop") & *2747-3174 Québec Inc. v. Quebec*, [1996] 3 S.C.R. 919, 972 per L'Heureux-Dubé, J. (the common law is a "basic fabric" or "background canvas").

[388] *2747-3174 Québec Inc. v. Quebec*, [1996] 3 S.C.R. 919, 978 per L'Heureux-Dubé, J. ("To determine what interaction there is between the common law and statute law, it is necessary to begin by analysing, identifying and setting out the applicable common law, after which the statute law's effect on the common law must be specified by determining what common law rule the statute law codifies, replaces or repeals, whether the statute law leaves gaps that the common law must fill and whether the statute law is a complete code that excludes or supplants all of the common law in the specific area of law involved") & *Cuthbertson v. Rasouli*, 2013 SCC 53, ¶22; [2013] 3 S.C.R. 341, 358 ("Many provinces found the common law regime for the treatment of incapable patients unsatisfactory and devised new approaches through legislation").

[389] *Slaight Communications Inc. v. Davidson*, [1989] 1 S.C.R. 1038, 1077 ("in the absence of a clear provision to the contrary, the legislator should not be assumed to have intended to alter the pre-existing ordinary rules of common law"); *The Queen v. Corbett*, [1988] 1 S.C.R. 670, 700-01 per McIntyre J. ("To admit such a discretion would be

[407] If my determination that the fraud-on-the-bankruptcy-law principle is not a part of the Canadian common law is correct, this principle does not come into play. There is no common law to change.

[408] But if this assessment is incorrect and the fraud-on-the-bankruptcy-law principle is an integral part of the Canadian common law, the next logical inquiry is this: Does the text of the *Bankruptcy and Insolvency Act* clearly reveal an intention to alter the common law?

[409] In order to answer this query, consideration must be given to the third important statutory interpretation principle – the negative-implication canon. A text that attaches either positive or negative consequences to one thing and makes no mention of related things implies that the consequences linked to the existence of other things does not attach to the unmentioned other thing.[390]

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tantamount to holding that Parliament could not by clear legislative enactment alter the common law"); *Schiell v. Morrison*, [1930] 2 W.W.R. 737, 741 (Sask. C.A. 1930) ("if it is clear that [the legislature intended] ... to abrogate the common law ... the provisions of the statute must prevail"); *Canada v. Khosa*, 2009 SCC 12, ¶50; [2009] 1 S.C.R. 339, 373 per Binnie, J. ("I readily accept, of course, that the legislature can by clear and explicit language oust the common law in this as in other matters"); *Ocean Port Hotel Ltd. v. British Columbia*, 2001 SCC 52, ¶27; [2001] 2 S.C.R. 781, 796 ("Where the intention of the legislature, as here, is unequivocal, there is no room to import common law doctrines of independence"); *Valard Construction Ltd. v. Bird Construction Co.*, 2016 ABCA 249, n. 150; 57 C.L.R. 4th 171, n. 150 per Wakeling, J.A. ("A statute does not alter the common law unless a fair reading supports the contrary conclusion"); R. Sullivan, Sullivan on the Construction of Statutes 538-39 (6th ed. 2014)("Although legislation is paramount, it is presumed that legislatures do not intend to interfere with common law rights ... or generally to change the policy of the common law") & A. Scalia & B. Garner, Reading Law: The Interpretation of Legal Texts 319 (2012)("statutes will not be interpreted as changing the common law unless they effect the change with clarity. ... [T]he alteration of prior law must be clear – but it need not be express, nor should its clear implication be distorted").

[390] *Century Services Inc. v. Canada*, 2010 SCC 60, ¶¶45-46; [2010] 3 S.C.R. 379, 406-07 ("there is no express statutory basis for concluding that GST claims enjoy a preferred treatment under the ... [*Companies' Creditors Arrangement Act*] or the ... [*Bankruptcy and Insolvency Act*]. Unlike source deductions, which are clearly and expressly dealt with under both these insolvency statutes, no such clear and express language exists in these Acts carving out an exception for GST claims. ... The internal logic of the ... [*Companies' Creditors Arrangement Act*] also militates against upholding the ... [*Excise Tax* Act] deemed trust for GST. The ... [*Companies' Creditors Arrangement Act*] imposes limits on a suspension by the court of the Crown's rights in respect of source deductions but does not mention the ... [*Excise Tax Act*] ... . Since source deductions deemed trusts are granted explicit protection under the ... [*Companies' Creditors Arrangement Act*], it would be inconsistent to afford a better protection to the ... [*Excise Tax Act*] deemed trust absent explicit language in the ... [*Companies' Creditors Arrangement Act*]"); *Schreyer v. Schreyer*, 2011 SCC 35, ¶20; [2011] 2 S.C.R. 605, 617 (the Court expressly approved the following statement from *Thibodeau v. Thibodeau*, 2011 ONCA 110, ¶37; 104 O.R. 3d 161, 172: "unsecured creditors are to be treated equally and the bankrupt's assets to be distributed amongst them equally subject to the scheme provided in s. 136 of the ... [*Bankruptcy and Insolvency Act*]. *Parliament has not accorded any preferred or secured position to a [family law] claim for an equalization payment. While it has recently chosen to amend the ... [Bankruptcy and Insolvency Act] to give certain debts or liabilities arising in relation to claims for support and/or alimony a preferred status, Parliament has made no such provision for equalization claims in relation to family property*") (emphasis in original); *Newfoundland and Labrador v. AbitibiBowater Inc.*, 2012 SCC 67, ¶33; [2012] 3 S.C.R. 443, 462 ("If Parliament had intended that the debtor always satisfy all remediation costs, it would have granted the Crown a priority with respect to the totality of

[410] Suppose that railway-safety legislation declares that railroads must equip locomotives and passenger cars with heart defibrillator machines. The negative-implication canon supports the conclusion that the statute lists all the rolling stock that must have heart defibrillators on them and that no other type of rolling stock must be so equipped. This means that the railroads have no statutory obligation to place these expensive machines on freight cars or any other rolling stock that is not either a locomotive or a passenger car. A related inference is that the text would have listed freight cars and cabooses had the legislators intended the statute to apply to them.

[411] Section 84.2(1) of the *Bankruptcy and Insolvency Act* attaches specific consequences to a natural person's bankruptcy.[391] It prohibits a party who has a contract with a bankrupt natural

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the debtor's assets. ... [T]he fact that the Crown's priority under s. 11.8(8) of the ... [*Companies' Creditors Arrangement Act]* is limited to the contaminated property and certain related property leads me to conclude that to exempt environmental orders would be inconsistent with the insolvency legislation"); *Grigby v. Oakes*, 126 Eng. Rep. 1420, 1422 (Ex. Ct. 1801) per Heath J. ("the several provisions of the [recently passed *Bank Act*] making ... [Bank of England notes] good legal tender in certain excepted cases excludes the idea of their being so generally in cases not provided for by the act") & per Chambre, J. ("If the legislature have not gone far enough, it is for them, not for us to remedy the defect. Indeed, making bank notes a good tender in certain cases specifically provided for, they appear to me to have negatived the construction we are now desired to put upon the act"); *Patrolmen's Benevolent Assoc. v. City of New* York, 359 N.E. 2d 1338, 1341 (N.Y. Ct. App. 1976)("Had the Legislature intended that the wage freeze also apply to situations involving judicially mandated salary increases, they were free, assuming *arguendo* constitutional validity, to draft appropriately worded legislation … . We could but note that the statute in question was adopted some two months after the July 1 judgment requiring that the city pay the salary increase and we must assume the Legislature was well aware of this fact when the statute was passed. Other statutes, adopted at the same time as the wage freeze law and also seeking to alleviate the financial plight of the city, by their very terms have specific application to judgments"); R. Sullivan, Sullivan on the Construction of Statutes 248 (6th ed. 2014) ("An implied exclusion argument lies whenever there is reason to believe that if the legislature had meant to include a particular thing within its legislation, it would have referred to that thing expressly. Because of this expectation, the legislature's failure to mention the thing becomes grounds for inferring that it was deliberately excluded. Although there is no express exclusion, exclusion is implied"); Corry, "Administrative Law and the Interpretation of Statutes", 1 U. Toronto L.J. 286, 298 (1936) ("if Parliament in legislating speaks only of specific things and specific situations, it is a legitimate inference that the particulars exhaust the legislative will") & A. Scalia & B. Garner, Reading Law: The Interpretation of Legal Texts 107 (2012) ("The [negative-implication] doctrine applies only when ... the thing specified ... can reasonably be thought to be an expression of *all* that shares in the grant or prohibition involved") (emphasis in original).

[391] Sections 365(e)(1) and 541(c)(1)(B) of the *Bankruptcy Code* does so for natural person and corporate *ipso facto* terms. See *Lehman Brothers Holdings Inc. v. BNY Corporate Trustee Services Ltd.,* 422 B.R. 407, 414-15 (S.D.N.Y 2010)("The Bankruptcy Code of 1978 effected a change in the treatment of contract or lease clauses that would seek to modify the relationships of contracting parties due to the filing of a bankruptcy petition-so-called *ipso facto* clauses. ... It is now axiomatic that *ipso facto* clauses are, as a general matter, unenforceable"); *Reloeb Co. v. LTV Corp,* 1993 U.S. Dist. LEXIS 6130, 15-16 ("Section 365 [of the *Bankruptcy Code*] abrogates the power of *ipso facto* clauses. No default may occur pursuant to an *ipso facto* clause and no reliance may be placed upon an alleged default where the only cause for default is the debtor's commencement of a bankruptcy case") & *Lyons Savings & Loan Assoc. v. Westside Bancorporation, Inc.,* 828 F. 2d 387, 393 n 6 (7th Cir. 1987) ("Section 365(e) of the *Bankruptcy Code* invalidates *ipso facto* or bankruptcy termination clauses which permit one contracting party to terminate or even modify an executory contract or unexpired lease in the event of the bankruptcy of the other contracting party"). See also *Bankruptcy Act 1966* (Cth), No. 33, s. 301 (1)(a) (Austl.) ("A provision in a contract or agreement for the sale of

person from terminating or amending the agreement "by reason only of the individual's bankruptcy". It also prohibits a counterparty from invoking a provision in the agreement that obliges the bankrupt natural person to make an accelerated payment or forfeit something to which the bankrupt natural person is otherwise entitled. Section 84.2(5) expressly declares that "[a]ny provision in an agreement that has the effect of providing for, or permitting, anything that, in substance, is contrary to this section is of no force or effect".[392]

[412] No other provision of the *Bankruptcy and Insolvency Act* attached comparable consequences like those recorded in s. 84.2 to corporate *ipso facto* clauses.

[413] Section 34 of the *Companies' Creditors Arrangement Act* declares that corporate restructuring *ipso facto* terms are of no force or effect.

[414] Parliament's decision to treat corporate bankruptcy and receiverships differently than natural person bankruptcies and corporate restructuring might be attributable, as Ms. Ho suggests, to the fact that "the debtor is not expected to continue as a going concern and its assets are simply awaiting liquidators. In contrast, in a proceeding under the *CCAA*, the objective is for the debtor company to successfully restructure, so there is greater concern to maintain the statutes quo."[393]

[415] What is the consequence of this disparate treatment of natural person and corporate *ipso facto* clauses and corporate restructuring *ipso facto* terms?

[416] Professor Wood opines that "[i[f the debtor is a corporation or other artificial entity, the validity of the provision will be determined through the application of the common law anti-deprivation principle".[394]

[417] I cannot agree.

[418] Parliament, with the introduction in 2009[395] of s. 84.2 of the *Bankruptcy and Insolvency Act* and s. 34 of the *Companies Creditors' Arrangement Act*, has occupied the field[396] and the common

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property, in a lease of property, in a hire-purchase agreement, in a licence or in a PPSA security agreement to the effect that ... the contract, agreement, lease, hire-purchase agreement, license or PPSA security agreement is to terminate ... if the purchaser, lessee, hirer, licensee or PPSA grantor or debtor becomes a bankrupt or commits an act of bankruptcy ... under this Act is void").

[392] This is an example of a statutory provision that explicitly declares an agreement inconsistent with the statute unenforceable. As Professor Farnsworth explains, "[t]he court's function ... is merely statutory interpretation"). E. Farnsworth, Contracts 315 (4th ed. 2004).

[393] Ho, "The Treatment of *Ipso Facto* Clauses in Canada", 61 McGill L.J. 139, 182 (2015).

[394] R. Wood, Bankruptcy and Insolvency Law 179 (2d ed. 2015). No explanation is provided for this assertion.

[395] *Economic Recovery Act (Stimulus),* S.C. 2009, c. 31, s. 64.

[396] *Century Services Inc. v. Canada*, 2010 SCC 60, ¶13; [2010] 3 S.C.R. 379, 393 ("The [*Bankruptcy and Insolvency Act*] ... offers a self-contained legal regime providing for both reorganization and liquidation"). See also *Perpetual*

law on *ipso facto* clauses, whatever form it assumed, is not applicable. Because the *Bankruptcy and Insolvency Act* does not declare corporate *ipso facto* terms unenforceable, they must be enforced as written.[397]

[419] I am unable to conclude that Parliament's failure to declare corporate *ipso facto* terms unenforceable supports any other inference but that it came to the conclusion that these provisions were not sufficiently harmful, if at all, to the integrity of the bankruptcy regime to warrant the same treatment as s. 84.2 accords natural person *ipso facto* terms and s. 34 gives corporate restructuring *ipso facto* terms.[398]

[420] Parliament's decision to establish a separate regime for natural person and corporate bankruptcy *ipso facto* terms and not follow the framework American[399] and Australian[400] legislators favor is indisputable evidence that Parliament does not regard corporate *ipso facto* clauses as a significant threat to the welfare of Canada's corporate bankruptcy regime.[401]

[421] If Parliament had intended the skeletal Canadian common law on *ipso facto* terms to apply to corporate *ipso facto* clauses, it would have said so.[402] Given the paucity of pre-2009 cases on this

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Trustee Co. v. BNY Corp. Trustee Services Ltd.,[2009] EWCA Civ 1160, ¶172; [2010] Ch. 347, 410 per Patten L.J. ("Whatever may have been the position in the nineteenth century, the Insolvency Act now contains a detailed code for determining and regulating the property of a bankrupt or insolvent company for the benefit of its general creditors. The *Act* itself says and does all that is necessary. ...When Parliament has expressly considered the categories of transactions which should not be allowed to survive bankruptcy or liquidation I can see no proper basis on which the court can arrogate to itself the right to widen the sanction of invalidity so as to encompass transactions which the application of the Insolvency Act would leave untouched. That should be something for the legislature alone to decide").

[397] *Bankruptcy Code*, 11 U.S.C. §§ 365(e) & 541(c) (most corporate *ipso facto* terms are unenforceable); *Lehman Brothers Holdings Inc. v. BNY Corporate Trustee Services Ltd.*, 422 B.R. 407, 415 (S.D.N.Y. 2010)("It is now axiomatic that *ipso facto* clauses are, as a general matter, unenforceable") & *Treasury Laws Amendment (2017 Enterprise Incentives No. 2) Act*, No. 112 (Austl. Cth)(prohibits the enforcement of some corporate *ipso facto* clauses).

[398] See *Century Services Inc. v. Canada*, 2010 SCC 60, ¶¶45-46; [2010] 3 S.C.R. 379, 406-07 (the Court refused to grant the Crown priority to GST claims, given that the applicable insolvency legislation expressly accorded priority to Crown claims over source deduction funds held by the insolvent debtor and made no mention of GST claims) & *Newfoundland and Labrador v. AbitibiBowater Inc*., 2012 SCC 67; [2012] 3 S.C.R. 443(the Court concluded that the Crown's priority under the *Companies' Creditors Arrangement Act* was restricted to contaminated property, as expressly stated in the Act, and not all remediation costs, which was not stated in the Act).

[399] *Bankruptcy Code*, 11 U.S.C. §§ 363, 365(e) & 541(c).

[400] *Bankruptcy Act 1966*, No. 33, s. 301 (Cth) & *Treasury Laws Amendment (2017 Enterprise Incentives No. 2) Act*, No. 112 (Cth).

[401] See Parliament of the Commonwealth of Australia, House of Representatives, Treasury Laws Amendment (2017 Enterprise Incentives No. 2) Bill 2017 Explanatory Memorandum, Chptr 2.

[402] E.g., *Bankruptcy Code*, 11 U.S.C. §510(c)(1) ("the Court may ... under principles of equitable subordination, subordinate for purposes of distribution all or part of an allowed claim to all or part of another allowed claim"). See C.

topic, I cannot conclude that the common law was sufficiently developed to justify Parliamentarians relying on it for any purpose. If the common law was hostile to *ipso facto* provisions, why did Parliament have to legislate in 2009 to prohibit their enforcement in the context of natural person bankruptcies?[403] In the United States a comprehensive ban on the enforcement of *ipso facto* terms was introduced in 1978 because courts regularly applied *ipso facto* terms.[404]

[422] As well, there are several mechanisms built into the *Bankruptcy and Insolvency Act* that are designed to protect the bankrupt's estate or property pool. For example, as Professor Wood notes "[t]he trustee has a variety of powers that can be used to impeach pre-bankruptcy transactions".[405] If Parliamentarians believed that the prohibition of corporate bankruptcy *ipso facto* terms was a sound pool-preservation measure, would the *Bankruptcy and Insolvency Act* not have said so? Yes.

[423] In short, the *Bankruptcy and Insolvency Act* occupies the field.[406] Natural person bankruptcy *ipso facto* terms captured by s. 84.2 are unenforceable. Corporate bankruptcy *ipso*

Tabb, The Law of Bankruptcy 723 (2d ed. 2009) ("Codification of the doctrine of equitable subordination ... was not intended either to alter existing practice or to freeze the doctrine in place").

[403] I accept Professor Wood's observation that s. 84.2 of the *Bankruptcy and Insolvency Act* rejected "the traditional exclusion of determinable interests such as leases and intellectual property licences". R. Wood, Bankruptcy and Insolvency Law 90 (2d ed. 2015). But s. 84.2 has wider scope than this.

[404] The *Bankruptcy Reform Act of 1978,* Pub. L. No. 95-598, 92 Stat. 2549 prohibited the enforcement of *ipso facto* terms. Previously courts had routinely enforced *ipso facto* clauses. C. Tabb, The Law of Bankruptcy 854 (2d ed. 2009) & *In Re Chateaugay Corp.*, 1993 U.S. Dist. LEXIS 6130, 14 (S.D.N.Y) ("The Bankruptcy Code of 1978 effected a change in the treatment of contract or lease clauses that modify the relationships of contracting parties due to the filing of a bankruptcy petition. Although such clauses were enforced prior to 1978, the new code rendered unenforceable contract provisions that altered the rights or obligations of a debtor as a result of the debtor's commencement of a case under the Bankruptcy Code. ... Section 365 [of the Bankruptcy Code] abrogates the power of *ipso facto* clauses").

[405] R. Wood, Bankruptcy and Insolvency Law 188 (2d ed. 2015).

[406] *Frame v. Smith*, [1987] 2 S.C.R. 99, 112 ("It seems obvious to me that the Legislature intended to devise a comprehensive scheme for dealing with these [family law custody] issues. If it had contemplated additional support by civil action, it would have made provision for this, especially given the rudimentary state of the common law"); *1183882 Alberta Ltd. v. Valin Industrial Mill Installation Ltd.*, 2012 ABCA 62, ¶34; 64 Alta. L.R. 5th 163, 176 per McDonald, J.A. ("This principle [common law anti-deprivation rule] has been largely codified in section 65.1 of the ... *Bankruptcy and Insolvency Act*") & *Foley v. Imperial Oil Ltd.*, 2011 BCCA 262, ¶29; [2011] 9 W.W.R. 652, 661-62 ("The [*Occupier's Liability*] *Act* provides a complete code regarding the duty of an occupier of land. Reference to earlier common law cases ... may ... result in legal error if the wrong standard of care (one based on the common law categories) is applied, rather than the statutory standard of care"). The United Kingdom Supreme Court came to a different conclusion in *Belmont Park Investments Pty Ltd. v. BNY Corporate Trustee Services Ltd.*,[2011] UKSC 38; [2012] 1 A.C. 383. Lord Collins of Mapesbury said this: "The anti-deprivation rule is too well-established to be discarded despite the detailed provisions set out in modern insolvency legislation, all of which must be taken to have been enacted against the background of the rule". Id at ¶102; [2012] 1 A.C. at 421. As noted above, the anti-deprivation is not a "well-established" feature of Canadian bankruptcy law. Several lower court opinions that apply a principle does not justify the claim that the principle is "well-established". *Valard Construction Ltd. v. Bird Construction Co.*, 2016 ABCA 249, ¶172; 57 C.L.R. 4th 171, 231 per Wakeling, J.A. ("It is not obvious to me that

facto terms that do not contravene any provisions of the *Bankruptcy and Insolvency Act* are valid and enforceable.[407]

[424] A prohibition against corporate bankruptcy *ipso facto* clauses may be sound, but this is an assessment that Parliament must make.[408] Until Parliament acts, the courts must respect party autonomy and the freedom of contract and enforce corporate bankruptcy *ipso facto* terms.

VII. Conclusion

[425] I would dismiss the appeal.

Appeal heard on November 28, 2017

Reasons filed at Edmonton, Alberta
this 29th day of January, 2019

Wakeling J.A.

Alberta courts have ever applied *Dominion Bridge* and that Alberta's construction community has proceeded on the assumption that a labour and material performance bond trustee has no obligation to take reasonable measures to bring the bond's existence to the attention of beneficiaries or potential beneficiaries") & 2018 SCC 8, ¶23 per Brown, J. ("case authorities from a single province [do not constitute a practice in an industry]"). See also *Official Assignee v. NZL Life Superannuation Nominees Ltd.*, [1995] 1 N.Z.L.R. 684, 691-92 (H. Ct. 1994)(the Court rejected the defendant's argument that the *Insolvency Act 1867* constituted a complete code and that an *ipso facto* term was enforceable unless the enactment said otherwise).

[407] Ho, "The Treatment of *Ipso Facto* Clauses in Canada", 61 McGill L.J. 139, 173 (2015)("Corporate bankrupts and receiverships are notable exceptions from these provisions governing *ipso facto* clauses in the *BIA* and *CCAA*, which suggests that such clauses are still enforceable in both of these cases").

[408] *Schreyer v. Schreyer*, 2011 SCC 35, ¶38; [2011] 2 S.C.R. 605, 625 ("The best way to address the potentially inequitable impact of bankruptcy law on the division of family assets would be to amend the ... [*Bankruptcy and Insolvency Act*]"); *Sun Indalex Finance, LLC v. United Steelworkers*, 2013 SCC 6, ¶82; [2013] 1 S.C.R. 271, 316 ("courts should not use equity to do what they wish Parliament had done through legislation"); *Zeitel v. Ellscheid*, [1994] 2 S.C.R. 142, 152 ("It is beyond the power of a court to interfere in a carefully crafted legislative scheme merely because it does not approve of the result produced by a statute in a particular case") & *Money Markets Ltd. v. London Stock Exchange*, [2002] 1 W.L.R. 1150, 1175 (Ch. 2001)("This argument could be said to have particular force in light of the sophisticated and detailed legislative apparatus enshrined in the *Insolvency Act 1986* and *Insolvency Rules 1986*").

Appearances:

V.L. Merritt
for the Appellant

D.R. Bieganek, Q.C.
for the Respondent

TAB 3

Chandos Construction Ltd. *Appellant*

v.

Deloitte Restructuring Inc. in its capacity as Trustee in Bankruptcy of Capital Steel Inc., a bankrupt *Respondent*

and

Attorney General of Canada, Canadian Association of Insolvency and Restructuring Professionals and Insolvency Institute of Canada *Interveners*

Chandos Construction Ltd. *Appelante*

c.

Restructuration Deloitte Inc. en sa qualité de syndic de faillite de Capital Steel Inc., une faillie *Intimée*

et

Procureur général du Canada, Association canadienne des professionnels de l'insolvabilité et de la réorganisation et Institut d'insolvabilité du Canada *Intervenants*

Indexed as: Chandos Construction Ltd. *v.* Deloitte Restructuring Inc.

2020 SCC 25

File No.: 38571.

2020: January 20; 2020: October 2.

Present: Wagner C.J. and Abella, Moldaver, Karakatsanis, Côté, Brown, Rowe, Martin and Kasirer JJ.

Répertorié : Chandos Construction Ltd. *c.* Restructuration Deloitte Inc.

2020 CSC 25

N° du greffe : 38571.

2020 : 20 janvier; 2020 : 2 octobre.

Présents : Le juge en chef Wagner et les juges Abella, Moldaver, Karakatsanis, Côté, Brown, Rowe, Martin et Kasirer.

ON APPEAL FROM THE COURT OF APPEAL FOR ALBERTA

Bankruptcy and insolvency — Anti-deprivation rule — Priority of claims — Clause in subcontract awarding fee to general contractor in the event of subcontractor's bankruptcy — Subcontractor filing assignment in bankruptcy prior to completing subcontract — Whether general contractor entitled to set fee off against amount owing to subcontractor — Whether anti-deprivation rule exists at common law — If so, whether clause invalid by virtue of anti-deprivation rule.

Chandos Construction Ltd. ("Chandos"), a general construction contractor, entered into a construction subcontract with Capital Steel Inc. ("Capital Steel"). Clause VII Q(d) of the subcontract provides that Capital Steel will pay Chandos 10 percent of the subcontract price as a fee for the inconvenience or for monitoring the work in the event of Capital Steel's bankruptcy. When Capital Steel filed an assignment in bankruptcy prior to completing its

EN APPEL DE LA COUR D'APPEL DE L'ALBERTA

Faillite et insolvabilité — Règle anti-privation — Priorité des créances — Clause d'un contrat de sous-traitance prévoyant l'octroi de frais à l'entrepreneur général en cas de faillite du sous-traitant — Dépôt d'une cession de biens par le sous-traitant avant l'achèvement des travaux — L'entrepreneur général a-t-il le droit de compenser les frais et de les soustraire du montant qu'il doit au sous-traitant? — La règle anti-privation existe-t-elle en common law? — Si oui, la clause est-elle invalide en raison de la règle anti-privation?

Chandos Construction Ltd. (« Chandos »), un entrepreneur général en construction, a conclu un contrat de sous-traitance en construction avec Capital Steel Inc. (« Capital Steel »). La clause VII Q(d) du contrat de sous-traitance prévoit que Capital Steel doit payer à Chandos 10 p. 100 du prix du contrat de sous-traitance à titre de frais pour les dérangements ou pour la surveillance des travaux advenant la faillite de Capital Steel. Lorsque cette dernière a procédé

subcontract with Chandos, Chandos argued it was entitled to set off the costs it had incurred to complete Capital Steel's work and to set off 10 percent of the subcontract price, as provided for by clause VII Q(d). Capital Steel's trustee in bankruptcy applied for advice and directions as to whether clause VII Q(d) was valid. The application judge found the provision to be a valid liquidated damages clause, but the Court of Appeal reversed the decision.

Held (Côté J. dissenting): The appeal should be dismissed.

Per Wagner C.J. and Abella, Moldaver, Karakatsanis, Brown, Rowe, Martin and Kasirer JJ.: Clause VII Q(d) is invalid by virtue of the anti-deprivation rule. This rule renders void any provision in an agreement which provides that upon an insolvency (or bankruptcy), value is removed from the reach of the insolvent person's creditors which would otherwise have been available to them, and places that value in the hands of others.

The anti-deprivation rule has existed in Canadian common law since before federal bankruptcy legislation existed, and has not been eliminated by any decision of the Court or by Parliament. Parliament's actions are better understood as gradually codifying limited parts of the common law rather than seeking to oust all related common law. The anti-deprivation rule prevents contractual provisions from frustrating the scheme of the *Bankruptcy and Insolvency Act* ("*BIA*") as it renders void contractual provisions that would prevent property from passing to the trustee. This helps maximize the global recovery for all creditors in accordance with the priorities set out in the *BIA*.

The test under the anti-deprivation rule has two parts: the relevant clause is triggered by an event of insolvency or bankruptcy, and the effect of the clause is to remove value from the insolvent's estate. This is an effects-based test. What should be considered is whether the effect of the contractual provision was to deprive the estate of assets upon bankruptcy, not whether the intention of the contracting parties was commercially reasonable. Adopting a purpose-based test would create new and greater difficulties. It would require courts to determine the intention of contracting parties long after the fact, detract from the efficient administration of corporate bankruptcies, and encourage parties who can plausibly pretend to have *bona fide* intentions to create a preference over other creditors by inserting such clauses. It would also be inconsistent

à une cession de ses biens avant de terminer son contrat de sous-traitance avec Chandos, celle-ci a soutenu qu'elle avait le droit de compenser les coûts qu'elle avait engagés pour terminer les travaux commencés par Capital Steel et de déduire 10 p. 100 du prix du contrat de sous-traitance, comme le prévoit la clause VII Q(d). Le syndic de faillite de Capital Steel a demandé des conseils et des directives quant à la validité de la clause VII Q(d). Le juge de première instance a conclu que la stipulation est une clause de dommages-intérêts liquidés valide, mais la Cour d'appel a infirmé la décision.

Arrêt (la juge Côté est dissidente) : Le pourvoi est rejeté.

Le juge en chef Wagner et les juges Abella, Moldaver, Karakatsanis, Brown, Rowe, Martin et Kasirer : La clause VII Q(d) est invalide en raison de la règle anti-privation. Cette règle rend nulle toute stipulation d'un contrat qui prévoit qu'en cas d'insolvabilité (ou de faillite), la valeur des actifs à laquelle les créanciers de la personne insolvable auraient autrement accès est réduite, et place cette valeur entre les mains d'autres personnes.

La règle anti-privation existait déjà dans la common law canadienne avant qu'il n'existe de loi fédérale en matière de faillite, et elle n'a été éliminée, ni par une décision de la Cour, ni par le Parlement. Les interventions du Parlement doivent être considérées comme codifiant graduellement certains aspects de la common law, plutôt que comme cherchant à écarter tous les principes de common law connexes. La règle anti-privation empêche de contourner, au moyen de stipulations contractuelles, le régime de la *Loi sur la faillite et l'insolvabilité* (« *LFI* »), puisqu'elle rend nulles les stipulations qui empêchent que des biens soient dévolus au syndic. Cela contribue à maximiser le recouvrement global pour tous les créanciers en conformité avec les priorités énoncées dans la *LFI*.

Le test applicable à la règle anti-privation comporte deux volets : l'application de la clause pertinente est déclenchée par une insolvabilité ou une faillite, et la clause a pour effet de réduire la valeur de l'actif de la personne insolvable. Ce test est fondé sur les effets. La question sur laquelle il faut se pencher est celle de savoir si l'effet de la stipulation était de réduire la valeur de l'actif en cas de faillite, et non celle de savoir si l'intention des parties contractantes était raisonnable sur le plan commercial. L'adoption d'un test fondé sur l'objet aurait pour effet de créer des difficultés nouvelles plus grandes. Cela obligerait les tribunaux à déterminer l'intention des parties contractantes bien après les faits, nuirait à l'administration efficace des faillites d'entreprise et encouragerait les parties qui peuvent plausiblement prétendre être de bonne foi à

with the general principles of contractual freedom — parties do not negotiate with a view to protecting the interests of their creditors in the event of their bankruptcy. Finally, under a purpose-based rule, unsecured creditors would receive even less than they do now. An effects-based approach provides parties with the confidence that contractual agreements, absent a provision providing for the withdrawal of assets upon bankruptcy or insolvency, will generally be upheld.

Clause VII Q(d) violates the anti-deprivation rule and is thus void. It provides that, in the event Capital Steel commits any act of bankruptcy, Capital Steel shall forfeit 10 percent of the subcontract price — this is a direct and blatant violation of the rule. It cannot be rescued by the law of set-off, as set-off only applies to enforceable debts or claims. It applies to debts owed by the bankrupt that were not triggered by the bankruptcy, since the anti-deprivation rule only makes deprivations triggered by insolvency unenforceable.

Per Côté J. (dissenting): There is agreement with the majority that the anti-deprivation rule has a longstanding and strong jurisprudential footing in Canadian law and that it has not been eliminated by the Court or through legislation. However, this rule should not apply to transactions or contractual provisions which serve a *bona fide* commercial purpose. As clause VII Q(d) furthers a *bona fide* commercial purpose, it is enforceable and does not offend the anti-deprivation rule. Accordingly, the application judge's order should be restored.

The anti-deprivation rule should not apply to transactions or contractual provisions which serve a *bona fide* commercial purpose for three reasons. First, courts applying the anti-deprivation rule in Canada have not been content to rest their reasons for decision merely on a finding that the effect of a transaction or contractual provision was to deprive a bankrupt's estate of value — the golden thread weaving its way through the jurisprudence is the presence or absence of a *bona fide* commercial purpose behind the deprivation. In the minority of cases where *bona fide* commercial purpose has not been discussed, its absence has been readily inferable from the circumstances.

Second, there is a principled legal basis for retaining a *bona fide* commercial purpose test. The anti-deprivation rule is based on the common law public policy against agreements entered into for the unlawful purpose of

s'accorder une préférence à l'encontre des autres créanciers en insérant de telles clauses dans leurs contrats. Cela serait en outre incompatible avec les principes généraux de liberté contractuelle — les parties ne négociant pas dans le but de protéger les intérêts de leurs créanciers en cas de faillite. Enfin, suivant une règle fondée sur l'objet, les créanciers non garantis recevraient encore moins que ce qu'ils reçoivent à l'heure actuelle. Une approche fondée sur les effets assure aux parties que les ententes contractuelles, en l'absence d'une stipulation prévoyant le retrait d'actifs en cas de faillite ou d'insolvabilité, seront généralement maintenues.

La clause VII Q(d) enfreint la règle anti-privation et est donc nulle. Elle prévoit que, dans le cas où Capital Steel fait faillite, elle renonce à 10 p. 100 du prix du contrat de sous-traitance — ce qui constitue une violation directe et évidente de la règle anti-privation. La clause ne peut être sauvegardée par les règles de la compensation, car celle-ci ne s'applique qu'aux dettes ou aux réclamations exigibles. Elle s'applique aux dettes du failli qui n'ont pas été provoquées par la faillite, puisque la règle anti-privation rend seulement inexigibles les réclamations fondées sur des privations déclenchées par une insolvabilité.

La juge Côté (dissidente) : Il y a accord avec les juges majoritaires que la règle anti-privation est bien ancrée depuis longtemps dans la jurisprudence canadienne et qu'elle n'a été éliminée ni par la Cour ni par une loi. Toutefois, cette règle ne devrait pas s'appliquer aux transactions ou aux stipulations qui poursuivent un objectif commercial véritable. Comme la clause VII Q(d) poursuit un objectif commercial véritable, elle est exécutoire et n'enfreint pas la règle anti-privation. L'ordonnance du juge de première instance devrait donc être rétablie.

La règle anti-privation ne devrait pas s'appliquer aux transactions ou aux stipulations qui poursuivent un objectif commercial véritable, et ce, pour trois motifs. Premièrement, les tribunaux qui appliquent la règle anti-privation au Canada ne se sont pas contentés de fonder leurs décisions sur une simple conclusion voulant qu'une transaction ou une stipulation ait pour effet de réduire la valeur de l'actif du failli — le lien qui relie la jurisprudence est la présence ou l'absence d'une finalité commerciale objective qui sous-tend la privation. Dans les rares cas où l'examen de la question de l'objectif commercial véritable n'a pas été réalisé, il était facile d'en inférer l'absence des circonstances.

Deuxièmement, le recours à un test fondé sur l'objectif commercial véritable repose sur un fondement juridique valable. La règle anti-privation s'appuie sur le principe de common law voulant que les accords conclus dans le but

defrauding or otherwise injuring third parties. It thus requires an objective assessment of the parties' intentions. In contrast, the *pari passu* rule has an effects-based test because it is based on an implied prohibition in the *BIA* that operates regardless of the parties' intentions. The *pari passu* provision in the *BIA* establishes a very clear bright line rule that all claims proved in a bankruptcy shall be paid rateably. This clear and straightforward statutory language readily supports a conclusion that Parliament intended to prohibit a debtor from contracting with creditors for a different distribution of the debtor's assets in bankruptcy than that provided in s. 141 of the *BIA*.

The anti-deprivation rule does not derive from a strained interpretation of s. 71 of the *BIA*. But even if the anti-deprivation rule was an implied prohibition in the *BIA*, it is a well-established principle that the *BIA* does not grant a trustee any greater interest in a bankrupt's property than that enjoyed by the bankrupt prior to the bankruptcy. Holding that s. 71 of the *BIA* converts the bankrupt's qualified interest in an asset into an absolute or unqualified interest in the hands of the trustee breaks with this principle. The statutory context includes numerous provisions indicating that arm's-length *bona fide* commercial transactions are valid as against the trustee of a bankrupt's estate.

Third, as a matter of public policy, the considerations cited in support of an effects-based test are not sufficient to override the otherwise strong countervailing public interest in the enforcement of contracts. Despite being a judicially-derived public policy, it is still prudent for courts to take into account the policies embodied in legislation as a reflection of society's public policy concerns. Therefore, anti-deprivation rule's common law character does not preclude a court from taking into account Parliament's objective of maximizing global recovery for all creditors, when considering how to formulate the anti-deprivation rule. However, Parliament's objectives must be weighed against the other policy interests protected by the common law when considering how to best formulate the rule. The common law places great weight on the freedom of contracting parties to pursue their individual self-interest, and the public policy considerations which have been cited in support of an effects-based test are not sufficient to override the otherwise strong countervailing public interest in the enforcement of contracts.

illégal de commettre une fraude ou de causer un préjudice à un tiers soient contraires à l'intérêt public. Par conséquent, il requiert une évaluation objective de l'intention des parties. En revanche, la règle du *pari passu* entraîne le recours à un test fondé sur les effets, car elle est fondée sur une prohibition implicite contenue dans la *LFI* qui s'applique indépendamment de l'intention des parties. La disposition de la *LFI* qui énonce la règle *pari passu* établit une règle de démarcation très nette selon laquelle toutes les réclamations établies dans la faillite sont acquittées au prorata. Ce libellé clair et précis de la loi appuie d'emblée la conclusion selon laquelle le législateur avait pour intention d'interdire à un débiteur de conclure un contrat avec des créanciers en vue de distribuer ses biens en cas de faillite d'une manière autre que celle prévue à l'art. 141 de la *LFI*.

La règle anti-privation n'émane pas d'une interprétation forcée de l'art. 71 de la *LFI*. Or, même si la règle anti-privation était une prohibition implicite contenue dans la *LFI*, il est un principe bien établi que la *LFI* n'accorde pas au syndic, à l'égard d'un bien du failli, un intérêt supérieur à celui qu'avait le failli avant la faillite. Conclure que l'art. 71 de la *LFI* convertit l'intérêt relatif du failli à l'égard d'un bien en intérêt absolu pour le syndic s'écarte de ce principe. Le contexte statutaire comprend de nombreuses dispositions prévoyant que les transactions commerciales de bonne foi sans lien de dépendance sont valides contre le syndic de l'actif du failli.

Troisièmement, en ce qui concerne l'intérêt public, les considérations qui ont été citées en appui au test fondé sur les effets ne suffisent pas à transcender l'importance de l'intérêt public opposé dans l'exécution des contrats. Même si la règle d'intérêt public émane des tribunaux, ceux-ci doivent néanmoins faire preuve de prudence et tenir compte des politiques intégrées dans les lois comme le reflet des préoccupations de la société en matière d'intérêt public. Par conséquent, le fait que la règle anti-privation soit issue de la common law n'empêche pas un tribunal de tenir compte de l'objectif du Parlement qui est de maximiser le recouvrement global pour tous les créanciers lorsqu'il se penche sur la façon de formuler la règle anti-privation. Toutefois, les objectifs du Parlement doivent être évalués par rapport aux autres intérêts publics protégés par la common law au moment de décider de la meilleure façon de formuler la règle. La common law accorde beaucoup de poids à la liberté des parties contractantes dans la poursuite de leur intérêt personnel, et les considérations d'intérêt public qui ont été citées en appui au test fondé sur les effets ne suffisent pas à transcender l'importance de l'intérêt public opposé dans l'exécution des contrats.

A purely effects-based test gives too little weight to freedom of contract, party autonomy, and the elbow-room which the common law traditionally accords for the aggressive pursuit of self-interest. It may also create significant uncertainty by introducing a vague standard which unduly restricts the scope of the anti-deprivation rule. By contrast, a subjective purpose test would place too little weight on Parliament's objective of maximizing global recovery for all creditors. The middle path — the objective *bona fide* commercial purpose test — is the best way to balance freedom of contract, the interests of third party creditors, and commercial certainty. Certainty in commercial affairs is typically better served by giving effect to contracts which were freely entered into, particularly when they serve commercial purposes and are not directed at an unlawful objective.

In addition, applying a *bona fide* commercial purpose test would not require a significantly more onerous analysis into the parties' intentions than that entailed by an effects-based test. Moreover, while debtors are not properly incentivized to protect their creditors' interests when dealing with third parties, creditors can access a full range of options to protect their rights: the oppression remedy, the directors' duty of care, the various anti-avoidance provisions in the *BIA* and in provincial statutes, as well as the ability of creditors to bargain for contractual protections. Parliament has also occupied much of the ground formerly covered by the common law such that there is a reduced need for a general anti-deprivation rule. Indeed, the many statutory protections already in place to safeguard the interests of creditors undermine any perceived policy need to expand the reach of the anti-deprivation rule. These provisions reflect Parliament's policy preference for upholding the validity of *bona fide* commercial arrangements, even when they have the effect of reducing the pool of assets available to a debtor's creditors in bankruptcy.

In the instant case, clause VII Q(d) furthers a *bona fide* commercial purpose. A general contractor's role is essentially to oversee and coordinate the construction of a project by various subcontractors according to a set schedule. It is evident that a subcontractor's bankruptcy during the construction of the project would require the general contractor to redirect significant administrative and management resources. The general contractor would also incur administrative and management costs from mitigating the fallout up and down the construction pyramid.

Un test fondé purement sur les effets accorde trop peu de poids à la liberté contractuelle, à l'autonomie des parties et à la liberté d'action traditionnellement conférée par la common law en vue de la poursuite agressive d'intérêts personnels. Il pourrait également entraîner une incertitude considérable, car on introduirait une norme vague qui restreindrait indûment la portée de la règle anti-privation. En revanche, un test subjectif fondé sur la finalité accorderait trop peu de poids à l'objectif du Parlement de maximiser le recouvrement global pour tous les créanciers. Un moyen terme, soit l'adoption d'un test objectif fondé sur la finalité commerciale véritable, est la meilleure solution pour respecter l'équilibre entre la liberté contractuelle, les intérêts des créanciers tiers et la certitude commerciale. La certitude dans les affaires commerciales est habituellement mieux servie en donnant effet aux contrats conclus librement, surtout lorsque les ententes en question poursuivent des fins commerciales et non un objectif illégal.

Par ailleurs, le fait d'appliquer un test fondé sur la finalité ou l'objectif commercial véritable n'exigerait pas une analyse considérablement plus détaillée des intentions des parties que celle associée au test fondé sur les effets. Qui plus est, même si les débiteurs ne sont pas motivés à protéger les intérêts de leurs créanciers lorsqu'ils traitent avec des tiers, un ensemble d'options s'offrent aux créanciers pour protéger leurs droits : le redressement en cas d'abus de droit, l'obligation de diligence des administrateurs, les diverses dispositions anti-évitement de la *LFI* et des lois provinciales ainsi que la capacité des créanciers de négocier des protections contractuelles. Le Parlement occupe en outre aujourd'hui une grande partie du terrain qui relevait autrefois de la common law, ce qui diminue la nécessité d'avoir une règle anti-privation générale. En effet, les nombreuses protections déjà prévues par les lois destinées à protéger les intérêts des créanciers remettent en question le besoin d'élargir la portée de la règle anti-privation. Ces dispositions reflètent une préférence du Parlement pour le maintien de la validité des transactions commerciales de bonne foi, même lorsque celles-ci ont pour effet de réduire l'ensemble de biens accessibles aux créanciers en cas de faillite.

En l'espèce, la clause VII Q(d) vise un objectif commercial véritable. Le rôle d'un entrepreneur général consiste essentiellement à superviser et à coordonner la construction d'un projet par différents sous-traitants conformément au calendrier fixé. Il est évident que la faillite d'un sous-traitant durant la construction du projet oblige l'entrepreneur général à réaffecter beaucoup de ressources administratives et de gestion. L'entrepreneur général a également à assumer des coûts administratifs et de gestion pour atténuer les répercussions dans toute la

Costly delays would ensue as well. Thus, a fee for the inconvenience of completing the work using alternate means is legitimate. Clause VII Q(d) does not demonstrate any intent on the part of Chandos or Capital Steel to avoid the operation on bankruptcy laws or to prejudice Capital Steel's creditors.

Cases Cited

By Rowe J.

Distinguished: *Coopérants, Mutual Life Insurance Society (Liquidator of) v. Dubois*, [1996] 1 S.C.R. 900; **referred to:** *Belmont Park Investments Pty. Ltd. v. BNY Corporate Trustee Services Ltd.*, [2011] UKSC 38, [2012] 1 A.C. 383; *A.N. Bail Co. v. Gingras*, [1982] 2 S.C.R. 475; *Canadian Imperial Bank of Commerce v. Bramalea Inc.* (1995), 33 O.R. (3d) 692; *In Re Hoskins and Hawkey, Insolvents* (1877), 1 O.A.R. 379; *Re Wetmore*, [1924] 4 D.L.R. 66; *Westerman (Bankrupt), Re*, 1998 ABQB 946, 234 A.R. 371, rev'd 1999 ABQB 708, 275 A.R. 114; *Re Knechtel Furniture Ltd.* (1985), 56 C.B.R. (N.S.) 258; *Re Frechette* (1982), 138 D.L.R. (3d) 61; *Aircell Communications Inc. (Trustee of) v. Bell Mobility Cellular Inc.*, 2013 ONCA 95, 14 C.B.R. (6th) 276; *HGC v. IESO*, 2019 ONSC 259; *1183882 Alberta Ltd. v. Valin Industrial Mill Installations Ltd.*, 2012 ABCA 62, 522 A.R. 285; *Watson v. Mason* (1876), 22 Gr. 574; *Hobbs v. Ontario Loan and Debenture Company* (1890), 18 S.C.R. 483; *Parry Sound (District) Social Services Administration Board v. O.P.S.E.U., Local 324*, 2003 SCC 42, [2003] 2 S.C.R. 157; *Heritage Capital Corp. v. Equitable Trust Co.*, 2016 SCC 19, [2016] 1 S.C.R. 306; *Royal Bank of Canada v. North American Life Assurance Co.*, [1996] 1 S.C.R. 325; *Alberta (Attorney General) v. Moloney*, 2015 SCC 51, [2015] 3 S.C.R. 327; *Husky Oil Operations Ltd. v. Minister of National Revenue*, [1995] 3 S.C.R. 453; *Bhasin v. Hrynew*, 2014 SCC 71, [2014] 3 S.C.R. 494; *Watkins v. Olafson*, [1989] 2 S.C.R. 750; *Borland's Trustee v. Steel Brothers & Co., Limited*, [1901] 1 Ch. 279; *Holt v. Telford*, [1987] 2 S.C.R. 193.

By Côté J. (dissenting)

A.I. Enterprises Ltd. v. Bram Enterprises Ltd., 2014 SCC 12, [2014] 1 S.C.R. 177; *Sattva Capital Corp. v. Creston Moly Corp.*, 2014 SCC 53, [2014] 2 S.C.R. 633; *Symes v. Canada*, [1993] 4 S.C.R. 695; *Ludco Enterprises Ltd. v. Canada*, 2001 SCC 62, [2001] 2 S.C.R. 1082; *Belmont Park Investments Pty. Ltd. v. BNY Corporate Trustee Services Ltd.*, [2011] UKSC 38, [2012] 1 A.C.

pyramide de ceux qui participent à la construction. Cela entraîne en outre des retards coûteux. Par conséquent, il est légitime de prévoir des frais pour les dérangements qu'il subit lorsque les travaux sont achevés par d'autres moyens. La clause VII Q(d) ne démontre aucune intention de la part de Chandos ou de Capital Steel d'éviter l'application des lois en matière de faillite ou de nuire aux créanciers de Capital Steel.

Jurisprudence

Citée par le juge Rowe

Distinction d'avec l'arrêt : *Coopérants (Les), Société mutuelle d'assurance-vie (Liquidateur de) c. Dubois*, [1996] 1 R.C.S. 900; **arrêts mentionnés :** *Belmont Park Investments Pty. Ltd. c. BNY Corporate Trustee Services Ltd.*, [2011] UKSC 38, [2012] 1 A.C. 383; *A.N. Bail Co. c. Gingras*, [1982] 2 R.C.S. 475; *Canadian Imperial Bank of Commerce c. Bramalea Inc.* (1995), 33 O.R. (3d) 692; *In Re Hoskins and Hawkey, Insolvents* (1877), 1 O.A.R. 379; *Re Wetmore*, [1924] 4 D.L.R. 66; *Westerman (Bankrupt), Re*, 1998 ABQB 946, 234 A.R. 371, inf. par 1999 ABQB 708, 275 A.R. 114; *Re Knechtel Furniture Ltd.* (1985), 56 C.B.R. (N.S.) 258; *Re Frechette* (1982), 138 D.L.R. (3d) 61; *Aircell Communications Inc. (Trustee of) c. Bell Mobility Cellular Inc.*, 2013 ONCA 95, 14 C.B.R. (6th) 276; *HGC c. IESO*, 2019 ONSC 259; *1183882 Alberta Ltd. c. Valin Industrial Mill Installations Ltd.*, 2012 ABCA 62, 522 A.R. 285; *Watson c. Mason* (1876), 22 Gr. 574; *Hobbs c. Ontario Loan and Debenture Company* (1890), 18 R.C.S. 483; *Parry Sound (district), Conseil d'administration des services sociaux c. S.E.E.F.P.O., section locale 324*, 2003 CSC 42, [2003] 2 R.C.S. 157; *Heritage Capital Corp. c. Équitable, Cie de fiducie*, 2016 CSC 19, [2016] 1 R.C.S. 306; *Banque Royale du Canada c. Nord-Américaine, cie d'assurance-vie*, [1996] 1 R.C.S. 325; *Alberta (Procureur général) c. Moloney*, 2015 CSC 51, [2015] 3 R.C.S. 327; *Husky Oil Operations Ltd. c. Ministre du Revenu national*, [1995] 3 R.C.S. 453; *Bhasin c. Hrynew*, 2014 CSC 71, [2014] 3 R.C.S. 494; *Watkins c. Olafson*, [1989] 2 R.C.S. 750; *Borland's Trustee c. Steel Brothers & Co., Limited*, [1901] 1 Ch. 279; *Holt c. Telford*, [1987] 2 R.C.S. 193.

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A.I. Enterprises Ltd. c. Bram Enterprises Ltd., 2014 CSC 12, [2014] 1 R.C.S. 177; *Sattva Capital Corp. c. Creston Moly Corp.*, 2014 CSC 53, [2014] 2 R.C.S. 633; *Symes c. Canada*, [1993] 4 R.C.S. 695; *Entreprises Ludco Ltée c. Canada*, 2001 CSC 62, [2001] 2 R.C.S. 1082; *Belmont Park Investments Pty. Ltd. c. BNY Corporate Trustee Services Ltd.*, [2011] UKSC 38, [2012] 1 A.C.

383; *Hobbs v. Ontario Loan and Debenture Company* (1890), 18 S.C.R. 483; *Ex parte Voisey* (1882), 21 Ch. D. 442; *Ex parte Williams* (1877), 7 Ch. D. 138; *Coopérants, Mutual Life Insurance Society (Liquidator of) v. Dubois*, [1996] 1 S.C.R. 900; *A.N. Bail Co. v. Gingras*, [1982] 2 S.C.R. 475; *British Eagle International Airlines Ltd. v. Cie Nationale Air France*, [1975] 1 W.L.R. 758; *In Re Hoskins and Hawkey, Insolvents* (1877), 1 O.A.R. 379; *Murphy, a Bankrupt* (1803), 1 Ch. 44; *Watson v. Mason* (1876), 22 Gr. 574; *Re Frechette* (1982), 138 D.L.R. (3d) 61; *Borland's Trustee v. Steel Brothers & Co., Limited*, [1901] 1 Ch. 279; *Re Knechtel Furniture Ltd.* (1985), 56 C.B.R. (N.S.) 258; *Canadian Imperial Bank of Commerce v. Bramalea Inc.* (1995), 33 O.R. (3d) 692; *Aircell Communications Inc. (Trustee of) v. Bell Mobility Cellular Inc.*, 2013 ONCA 95, 14 C.B.R. (6th) 276; *Westerman (Bankrupt), Re*, 1998 ABQB 946, 234 A.R. 371, rev'd 1999 ABQB 708, 275 A.R. 114; *R. v. Salituro*, [1991] 3 S.C.R. 654; *Shafron v. KRG Insurance Brokers (Western) Inc.*, 2009 SCC 6, [2009] 1 S.C.R. 157; *Transport North American Express Inc. v. New Solutions Financial Corp.*, 2004 SCC 7, [2004] 1 S.C.R. 249; *Higinbotham v. Holme* (1812), 19 Ves. Jr. 88, 34 E.R. 451; *In re Stephenson*, [1897] 1 Q.B. 638; *Whitmore v. Mason* (1861), 2 J. & H. 204, 70 E.R. 1031; *Ex parte Mackay* (1873), L.R. 8 Ch. App. 643; *Elford v. Elford* (1922), 64 S.C.R. 125; *Campbell River Lumber Co. v. McKinnon* (1922), 64 S.C.R. 396; *Zimmermann v. Letkeman*, [1978] 1 S.C.R. 1097; *Giffen (Re)*, [1998] 1 S.C.R. 91; *Lefebvre (Trustee of)*, 2004 SCC 63, [2004] 3 S.C.R. 326; *Flintoft v. Royal Bank of Canada*, [1964] S.C.R. 631; *Saulnier v. Royal Bank of Canada*, 2008 SCC 58, [2008] 3 S.C.R. 166; *Alberta (Attorney General) v. Moloney*, 2015 SCC 51, [2015] 3 S.C.R. 327; *St. John Shipping Corp. v. Joseph Rank Ltd.*, [1957] 1 Q.B. 267; *Still v. M.N.R.*, [1998] 1 F.C. 549; *Tercon Contractors Ltd. v. British Columbia (Transportation and Highways)*, 2010 SCC 4, [2010] 1 S.C.R. 69; *Bhasin v. Hrynew*, 2014 SCC 71, [2014] 3 S.C.R. 494; *In re Estate of Charles Millar, Deceased*, [1938] S.C.R. 1; *Fender v. St. John-Mildmay*, [1938] A.C. 1; *Lomas v. JFB Firth Rixson Inc.*, [2010] EWHC 3372 (Ch.), [2011] 2 B.C.L.C. 120, aff'd [2012] EWCA Civ. 419, [2012] 2 All E.R. (Comm.) 1076; *Watkins v. Olafson*, [1989] 2 S.C.R. 750; *Peoples Department Stores Inc. (Trustee of) v. Wise*, 2004 SCC 68, [2004] 3 S.C.R. 461; *Heritage Capital Corp. v. Equitable Trust Co.*, 2016 SCC 19, [2016] 1 S.C.R. 306; *Ledcor Construction Ltd. v. Northbridge Indemnity Insurance Co.*, 2016 SCC 37, [2016] 2 S.C.R. 23; *BG Checo International Ltd. v. British Columbia Hydro and Power Authority*, [1993] 1 S.C.R. 12; *Douez v. Facebook, Inc.*, 2017 SCC 33, [2017] 1 S.C.R.

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751; *Consolidated-Bathurst Export Ltd. v. Mutual Boiler and Machinery Insurance Co.*, [1980] 1 S.C.R. 888.

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APPEAL from a judgment of the Alberta Court of Appeal (Rowbotham, Veldhuis and Wakeling JJ.A.), 2019 ABCA 32, 438 D.L.R. (4th) 195, 70 C.B.R. (6th) 1, 91 B.L.R. (5th) 1, [2019] A.J. No. 99 (QL), 2019 CarswellAlta 125 (WL Can.), setting aside a decision of Nielsen J., Alta. Q.B., Edmonton,

751; *Exportations Consolidated Bathurst Ltée c. Mutual Boiler and Machinery Insurance Co.*, [1980] 1 R.C.S. 888.

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POURVOI contre un arrêt de la Cour d'appel de l'Alberta (les juges Rowbotham, Veldhuis et Wakeling), 2019 ABCA 32, 438 D.L.R. (4th) 195, 70 C.B.R. (6th) 1, 91 B.L.R. (5th) 1, [2019] A.J. No. 99 (QL), 2019 CarswellAlta 125 (WL Can.), qui a infirmé une décision du juge Nielsen, Cour

No. 24-2169632, March 17, 2017. Appeal dismissed, Côté J. dissenting.

Darren Bieganek, *Q.C.*, and *Ryan Quinlan*, for the appellant.

Shauna N. Finlay and *Victoria Merritt*, for the respondent.

Zoe Oxaal, for the intervener the Attorney General of Canada.

Ashley Taylor and *Sinziana R. Hennig*, for the intervener the Canadian Association of Insolvency and Restructuring Professionals.

Sean F. Collins, *Brandon Kain* and *Cassidy Thomson*, for the intervener the Insolvency Institute of Canada.

The judgment of Wagner C.J. and Abella, Moldaver, Karakatsanis, Brown, Rowe, Martin and Kasirer JJ. was delivered by

[1] Rowe J. — This case concerns a common law rule ("anti-deprivation rule") that operates to prevent contracts from frustrating statutory insolvency schemes. Chandos Construction Ltd. ("Chandos") entered into a construction contract ("Subcontract") with Capital Steel Inc. ("Capital Steel"). A provision of the Subcontract would award Chandos a sum of money in the event of Capital Steel's bankruptcy, which later occurred. This case deals with whether that provision was invalid by virtue of the anti-deprivation rule.

[2] I conclude that it is, essentially for the reasons of the majority of the Court of Appeal of Alberta. Accordingly, the appeal is dismissed.

I. Facts

[3] Chandos, a general construction contractor, entered into the Subcontract with Capital Steel, a subcontractor. The value of the Subcontract

du Banc de la Reine d'Alberta, Edmonton, No. 24-2169632, 17 mars 2017. Pourvoi rejeté, la juge Côté est dissidente.

Darren Bieganek, *c.r.*, et *Ryan Quinlan*, pour l'appelante.

Shauna N. Finlay et *Victoria Merritt*, pour l'intimée.

Zoe Oxaal, pour l'intervenant le procureur général du Canada.

Ashley Taylor et *Sinziana R. Hennig*, pour l'intervenante l'Association canadienne des professionnels de l'insolvabilité et de la réorganisation.

Sean F. Collins, *Brandon Kain* et *Cassidy Thomson*, pour l'intervenant l'Institut d'insolvabilité du Canada.

Version française du jugement du juge en chef Wagner et des juges Abella, Moldaver, Karakatsanis, Brown, Rowe, Martin et Kasirer rendu par

[1] Le juge Rowe — La présente cause porte sur une règle de common law (« règle anti-privation ») qui a pour effet d'empêcher de contourner les régimes législatifs d'insolvabilité par voie contractuelle. Chandos Construction Ltd. (« Chandos ») a conclu un contrat de construction (« contrat de sous-traitance ») avec Capital Steel Inc. (« Capital Steel »). Une stipulation du contrat de sous-traitance prévoit que Chandos recevrait une somme d'argent advenant la faillite de Capital Steel, ce qui est arrivé. Il s'agit pour la Cour de déterminer si cette stipulation est invalide en raison de la règle anti-privation.

[2] Je conclus que c'est le cas, essentiellement pour les motifs exprimés par les juges majoritaires de la Cour d'appel de l'Alberta. Par conséquent, le pourvoi est rejeté.

I. Faits

[3] Chandos, un entrepreneur général en construction, a conclu un contrat de sous-traitance avec Capital Steel, un sous-traitant. La valeur de ce

was $1,373,300.47. The provision at issue is in clause VII Q, one of the "Conditions" of the subcontract:

Q Subcontractor Ceases Operation

In the event the Subcontractor commits any act of insolvency, bankruptcy, winding up or other distribution of assets, or permits a receiver of the Subcontractor's business to be appointed, or ceases to carry on business or closes down its operations, then in any of such events:

(a) this Subcontract Agreement shall be suspended but may be reinstated and continued if the Contractor, the liquidator or Trustee of the Subcontractor and the surety, if any, so agree. If no agreement is reached, the Subcontractor shall be considered to be in default and the Contractor may give written notice of default to the Subcontractor and immediately proceed to complete the Work by other means as deemed appropriate by the Contractor, and

(b) any cost to the Contractor arising from the suspension of this Subcontract Agreement or the completion of the Work by the Contractor, plus a reasonable allowance for overhead and profit, will be payable by the Subcontractor and or his sureties, and

(c) the Contractor is entitled to withhold up to 20% of the within Subcontract Agreement price until such time as all warranty and or guarantee periods which are the responsibility of the Subcontractor have expired and,

(d) the Subcontractor shall forfeit 10% of the within Subcontract Agreement price to the Contractor as a fee for the inconvenience of completing the work using alternate means and/or for monitoring the work during the warranty period.

(A. R., at p. 157)

[4] This clause provides four consequences that follow from the insolvency, bankruptcy, or cease of business of Capital Steel. First, clause VII Q(a) provides that the Subcontract will be suspended and can only be continued if the Trustee in bankruptcy and

contrat de sous-traitance s'élevait à 1 373 300,47 $. La stipulation en litige est la clause VII Q, l'une des « Conditions » du contrat de sous-traitance :

[TRADUCTION]

Q Cessation des activités du sous-traitant

Dans le cas où le sous-traitant devient insolvable, fait faillite, liquide ou distribue autrement ses actifs, permet la nomination d'un séquestre pour son entreprise, cesse d'exercer ses activités ou ferme ses chantiers :

(a) le présent contrat de sous-traitance est suspendu, mais peut être rétabli et maintenu si l'entrepreneur, le liquidateur ou le syndic de faillite du sous-traitant et la caution, le cas échéant, s'entendent. Si aucune entente n'est conclue, le sous-traitant est considéré comme ayant manqué à ses obligations et l'entrepreneur peut lui remettre un avis de défaut par écrit et procéder immédiatement à l'achèvement des travaux par d'autres moyens qu'il juge appropriés;

(b) tous les coûts engagés par l'entrepreneur découlant de la suspension du présent contrat de sous-traitance ou de l'achèvement des travaux par l'entrepreneur, plus une indemnisation raisonnable pour les frais généraux et le profit, sont payables par le sous-traitant et/ou ses cautions;

(c) l'entrepreneur peut retenir jusqu'à 20 % du prix du présent contrat de sous-traitance jusqu'à ce que toutes les garanties et/ou toutes les périodes de garantie qui relèvent de la responsabilité du sous-traitant soient expirées;

(d) le sous-traitant renonce à 10 % du prix du présent contrat de sous-traitance en faveur de l'entrepreneur à titre de frais pour les dérangements liés à l'achèvement des travaux par d'autres moyens et/ou pour la surveillance des travaux durant la période de garantie.

(d.a., p. 157)

[4] Cette stipulation prévoit quatre conséquences en cas d'insolvabilité, de faillite ou de cessation des activités de Capital Steel. Premièrement, la clause VII Q(a) prévoit que le contrat de sous-traitance est suspendu et ne peut être rétabli que

Chandos agree. Second, clause VII Q(b) provides that Capital Steel will pay Chandos "any cost . . . arising from the suspension" of the Subcontract or from Chandos having to complete the work, plus a "reasonable allowance for overhead and profit". Third, clause VII Q(c) allows Chandos to withhold certain funds from Capital Steel until the warranty and guarantee periods run out. Fourth, clause VII Q(d) provides that Capital Steel will pay Chandos 10 percent of the Subcontract price "as a fee for the inconvenience . . . and/or for monitoring the work".

si le syndic de faillite et Chandos s'entendent. Deuxièmement, la clause VII Q(b) prévoit que Capital Steel doit payer à Chandos [TRADUCTION] « tous les coûts [. . .] découlant de la suspension » du contrat de sous-traitance ou de l'achèvement des travaux par Chandos, plus une « indemnisation raisonnable pour les frais généraux et le profit ». Troisièmement, la clause VII Q(c) permet à Chandos de retenir certains fonds destinés à Capital Steel jusqu'à l'expiration de la garantie ou des périodes de garantie. Quatrièmement, la clause VII Q(d) prévoit que Capital Steel doit payer à Chandos 10 p. 100 du prix du contrat de sous-traitance à titre de « frais pour les dérangements [. . .] et/ou pour la surveillance des travaux ».

[5] When Capital Steel filed an assignment in bankruptcy prior to completing its Subcontract with Chandos, Deloitte Restructuring Inc. was appointed as its Trustee in bankruptcy. At the time, Chandos owed Capital Steel $149,618.39 under the Subcontract. Chandos argued that it was entitled to set off $22,800 — the costs it had incurred to complete Capital Steel's work — such that it would owe Capital Steel only $126,818.39 ($149,618.39 less $22,800). In so arguing, Chandos did not have to rely on clause VII Q as it could rely on the ordinary common law rules relating to damages for breach of contract and the law of set-off, which persists in bankruptcy under s. 97(3) of the *Bankruptcy and Insolvency Act*, R.S.C. 1985, c. B-3 ("*BIA*").

[5] Lorsque Capital Steel a procédé à une cession de ses biens avant de terminer son contrat de sous-traitance avec Chandos, Restructuration Deloitte Inc. a été nommée syndic de la faillite. À ce moment-là, Chandos devait une somme de 149 618,39 $ à Capital Steel en application du contrat de sous-traitance. Chandos a soutenu qu'elle avait le droit de déduire la somme de 22 800 $ — soit les coûts qu'elle avait engagés pour terminer les travaux commencés par Capital Steel —, de sorte qu'elle ne devait plus à celle-ci que 126 818,39 $ (149 618,39 $ moins 22 800 $). Pour faire valoir cet argument, Chandos n'avait pas besoin de recourir à la clause VII Q puisqu'elle pouvait simplement invoquer les règles ordinaires de common law relatives aux dommages-intérêts pour rupture de contrat et à la compensation, qui s'appliquent en matière de faillite aux termes du par. 97(3) de la *Loi sur la faillite et l'insolvabilité*, L.R.C. 1985, c. B-3 (« *LFI* »).

[6] Chandos argued that it was also entitled to set off the amount triggered by the bankruptcy according to clause VII Q(d), under which Capital Steel forfeits 10 percent of the Subcontract price in the event of insolvency. The Subcontract price was $1,373,300.47, so, by its terms, clause VII Q(d) created a debt owed by Capital Steel to Chandos of $137,330.05. If clause VII Q(d) applied, it would mean Chandos had a $10,511.66 claim provable in bankruptcy proceedings rather than a debt to Capital Steel of $126,818.39.

[6] Chandos a fait valoir qu'elle avait également le droit de déduire le montant qui lui était dû en cas de faillite suivant la clause VII Q(d), qui prévoit que Capital Steel doit renoncer à 10 p. 100 du prix du contrat de sous-traitance en cas d'insolvabilité. Le prix du contrat de sous-traitance étant de 1 373 300,47 $, la clause VII Q(d) crée une dette de 137 330,05 $ payable par Capital Steel à Chandos. Si la clause VII Q(d) s'applique, cela veut dire que Chandos a une réclamation prouvable de 10 511,66 $ dans le cadre de la faillite plutôt qu'une dette de 126 818,39 $ envers Capital Steel.

[7] Faced with these arguments, the Trustee applied for advice and directions from the Court of Queen's Bench as to whether clause VII Q(d) was valid.

II. Judgments Below

[8] The application judge found the provision to be valid (Alta. Q.B., Edmonton, No. 24-2169632, March 17, 2017). He concluded that, so long as the provision was not an attempt to avoid the effect of bankruptcy laws, the anti-deprivation rule does not prevent contracting parties from agreeing that upon the insolvency of one party, the other party can make a liquidated damages claim. He found that, in this case, Chandos had not attempted to avoid the effect of bankruptcy laws. He also found that the provision was a (valid) liquidated damages clause, not an (invalid) penalty clause.

[9] On appeal, the majority of the Court of Appeal reversed the decision, finding the provision invalid (2019 ABCA 32, 438 D.L.R. (4th) 195).

[10] As Rowbotham J.A., for the majority, explained, whether a provision is a liquidated damages clause or a penalty clause is a separate and distinct analysis from whether the provision violates the anti-deprivation rule. A provision can be invalid if it violates either the anti-deprivation rule or the penalty clause rule.

[11] Justice Rowbotham's reasons proceeded in three stages. First, she identified the long history of the anti-deprivation rule in Canadian jurisprudence. Second, she found that the rule has not been eliminated by either subsequent decisions or by statutory amendments. Finally, she determined that the content of the rule should remain as articulated in the Canadian jurisprudence rather than adopt the approach taken by the United Kingdom Supreme Court in *Belmont Park Investments Pty. Ltd. v. BNY Corporate Trustee Services Ltd.*, [2011] UKSC 38,

[7] Face à ces arguments, le syndic a demandé des conseils et des directives à la Cour du Banc de la Reine quant à la validité de la clause VII Q(d).

II. Jugements des juridictions d'instances inférieures

[8] Le juge de première instance a conclu que la stipulation est valide (B.R. Alb., Edmonton, nº 24-2169632, 17 mars 2017). Selon lui, tant que celle-ci ne vise pas à éviter l'effet des lois en matière de faillite, la règle anti-privation n'empêche pas les parties contractantes de convenir que, en cas d'insolvabilité de l'une d'entre elles, l'autre peut réclamer des dommages-intérêts liquidés. À son avis, en l'espèce, Chandos n'avait pas tenté d'éviter l'effet des lois en matière de faillite, et la stipulation était une clause de dommages-intérêts liquidés (valide) et non une clause pénale (invalide).

[9] En appel, ayant conclu que la stipulation était invalide, les juges majoritaires de la Cour d'appel ont infirmé la décision (2019 ABCA 32, 438 D.L.R. (4th) 195).

[10] La juge Rowbotham, écrivant au nom des juges majoritaires, a expliqué que la question de savoir si une stipulation est une clause établissant des dommages-intérêts liquidés ou une clause pénale commande une analyse distincte de celle visant à savoir si la stipulation viole la règle anti-privation. Une stipulation peut être invalide si elle viole la règle anti-privation ou s'il s'agit d'une clause pénale inexécutoire.

[11] Dans ses motifs, la juge Rowbotham a procédé en trois étapes. D'abord, elle a fait l'historique de l'existence de longue date de la règle anti-privation dans la jurisprudence canadienne. Ensuite, elle a conclu que la règle n'a été éliminée ni par des décisions subséquentes ni par des modifications législatives. Enfin, elle a jugé que le contenu de la règle doit rester tel qu'il est énoncé dans la jurisprudence canadienne, et qu'on doit s'abstenir d'adopter l'approche utilisée par la Cour suprême du Royaume-Uni dans l'arrêt *Belmont Park Investments Pty. Ltd. c. BNY*

[2012] 1 A.C. 383 ("*Belmont Park*", earlier know as "*Perpetual Trustee*").

[12] As Rowbotham J.A. explained, the common law has two distinct rules that both invalidate contracts that affect the distribution of proceeds in bankruptcy, although they had earlier been combined under the moniker of a "fraud upon the bankruptcy law". The rules do not stand on their own, but rather exist to give effect to an implicit prohibition in bankruptcy legislation. First, the *pari passu* rule forbids contractual provisions that would allow certain creditors to receive more than their fair share. It does not matter whether the provision is triggered by insolvency or bankruptcy, so long as it would alter the scheme of distribution after proceedings begin. Second, the anti-deprivation rule prevents parties from agreeing to remove property from a bankrupt's estate that would otherwise have vested in the trustee. It invalidates provisions that are "engaged by a debtor's insolvency and remove value from the debtor's estate to the prejudice of creditors" (para. 32). Put another way, although both rules concern creditors receiving an appropriately-sized slice of the proverbial pie, the anti-deprivation rule relates to the size of the pie and the *pari passu* rule relates to the slicing of the pie, whatever size it may be (see R. Goode, "Perpetual Trustee and Flip Clauses in Swap Transactions" (2011), 127 *Law. Q. Rev.* 1, at p. 4).

[13] Justice Rowbotham concluded that both rules have been applied in Canadian jurisprudence. She cited *A.N. Bail Co. v. Gingras*, [1982] 2 S.C.R. 475, at para. 23, as an application of the *pari passu* rule, and the following cases as examples of the application of the anti-deprivation rule: *Canadian Imperial Bank of Commerce v. Bramalea Inc.* (1995), 33 O.R. (3d) 692 (C.J. (Gen. Div.)) ("*Bramalea*"); *In Re Hoskins and Hawkey, Insolvents* (1877), 1 O.A.R. 379 (C.A.); *Re Wetmore*, [1924] 4 D.L.R. 66 (N.B.S.C. (App. Div.)); *Westerman* (*Bankrupt*), *Re*, 1998 ABQB 946, 234 A.R. 371, rev'd on other grounds 1999 ABQB 708, 275 A.R. 114; *Re Knechtel Furniture Ltd.* (1985), 56 C.B.R. (N.S.) 258 (Ont.

Corporate Trustee Services Ltd., [2011] UKSC 38, [2012] 1 A.C. 383 (« *Belmont Park* », autrefois connu sous le nom « *Perpetual Trustee* »).

[12] Comme la juge Rowbotham l'a expliqué, il existe en common law deux règles distinctes qui invalident chacune les contrats touchant la distribution de l'actif en cas de faillite, même si on parlait autrefois dans les deux cas du « principe de fraude contre les lois en matière de faillite ». Ces règles ne sont pas autonomes; elles existent plutôt pour donner effet à une interdiction implicite dans les lois en matière de faillite. Premièrement, la règle du *pari passu* interdit les stipulations qui permettent à certains créanciers de recevoir plus que leur juste part. Il n'importe pas que l'application de la stipulation soit déclenchée par une insolvabilité ou une faillite, tant qu'elle modifie le plan de distribution après le début des procédures. Deuxièmement, la règle anti-privation empêche des parties de s'entendre pour retirer de l'actif d'un failli certains biens qui auraient autrement été dévolus au syndic. Elle invalide les stipulations dont l'application [TRADUCTION] « est déclenchée par l'insolvabilité d'un débiteur et qui réduisent la valeur de son actif au détriment des créanciers » (par. 32). Autrement dit, même si les deux règles concernent l'obtention par les créanciers d'une part adéquate du gâteau, la règle anti-privation porte sur la taille du gâteau tandis que la règle du *pari passu* porte sur la répartition de celui-ci, peu importe sa taille (voir R. Goode, « Perpetual Trustee and Flip Clauses in Swap Transactions » (2011), 127 *Law. Q. Rev.* 1, p. 4).

[13] La juge Rowbotham a conclu que les deux règles ont été appliquées dans la jurisprudence canadienne. Elle a cité l'arrêt *A.N. Bail Co. c. Gingras*, [1982] 2 R.C.S. 475, par. 23, à titre d'application de la règle du *pari passu*, et les décisions suivantes à titre d'exemples d'application de la règle anti-privation : *Canadian Imperial Bank of Commerce c. Bramalea Inc.* (1995), 33 O.R. (3d) 692 (C.J. (Div. gén.)) (« *Bramalea* »); *In Re Hoskins and Hawkey, Insolvents* (1877), 1 O.A.R. 379 (C.A.); *Re Wetmore*, [1924] 4 D.L.R. 66 (C.S.N.-B. (Div. app.)); *Westerman (Bankrupt), Re*, 1998 ABQB 946, 234 A.R. 371, inf. pour d'autres motifs 1999 ABQB 708, 275 A.R. 114; *Re Knechtel Furniture*

S.C.); *Re Frechette* (1982), 138 D.L.R. (3d) 61 (Que. Sup. Ct.); *Aircell Communications Inc. (Trustee of) v. Bell Mobility Cellular Inc.*, 2013 ONCA 95, 14 C.B.R. (6th) 276, at paras. 10-12; *HGC v. IESO*, 2019 ONSC 259, at para. 100 (CanLII); *1183882 Alberta Ltd. v. Valin Industrial Mill Installations Ltd.*, 2012 ABCA 62, 522 A.R. 285, per McDonald J.A., dissenting.

[14] Justice Rowbotham identified no cases where the anti-deprivation rule had been eliminated. She considered *Coopérants, Mutual Life Insurance Society (Liquidator of) v. Dubois*, [1996] 1 S.C.R. 900 ("*Coopérants*"), because, even though it involved a contractual provision triggered by liquidation, this Court did not discuss the anti-deprivation rule. She noted, however, that there was no evidence the provision at issue prejudiced creditors, so the anti-deprivation rule would not have been engaged.

[15] Justice Rowbotham also found that no statutory changes had eliminated the anti-deprivation rule, either explicitly or by negative implication, as when Parliament occupies the field. The only changes that might arguably be relevant were to the *BIA*. They, however, addressed a different problem than that addressed by the anti-deprivation rule: whereas the anti-deprivation rule protects creditors, the changes in question protect debtors.

[16] One such change came when Parliament enacted ss. 65.1 and 66.34 of the *BIA*. These sections invalidate contractual provisions triggered by insolvency in both commercial and consumer restructurings. Parliament's focus was on ensuring that debtors have time necessary to restructure their affairs. There was no suggestion that these sections were meant to affect the anti-deprivation rule, which is aimed at protecting the interest of creditors.

[17] Similarly, when Parliament enacted s. 84.2 of the *BIA*, it intended to protect consumer debtors

Ltd. (1985), 56 C.B.R. (N.S.) 258 (C.S. Ont.); *Re Frechette* (1982), 138 D.L.R. (3d) 61 (C.S. Qc); *Aircell Communications Inc. (Trustee of) c. Bell Mobility Cellular Inc.*, 2013 ONCA 95, 14 C.B.R. (6th) 276, par. 10-12; *HGC c. IESO*, 2019 ONSC 259, par. 100 (CanLII); *1183882 Alberta Ltd. c. Valin Industrial Mill Installations Ltd.*, 2012 ABCA 62, 522 A.R. 285, le juge McDonald, dissident.

[14] La juge Rowbotham n'a trouvé aucune affaire dans laquelle la règle anti-privation a été éliminée. Elle a examiné l'arrêt *Coopérants (Les), Société mutuelle d'assurance-vie (Liquidateur de) c. Dubois*, [1996] 1 R.C.S. 900 (« *Coopérants* »), parce que, même s'il porte sur une stipulation dont l'application a été déclenchée par une liquidation, la Cour n'y a pas traité de la règle anti-privation. Cela dit, elle a noté que rien n'indiquait que la stipulation en cause avait porté préjudice aux créanciers, de sorte que la règle anti-privation ne se serait pas appliquée.

[15] La juge Rowbotham a également conclu qu'aucune modification législative n'a éliminé la règle anti-privation, ni explicitement ni implicitement, comme c'est le cas lorsque le Parlement occupe le terrain quant à une question. Les seules modifications qui pourraient être pertinentes sont celles apportées à la *LFI*. Or, elles concernent un problème différent de celui visé par la règle anti-privation : en effet, alors que cette dernière protège les créanciers, les modifications en question protègent les débiteurs.

[16] Une de ces modifications a été apportée lorsque le Parlement a adopté les art. 65.1 et 66.34 de la *LFI*. Ces dispositions invalident les stipulations dont l'application est déclenchée par une insolvabilité dans le contexte de la restructuration d'un débiteur commercial ou d'un débiteur consommateur. Le Parlement visait principalement à garantir que les débiteurs disposaient du temps nécessaire pour restructurer leurs affaires. Rien n'indique que ces dispositions législatives visaient à modifier la règle anti-privation, qui a pour but de protéger les intérêts des créanciers.

[17] De même, lorsque le Parlement a adopté l'art. 84.2 de la *LFI*, il souhaitait protéger les débiteurs

from the deleterious consequences of provisions that trigger upon bankruptcy, not to protect one creditor from a debtor's contract with another creditor.

[18] Justice Rowbotham concluded that in none of these instances did Parliament intend to occupy the field and eliminate the anti-deprivation.

[19] Next, Rowbotham J.A. considered whether to follow the U.K. Supreme Court's approach to the anti-deprivation rule in *Belmont*. In *Belmont*, the U.K. Supreme Court concluded that the anti-deprivation rule does not apply to "bona fide commercial transactions which do not have as their predominant purpose, or one of their main purposes, the deprivation of the property of one of the parties on bankruptcy" (para. 104).

[20] Justice Rowbotham declined to follow *Belmont*. She noted that this purpose-based test was contrary to the effects-based test applied by Canadian courts, and that this new test had been criticized by British legal scholars as defeating the purpose of the anti-deprivation rule. She further noted that a party who might become insolvent has no incentive to resist a clause that directs property out of its estate upon insolvency, since, upon that event, the insolvent party will no longer have an interest in that property.

[21] Finally, Rowbotham J.A. applied the common law anti-deprivation rule to clause VII Q(d). She determined that this clause triggered upon insolvency and that giving effect to it would remove value from the debtor's estate to the prejudice of creditors. The clause was therefore invalid.

[22] Justice Wakeling dissented. In his view, the anti-deprivation rule has never existed in Canadian common law or, if it did, it ceased to exist after amendments to the *BIA* and the *Companies' Creditors Arrangement Act*, R.S.C. 1985, c. C-36, in 2009. Even if it did exist, he would have adopted the

consommateurs contre les conséquences néfastes des stipulations dont l'application est déclenchée par une faillite et non à protéger des créanciers des effets d'un contrat entre le débiteur et un autre créancier.

[18] La juge Rowbotham a conclu que dans aucun de ces cas le Parlement n'a eu l'intention d'occuper le terrain relatif à la question en cause et d'éliminer la règle anti-privation.

[19] Ensuite, la juge Rowbotham a examiné s'il y avait lieu de suivre l'approche adoptée par la Cour suprême du Royaume-Uni relativement à la règle anti-privation dans l'arrêt *Belmont*. Dans cet arrêt, la Cour suprême du Royaume-Uni a conclu que la règle ne s'applique pas aux [TRADUCTION] « opérations commerciales de bonne foi dont l'objectif prédominant ou l'un des objectifs principaux n'est pas de priver certains acteurs concernés des biens d'une des parties en cas de faillite » (par. 104).

[20] La juge Rowbotham a refusé de suivre l'arrêt *Belmont*. Elle a mentionné que le test fondé sur l'objet du contrat était contraire à celui fondé sur les effets appliqué par les tribunaux canadiens et que ce nouveau test avait été critiqué par des juristes britanniques, qui estiment qu'il contrecarre l'objet de la règle anti-privation. La juge Rowbotham a ajouté qu'une partie susceptible de devenir insolvable n'a pas d'intérêt à s'opposer à une clause qui réduit la valeur de son actif en cas d'insolvabilité, car, dans une telle situation, la partie insolvable n'a plus d'intérêt à l'égard de cet actif.

[21] Enfin, la juge Rowbotham a appliqué la règle anti-privation de common law à la clause VII Q(d). Elle a déterminé que l'application de cette clause est déclenchée en cas d'insolvabilité et que, en lui donnant effet, on réduit la valeur de l'actif du débiteur au détriment des créanciers. À son avis, la clause est donc invalide.

[22] Le juge Wakeling a rédigé des motifs dissidents. À son avis, la règle anti-privation n'a jamais existé dans la common law canadienne ou, subsidiairement, elle a cessé d'exister après les modifications apportées à la *LFI* et à la *Loi sur les arrangements avec les créanciers des compagnies*, L.R.C. 1985,

purpose-based test from *Belmont*. These conclusions were advanced by Chandos before this court. Justice Wakeling also would have reformulated the penalty rule. Given my conclusions as to the anti-deprivation rule, I do not address the penalty rule.

III. Issues on appeal

[23] On appeal before us, Chandos alleges the majority at the Court of Appeal made five errors, by:

(a) emphasizing bankruptcy law over contract law;

(b) failing to abandon the classic penalty rule of contract law;

(c) finding an anti-deprivation rule exists at common law;

(d) applying an effects-based anti-deprivation rule; and

(e) failing to consider the effect of set off.

[24] The first issue is readily dealt with: contract law and bankruptcy law work together, in this instance through the operation of the anti-deprivation rule. The second issue can also be disposed of summarily: if the provision is invalid for one reason (the anti-deprivation rule in bankruptcy law), it does not matter whether it is or is not invalid for another (the penalty rule in contract law). I will discuss the other issues below.

IV. The Existence of the Common Law Anti-Deprivation Rule

[25] As to the existence of the anti-deprivation rule, I see no error in Rowbotham J.A.'s consideration of this issue, in that the rule has existed in Canadian common law and has not been eliminated by either this Court or Parliament.

[26] Justice Rowbotham correctly found that there has been support for the anti-deprivation rule in the

c. C-36, en 2009. Même si la règle existait, il aurait adopté le test fondé sur l'objet établi dans l'arrêt *Belmont*. Chandos a repris ses conclusions devant la Cour. Le juge Wakeling aurait reformulé aussi la règle relative à la clause pénale. Étant donné mes conclusions concernant la règle anti-privation, je n'aborderai pas la règle relative à la clause pénale.

III. Questions en litige

[23] Dans le pourvoi dont nous sommes saisis, Chandos allègue que les juges majoritaires de la Cour d'appel ont commis cinq erreurs :

a) ils ont mis l'accent sur le droit de la faillite plutôt que sur le droit contractuel;

b) ils n'ont pas abandonné la règle classique relative à la pénalité du droit contractuel;

c) ils ont conclu que la règle anti-privation existe en common law;

d) ils ont appliqué une règle anti-privation fondée sur les effets;

e) ils n'ont pas examiné l'effet de la compensation.

[24] La première question se tranche facilement : le droit contractuel et le droit de la faillite s'appliquent conjointement, en l'occurrence par l'application de la règle anti-privation. On peut également répondre à la deuxième question sommairement : si la stipulation est invalide pour une raison (la règle anti-privation en droit de la faillite), il importe peu de savoir si elle est invalide pour d'autres raisons (la règle relative à la clause pénale en droit contractuel). J'examinerai les autres questions ci-après.

IV. L'existence de la règle anti-privation en common law

[25] Je ne vois pas d'erreur dans la façon dont la juge Rowbotham a examiné la question de l'existence de la règle anti-privation, puisque cette règle existe dans la common law canadienne et n'a été éliminée, ni par la Cour, ni par le Parlement.

[26] La juge Rowbotham a conclu à bon droit que les décisions qu'elle a citées appuyaient la règle

decisions to which she referred; I would add *Watson v. Mason* (1876), 22 Gr. 574 (U.C. Ch.), and *Hobbs v. Ontario Loan and Debenture Company* (1890), 18 S.C.R. 483, at p. 502, per Strong J., even if *Hobbs* is from a period in Canadian history where no federal bankruptcy legislation existed (R. J. Wood, *Bankruptcy and Insolvency Law* (2nd ed. 2015), at pp. 33-35).

[27] No decision of this Court has eliminated the anti-deprivation rule. *Coopérants*, as Rowbotham J.A. stated, was not an anti-deprivation case as there was no deprivation (*Coopérants*, at paras. 43-44).

[28] Nor has Parliament eliminated the anti-deprivation rule. As Rowbotham J.A. observed, Parliament did not implement ss. 65.1, 66.34, or 84.2 of the *BIA* so as to eliminate the anti-deprivation rule: the anti-deprivation rule protects third party creditors, whereas Parliament's changes were directed toward protecting debtors (see *Bill C-22: Clause by clause Analysis*, cl. 87, s. 65.1 and cl. 89, s. 66.34, reproduced in the Attorney General of Canada's book of authorities, at Tab 4; Standing Senate Committee on Banking, Trade and Commerce, *Debtors and Creditors Sharing the Burden: A Review of the Bankruptcy and Insolvency Act and the Companies' Creditors Arrangement Act* (2003), at pp. 74-75). This goal of protecting the debtor is relevant only where the debtor persists after the proceedings conclude. It is common for the debtor to persist after a restructuring or after the bankruptcy of a natural person. It is uncommon for the debtor to persist after a corporate bankruptcy as, typically, no assets remain for the corporation after all creditors are paid.

[29] Moreover, as the intervenor Attorney General of Canada submitted, Parliament's actions are better understood as gradually codifying limited parts of the common law rather than seeking to oust all related common law. As this Court has repeatedly observed, Parliament is presumed to intend not to change the existing common law unless it does so clearly and unambiguously (*Parry Sound (District) Social Services Administration Board v. O.P.S.E.U.,*

anti-privation. J'ajouterais les décisions *Watson c. Mason* (1876), 22 Gr. 574 (U.C. Ch.), et *Hobbs c. Ontario Loan and Debenture Company* (1890), 18 R.C.S. 483, p. 502, le juge Strong, même si cette dernière date d'une période de l'histoire canadienne où il n'existait aucune loi fédérale en matière de faillite (R. J. Wood, *Bankruptcy and Insolvency Law* (2e éd. 2015), p. 33-35).

[27] Aucune décision de notre Cour n'a éliminé la règle anti-privation. L'arrêt *Coopérants*, comme la juge Rowbotham l'a indiqué, n'était pas une affaire portant sur la règle anti-privation, car il n'y avait eu aucune privation (*Coopérants*, par. 43-44).

[28] Le Parlement n'a pas non plus éliminé la règle anti-privation. Comme la juge Rowbotham l'a observé, le Parlement n'a pas mis en œuvre les art. 65.1, 66.34 ou 84.2 de la *LFI* afin d'éliminer la règle anti-privation : en effet, cette règle protège les tiers créanciers, tandis que les modifications apportées par le Parlement visent à protéger les débiteurs (voir la *Bill C-22: Clause by clause Analysis*, cl. 87, art. 65.1 et cl. 89, art. 66.34, reproduite dans le recueil de sources du procureur général du Canada, onglet 4; Comité sénatorial permanent des banques et du commerce, *Les débiteurs et les créanciers doivent se partager le fardeau : Examen de la Loi sur la faillite et l'insolvabilité et de la Loi sur les arrangements avec les créanciers des compagnies* (2003), p. 74-75). Cet objectif de protection des débiteurs n'est pertinent que lorsqu'il existe encore un débiteur après la fin de la procédure. Cela est fréquent dans les situations de restructuration et après la faillite d'un particulier, mais toutefois rare dans les situations de faillite d'une société, puisque, typiquement, il ne reste plus d'actifs de la société une fois que tous les créanciers ont été payés.

[29] De plus, comme l'intervenant le procureur général du Canada l'a fait valoir, les interventions du Parlement doivent être considérées comme codifiant graduellement certains aspects de la common law, plutôt que comme cherchant à écarter tous les principes de common law connexes. Comme la Cour l'a noté à maintes reprises, il est présumé que le législateur n'a pas l'intention de modifier la common law existante à moins qu'il ne l'exprime clairement et

Local 324, 2003 SCC 42, [2003] 2 S.C.R. 157, at para. 39; *Heritage Capital Corp. v. Equitable Trust Co.*, 2016 SCC 19, [2016] 1 S.C.R. 306, at paras. 29-30).

[30] Indeed, the most relevant statutory provision in the *BIA* is not s. 65.1, s. 66.34, or s. 84.2, but rather s. 71. As this Court recognized in *Royal Bank of Canada v. North American Life Assurance Co.*, [1996] 1 S.C.R. 325, s. 71 provides that the property of a bankrupt "passes to and vests in the trustee" (para. 44). This helps maximize the "global recovery for all creditors" in accordance with the priorities set out in the *BIA* (*Alberta (Attorney General) v. Moloney*, 2015 SCC 51, [2015] 3 S.C.R. 327, at para. 33; see also *Husky Oil Operations Ltd. v. Minister of National Revenue*, [1995] 3 S.C.R. 453, at paras. 7-9). The anti-deprivation rule renders void contractual provisions that would prevent property from passing to the trustee and thus frustrate s. 71 and the scheme of the *BIA*. This maximizes the assets that are available for the trustee to pass to creditors.

V. The Content of the Anti-Deprivation Rule

[31] As *Bramalea* described, the anti-deprivation rule renders void contractual provisions that, upon insolvency, remove value that would otherwise have been available to an insolvent person's creditors from their reach. This test has two parts: first, the relevant clause must be triggered by an event of insolvency or bankruptcy; and second, the effect of the clause must be to remove value from the insolvent's estate. This has been rightly called an effects-based test.

[32] Chandos submits that this Court should change the anti-deprivation rule to follow *Belmont* and adopt a purpose-based test. As noted above, *Belmont* held that the English anti-deprivation rule does not invalidate provisions of "bona fide commercial transactions which do not have as their predominant purpose, or one of their main purposes,

sans ambiguïté (*Parry Sound (district), Conseil d'administration des services sociaux c. S.E.E.F.P.O., section locale 324*, 2003 CSC 42, [2003] 2 R.C.S. 157, par. 39; *Heritage Capital Corp. c. Équitable, Cie de fiducie*, 2016 CSC 19, [2016] 1 R.C.S. 306, par. 29-30).

[30] Effectivement, la disposition la plus pertinente de la *LFI* n'est pas l'art. 65.1, l'art. 66.34 ou l'art. 84.2, mais plutôt l'art. 71. Comme la Cour l'a reconnu dans l'arrêt *Banque Royale du Canada c. Nord-Américaine, cie d'assurance-vie*, [1996] 1 R.C.S. 325, cette disposition prévoit que les biens du failli « passent et sont dévolus au syndic » (par. 44). Cela contribue à maximiser le « recouvrement global pour tous les créanciers », en conformité avec les priorités énoncées dans la *LFI* (*Alberta (Procureur général) c. Moloney*, 2015 CSC 51, [2015] 3 R.C.S. 327, par. 33; voir aussi *Husky Oil Operations Ltd. c. Ministre du Revenu national*, [1995] 3 R.C.S. 453, par. 7-9). La règle anti-privation rend nulles les stipulations qui empêchent de faire passer des biens au syndic et qui contrecarrent ainsi l'objectif de l'art. 71 et le régime de la *LFI*. Cela permet de maximiser la valeur des actifs que le syndic peut remettre aux créanciers.

V. Le contenu de la règle anti-privation

[31] Comme le décrit la décision *Bramalea*, la règle anti-privation rend nulle les stipulations qui, en cas d'insolvabilité, réduisent la valeur des actifs à laquelle les créanciers de la personne insolvable aurait autrement accès. Ce test comporte deux volets : premièrement, l'application de la clause pertinente doit être déclenchée par une insolvabilité ou une faillite; et, deuxièmement, la clause doit avoir pour effet de réduire la valeur de l'actif de la personne insolvable. C'est ce qu'on appelle à juste titre un test fondé sur les effets.

[32] Chandos soutient que la Cour devrait modifier la règle anti-privation afin de suivre l'arrêt *Belmont* et adopter un test fondé sur l'objet. Comme je l'ai mentionné, dans l'arrêt *Belmont*, il a été conclu que la règle anti-privation anglaise n'invalide pas les stipulations des « opérations commerciales de bonne foi dont l'objectif prédominant ou l'un des

the deprivation of the property of one of the parties on bankruptcy". Chandos says we should follow this reasoning because upholding *bona fide* commercial agreements would strike the best balance of public policy considerations and contribute to commercial certainty. It also submits that the side-effects of such a rule would not be so deleterious, as unsecured creditors tend to receive little in bankruptcy; as well, courts would be able to tell who had inserted provisions that remove value from the debtor's estate for *bona fide* commercial reasons. None of these reasons holds water.

objectifs principaux n'est pas de priver certains acteurs concernés des biens d'une des parties en cas de faillite ». Selon Chandos, nous devrions suivre ce raisonnement, car c'est le maintien des ententes commerciales conclues de bonne foi qui permettrait le mieux d'établir le juste équilibre entre les considérations d'intérêt public et de contribuer à la stabilité commerciale. Elle soutient également que les effets secondaires d'une telle règle ne seraient pas si néfastes, car les créanciers non garantis ont tendance à recevoir peu dans les cas de faillite; en outre, les tribunaux seraient en mesure de déterminer qui a convenu d'une stipulation réduisant la valeur des actifs du débiteur de bonne foi pour des motifs commerciaux véritables. Aucun de ces arguments ne tient la route.

[33] The goal of public policy, in this instance, is not decided by the common law; rather, that policy has been established in the legislation. What is left to the common law is the choice of means that best gives effect to the statutory scheme adopted by Parliament. Thus, once a court ascertains that Parliament intended, by virtue of s. 71, that all of the bankrupt's property is to be collected in the trustee, it is not for the court to substitute a competing goal that would give rise to a different result. In this, I agree with Professor Worthington that "[a]ny avoidance, whether intentional or inevitable, is surely a fraud on the statute" ("Good Faith, Flawed Assets and the Emasculation of the UK Anti-Deprivation Rule" (2012), 75 *Mod. L. Rev.* 112, at p. 121).

[33] L'objectif d'intérêt public en l'espèce n'est pas établi par la common law. Il a plutôt été établi par les lois. Dans ce contexte, le rôle de la common law se limite à choisir le moyen qui permet le mieux de mettre en œuvre le régime législatif adopté par le législateur. Par conséquent, lorsqu'un tribunal conclut que, en adoptant l'art. 71, le législateur avait l'intention que l'ensemble des biens d'un failli soit dévolu au syndic, il ne lui appartient pas de substituer à cette intention un objectif concurrent qui donnerait lieu à un résultat différent. À cet égard, je suis d'accord avec la professeure Worthington, lorsqu'elle écrit que [TRADUCTION] « [t]out évitement, qu'il soit intentionnel ou inéluctable, est assurément une fraude envers la loi » (« Good Faith, Flawed Assets and the Emasculation of the UK Anti-Deprivation Rule » (2012), 75 *Mod. L. Rev.* 112, p. 121).

[34] In addition, I would disagree that adopting a purpose-based test would create commercial certainty. To the contrary, applying such a test would require courts to determine the intention of contracting parties long after the fact and it would detract from the efficient administration of corporate bankruptcies. Parties cannot know at the time of contracting whether a court, possibly years later, will find their contract had been entered into for *bona fide* commercial reasons. This will give rise to uncertainty at the time of contracting.

[34] En outre, je ne suis pas d'accord pour dire qu'adopter un test fondé sur l'objet créerait une stabilité commerciale. Au contraire, l'application d'un tel test obligerait les tribunaux à déterminer l'intention des parties contractantes bien après les faits, ce qui nuirait à l'administration efficace des faillites d'entreprise. Les parties ne peuvent pas savoir au moment de la conclusion d'un contrat si un tribunal, possiblement des années plus tard, jugera que leur contrat a été conclu de bonne foi pour des motifs commerciaux véritables. Cela entraînerait de l'incertitude au moment de la conclusion des contrats.

[35] The effects-based rule, as it stands, is clear. Courts (and commercial parties) do not need to look to anything other than the trigger for the clause and its effect. The effect of a clause can be far more readily determined in the event of bankruptcy than the intention of contracting parties. An effects-based approach also provides parties with the confidence that contractual agreements, absent a provision providing for the withdrawal of assets upon bankruptcy or insolvency, will generally be upheld. Maintaining an effects-based test is also consistent with the existing effects-based test recognized in *Gingras*, at p. 487, for the *pari passu* rule founded on s. 141 of the *BIA* (previously s. 112 of the *Bankruptcy Act*, R.S.C. 1970, c. B-3), as well as the effects-based test set out in ss. 65.1, 66.34 and 84.2 of the *BIA*. These tests should remain consistent to prevent duplicative proceedings and avoid arcane disputes over whether the *pari passu* rule or the anti-deprivation rule is engaged by a particular provision. Although it is often easy to tell that a provision would affect the amount a creditor will receive, determining whether this is because it deprives the estate of value (thus violating the anti-deprivation rule) or because it reallocates the estate among creditors (thus violating the *pari passu* rule) depends on the precise machinery of law, disputes over such intricacies can be avoided if both rules apply an effects-based test.

[35] La règle fondée sur les effets, telle qu'elle existe actuellement, est claire. Les tribunaux (et les parties commerciales) n'ont qu'à déterminer ce qui déclenche l'application de la clause et ses effets. Il est bien plus facile de déterminer l'effet d'une clause en cas de faillite que l'intention des parties contractantes. Une approche fondée sur les effets assure également aux parties que les ententes contractuelles, en l'absence d'une stipulation prévoyant le retrait d'actifs en cas de faillite ou d'insolvabilité, seront généralement maintenues. Le maintien d'un test fondé sur les effets est également compatible avec le test existant fondé sur les effets, reconnu dans l'arrêt *Gingras*, p. 487, applicable à la règle du *pari passu* fondée sur l'art. 141 de la *LFI* (anciennement l'art. 112 de la *Loi sur la faillite*, L.R.C. 1970, c. B-3), ainsi qu'avec le test fondé sur les effets établi aux art. 65.1, 66.34 et 84.2 de la *LFI*. Ces tests devraient rester cohérents afin d'éviter un dédoublement de procédures et des litiges complexes sur la question de savoir si la règle du *pari passu* ou la règle anti-privation est déclenchée par une stipulation en particulier. Bien qu'il soit souvent facile de dire qu'une stipulation aura un effet sur le montant que touchera un créancier, la question de savoir si c'est parce qu'elle réduit la valeur de l'actif (violant ainsi la règle anti-privation) ou parce qu'elle réattribue l'actif parmi les créanciers (violant ainsi la règle du *pari passu*) dépend de subtilités juridiques précises, et les litiges concernant de telles complexités peuvent être évités si les deux règles sont appliquées à la lumière d'un test fondé sur les effets.

[36] Moreover, an intention-based test would encourage parties who can plausibly pretend to have *bona fide* intentions to create a preference over other creditors by inserting such clauses. Parties will often be able to state some commercial rationale for provisions altering contractual rights in the event of a counterparty's insolvency, such as guarding against the risk of the counterparty's non-performance. An intention-based test would render the rule ineffectual, save in the most flagrant cases of deliberate circumvention of insolvency law. This would threaten to undermine the statutory scheme of the *BIA*.

[36] En outre, un test fondé sur l'intention encouragerait les parties qui peuvent plausiblement prétendre être de bonne foi à s'accorder une préférence à l'encontre des autres créanciers en insérant de telles clauses dans leurs contrats. Les parties seront souvent en mesure de fournir une justification commerciale pour expliquer l'existence des stipulations qui modifient les droits contractuels en cas d'insolvabilité de l'une d'entre elles, comme la protection contre le risque d'inexécution par un cocontractant. Un test fondé sur l'intention rendrait la règle inefficace, sauf dans les cas les plus évidents de contournement délibéré des lois en matière de faillite. Cela risquerait de nuire au régime législatif de la *LFI*.

[37] Reliance on general principles of contractual freedom to support an intention-based test is no less misplaced. As noted in *Bhasin v. Hrynew*, 2014 SCC 71, [2014] 3 S.C.R. 494, at para. 70, the common law of contract "generally places great weight on the freedom of contracting parties to pursue their individual self-interest" but, by definition, an assignment in bankruptcy strips the insolvent party of their interest. As Rowbotham J.A. observed, a party who might become insolvent has no incentive to resist a clause that deprives their estate of value upon bankruptcy. Parties do not negotiate with a view to protecting the interests of their creditors in the event of their bankruptcy. The costs of accepting the clause are borne solely by the unsecured creditors of the insolvent company (who are without a seat at the bargaining table) while the benefits are enjoyed only by the company while it is solvent.

[37] Il serait tout aussi mal avisé de se fonder sur des principes généraux de liberté contractuelle pour appuyer un test fondé sur l'intention. Certes, comme la Cour l'a noté dans l'arrêt *Bhasin c. Hrynew*, 2014 CSC 71, [2014] 3 R.C.S. 494, par. 70, le droit des contrats en common law « accorde généralement beaucoup de poids à la liberté des parties contractantes dans la poursuite de leur intérêt personnel », or, par définition, après une cession de biens la partie insolvable n'a plus aucun intérêt. Comme la juge Rowbotham l'a mentionné, une partie susceptible de devenir insolvable n'a aucune raison de s'opposer à une clause qui réduit la valeur de son actif en cas de faillite. Les parties ne négocient pas dans le but de protéger les intérêts de leurs créanciers en cas de faillite. Les coûts de l'acceptation d'une telle clause ne sont assumés que par les créanciers non garantis de l'entreprise insolvable (lesquels n'ont pas de place à la table de négociation), tandis que les avantages ne reviennent qu'à l'entreprise pendant qu'elle est solvable.

[38] Finally, while it may be true that unsecured creditors tend to receive relatively little now, the effect of a purpose-based rule is that they would receive less.

[38] Enfin, bien qu'il puisse être vrai que les créanciers non garantis ont tendance à recevoir bien peu de nos jours, l'application d'une règle fondée sur l'objet aurait pour effet de leur en faire recevoir encore moins.

[39] Overall, Chandos has not shown us good reason to adopt a purpose-based test. In my view, adopting the purpose-based test would create "new and greater difficulties" of the sort cautioned against in *Watkins v. Olafson*, [1989] 2 S.C.R. 750, at p. 762. As recognized in *Bhasin*, at para. 40, although a change to the Canadian common law may be appropriate when it creates greater certainty and coherence, it is not when the change would foster uncertainty and incoherence.

[39] En somme, Chandos n'a fait valoir aucune raison valable justifiant l'adoption d'un test fondé sur l'objet. À mon avis, adopter un tel test aurait pour effet de créer « des difficultés nouvelles plus grandes » comme celles contre lesquelles l'arrêt *Watkins c. Olafson*, [1989] 2 R.C.S. 750, p. 762, nous met en garde. Comme l'a reconnu l'arrêt *Bhasin*, par. 40, même s'il peut être approprié de modifier la common law canadienne afin d'apporter une plus grande certitude et une meilleure cohérence, ce n'est pas le cas lorsqu'une telle modification entraînerait de l'incertitude et de l'incohérence.

[40] All that said, we should recognize that there are nuances with the anti-deprivation rule as it stands. For example, contractual provisions that eliminate property from the estate, but do not eliminate value, may not offend the anti-deprivation rule (see *Belmont*, at para. 160, per Lord Mance; *Borland's Trustee v. Steel Brothers & Co., Limited*, [1901]

[40] Cela étant dit, nous devons reconnaître que la règle anti-privation actuelle comporte des nuances. Par exemple, les stipulations contractuelles qui retirent certains biens de l'actif, sans pour autant réduire la valeur de ce dernier, peuvent ne pas violer la règle anti-privation (voir l'arrêt *Belmont*, par. 160, motifs de lord Mance; *Borland's Trustee c. Steel*

1 Ch. 279; see also *Coopérants*). Nor do provisions whose effect is triggered by an event other than insolvency or bankruptcy. Moreover, the anti-deprivation rule is not offended when commercial parties protect themselves against a contracting counterparty's insolvency by taking security, acquiring insurance, or requiring a third-party guarantee.

[41] In sum, the Court of Appeal was correct to consider whether the effect of the contractual provision was to deprive the estate of assets upon bankruptcy rather than whether the intention of the contracting parties was commercially reasonable.

VI. Application and the Effect of Set-Off

[42] This brings us to Chandos' final argument concerning the effect of set-off on the application of the anti-deprivation rule in this case. Set-off is given statutory approval in s. 97(3) of the *BIA*:

> **(3)** The law of set-off or compensation applies to all claims made against the estate of the bankrupt and also to all actions instituted by the trustee for the recovery of debts due to the bankrupt in the same manner and to the same extent as if the bankrupt were plaintiff or defendant, as the case may be, except in so far as any claim for set-off or compensation is affected by the provisions of this Act respecting frauds or fraudulent preferences.

As this Court described in *Husky Oil*, at para. 3, s. 97(3) incorporates the provincial law of set-off (and the related civil law concept of compensation) into the federal bankruptcy regime. Set-off is a defence to the payment of a debt. The effect of set-off is to allow a creditor who happens to be also a debtor to recover ahead of their priority.

[43] The *BIA*'s affirmation of set-off and the anti-deprivation rule are not incompatible. While set-off reduces the value of assets that are transferred to the Trustee for redistribution, it is applicable only to enforceable debts or claims (see, e.g., *Holt v. Telford*, [1987] 2 S.C.R. 193, at pp. 204-6). The

Brothers & Co., Limited, [1901] 1 Ch. 279; voir aussi l'arrêt *Coopérants*). Il en va de même pour les stipulations dont l'effet est déclenché par autre chose qu'une insolvabilité ou une faillite. De plus, il n'y a pas de violation de la règle anti-privation lorsque des parties commerciales se protègent contre l'insolvabilité d'un cocontractant en obtenant une garantie ou une assurance ou en exigeant une garantie d'un tiers.

[41] En somme, la Cour d'appel s'est penchée à juste titre sur la question de savoir si l'effet de la stipulation était de réduire la valeur de l'actif en cas de faillite plutôt que sur celle de savoir si l'intention des parties contractantes était raisonnable sur le plan commercial.

VI. Application et effet de la compensation

[42] Cela nous amène à l'argument final de Chandos concernant l'effet de la compensation sur l'application de la règle anti-privation en l'espèce. La compensation est autorisée par le par. 97(3) de la *LFI* :

> **(3)** Les règles de la compensation s'appliquent à toutes les réclamations produites contre l'actif du failli, et aussi à toutes les actions intentées par le syndic pour le recouvrement des créances dues au failli, de la même manière et dans la même mesure que si le failli était demandeur ou défendeur, selon le cas, sauf en tant que toute réclamation pour compensation est atteinte par les dispositions de la présente loi concernant les fraudes ou préférences frauduleuses.

Comme la Cour l'a décrit au par. 3 de l'arrêt *Husky Oil*, le par. 97(3) incorpore les règles provinciales de la compensation (issues de la common law et du droit civil) au régime fédéral en matière de faillite. La compensation est un moyen de défense opposable au paiement d'une créance. Elle a pour effet d'autoriser un créancier qui se trouve être également un débiteur à être colloqué plus favorablement qu'il ne le serait suivant l'ordre de priorité établi par la loi.

[43] La reconnaissance de la compensation par la *LFI* et la règle anti-privation ne sont pas incompatibles. S'il est vrai que la compensation réduit la valeur des biens qui sont transférés au syndic pour redistribution, elle ne s'applique qu'aux dettes ou aux réclamations exigibles (voir, p. ex., *Holt c. Telford*,

anti-deprivation rule makes deprivations triggered by insolvency unenforceable. The combination means that set-off applies to debts owed by the bankrupt that were not triggered by the bankruptcy.

[44] The case at bar is quite different. The chapeau of clause VII Q provides that the clause triggers "[i]n the event [Capital Steel] commits any act of insolvency, bankruptcy, winding up or other distribution of assets". Since, here, the clause was triggered by bankruptcy, the threshold for considering the anti-deprivation rule had been met.[1] Clause VII Q(d) itself provides the deprivation: "[Capital Steel] shall forfeit 10% of the within Subcontract Agreement price to [Chandos] as a fee". The effect of this provision is to create a debt from Capital Steel to Chandos that would not exist but for the insolvency. It is this "debt" created by Clause VII Q(d) because of the insolvency that Chandos seeks to "set off" against the amount it owed to Capital Steel. One can hardly imagine a more direct and blatant violation of the anti-deprivation rule.

[45] Accordingly, I conclude that clause VII Q(d) violates the anti-deprivation rule and is thus void.

VII. Conclusion

[46] I would dismiss the appeal with costs throughout.

The following are the reasons delivered by

CÔTÉ J. (dissenting) —

I. Introduction

[47] I have had the advantage of reading the reasons of my colleague, Rowe J., and there is much

[1] Whether clause VII Q(d) would have been enforceable if Capital Steel had stopped operations in other circumstances is not before us and not relevant here (*Aircell*, at para. 12).

[1987] 2 R.C.S. 193, p. 204-206). La règle anti-privation rend inexigibles les réclamations fondées sur des privations déclenchées par une insolvabilité. La combinaison des deux fait en sorte que la compensation s'applique aux dettes du failli qui n'ont pas été provoquées par la faillite.

[44] En l'espèce, la situation est très différente. Le texte introductif de la clause VII Q prévoit que son application est déclenchée [TRADUCTION] « [d]ans le cas où [Capital Steel] devient insolvable, fait faillite, liquide ou distribue autrement ses actifs ». Comme l'application de la clause a été déclenchée par une faillite, il y a ouverture à l'examen de la règle anti-privation[1]. La clause VII Q(d) en soi prévoit une privation : « [Capital Steel] renonce à 10 % du prix du présent contrat de sous-traitance en faveur de [Chandos] à titre de frais ». La stipulation a pour effet de créer une dette pour Capital Steel en faveur de Chandos, dette qui n'aurait pas existé, n'eût été l'insolvabilité. C'est cette « dette » créée par la clause VII Q(d) en raison de l'insolvabilité que Chandos cherche à « compenser » en la déduisant du montant qu'elle doit à Capital Steel. On peut difficilement imaginer une violation plus directe et évidente de la règle anti-privation.

[45] En conséquence, je conclus que la clause VII Q(d) viole la règle anti-privation et est donc nulle.

VII. Conclusion

[46] Je rejetterais le pourvoi avec dépens devant toutes les cours.

Version française des motifs rendus par

LA JUGE CÔTÉ (dissidente) —

I. Introduction

[47] J'ai eu l'avantage de lire les motifs de mon collègue le juge Rowe et j'y souscris en bonne partie.

[1] La question de savoir si la clause VII Q(d) aurait été exécutoire si Capital Steel avait cessé ses activités dans d'autres circonstances n'est pas celle dont nous sommes saisis et n'est pas pertinente en l'espèce (*Aircell*, par. 12).

with which I agree in them. In particular, I agree that the anti-deprivation rule has a longstanding and strong jurisprudential footing in Canadian law and that it has not been eliminated by this Court or through legislation. However, I write to express a different view on a point of law which is central to the outcome of this appeal. In short, my view is that the anti-deprivation rule should not apply to transactions or contractual provisions which serve a *bona fide* commercial purpose. I reach this conclusion essentially for three reasons.

[48] First, my reading of the jurisprudence is that courts applying the anti-deprivation rule in Canada have not been content to rest their reasons for decision merely on a finding that the effect of a transaction or contractual provision was to deprive a bankrupt's estate of value. As I explain below, Canadian courts have looked past the effects of the arrangement and inquired into the presence or absence of a *bona fide* commercial purpose behind the deprivation.

[49] Second, there is a principled legal basis for retaining a *bona fide* commercial purpose test. The anti-deprivation rule has its origins in the common law public policy against agreements entered into for the unlawful purpose of defrauding or otherwise injuring third parties. Unlike the related *pari passu* rule, the anti-deprivation rule should not be regarded as arising from an implied prohibition in the *Bankruptcy and Insolvency Act*, R.S.C. 1985, c. B-3 ("*BIA*"). Thus, the different legal bases of the two rules explain why the *pari passu* rule operates regardless of the parties' intentions while the anti-deprivation rule takes into account the parties' *bona fide* commercial purposes.

[50] Third, as a matter of public policy, the considerations cited in support of an effects-based test are not sufficient to override the otherwise strong countervailing public interest in the enforcement of contracts. A purely effects-based test gives too little weight to freedom of contract, party autonomy,

Plus particulièrement, je conviens que la règle anti-privation est bien ancrée depuis longtemps dans la jurisprudence canadienne et qu'elle n'a été éliminée ni par la Cour ni par une loi. Cependant, je souhaite exprimer une opinion différente sur un point de droit central pour l'issue du présent pourvoi. En bref, je suis d'avis que la règle anti-privation ne devrait pas s'appliquer aux transactions ou aux stipulations qui poursuivent un objectif commercial véritable. Ma conclusion repose essentiellement sur trois motifs.

[48] Premièrement, d'après ma lecture de la jurisprudence, les tribunaux qui appliquent la règle anti-privation au Canada ne se sont pas contentés de fonder leurs décisions sur une simple conclusion voulant qu'une transaction ou une stipulation ait pour effet de réduire la valeur de l'actif du failli. Comme je l'explique ci-après, les tribunaux canadiens regardent au-delà des effets de l'arrangement et vérifient si la privation poursuit un objectif commercial véritable.

[49] Deuxièmement, le recours à un test fondé sur l'objectif commercial véritable repose sur un fondement juridique valable. La règle anti-privation tire son origine du principe de common law voulant que les accords conclus dans le but illégal de commettre une fraude ou de causer un préjudice à un tiers soient contraires à l'intérêt public. À l'inverse de la règle du *pari passu*, la règle anti-privation ne devrait pas être considérée comme découlant d'une prohibition implicite contenue dans la *Loi sur la faillite et l'insolvabilité*, L.R.C. 1985, c. B-3 (« *LFI* »). Les différents fondements juridiques qui sous-tendent la règle anti-privation et la règle du *pari passu* expliquent donc pourquoi cette dernière s'applique indépendamment de l'intention des parties, tandis que la première tient compte des objectifs commerciaux véritables des parties.

[50] Troisièmement, en ce qui concerne l'intérêt public, les considérations qui ont été citées en appui au test fondé sur les effets ne suffisent pas à transcender l'importance de l'intérêt public opposé dans l'exécution des contrats. Un test fondé purement sur les effets accorde trop peu de poids à la

and the "elbow-room" which the common law traditionally accords for the aggressive pursuit of self-interest: see *A.I. Enterprises Ltd. v. Bram Enterprises Ltd.*, 2014 SCC 12, [2014] 1 S.C.R. 177, at para. 31. In addition, Parliament has occupied much of the ground formerly covered by the common law such that there is a reduced need for a general anti-deprivation rule. Indeed, the many statutory protections already in place to safeguard the interests of creditors undermine any perceived policy need to expand the reach of the anti-deprivation rule for that purpose.

[51] Therefore, like Wakeling J.A., dissenting in the Court of Appeal below, I would hold that the anti-deprivation rule does not apply to transactions or contractual provisions which serve a *bona fide* commercial purpose. As the chambers judge (Alta. Q.B., Edmonton, No. 24-2169632, March 17, 2017; A.R., at pp. 9-10) and the Court of Appeal (2019 ABCA 32, 438 D.L.R. (4th) 195, at paras. 55 and 394-97) were unanimous in finding a *bona fide* commercial purpose behind the contractual provision at issue, I would allow the appeal and restore the order made at first instance.

II. Background

[52] My colleague provides a helpful summary of the essential facts in his reasons, and I am content to rely on it. I will therefore only highlight a few important aspects of the contractual relationships in this case.

[53] The appellant, Chandos Construction Ltd., hired Capital Steel Inc. to perform important structural steel subcontract work on a condominium project in St. Albert, Alberta ("Subcontract"). The appeal revolves around whether clause VII Q(d) ("clause Q(d)") of the Subcontract offends the anti-deprivation rule. Clause Q(d) is reproduced in my colleague's reasons. Capital Steel also provided a guarantee by which it agreed to repair and make good any defect in its work and all resulting damages that might appear as a result of any improper work: clause III, "Guarantee", A.R., at p. 155. In addition,

liberté contractuelle, à l'autonomie des parties et à la « liberté d'action » traditionnellement conférée par la common law en vue de la poursuite aggressive d'intérêts personnels : voir *A.I. Enterprises Ltd. c. Bram Enterprises Ltd.*, 2014 CSC 12, [2014] 1 R.C.S. 177, par. 31. En outre, le Parlement occupe aujourd'hui une grande partie du terrain qui relevait autrefois de la common law, ce qui diminue la nécessité d'avoir une règle anti-privation générale. En effet, les nombreuses protections déjà prévues par les lois destinées à protéger les intérêts des créanciers remettent en question le besoin d'élargir la portée de la règle anti-privation à cette même fin.

[51] Par conséquent, à l'instar du juge Wakeling, dissident en Cour d'appel, je suis d'avis que la règle anti-privation ne s'applique pas aux transactions ou aux stipulations qui visent un objectif commercial véritable. Puisque le juge siégeant en cabinet (B.R. Alb., Edmonton, nº 24-2169632, 17 mars 2017; d.a., p. 9-10) et la Cour d'appel (2019 ABCA 32, 438 D.L.R. (4th) 195, par. 55 et 394-397) ont conclu à l'unanimité que la stipulation en litige poursuivait un objectif commercial véritable, j'accueillerais le pourvoi et je rétablirais l'ordonnance rendue en première instance.

II. Contexte

[52] Mon collègue fournit dans ses motifs un résumé utile des faits essentiels, auquel je trouve peu à redire. Je me contenterai de souligner quelques aspects importants des relations contractuelles en l'espèce.

[53] L'appelante, Chandos Construction Ltd., a retenu les services de la sous-traitante Capital Steel Inc. pour construire une importante structure en acier dans le cadre d'un projet de copropriétés à St. Albert, en Alberta (« contrat de sous-traitance »). Le pourvoi porte sur la question de savoir si la clause VII Q(d) (« clause Q(d) ») du contrat de sous-traitance — reproduite dans les motifs de mon collègue — enfreint la règle anti-privation. Capital Steel a fourni une garantie selon laquelle elle s'engageait à réparer tout défaut dans ses travaux et tout dommage découlant d'un travail mal fait : clause III

Clause VII G of the Subcontract required Capital Steel to indemnify Chandos and hold it harmless "from any and all claims, costs, liabilities and causes of action" and for "any loss or damage" caused to Chandos or the owner of the condominium project by Capital Steel or any of Capital Steel's subcontractors, employees, agents, licensees, and permitees in carrying out the Subcontract. The same indemnity also applied between Capital Steel and the owner.

[54] The Stipulated Price Contract between Chandos and the owner-developer, Boudreau Developments Ltd., required Chandos to be "as fully responsible to the *Owner* for acts and omissions" of its subcontractors as it was for "acts and omissions of persons directly employed by" it: clause GC 3.7.1.3 (emphasis in original). Chandos also agreed that it would promptly correct defects or deficiencies in the work which appeared during the warranty period at its own expense: clause GC 12.3.4. As well, Chandos was obliged to correct or pay for damage resulting from such corrections: clause GC 12.3.5.

III. Issues

[55] The focus of these reasons is whether the anti-deprivation rule applies regardless of the parties' *bona fide* commercial purposes.

[56] Another issue raised by the parties is whether clause Q(d) is a valid liquidated damages provision or an unenforceable penalty clause. The chambers judge, Justice Nielsen, concluded that the clause was a valid liquidated damages provision. That finding was not disturbed on appeal, and I do not see any extricable error of law which would justify appellate interference with it. I therefore decline to address this issue further.

[TRADUCTION] « Garantie », d.a., p. 155. De plus, selon la clause VII G du contrat de sous-traitance, Capital Steel s'est engagée à indemniser Chandos et à la dégager de toute responsabilité « relativement à toute réclamation, dépense, dette et cause d'action » et pour « toute perte ou tout dommage » causé, dans l'exécution du contrat de sous-traitance, à Chandos ou au promoteur du projet immobilier par Capital Steel ou par un de ses sous-traitants, employés, mandataires et titulaires de licences et de permis. Capital Steel assumait la même obligation d'indemniser à l'égard du promoteur.

[54] Le contrat à forfait conclu entre Chandos et le propriétaire-promoteur, Boudreau Developments Ltd., prévoyait que Chandos serait [TRADUCTION] « aussi pleinement responsable à l'égard du *propriétaire* pour les actes et omissions » de ses sous-traitants qu'elle l'était pour les « actes et omissions des personnes qu'elle emploie directement » : clause GC 3.7.1.3 (en italique dans l'original). Chandos a également convenu qu'elle corrigerait rapidement, et à ses frais, les défauts apparaissant dans les travaux durant la période de garantie : clause GC 12.3.4. En outre, Chandos était tenue de corriger ou de payer les dommages découlant des corrections : clause GC 12.3.5.

III. Questions en litige

[55] Les présents motifs visent à déterminer si la règle anti-privation s'applique indépendamment des objectifs commerciaux véritables des parties.

[56] Les parties soulèvent par ailleurs la question de savoir si la clause Q(d) constitue une stipulation valide relative aux dommages-intérêts liquidés ou une clause pénale non exécutoire. Le juge Nielsen, siégeant en son cabinet, a conclu qu'il s'agissait d'une disposition valide relative aux dommages-intérêts liquidés. Cette conclusion n'a pas été infirmée en appel et je ne vois aucune erreur de droit identifiable qui justifierait une intervention en appel. Je m'abstiendrai donc d'examiner cette question plus attentivement.

IV. Analysis

A. *The Anti-Deprivation Rule Does Not Apply Where a Transaction or Contractual Provision Serves a Bona Fide Commercial Purpose*

[57] Before embarking upon an analysis of whether the jurisprudence on the anti-deprivation rule has traditionally included a purpose element, I find it useful to clearly state what I mean by a "*bona fide* commercial purpose".

[58] The inquiry I propose is primarily objective and centres around the presence or absence of a legitimate commercial basis for a transaction or contractual provision. An objective approach dovetails with the approach taken in another important and related area of commercial law, the interpretation of contracts, where "the goal of the exercise is to ascertain the objective intent of the parties": *Sattva Capital Corp. v. Creston Moly Corp.*, 2014 SCC 53, [2014] 2 S.C.R. 633, at para. 49. It also parallels this Court's approach to ascertaining the purpose behind commercial transactions in tax characterization cases. As this Court stated in *Symes v. Canada*, [1993] 4 S.C.R. 695, at p. 736:

> As in other areas of law where purpose or intention behind actions is to be ascertained, it must not be supposed that in responding to this question, courts will be guided only by a taxpayer's statements, *ex post facto* or otherwise, as to the subjective purpose of a particular expenditure. Courts will, instead, look for objective manifestations of purpose, and purpose is ultimately a question of fact to be decided with due regard for all of the circumstances.

(See also *Ludco Enterprises Ltd. v. Canada*, 2001 SCC 62, [2001] 2 S.C.R. 1082, at para. 54.)

[59] Obviously, evidence of a lack of subjective good faith is relevant to such an inquiry; however, positive assertions of good faith, while relevant, are not determinative. Courts applying the anti-deprivation rule should (and do) have due regard to the parties' objective manifestations of purpose.

IV. Analyse

A. *La règle anti-privation ne s'applique pas lorsque la transaction ou la stipulation vise un objectif commercial véritable*

[57] Avant de débuter l'analyse de la question de savoir si la jurisprudence concernant la règle anti-privation a toujours inclus une notion d'objectif, je crois qu'il est utile d'énoncer clairement ce que je veux dire par « objectif commercial véritable ».

[58] L'examen que je propose est principalement objectif et est centré sur la présence ou l'absence d'un fondement commercial légitime pour justifier une transaction ou une stipulation. Une approche objective concorde bien avec l'approche adoptée dans un autre domaine du droit commercial important et connexe, soit l'interprétation contractuelle, où « le but de l'exercice consiste à déterminer l'intention objective des parties » : *Sattva Capital Corp. c. Creston Moly Corp.*, 2014 CSC 53, [2014] 2 R.C.S. 633, par. 49. Elle concorde également avec l'approche adoptée par la Cour pour déterminer l'objectif des transactions commerciales dans les affaires de qualification fiscale. Comme la Cour l'a déclaré dans l'arrêt *Symes c. Canada*, [1993] 4 R.C.S. 695, p. 736 :

> Comme dans d'autres domaines du droit, lorsqu'il faut établir l'objet ou l'intention des actes, on ne doit pas supposer que les tribunaux se fonderont seulement, en répondant à cette question, sur les déclarations du contribuable, *ex post facto* ou autrement, quant à l'objet subjectif d'une dépense donnée. Ils examineront plutôt comment l'objet se manifeste objectivement, et l'objet est en définitive une question de fait à trancher en tenant compte de toutes les circonstances.

(Voir aussi *Entreprises Ludco Ltée c. Canada*, 2001 CSC 62, [2001] 2 R.C.S. 1082, par. 54.)

[59] Évidemment, une preuve démontrant l'absence de bonne foi subjective est pertinente dans un tel examen, mais les affirmations positives de bonne foi, bien qu'elles soient pertinentes, ne sont pas déterminantes. Les tribunaux qui appliquent la règle anti-privation devraient tenir dûment compte (et ils

In the case of the anti-deprivation rule, the primary means by which the parties objectively manifest their intentions is through the terms of the contractual agreements by which they bind themselves. Therefore, careful regard should be had to the terms of the contractual arrangements which are said to offend the anti-deprivation rule.

[60] I add that the leading English authority on the anti-deprivation rule also employs a similar approach to determining the purpose behind the transaction or contractual provision at issue: *Belmont Park Investments Pty. Ltd. v. BNY Corporate Trustee Services Ltd.*, [2011] UKSC 38, [2012] 1 A.C. 383, at paras. 74-79, per Lord Collins; and para. 151, per Lord Mance.

[61] With this understanding in hand, I now turn to consider, as an empirical question, whether courts applying the anti-deprivation rule inquire into the presence or absence of such a purpose.

(1) Courts Applying the Anti-Deprivation Rule Inquire into the Existence of a *Bona Fide* Commercial Purpose

[62] As Canadian courts considering the anti-deprivation rule have often had recourse to English jurisprudence on the rule, I begin by briefly looking at whether the English jurisprudence has traditionally included a *bona fide* commercial purpose test. I then turn to a more thorough consideration of the Canadian jurisprudence to determine whether Canadian courts inquire into the presence or absence of a *bona fide* commercial purpose when applying the anti-deprivation rule.

(a) *English Jurisprudence*

[63] I do not intend to undertake an extended review of the English anti-deprivation rule in these reasons. The United Kingdom Supreme Court recently did so in *Belmont*, and I cannot hope to add much of value to the thorough analysis offered in that decision. I will therefore confine my general comments on the English jurisprudence to *Belmont*.

le font) des manifestations objectives de l'intention des parties. Dans le cas de la règle anti-privation, les termes des contrats qui les lient sont le principal moyen par lequel les parties manifestent objectivement leurs intentions. Par conséquent, on doit examiner attentivement les termes des contrats qui contreviendraient à la règle anti-privation.

[60] J'ajoute que l'arrêt de principe anglais sur la règle anti-privation adopte une approche similaire pour déterminer l'objectif de la transaction ou de la stipulation en litige : *Belmont Park Investments Pty. Ltd. c. BNY Corporate Trustee Services Ltd.*, [2011] UKSC 38, [2012] 1 A.C. 383, par. 74-79, le lord Collins; et par. 151, le lord Mance.

[61] Ayant ces considérations à l'esprit, je me tourne maintenant vers la question empirique de savoir si les tribunaux s'enquièrent de la présence ou de l'absence d'un tel objectif lorsqu'ils appliquent la règle anti-privation.

(1) Les tribunaux s'enquièrent de l'existence d'un objectif commercial véritable lorsqu'ils appliquent la règle anti-privation

[62] Comme les tribunaux canadiens qui se sont penchés sur la règle anti-privation ont souvent eu recours à la jurisprudence anglaise portant sur cette règle, je vérifierai d'abord si la jurisprudence anglaise a traditionnellement eu recours à un test fondé sur l'objectif commercial véritable. J'examinerai ensuite plus attentivement la jurisprudence canadienne afin de déterminer si les tribunaux canadiens se penchent sur la présence ou l'absence d'un objectif commercial véritable lorsqu'ils appliquent la règle anti-privation.

a) *La jurisprudence anglaise*

[63] Je n'ai pas l'intention d'entreprendre un examen exhaustif de la règle anti-privation anglaise dans les présents motifs. La Cour suprême du Royaume-Uni s'est prêtée à un tel exercice dans le récent arrêt *Belmont*, et je ne peux espérer ajouter à son analyse exhaustive. Mes observations générales concernant la jurisprudence anglaise ne porteront donc que sur cet arrêt.

[64] The respondent, Deloitte Restructuring Inc., argues that *Belmont* "shifted" the English common law from an effects-based test to a purpose-based test for the anti-deprivation rule: R.F., at para. 115. However, in my view, *Belmont* recognized that a purpose requirement has always been an element of the English anti-deprivation rule. Lord Collins undertook an extensive review of the English jurisprudence on the anti-deprivation rule: paras. 58-73. He found that, "where the rule has been applied, it has been an almost invariably expressed element that the party seeking to take advantage of the deprivation was intending to evade the bankruptcy rules": para. 75. Further, in the English authorities "where the either . . . or anti-deprivation rule was held not to apply, good faith and the commercial sense of the transaction have been important factors": para. 77. Lord Collins was thus able to conclude that the English jurisprudence reflected "an impressive body of opinion from some of the most distinguished judges that, in the case of the anti-deprivation rule, a deliberate intention to evade the insolvency laws is required": para. 78; see also paras. 152-53, per Lord Mance.

[65] I find Lord Collins's review of the English jurisprudence, as well as the conclusions of law he drew from it, to be authoritative characterizations of the English position on the anti-deprivation rule. I therefore cannot accept that *Belmont*'s recognition of a purpose requirement for the anti-deprivation rule was as novel as Deloitte suggests. Further, as I demonstrate below, the Canadian jurisprudence on the anti-deprivation rule also supports the conclusion that a purpose requirement is not a novel feature of the anti-deprivation rule.

(b) *Canadian Jurisprudence*

(i) Supreme Court of Canada Jurisprudence

[66] While this appeal gives this Court its first opportunity to fully consider and apply the anti-deprivation rule, in three previous decisions the Court either commented in *obiter* on this area of the

[64] L'intimée, Restructuration Deloitte Inc., a plaidé que l'arrêt *Belmont* a [TRADUCTION] « fait passer » la règle anti-privation anglaise d'un test fondé sur l'effet à un test fondé sur l'objectif : m.i., par. 115. Selon moi, l'arrêt *Belmont* a plutôt reconnu que l'objectif a toujours été un élément constitutif de la règle anti-privation anglaise. Lord Collins a effectué un examen exhaustif de la jurisprudence anglaise sur la règle anti-privation : par. 58-73. Il a constaté que, [TRADUCTION] « dans les cas où la règle a été appliquée, on relevait presque toujours le fait que la partie cherchant à profiter de la privation tentait d'éviter les règles en matière de faillite » : par. 75. En outre, dans les précédents anglais faisant autorité [TRADUCTION] « où il a été jugé que la règle anti-privation ne s'appliquait pas, la bonne foi et l'objectif commercial de la transaction ont été des facteurs importants » : par. 77. Lord Collins a donc pu conclure que la jurisprudence anglaise représentait [TRADUCTION] « un corpus impressionnant relatant l'opinion de certains des juges les plus éminents selon qui, dans le cas de la règle anti-privation, il devait y avoir une intention délibérée de contourner les lois en matière d'insolvabilité » : par. 78; voir aussi par. 152-153, le lord Mance.

[65] Je considère que l'examen de la jurisprudence anglaise par lord Collins ainsi que les conclusions de droit qu'il en a tirées font autorité quant à la position du droit anglais sur la règle anti-privation. Je ne saurais donc accepter que la reconnaissance, exprimée dans l'arrêt *Belmont*, de l'objectif comme élément constitutif de la règle anti-privation soit aussi nouvelle que Deloitte le laisse entendre. En outre, comme je le démontre ci-après, la jurisprudence canadienne relative à la règle anti-privation appuie elle aussi la conclusion selon laquelle une exigence relative à l'objectif n'est pas une caractéristique nouvelle de la règle anti-privation.

b) *La jurisprudence canadienne*

(i) Jurisprudence de la Cour suprême du Canada

[66] Bien que le présent pourvoi soit la première occasion qu'a la Cour d'examiner pleinement et d'appliquer la règle anti-privation, elle a déjà, à trois reprises, soit formulé des commentaires incidents

law or considered contractual arrangements which would have been subject to the anti-deprivation rule or the *pari passu* rule had the contracts in question been governed by the common law. On my reading, this Court's jurisprudence favours a *bona fide* commercial purpose test for the anti-deprivation rule.

[67] This Court had an opportunity to comment in *obiter* on the fraud upon the bankruptcy laws principle in *Hobbs v. Ontario Loan and Debenture Company* (1890), 18 S.C.R. 483. A mortgage provided that the mortgagees leased the mortgaged property to the mortgagor and that the rent was equal to the principal payments under the mortgage. The issue was whether the rights created by the lease were enforceable as against a third party execution creditor.

[68] Chief Justice Ritchie (Taschereau J., as he then was, concurring) concluded that a sham lease in a mortgage which is not intended to create a *bona fide* landlord-tenant relationship is void as against assignees in bankruptcy: pp. 486-89. Justice Strong, as he then was (Fournier J., concurring) agreed: pp. 502-3 and 507. However, they disagreed as to the result. Chief Justice Ritchie found that there was a *bona fide* arrangement because there was no bankruptcy law in force, whereas Strong J. found that there was not such an arrangement because the principle has wider application outside of bankruptcy: pp. 485-87 and 508-9.

[69] The authorities on which Ritchie C.J. and Strong J. relied were based on the English fraud upon the bankruptcy laws principle. Chief Justice Ritchie relied heavily upon the decision of the English Court of Appeal in *Ex parte Voisey* (1882), 21 Ch. D. 442 (C.A.), quoting the reasons of Lord Brett, at pp. 459 and 461:

sur ce domaine du droit, soit examiné des ententes contractuelles qui auraient été assujetties à la règle anti-privation ou à la règle du *pari passu* si les contrats en question avaient été régis par la common law. D'après ma lecture, la jurisprudence de la Cour favorise le recours à un test fondé sur l'objectif commercial véritable lorsqu'il s'agit d'appliquer la règle anti-privation.

[67] La Cour a eu l'occasion de formuler des commentaires incidents sur le principe de fraude contre les lois en matière de faillite dans l'arrêt *Hobbs c. Ontario Loan and Debenture Company* (1890), 18 R.C.S. 483. Un contrat hypothécaire prévoyait que le créancier hypothécaire louait la propriété hypothéquée au débiteur hypothécaire et que le loyer équivalait aux paiements du capital prévus par le contrat. Il s'agissait de savoir si les droits créés par le bail étaient exécutoires contre un tiers créancier saisissant.

[68] Le juge en chef Ritchie (le juge Taschereau, plus tard juge en chef, souscrivant à ses motifs) a conclu qu'un faux bail prévu dans un contrat hypothécaire qui n'a pas pour but de créer une relation propriétaire-locataire véritable est nul à l'égard des cessionnaires dans le cadre d'une faillite : p. 486-489. Le juge Strong, plus tard juge en chef, a souscrit à cette position (avec l'appui du juge Fournier) : p. 502-503 et 507. Ils n'étaient toutefois pas d'accord quant à l'issue de l'appel. Le juge en chef Ritchie a conclu à un arrangement de bonne foi, car aucune loi en matière de faillite n'était en vigueur. Le juge Strong a plutôt conclu à l'absence d'un tel arrangement, car le principe avait un vaste champ d'application qui allait au-delà de la faillite : p. 485-487 et 508-509.

[69] La jurisprudence sur laquelle le juge en chef Ritchie et le juge Strong se sont fondés reposait sur le principe anglais de fraude contre les lois en matière de faillite. Le juge en chef Ritchie s'est appuyé fortement sur la décision rendue par la Cour d'appel de l'Angleterre dans l'arrêt *Ex parte Voisey* (1882), 21 Ch. D. 442 (C.A.), citant les motifs de lord Brett, qui a déclaré ce qui suit, aux p. 459 et 461 :

The only way in which it can cease to be a *bona fide* contract is if it was not intended to be acted upon between the parties at all, and was only a device to evade the bankruptcy laws. That would not be what is ordinarily called a fraud, but it would be what is called a fraud upon the bankruptcy laws, that is, an attempt to evade the bankruptcy laws in case of a bankruptcy. Now that attempted evasion, that want of *bona fides* with regard to the bankruptcy laws, must exist, if at all, at the moment when the contract is made. . . .

. . .

. . . the question is whether there was a real honest stipulation between the parties, intended to be acted upon whether there should be a bankruptcy or not, or whether it was a stipulation which they intended to be acted upon only for the purpose of defeating the bankruptcy law.

[70] Justice Strong also relied on *Ex parte Williams* (1877), 7 Ch. D. 138 (C.A.), the *ratio decidendi* of which he described as being that "any provision by a debtor that in the event of his becoming bankrupt or insolvent there shall be a different distribution of his effects from that which the law provides is void": p. 502. While noting that *Williams* was of limited value due to the lack of bankruptcy legislation in Canada, Strong J. went on to comment favourably upon the English cases which followed it, including *Voisey*. He described the law established by those authorities as being that, if it appears that the tenancy for which a mortgage provides is not intended by the parties to be a *bona fide* agreement, and is instead a sham or pretence, then such a lease is "void . . . as against the assignees in bankruptcy": p. 503. Justice Strong adopted these principles, adding that they must have a wider application beyond the bankruptcy context in order to protect third parties more generally.

[71] The separate opinion of Patterson J. is also noteworthy because he stated that the enforceability of the tenancy between the mortgagor and a third party depended in part on the "*bona fides* of the transaction": p. 543. He noted that the *bona fides* of a transaction "has usually been tested in England in the light of the bankruptcy law", and, while Canada did not have a bankruptcy law at that time, it did "not

[TRADUCTION] Un contrat ne peut cesser d'être un contrat de bonne foi que si les parties n'avaient aucune intention de l'exécuter et s'il n'était qu'un moyen de contourner les lois en matière de faillite. Il ne s'agirait pas de ce que l'on appelle généralement une fraude, mais plutôt d'une fraude contre les lois en matière de faillite, c'est-à-dire une tentative de contourner ces lois en cas de faillite. Cela étant, cette tentative de contournement ou ce défaut de bonne foi à l'égard des lois en matière de faillite doit exister, à tout le moins, au moment de la conclusion du contrat . . .

. . .

. . . la question est de savoir si les parties ont véritablement et honnêtement conclu un contrat qu'elles avaient l'intention d'exécuter, qu'il y ait faillite ou non, ou s'il s'agit plutôt d'un contrat qu'elles avaient l'intention d'exécuter seulement afin de contourner les lois en matière de faillite.

[70] Le juge Strong s'est également fondé sur l'arrêt *Ex parte Williams* (1877), 7 Ch. D. 138 (C.A.), dont il a décrit la *ratio decidendi* comme établissant que [TRADUCTION] « toute disposition par laquelle un débiteur prévoit que ses biens seront distribués différemment de ce que prévoit la loi en cas de faillite ou d'insolvabilité est nulle » : p. 502. Bien qu'il ait noté que l'arrêt *Williams* avait peu de valeur en raison de l'absence de lois sur la faillite au Canada, le juge Strong a commenté favorablement les décisions anglaises qui ont suivi cet arrêt, y compris l'arrêt *Voisey*. D'après sa description du droit établi par ces précédents, s'il semble que la location prévue par le contrat hypothécaire n'est pas considérée comme un contrat de bonne foi par les parties et s'il s'agit plutôt d'un leurre ou d'une escroquerie, alors le bail est [TRADUCTION] « nul [. . .] à l'égard des cessionnaires dans le cadre d'une faillite » : p. 503. Le juge Strong a adopté ces principes, ajoutant qu'ils doivent s'appliquer bien au-delà du contexte de la faillite afin de protéger les tiers plus généralement.

[71] L'opinion du juge Patterson est également digne de mention, car il a déclaré que le caractère exécutoire d'un bail entre le créancier hypothécaire et un tiers dépendait en partie de [TRADUCTION] « l'authenticité de la transaction » : p. 543. Il a mentionné que cette authenticité de la transaction [TRADUCTION] « a habituellement été examinée en Angleterre dans le contexte du droit de la faillite » et,

therefore follow that the intention with which the lease is made is to be disregarded": p. 543.

[72] In my view, the reasons of Ritchie C.J. and Strong and Patterson JJ. indicate this Court's nearly unanimous *obiter* approval both of the existence of a general fraud upon the bankruptcy laws principle, even if it could not be applied at the time, and of a *bona fide* commercial purpose test corresponding to that principle.

[73] This Court addressed a set of circumstances resembling those governed by the common law anti-deprivation rule in *Coopérants, Mutual Life Insurance Society (Liquidator of) v. Dubois*, [1996] 1 S.C.R. 900. Mr. Dubois and Coopérants were the undivided co-owners of two immovables situated in Laval, Quebec. Their interests in the immovables were governed by two agreements in which they waived the right to demand a partition of the immovables for 35 years. Each agreement also provided that, in the event that one of the parties applied to a court for the appointment of a liquidator for the party's property, that party's interest in the immovable in question had to be sold to the counterparty. If the parties did not agree on the price, the defaulting party's interest would be sold to the counterparty at 75 percent of its fair market value, which was to be determined without regard to the fact that the immovable was held in undivided co-ownership. Subsequently, Coopérants applied to a court for the appointment of a liquidator due to insolvency, and Mr. Dubois sought to rely on the forced sale clause in their agreements.

[74] This Court held that the liquidator was bound by the clause because there was no evidence that the contractual method for determining the sale price resulted in a price which was less than fair market value, nor was there any evidence that the clause gave Mr. Dubois an "unjust preference": para. 41.

[75] I caution against overreliance on *Coopérants* for the purposes of ascertaining the content of a common law rule. The agreements at issue were governed by the *Civil Code of Lower Canada*, not

bien que le Canada n'ait pas eu de loi sur la faillite à cette époque, cela « ne voulait pas dire que l'intention derrière le bail devait être négligée » : p. 543.

[72] À mon avis, les motifs du juge en chef Ritchie et des juges Strong et Patterson indiquent que la Cour a approuvé, dans un *obiter* presque unanime, tant l'existence d'un principe général de fraude contre les lois en matière de faillite, même s'il s'avérait inapplicable à cette époque, que le test fondé sur l'objectif commercial véritable correspondant à ce principe.

[73] La Cour a examiné un ensemble de circonstances qui ressemblent à celles régies par la règle antiprivation de common law dans l'arrêt *Coopérants (Les), Société mutuelle d'assurance-vie (Liquidateur de) c. Dubois*, [1996] 1 R.C.S. 900. M. Dubois et Les Coopérants étaient les copropriétaires indivis de deux immeubles situés à Laval, au Québec. Leurs intérêts dans les immeubles étaient régis par deux conventions qui prévoyaient une renonciation au droit de demander le partage des biens immeubles pour une période de 35 ans. Chaque convention prévoyait également que si l'une des parties présentait une demande judiciaire pour la nomination d'un liquidateur de ses biens, l'intérêt de cette partie dans l'immeuble devait être vendu à l'autre. Si les parties ne s'entendaient pas sur le prix, l'intérêt de la partie défaillante devait être vendu à l'autre partie à 75 p. 100 de la juste valeur marchande, laquelle devait être établie sans égard au fait que l'immeuble était détenu en indivision. Subséquemment, Les Coopérants a présenté une demande judiciaire pour la nomination d'un liquidateur pour motif d'insolvabilité et M. Dubois a cherché à faire exécuter la clause de vente forcée prévue par leurs conventions.

[74] La Cour a conclu que le liquidateur était tenu de respecter la clause de vente forcée, car rien ne prouvait que la méthode prévue au contrat pour déterminer le prix de vente résultait en un prix inférieur à la juste valeur marchande et que la clause accordait à M. Dubois une « préférence injuste » : par. 41.

[75] Je conseille d'éviter un recours immodéré à l'arrêt *Coopérants* pour déterminer le contenu d'une règle de common law. Les contrats en cause étaient régis par le *Code civil du Bas-Canada* et

the common law, and the Court's comments regarding the enforceability of the clause in question were directed at how a court should exercise its discretion under what is now the *Winding-up and Restructuring Act*, R.S.C. 1985, c. W-11. Nonetheless, *Coopérants* is significant for having recognized the importance of enforcing arrangements which reflect a *bona fide* commercial purpose. The Court noted that the clause at issue created an obligation to sell a unique, non-fungible and indivisible property in which Mr. Dubois, as co-owner, had a specific interest. The Court also observed that the agreements in which the clause was found included reciprocal obligations between the co-owners, which called for ongoing performance. This Court stated that "[i]t is advisable to respect such contracts and ensure that they are as stable as possible": para. 38. Thus, this Court acknowledged that the clause at issue served a *bona fide* commercial purpose which the law should strive to uphold, even if doing so granted a degree of preference over other creditors.

[76] Finally, this Court addressed a set of circumstances resembling those governed by the *pari passu* rule in *A.N. Bail Co. v. Gingras*, [1982] 2 S.C.R. 475. A contract between a general contractor and a subcontractor authorized the general contractor to pay the subcontractor's suppliers directly in order to discharge obligations arising out of a construction project. The subcontractor entered into bankruptcy proceedings and the general contractor made use of the provision in question to pay one of the subcontractor's suppliers, which was a creditor of the subcontractor. This Court held that in the bankruptcy context such arrangements could not be used to supplant the *pari passu* distribution scheme in the *BIA*. This was so notwithstanding the general contractor's good faith.

[77] *Gingras* is consistent with the English approach to the *pari passu* rule. The House of Lords held in *British Eagle International Airlines Ltd. v. Cie Nationale Air France*, [1975] 1 W.L.R. 758 (H.L.), that the *pari passu* rule applies where the effect of a contract is that a bankrupt's assets would

non par la common law, et les commentaires de la Cour concernant l'applicabilité de la clause portaient sur la façon dont un tribunal doit exercer le pouvoir discrétionnaire qui lui est aujourd'hui conféré par la *Loi sur les liquidations et les restructurations*, L.R.C. 1985, c. W-11. L'arrêt *Coopérants* est néanmoins crucial puisqu'il a reconnu l'importance d'exécuter les conventions qui reflètent un objectif commercial véritable. La Cour a noté que la clause dont il était question créait l'obligation de vendre un bien unique, non fongible et indivisible à l'égard duquel M. Dubois, en tant que copropriétaire, avait un intérêt particulier. Elle a également observé que les conventions dans lesquelles se trouvait la clause comportaient des obligations réciproques pour les deux copropriétaires qui nécessitaient une continuité dans le temps. Elle a indiqué qu'« [i]l y a intérêt à respecter de tels contrats et à assurer leur stabilité dans la mesure du possible » : par. 38. Par conséquent, la Cour a reconnu que la clause en litige visait un objectif commercial véritable que les tribunaux doivent s'efforcer de respecter, même si cela accorde une préférence à certains créanciers plutôt qu'à d'autres.

[76] Enfin, la Cour a examiné un ensemble de circonstances ressemblant à celles régies par la règle du *pari passu* dans l'arrêt *A.N. Bail Co. c. Gingras*, [1982] 2 R.C.S. 475. Un contrat conclu entre un entrepreneur général et un sous-entrepreneur autorisait l'entrepreneur général à payer directement les fournisseurs du sous-entrepreneur pour les obligations liées au projet de construction. Le sous-entrepreneur a entamé une procédure de faillite et l'entrepreneur général s'est prévalu de la disposition contractuelle pour payer un des fournisseurs du sous-entrepreneur, qui était un créancier de ce dernier. La Cour a conclu que, dans le contexte d'une faillite, de tels contrats ne peuvent être utilisés pour supplanter le régime de distribution *pari passu* prévu par la *LFI*. Et cela, malgré la bonne foi de l'entrepreneur général.

[77] L'arrêt *Gingras* est compatible avec l'approche anglaise de la règle du *pari passu*. La Chambre des lords a conclu, dans l'arrêt *British Eagle International Airlines Ltd. c. Cie Nationale Air France*, [1975] 1 W.L.R. 758 (H.L.), que la règle du *pari passu* s'applique lorsque l'effet d'un contrat

be distributed to the bankrupt's creditors otherwise than in accordance with the bankruptcy laws, notwithstanding the parties' legitimate commercial purposes. However, as I explain in detail below, it does not follow that the anti-deprivation rule must adopt a similar effects-based test. Certainly, the United Kingdom Supreme Court did not regard *British Eagle* as precluding it from holding that the English anti-deprivation rule includes a *bona fide* commercial purpose element: *Belmont*. Therefore, I do not view *Gingras* as undermining the existence of a *bona fide* commercial purpose test for the anti-deprivation rule.

[78] In summary, *Hobbs* and *Coopérants* include significant *obiter dicta* which are suggestive of a *bona fide* commercial purpose test for the common law anti-deprivation rule. *Gingras* neither contradicts those *obiter dicta* nor departs from the law of England as stated in *Belmont* and *British Eagle*. Therefore, I am of the view that this Court's jurisprudence favours a *bona fide* commercial purpose test for the anti-deprivation rule — though, to be clear, this Court has not previously bound itself as a matter of *stare decisis* in this regard. My empirical inquiry must, therefore, live or die on the jurisprudence of the courts that have actually applied the common law anti-deprivation rule.

(ii) Superior Court and Appellate Jurisprudence

[79] On my reading of the jurisprudence, courts applying the anti-deprivation rule in Canada have not been content to rest their reasons for decision merely on a finding that the effect of a transaction or contractual provision was to deprive a bankrupt's estate of value. As I explain below, courts have looked past the effects of the arrangement and inquired into the presence or absence of a *bona fide* commercial purpose behind the deprivation. In the minority of cases where this discussion has not occurred, the absence of a *bona fide* commercial purpose has been readily inferable from the circumstances. These observations

sera d'entraîner une distribution des biens d'un failli à ses créanciers différente de celle prévue par les lois en matière de faillite, et ce, en dépit des objectifs commerciaux légitimes des parties. Cependant, comme je l'explique en détail, cela ne veut pas dire que la règle anti-privation doive entraîner le recours à un test similaire fondé sur les effets. Clairement, la Cour suprême du Royaume-Uni n'a pas considéré que l'affaire *British Eagle* l'empêchait de conclure que la règle anti-privation anglaise comprend une notion d'objectif commercial véritable : *Belmont*. Par conséquent, je considère que l'affaire *Gingras* ne nie pas l'existence d'un test fondé sur l'objectif commercial véritable auquel il faut recourir pour l'application de la règle anti-privation.

[78] En résumé, les arrêts *Hobbs* et *Coopérants* énoncent des *obiter dicta* importants qui évoquent un test fondé sur l'objectif commercial véritable auquel il faut recourir pour l'application de la règle anti-privation de common law. L'arrêt *Gingras* ne contredit pas ces *obiter dicta* ni ne s'écarte du droit anglais, tel qu'il a été énoncé dans les affaires *Belmont* et *British Eagle*. Je suis donc d'avis que la jurisprudence de la Cour favorise le recours à un test fondé sur l'objectif commercial véritable des parties pour l'application de la règle anti-privation — quoique, je le précise, la Cour ne se soit pas liée par le principe de *stare decisis* à cet égard. Mon examen empirique doit donc reposer sur la jurisprudence des tribunaux qui ont appliqué la règle anti-privation de common law.

(ii) Jurisprudence de la Cour supérieure et de la Cour d'appel

[79] D'après ma lecture de la jurisprudence, les tribunaux qui ont appliqué la règle anti-privation au Canada ne se sont pas contentés de fonder leurs décisions sur une simple conclusion voulant qu'une transaction ou une stipulation ait pour effet de réduire la valeur de l'actif du failli. Comme je l'explique ci-après, les tribunaux ont regardé au-delà des effets du contrat et ont vérifié si la privation poursuivait un objectif commercial véritable. Dans les rares cas où cet examen n'a pas été réalisé, il était facile d'inférer des circonstances l'absence d'un objectif commercial véritable. Ces observations me mènent

lead me to conclude that a *bona fide* commercial purpose element has a strong jurisprudential footing in Canadian law.

[80] The Ontario Court of Appeal, in *In Re Hoskins and Hawkey, Insolvents* (1877), 1 O.A.R. 379, applied the anti-deprivation rule to a lease which provided that upon the insolvency of the tenant, the current year's rent and the succeeding year's rent would be due and payable. The landlord argued that the additional year's rent was intended as compensation for his loss of a tenant. If the test the Court of Appeal applied had been focused solely on the effects of the provision, it would not have had to address this argument. Nonetheless, it did. The court rejected the landlord's argument, noting that it was "discredited by the circumstance that a surrender by a tenant, who had become insolvent, imports advantage rather than loss" for the landlord: p. 384. At p. 385, the court quoted with approval the decision of Lord Chancellor Redesdale in *Murphy, a Bankrupt* (1803), 1 Ch. 44, at p. 49, which has often been cited in Canada:

> The question is, whether a person can be admitted to prove as a creditor, on the foundation of an instrument contrived for the purpose of defeating the effect of the bankrupt laws; where the only ground of the claim is an instrument executed for the purpose of giving a right against creditors, which would not exist against the bankrupt if he were solvent. All the cases in England have held this to be a fraud upon the bankrupt laws, which cannot be supported . . . . [Emphasis added.]

[81] Applying *Murphy*, the Court of Appeal concluded that the provision stipulating the payment of an additional year's rent to the landlord was invalid. In essence, the court found that there was no legitimate commercial purpose for the landlord to receive what would effectively be a gratuitous payment of an additional year's worth of rent long after the tenancy had come to an end.

[82] The same Court of Appeal applied the anti-deprivation rule to void an agreement in *Watson v. Mason* (1876), 22 Gr. 574 (U.C. Ch.). A partnership and the creditors of an insolvent business entered into

à conclure que la notion d'objectif commercial véritable est bien ancrée dans le droit canadien.

[80] Dans l'arrêt *In Re Hoskins and Hawkey, Insolvents* (1877), 1 O.A.R. 379, la Cour d'appel de l'Ontario a appliqué la règle anti-privation à un bail qui prévoyait que si le locataire devenait insolvable, le loyer de l'année en cours de même que celui de l'année suivante devait tout de même être payé. Le propriétaire a soutenu que le loyer de l'année additionnelle servait d'indemnisation pour sa perte de locataire. Si le test que la cour a appliqué n'avait été axé que sur les effets de la stipulation, elle n'aurait pas eu à aborder cet argument. Or, elle l'a fait. La cour a rejeté l'argument du propriétaire, mentionnant qu'il était [TRADUCTION] « infirmé par le fait que le départ d'un locataire devenu insolvable entraîne un avantage plutôt qu'une perte » pour le propriétaire : p. 384. À la p. 385, la Cour d'appel a cité avec approbation la décision rendue par le lord chancelier Redesdale dans l'arrêt *Murphy, a Bankrupt* (1803), 1 Ch. 44, p. 49, qui est souvent cité au Canada :

> [TRADUCTION] La question est de savoir si une personne peut être autorisée à prouver sa réclamation à titre de créancier en se fondant sur un instrument créé aux fins d'annuler l'effet des lois en matière de faillite lorsque le seul fondement de la réclamation est un instrument conclu dans le but d'accorder un droit contre les créanciers, qui n'existerait pas contre le failli s'il était solvable. Dans toutes les affaires examinées en Angleterre, il a été conclu qu'il s'agissait d'une fraude contre les lois en matière de faillite qu'il est impossible d'appuyer . . . [Je souligne.]

[81] Appliquant l'arrêt *Murphy*, la Cour d'appel a conclu que la stipulation prévoyant le paiement au propriétaire d'un loyer pour une année additionnelle était invalide. Essentiellement, elle a jugé qu'il n'existait pas d'objectif commercial légitime pouvant justifier que le propriétaire reçoive ce qui serait en réalité le paiement à titre gratuit d'une année supplémentaire de loyer après la fin du bail.

[82] La même Cour d'appel a appliqué la règle anti-privation pour annuler une entente dans l'arrêt *Watson c. Mason* (1876), 22 Gr. 574 (U.C. Ch.). Une société de personnes et les créanciers d'une

an arrangement which permitted the partnership to purchase the assets of the business, with the stipulation that, upon the insolvency of the partnership, the partnership would then owe the creditors the balance of the business's unpaid debt. Justice Burton (as he then was) held that there was no authority to support the validity of an agreement "where the only ground of the claim is an instrument executed for the purpose of giving a right against creditors": p. 588 (emphasis added). Justice Patterson (then a member of the Court of Appeal) noted there was no evidence that the partnership had paid a discounted price on the assets in exchange for this *quid pro quo* and Burton J.A. was of the view that the partnership had paid the full value of the assets, rendering the contingent debt obligation essentially gratuitous. When I consider these comments in conjunction with the various judges' approving citations of English authorities referring to intention or purpose (pp. 583-84, for example), I take the court to have found that there was no legitimate commercial interest in conjuring the insolvent business's debt into existence upon the insolvency of the partnership after the partnership had already agreed to pay the creditors the full value of the goods which had belonged to the business.

[83] The anti-deprivation rule was also applied by Meyer J. in *Re Frechette* (1982), 138 D.L.R. (3d) 61 (Que. Sup. Ct.). The bankrupt was a shareholder in a private company. The shareholders' agreement provided for a right of first refusal should a shareholder voluntarily wish to dispose of his shares to a third party, and also included a right to purchase the shares of any shareholder who became bankrupt. The agreement further provided that the price to be paid on the forced sale of a bankrupt's shares was to be 80 percent of the price which would otherwise be paid if the shares were sold voluntarily through the right of first refusal.

[84] Justice Meyer concluded that the provision requiring the sale of a bankrupt shareholder's shares for 80 percent of their value was contrary to public policy because it granted the shareholders a special reduction in the price to be paid for those shares. If the standard he was applying had looked only to

entreprise insolvable ont conclu une entente qui permettait à la société de personnes d'acheter les actifs de l'entreprise, et qui prévoyait qu'en cas d'insolvabilité, la société devrait aux créanciers le reste des dettes impayées de l'entreprise. Le juge Burton (plus tard juge en chef) a conclu qu'aucun précédent n'appuyait la validité d'une entente [TRADUCTION] « alors que l'unique fondement de la réclamation est un instrument conçu dans le but d'accorder un droit contre les créanciers » : p. 588 (je souligne). Le juge Patterson (alors membre de la Cour d'appel) a mentionné que rien ne prouvait que la société de personnes avait payé un prix réduit pour les actifs en échange de cette contrepartie, et le juge Burton était d'avis que la société de personnes avait payé la valeur complète des actifs, ce qui transformait le paiement éventuel des dettes en un avantage concédé essentiellement à titre gratuit. Si je combine ces commentaires avec l'approbation par plusieurs juges de citations de décisions anglaises faisant référence à l'intention ou à l'objectif (p. 583-584, p. ex.), je comprends que la cour a conclu qu'il n'y avait aucun intérêt commercial légitime à faire assumer la dette d'une autre entreprise par la société de personnes, devenue insolvable, alors que cette société avait déjà convenu de payer aux créanciers la pleine valeur des biens de l'entreprise.

[83] Le juge Meyer a aussi appliqué la règle antiprivation dans la décision *Re Frechette* (1982), 138 D.L.R. (3d) 61 (C.S. Qc). Le failli était un actionnaire d'une société privée. La convention entre actionnaires prévoyait un droit de premier refus si l'un des actionnaires décidait de céder volontairement ses parts à un tiers, ainsi qu'un droit d'acheter la part de tout actionnaire ayant fait faillite. Cette entente prévoyait également que le prix à payer pour les parts d'un failli obtenues lors d'une vente forcée devait être de 80 p. 100 du prix qui serait autrement payé si les parts étaient vendues volontairement au moyen du droit de premier refus.

[84] Le juge Meyer a conclu que la stipulation exigeant la vente des parts du failli pour 80 p. 100 de leur valeur était contraire à l'intérêt public. Il est parvenu à cette conclusion parce qu'il a jugé que la stipulation accordait aux actionnaires une réduction spéciale du prix à payer pour les parts

the effects of the provision on bankruptcy, he could have ended his analysis there. However, he went on to consider the shareholders' purpose in entering into the arrangement.

[85] While Meyer J. accepted that the discount of 20 percent might have been agreed upon in good faith, he considered that it was essentially a gratuitous benefit granted by the shareholders to one another. Indeed, he analogized it to a "gift": p. 69. He observed that there "was no evidence before the court as to the existence of any consideration for such a reduction, other than a desire to confer a benefit on one's fellow shareholders in the event of one's bankruptcy": p. 69. In effect, this was a finding that there was no objectively ascertainable *commercial* interest behind the provision. A desire to give gifts to friends is plainly not a legitimate commercial interest which the law should protect over the interests of third party creditors in bankruptcy. Finally, I note that Meyer J. quoted and followed an English decision, *Borland's Trustee v. Steel Brothers & Co., Limited*, [1901] 1 Ch. 279, the significance of which I examine below when discussing another Canadian decision.

[86] Justice Saunders considered the anti-deprivation rule in *Re Knechtel Furniture Ltd.* (1985), 56 C.B.R. (N.S.) 258 (Ont. S.C.). The bankrupt, Knechtel Furniture, had an employee pension plan that had been wound up on the company's bankruptcy with a surplus of $471,300, after all the beneficiaries had been fully paid in accordance with the terms of the plan. The plan stated that in the event of its termination, any surplus would be paid over to the company, provided, however, that, in the event that the company had become bankrupt or insolvent, the surplus would be allocated to the beneficiaries. The company's trustee in bankruptcy argued that the provision entitling the beneficiaries to the funds was contrary to public policy.

[87] The beneficiaries argued that the provision had not been inserted to defeat the bankrupt's creditors. They submitted that its purpose was to provide additional benefits to employees who would probably suffer great hardship if the plan were to be wound up

de l'actionnaire failli. Si la règle qu'il a appliquée ne s'intéressait qu'aux effets de la stipulation sur la faillite, il aurait pu terminer son analyse à cette étape. Mais il a poursuivi en examinant la raison pour laquelle les actionnaires avaient conclu l'entente.

[85] Bien que le juge Meyer ait accepté que le rabais de 20 p. 100 puisse avoir été convenu de bonne foi, il a jugé qu'il s'agissait essentiellement d'un avantage gratuit accordé par les associés les uns aux autres. En effet, il a comparé cet avantage à un [TRADUCTION] « cadeau » : p. 69. Il a observé que « la cour ne disposait d'aucune preuve démontrant l'existence d'une contrepartie pour ce rabais, à part le désir d'accorder un avantage à un autre actionnaire en cas de faillite » : p. 69. Cette conclusion revient à dire que la stipulation ne reposait sur aucun intérêt *commercial* objectivement vérifiable. Le désir de faire des cadeaux à des amis n'est tout simplement pas un intérêt commercial légitime que le droit devrait protéger au détriment des intérêts des créanciers tiers en cas de faillite. Enfin, je constate que le juge Meyer a cité et invoqué la décision anglaise *Borland's Trustee c. Steel Brothers & Co., Limited*, [1901] 1 Ch. 279, dont j'examinerai l'importance ci-après en analysant une autre décision canadienne.

[86] Le juge Saunders a examiné la règle anti-privation dans la décision *Re Knechtel Furniture Ltd.* (1985), 56 C.B.R. (N.S.) 258 (C.S. Ont.). La faillie, Knechtel Furniture, avait un régime de retraite pour ses employés. Celui-ci a été liquidé, avec un surplus de 471 300 $ après que tous les bénéficiaires eurent été totalement payés conformément aux modalités du régime, lorsque la compagnie a fait faillite. Selon le régime, en cas de cessation, tout surplus devait être payé à la compagnie, mais si celle-ci avait fait faillite ou était devenue insolvable, il devait être distribué aux bénéficiaires. Le syndic de faillite de la compagnie a fait valoir que la clause qui accordait aux bénéficiaires un droit au surplus était contraire à l'intérêt public.

[87] Les bénéficiaires ont soutenu que la stipulation n'avait pas été incluse dans le but de contrecarrer le droit des créanciers de la faillie. Ils ont fait valoir qu'elle visait à accorder des avantages supplémentaires aux employés qui subiraient probablement de

after the company became bankrupt. In other words, they argued that the provision had a *bona fide* commercial purpose. Justice Saunders rejected this argument, not because he regarded it as irrelevant to his analysis, but rather because he found it "difficult to see why the hardship would necessarily be any less if the plan had been terminated when Knechtel was solvent": p. 264. In other words, he did not accept that there was a legitimate commercial interest in giving the beneficiaries what would amount to gratuitous pension benefits. He observed that the beneficiaries had already been paid their benefits in full under the plan, and that, if the plan had been terminated while the company was solvent, the beneficiaries would have had no entitlement to the surplus. As enforcing the provision would redirect funds which would otherwise have gone into the bankrupt's estate, the provision was contrary to public policy.

grandes difficultés si le régime était liquidé après la faillite de l'entreprise. Autrement dit, ils ont prétendu que la stipulation visait un objectif commercial véritable. Le juge Saunders a rejeté cet argument, non pas parce qu'il l'a jugé non pertinent pour son analyse, mais parce qu'il a estimé qu'il était [TRADUCTION] « difficile de voir pourquoi les difficultés auraient nécessairement été moindres si le régime avait été liquidé lorsque Knechtel était solvable » : p. 264. Autrement dit, il n'a pas accepté l'argument selon lequel il y avait un intérêt commercial légitime à accorder aux bénéficiaires ce qui équivaudrait à des prestations gratuites. Il a observé que les bénéficiaires avaient déjà reçu la totalité des prestations auxquelles ils avaient droit en vertu du régime et que, si celui-ci avait été liquidé alors que l'entreprise était solvable, les bénéficiaires n'auraient pas eu droit au surplus. Puisque l'application de la stipulation aurait pour effet de réaffecter les fonds qui auraient autrement fait partie de l'actif de la faillie, la stipulation était contraire à l'intérêt public.

[88] The anti-deprivation rule was also considered by Blair J. (as he then was) in *Canadian Imperial Bank of Commerce v. Bramalea Inc.* (1995), 33 O.R. (3d) 692 (C.J. (Gen. Div.)). Bramalea and the Canadian Imperial Bank of Commerce were in a partnership formed to develop and operate a shopping mall. A clause in their partnership agreement provided that, in the event of the insolvency of one of the partners, the solvent partner could purchase the insolvent partner's interest at the lesser of book value or fair market value. Bramalea entered into bankruptcy proceedings, and the bank sought to exercise its right under the partnership agreement. The book value of Bramalea's interest was estimated at $200,000, and the evidence suggested that the fair market value might exceed the book value by as much as $2 million to $3 million. Thus, the clause would have given the bank a rather staggering discount on the value of Bramalea's partnership interest. Justice Blair neither expressly accepted nor rejected these figures for the fair market valuation, but he did find that the difference in price was "more than minimal": p. 694.

[88] La règle anti-privation a aussi été examinée par le juge Blair (plus tard juge de la Cour d'appel) dans la décision *Canadian Imperial Bank of Commerce c. Bramalea Inc.* (1995), 33 O.R. (3d) 692 (C.J. (Div. gén.)). Bramalea et la CIBC étaient parties à un contrat de société conclu dans le but de construire et d'exploiter un centre commercial. Une des stipulations de l'entente prévoyait qu'en cas d'insolvabilité de l'un des associés, l'associé solvable pouvait acheter la participation de l'associé insolvable au prix le moins élevé entre la valeur comptable et la juste valeur marchande. Bramalea a entamé une procédure de faillite, et la banque a tenté d'exercer son droit prévu au contrat de société. La valeur comptable de la participation de Bramalea était évaluée à 200 000 $ et la preuve tendait à démontrer que la juste valeur marchande pouvait dépasser la valeur comptable d'un montant aussi élevé que 2 000 000 à 3 000 000 de dollars. La clause aurait donc accordé à la banque un rabais plutôt ahurissant sur la valeur de la participation de Bramalea dans la société. Le juge Blair n'a expressément ni accepté ni rejeté les montants invoqués pour la juste valeur marchande, mais a conclu que la différence de prix était [TRADUCTION] « plus que minime » : p. 694.

[89] Justice Blair stated that it was "clear from the provisions of the partnership agreement itself that the parties had contemplated a transfer to one of the partners of the other partner's partnership interest, solely in the event of insolvency of the latter, at a price which was less than what could be obtained for that interest on the market": p. 695 (emphasis deleted). Although he was at pains to point out that there was no suggestion of a fraudulent or dishonest intent in this case, he also observed that the parties had intended to sell an asset at an undervalue. As a result, he found that the clause was contrary to public policy. Thus, while Blair J. did not expressly discuss whether there was an absence of an objective commercial purpose, he clearly did engage in a search for an objective purpose.

[90] In addition, I take Blair J.'s statement that the rule encompasses "fraud in the effect" as meaning no more than that a subjective intent to defraud the bankrupt's creditors does not have to be shown in order for the anti-deprivation rule to apply: p. 694. In *Belmont*, Lord Mance explained that references in the jurisprudence to "fraud" of the bankruptcy law are not references to fraud "in a strict sense" or to "morally opprobrious" conduct: para. 151. Lord Brett also made this point clear at p. 459 of *Voisey*. Thus, a showing of subjective dishonesty or deceit is unnecessary. However, Lord Mance, at para. 151 of *Belmont*, and Lord Brett, at p. 461 of *Voisey*, both held that the anti-deprivation rule requires an assessment of whether there was a legitimate purpose behind a transaction. I see nothing contradictory in holding that deceit, dishonesty, or impropriety need not be shown, while also holding that the anti-deprivation rule does not apply to transactions or contractual provisions which serve a *bona fide* commercial purpose. I therefore do not see Blair J.'s comments regarding "fraud in the effect" as inconsistent with the view I put forward.

[89] Le juge Blair a déclaré qu'il [TRADUCTION] « ressortait clairement des clauses du contrat de société elles-mêmes que les parties envisageaient un transfert de la participation dans la société de l'un des associés à l'autre uniquement en cas d'insolvabilité du premier, à un prix moins élevé que ce que l'on aurait obtenu pour cette participation sur le marché » : p. 695 (italique omis). Ainsi, bien qu'il se soit efforcé de souligner que rien n'indiquait la présence d'une intention frauduleuse ou malhonnête dans cette affaire, il a observé que les parties voulaient vendre un actif à un prix sous-évalué. Par conséquent, il a conclu que la clause était contraire à l'intérêt public. Donc, bien que le juge Blair ne se soit pas expressément penché sur la question de savoir si la stipulation avait une finalité commerciale objective, il a manifestement tenté de trouver une finalité objective.

[90] De plus, je considère que la déclaration du juge Blair selon laquelle la règle englobe [TRADUCTION] l'« effet frauduleux » veut seulement dire qu'il n'est pas nécessaire de démontrer une intention subjective de commettre une fraude contre les créanciers du failli pour que la règle anti-privation s'applique : p. 694. Dans l'arrêt *Belmont*, lord Mance a expliqué que les mentions dans la jurisprudence de [TRADUCTION] « fraude » contre les lois en matière de faillite ne visent pas la fraude « au sens strict » ni les conduites « moralement scandaleuses » : par. 151. Lord Brett s'est également prononcé clairement en ce sens à la p. 459 de l'arrêt *Voisey*. En conséquence, il n'est pas nécessaire de démontrer une intention malhonnête subjective ou une tromperie. Toutefois, lord Mance, au par. 151 de l'arrêt *Belmont*, et lord Brett, à la p. 461 de l'arrêt *Voisey*, ont tous les deux conclu que la règle anti-privation exigeait d'évaluer si la transaction poursuivait un objectif légitime. Je ne vois rien de contradictoire à décider que la preuve d'une tromperie ou d'un acte malhonnête ou répréhensible n'est pas nécessaire, tout en concluant que la règle anti-privation ne s'applique pas aux transactions ou aux stipulations qui visent un objectif commercial véritable. Je ne considère donc pas les commentaires du juge Blair concernant la [TRADUCTION] « effet frauduleux » comme étant incompatibles avec le point de vue que j'avance.

[91] Further, Blair J., at p. 695, like Meyer J. in *Frechette*, at p. 68, quoted directly from the English case of *Borland*, in which Farwell J. stated the following in the context of a share purchase agreement:

> If I came to the conclusion that there was any provision in these articles compelling persons to sell their shares in the event of bankruptcy at something less than the price that they would otherwise obtain, such a provision would be repugnant to the bankruptcy law . . . . [p. 291]

This leaves open the question, however, of whether the repugnancy would arise because the provision would amount to a deprivation "in effect", notwithstanding the parties' *bona fide* intentions, or whether the sale at an undervalue would undermine the parties' claim that they had drafted the provision so as to serve legitimate commercial interests. I think the latter view reflects the better reading of Farwell J.'s reasons in *Borland*, to which I now turn.

[92] Mr. Borland was a shareholder in a private company which carried on business in Burma. The company's articles of association provided that each of the shareholders was "entitled to continue to hold the shares then held by him or any of them until he should die or voluntarily transfer the same or become bankrupt": p. 281. Mr. Borland was adjudicated bankrupt, the company attempted to force the sale of his shares, and the trustee of his estate resisted the sale, arguing that the provision was a fraud upon the bankruptcy laws.

[93] Justice Farwell found that the forced sale provision in the articles of association was not contrary to public policy. He found that the provision had been inserted *bona fide* and constituted a "fair agreement for the purpose of the business of the company": p. 291. Justice Farwell observed that the shares were difficult to value because they came with a number of restrictive clauses that made it "impossible to find a market value". He added that the price offered by the company likely represented the fair value of the shares, given that they were essentially incapable

[91] En outre, le juge Blair, à la p. 695, comme le juge Meyer dans l'affaire *Frechette*, p. 68, a cité directement la décision anglaise *Borland* où le juge Farwell a déclaré ce qui suit dans le contexte d'une convention d'achat d'actions :

> [TRADUCTION] Si j'en arrivais à la conclusion que l'une de ces stipulations obligeait quiconque à vendre ses parts en cas de faillite à un prix moins élevé que celui qu'il ou elle aurait autrement obtenu, cette disposition serait incompatible avec le droit de la faillite . . . [p. 291]

Toutefois, on peut se demander si cette incompatibilité découlerait du fait que la disposition constituerait une privation « compte tenu de ses effets », malgré la bonne foi des parties, ou si la vente à un prix sous-évalué nuirait à la prétention des parties voulant qu'elles aient rédigé la stipulation de façon à servir des intérêts commerciaux légitimes. Je crois que la dernière supposition constitue une meilleure interprétation des motifs du juge Farwell dans la décision *Borland*, que j'examinerai sans plus tarder.

[92] Monsieur Borland était actionnaire d'une entreprise privée qui conduisait ses activités en Birmanie. Les statuts constitutifs de l'entreprise prévoyaient que chaque actionnaire [TRADUCTION] « avait le droit de continuer à détenir ses actions ou celles des autres actionnaires jusqu'à sa mort, ou jusqu'à ce qu'il les transfère volontairement ou jusqu'à ce qu'il fasse faillite » : p. 281. Monsieur Borland ayant été déclaré failli, l'entreprise a tenté de l'obliger à vendre ses actions. Le syndic de faillite de M. Borland s'est opposé à la vente, faisant valoir que la stipulation constituait une fraude contre les lois en matière de faillite.

[93] Le juge Farwell a conclu que la disposition des statuts constitutifs relative à la vente forcée n'était pas contraire à l'intérêt public. Il a jugé qu'elle y avait été ajoutée [TRADUCTION] « de bonne foi » et constituait une « entente équitable aux fins des activités de l'entreprise » : p. 291. Il a constaté qu'il était difficile d'évaluer les actions parce qu'elles étaient assorties de plusieurs clauses restrictives qui « empêchaient d'en établir la valeur marchande ». Le juge Farwell a ajouté que le prix offert par l'entreprise représentait vraisemblablement la juste valeur

of valuation. The same share price applied to all shareholders and applied for sales of shares outside of bankruptcy as well as in bankruptcy.

[94] It was in this context that Farwell J. made the statement quoted by Blair J. in *Bramalea*. However, given Farwell J.'s observation that the shares were essentially impossible to value, his conclusion that the anti-deprivation rule did not apply depended more on his view that the arrangement was a *bona fide* commercial agreement than it did on establishing a fixed principle that the absence of evidence of a deprivation was determinative of the rule's application: see A. Ho, "The Treatment of *Ipso Facto* Clauses in Canada" (2015), 61 *McGill L.J.* 139, at p. 161. Therefore, to the extent that the courts in *Bramalea* and *Frechette* followed *Borland*, either they did so on a mistaken view of what it stands for, or (and I prefer this view) implicit in their reasons is the notion that the anti-deprivation rule does not apply to *bona fide* commercial agreements.

[95] The Ontario Court of Appeal relied on *Bramalea* to invalidate a contractual provision in *Aircell Communications Inc. (Trustee of) v. Bell Mobility Cellular Inc.*, 2013 ONCA 95, 14 C.B.R. (6th) 276. Aircell and Bell were parties to an independent dealer agreement which provided that Bell could terminate the agreement on notice if Aircell defaulted on its payments to Bell for purchases of inventory. It further provided that, should the agreement be terminated for specified reasons, Bell's obligations to pay commissions "shall cease immediately": para. 8. Owing to financial difficulties, Aircell defaulted on its payments and then entered into bankruptcy proceedings. It owed Bell $64,000 for inventory, and Bell retained $188,981 worth of commissions it owed to Aircell. As Bell was entitled to set-off under the *BIA*, Aircell's trustee brought an action against Bell to recover only the difference between the commissions retained by Bell and the amounts which Aircell owed to Bell. The Court of Appeal found that the clause at issue provided "a windfall to . . . Bell": para. 12. Applying *Bramalea*,

des actions étant donné qu'il était essentiellement impossible de les évaluer. Le même prix s'appliquait à tous les actionnaires ainsi qu'à la vente des actions dans le cadre d'une faillite et en dehors de celle-ci.

[94] C'est dans ce contexte que le juge Farwell a formulé le commentaire qu'a cité le juge Blair dans la décision *Bramalea*. Cependant, étant donné l'observation du juge Farwell selon laquelle il était essentiellement impossible d'établir la valeur des actions, sa conclusion quant à l'inapplicabilité de la règle anti-privation reposait davantage sur son impression que l'entente visait un objectif commercial véritable que sur l'établissement d'un principe fixe selon lequel l'absence de preuve démontrant une privation est déterminante eu égard à l'application de la règle : voir A. Ho, « The Treatment of *Ipso Facto* Clauses in Canada » (2015), 61 *R.D. McGill* 139, p. 161. Par conséquent, dans la mesure où les décisions *Bramalea* et *Frechette* ont suivi la décision *Borland*, elles l'ont fait soit sur la base d'une mauvaise interprétation, soit, et c'est l'interprétation que je privilégie, parce qu'il est implicite dans les motifs de ces jugements que la règle anti-privation ne s'applique pas aux ententes commerciales véritables.

[95] La Cour d'appel de l'Ontario s'est fondée sur la décision *Bramalea* pour invalider une stipulation dans l'arrêt *Aircell Communications Inc. (Trustee of) c. Bell Mobility Cellular Inc.*, 2013 ONCA 95, 14 C.B.R. (6th) 276. Aircell et Bell étaient parties à un contrat de concessionnaire indépendant qui prévoyait que Bell pouvait résilier le contrat moyennant un préavis si Aircell ne payait pas à Bell ses achats d'inventaire. Ce contrat prévoyait également qu'en cas de résiliation du contrat pour des motifs précisés, les obligations de Bell relatives au paiement de commissions [TRADUCTION] « pren[draient] fin immédiatement » : par. 8. En raison de difficultés financières, Aircell n'a pas fait certains paiements et a entamé des procédures de faillite. Elle devait à Bell 64 000 $ pour des articles en inventaire, tandis que Bell a retenu des commissions s'élevant à 188 981 $ qu'elle devait à Aircell. Comme Bell avait droit à une compensation en application de la *LFI*, le syndic d'Aircell a intenté un recours contre Bell afin de recouvrer seulement la différence entre les commissions retenues par Bell et les sommes qu'Aircell devait à cette dernière. La

it held that the clause was unenforceable as contrary to public policy.

[96] The Court of Appeal described the test from *Bramalea* as being essentially effects-based. However, as indicated by my analysis of *Bramalea* above, that is an oversimplification of Blair J.'s reasons. Further, and I admit that the court did not discuss the case on this basis, it is implicit in the court's description of the effect of the clause as a "windfall" that the clause was offensive not only because it deprived Aircell's estate of value, but also because there was no legitimate commercial basis in bankruptcy for Bell to withhold payments which were in excess of the debt it was owed by Aircell. I therefore do not view *Aircell* as inconsistent with my approach.

[97] The anti-deprivation rule was considered by Registrar Quinn in *Westerman (Bankrupt), Re*, 1998 ABQB 946, 234 A.R. 371, rev'd on other grounds, 1999 ABQB 708, 275 A.R. 114. The bankrupt was a party to a partnership agreement which provided that a bankrupt partner could be expelled from the partnership and the partnership would then be obliged to pay that partner only 50 percent of his capital account. Registrar Quinn found that allowing the partnership to take 50 percent of the bankrupt's capital account would grant it an unjust preference, as any losses incurred by the partnership as a result of the expulsion of the bankrupt partner were "purely speculative". He therefore concluded that the partnership was not entitled to retain the funds. As Registrar Quinn did not address the commercial purpose behind the provision, it does not appear that any commercial purpose was offered. As the provision was to the effect that the partner's capital account could be settled at a 50 percent discount in the event of bankruptcy, an objective commercial purpose is not readily apparent. I therefore do not view *Westerman* as authority against my reading of the jurisprudence.

Cour d'appel a conclu que la clause prévoyait un [TRADUCTION] « profit inattendu [. . .] pour Bell » : par. 12. Appliquant la décision *Bramalea*, la Cour d'appel a conclu que la clause était non exécutoire parce qu'elle était contraire à l'intérêt public.

[96] La Cour d'appel a décrit le test établi dans la décision *Bramalea* comme étant essentiellement fondé sur les effets. Cependant, comme l'indique mon analyse de cette décision, il s'agit d'une simplification à outrance des motifs du juge Blair. De plus, et j'admets que la Cour d'appel n'a pas examiné cette affaire sur ce fondement, le fait qu'elle décrive l'effet de la clause comme un [TRADUCTION] « profit inattendu » indique implicitement que cette clause était offensante non seulement parce qu'elle réduisait l'actif d'Aircell, mais aussi parce qu'aucun fondement commercial légitime en matière de faillite ne permettait à Bell de retenir les paiements qui dépassaient la dette d'Aircell envers elle. Selon moi, l'arrêt *Aircell* n'est donc pas incompatible avec mon approche.

[97] La règle anti-privation a été examinée par le registraire des faillites Quinn dans la décision *Westerman (Bankrupt), Re*, 1998 ABQB 946, 234 A.R. 371, inf. pour d'autres motifs, 1999 ABQB 708, 275 A.R. 114. Le failli était partie à un contrat de société qui prévoyait qu'un associé failli pouvait être exclu de la société de personnes et que cette dernière ne serait alors tenue de verser à l'associé failli que 50 p. 100 de son compte de capital. Le registraire Quinn a conclu que le fait de permettre à la société de personnes de s'attribuer 50 p. 100 du compte de capital du failli conférerait une préférence injuste à la société, car toutes les pertes subies par celle-ci à la suite de la faillite étaient [TRADUCTION] « purement spéculatives ». Il a donc conclu que la société de personnes n'avait pas le droit de retenir les fonds. Puisque le registraire Quinn n'a pas abordé l'objectif commercial qui sous-tendait la stipulation, il semble qu'aucun objectif commercial n'ait été porté à son attention. Comme la stipulation avait pour effet de priver le compte de capital de l'associé de 50 p. 100 de sa valeur en cas de faillite, aucune finalité commerciale objective n'était manifeste. Je considère donc que l'arrêt *Westerman* n'est pas un précédent qui réfute ma lecture de la jurisprudence.

[98] In his reasons, Registrar Quinn expressed the view that *Coopérants* was at odds with *Bramalea*, *Knetchel*, and *Frechette*. However, as the preceding analysis demonstrates, the golden thread weaving its way through the tapestry of the Canadian jurisprudence is the presence or absence of an objective commercial purpose behind the agreements under review. In *Coopérants*, there was such a purpose, whereas in *Bramalea*, *Knetchel*, and *Frechette*, there was not. Moreover, the analyses in *Coopérants*, *Bramalea*, *Knetchel*, and *Frechette* went past the question of whether the provisions in question had the effect of removing assets from the debtors' estates and extended to the legitimacy of the intentions behind them. This is also true of *Hoskins* and, arguably, of *Watson*, as well. Meanwhile, the more recent authorities applying the rule in which the parties' purposes are not expressly discussed — *Westerman* and *Aircell* — do not detract from my reading of the jurisprudence because they do not show any intent to break with past precedent and because an absence of a legitimate commercial purpose is discernable on the facts of those cases.

[99] In the weight of lower court cases in which the anti-deprivation rule was addressed, the rule has been found not to apply where the provision in question has a *bona fide* commercial purpose. When I consider this jurisprudence in light of *Hobbs* and *Coopérants*, I am led to the conclusion that a *bona fide* commercial purpose element has a strong jurisprudential footing in Canadian law. I therefore cannot accept my colleague's position that a *bona fide* commercial purpose test would amount to a change to the existing law: Rowe J.'s reasons, at paras. 32 and 39. With respect, it is my colleague's adoption of a purely effects-based test which represents a break with the past. To declare that an absence of a *bona fide* commercial purpose is required in order to apply the anti-deprivation rule is to discover the law as it has always been — as it has been handed down to us in the reasoned opinions of the jurists who preceded us.

[100] Of course, the law could be incrementally developed away from this position. Courts may adapt

[98] Dans ses motifs, le registraire Quinn a exprimé l'opinion selon laquelle l'arrêt *Coopérants* était incompatible avec les décisions *Bramalea*, *Knetchel* et *Frechette*. Toutefois, comme l'analyse qui précède le démontre, le lien qui relie les affaires canadiennes est la présence ou l'absence d'une finalité commerciale objective qui sous-tend les contrats examinés. Il y avait une telle finalité dans l'affaire *Coopérants*, mais non dans les affaires *Bramalea*, *Knetchel* et *Frechette*. En outre, il ressort des analyses menées dans ces quatre décisions que les juges, au lieu de s'en tenir à la question de savoir si les stipulations en litige avaient pour effet de retirer des biens de l'actif des débiteurs, se sont enquis de la légitimité des intentions exprimées par ces stipulations. C'est aussi le cas de l'arrêt *Hoskins*, et sans doute de l'arrêt *Watson*. Par ailleurs, les précédents plus récents qui ont appliqué la règle et qui n'ont pas abordé expressément la question de l'intention des parties — *Westerman* et *Aircell* — ne s'opposent pas à ma lecture de la jurisprudence, car ils n'expriment aucune intention de s'éloigner des précédents et les faits en cause démontraient une absence d'objectif commercial légitime.

[99] Dans les décisions des tribunaux d'instances inférieures qui en ont traité, il a été jugé que la règle anti-privation ne s'appliquait pas lorsque la stipulation en cause poursuivait un objectif commercial véritable. Lorsque j'examine cette jurisprudence à la lumière des arrêts *Hobbs* et *Coopérants*, j'arrive à la conclusion que la notion d'objectif commercial véritable est bien ancrée dans le droit canadien. Je ne peux donc accepter la position de mon collègue selon laquelle l'adoption d'un test fondé sur l'objectif commercial véritable constituerait une modification du droit existant : motifs du juge Rowe, par. 32 et 39. Avec égards, c'est l'adoption par mon collègue d'un test uniquement fondé sur les effets qui représente une rupture par rapport au passé. Déclarer la règle anti-privation inapplicable en l'absence d'un objectif commercial véritable reviendrait à reconnaître le droit tel qu'il a toujours été, tel qu'il nous a été légué par les opinions raisonnées des juristes qui nous ont précédés.

[100] Bien entendu, les règles de droit pourraient être progressivement modifiées pour s'éloigner de

the common law where they deem it necessary to keep the law in step with the dynamic and evolving fabric of society: see *R. v. Salituro*, [1991] 3 S.C.R. 654. In my view, when courts consider whether to introduce such innovations to the common law, they should base their decision making on sound legal principles and compelling considerations of public policy. Thus, I now turn to consider whether there is a principled legal basis for distinguishing between the *pari passu* rule, with its effects-based test, and the anti-deprivation rule, with its traditionally purpose-based test.

(2) There Is a Principled Legal Basis for Distinguishing Between the Anti-Deprivation Rule and the *Pari Passu* Rule

[101] One of the reasons my colleague cites in favour of an effects-based test for the anti-deprivation rule is that it would be consistent with the test for the *pari passu* rule: Rowe J.'s reasons, at para. 35. In my view, however, there is a principled legal basis upon which to distinguish the two rules: the anti-deprivation rule is based on a common law public policy, whereas the *pari passu* rule is based on an implied statutory prohibition in the *BIA*.

[102] The anti-deprivation rule and the *pari passu* rule form part of a more general and longstanding doctrine in the common law to the effect that an agreement that is contrary to public policy may be struck down as unenforceable: S. M. Waddams, *The Law of Contracts* (7th ed. 2017), at para. 562. This public policy doctrine has at least two branches: (1) common law public policy; and (2) statutory public policy: Waddams, at para. 566. The common law branch concerns agreements struck down on the basis of a judicial apprehension of a public policy interest which outweighs the general public interest in the enforcement of contracts: e.g., *Shafron v. KRG Insurance Brokers (Western) Inc.*, 2009 SCC 6, [2009] 1 S.C.R. 157, at paras. 15-20. The statutory branch concerns agreements struck down because they are expressly or impliedly prohibited by statute: *Transport North American Express Inc. v. New Solutions Financial Corp.*, 2004 SCC 7, [2004] 1

cette position. Les tribunaux peuvent adapter la common law lorsqu'ils le jugent nécessaire pour l'ajuster à la dynamique et à l'évolution du tissu social : voir *R. c. Salituro*, [1991] 3 R.C.S. 654. À mon avis, lorsque les tribunaux envisagent d'introduire de telles innovations dans la common law, ils doivent fonder leur décision sur des principes juridiques solides et des considérations d'ordre public impératives. Ainsi, j'examinerai maintenant s'il existe un fondement juridique valable pour établir une distinction entre la règle du *pari passu*, avec son test fondé sur les effets, et la règle anti-privation, avec son test traditionnellement fondé sur l'objectif.

(2) Il existe un fondement juridique valable pour établir une distinction entre la règle anti-privation et la règle du *pari passu*

[101] Mon collègue justifie le choix d'un test fondé sur les effets pour l'application de la règle anti-privation notamment parce qu'il s'harmoniserait avec le test applicable à la règle du *pari passu* : motifs du juge Rowe, par. 35. Or, à mon avis, il existe un fondement juridique valable pour établir une distinction entre les deux règles : la règle anti-privation repose sur un principe d'intérêt public de common law, tandis que la règle du *pari passu* repose sur une prohibition implicite contenue dans la *LFI*.

[102] La règle anti-privation et la règle du *pari passu* font partie d'une doctrine de common law plus générale établie depuis longtemps selon laquelle une entente contraire à l'intérêt public peut être jugée inexécutoire et annulée en conséquence : S. M. Waddams, *The Law of Contracts* (7e éd. 2017), par. 562. Cette doctrine de l'intérêt public comprend au moins deux volets : 1) l'intérêt public issu de la common law; 2) l'intérêt public d'origine statutaire : Waddams, par. 566. Le volet de common law vise les ententes annulées parce que les tribunaux craignent qu'une considération d'intérêt public l'emporte sur l'intérêt public général à l'égard de l'exécution des contrats : p. ex., *Shafron c. KRG Insurance Brokers (Western) Inc.*, 2009 CSC 6, [2009] 1 R.C.S. 157, par. 15-20. Le volet statutaire vise les ententes annulées parce qu'elles sont expressément ou implicitement interdites par une loi : *Transport North American Express Inc. c. New Solutions Financial*

S.C.R. 249, at paras. 20-26. On my reading of the jurisprudence, the anti-deprivation rule falls under the common law branch of the public policy doctrine, which includes a policy against agreements entered into for the purpose of defrauding or otherwise injuring third parties. I rest this conclusion on the following two observations about the jurisprudence.

[103] My first observation relates to the rule's origins. The early English authorities which underpin the Canadian anti-deprivation rule routinely described the agreements at issue as fraudulent, dishonest or evasive: see *Belmont*, at paras. 74-79, per Lord Collins; Ho, at pp. 151-52; R. J. Wood, "Direct Payment Clauses and the Fraud Upon the Bankruptcy Law Principle: *Re Horizon Earthworks Ltd. (Bankrupt)*" (2014), 52 *Alta. L.R.* 171, at p. 175. Lord Chancellor Eldon held that a term "adopted with the express object of taking the case out of reach of the Bankrupt Laws" was "a direct fraud upon the Bankrupt Laws" in *Higinbotham v. Holme* (1812), 19 Ves. Jr. 88, 34 E.R. 451, at p. 453. Justice Vaughan Williams held that an agreement that a debtor's interest in property would determine upon their bankruptcy was "evidence of an intention to defraud [their] creditors" in *In re Stephenson*, [1897] 1 Q.B. 638, at p. 640. Vice Chancellor Wood stated that "no one can be allowed to derive benefit from a contract that is in fraud of the bankrupt laws" in *Whitmore v. Mason* (1861), 2 J. & H. 204, 70 E.R. 1031, at p. 1035. Lord James described the contractual arrangement which he found void as "a clear attempt to evade the operation of the bankruptcy laws" in *Ex parte Mackay* (1873), L.R. 8 Ch. App. 643, p. 647: see also *Voisey*, per Brett L.J. and *Murphy*, per Redesdale L.C., both quoted above. The earliest Canadian decisions, *Hobbs*, *Hoskins*, and *Watson*, are to similar effect.

[104] The reasoning employed by these courts appears to have turned on their apprehension that the arrangements at issue were aimed at an unlawful

Corp., 2004 CSC 7, [2004] 1 R.C.S. 249, par. 20-26. D'après ma lecture de la jurisprudence, la règle anti-privation relève du volet de common law de la doctrine de l'intérêt public qui interdit les ententes conclues dans le but de commettre une fraude ou de causer autrement un préjudice à un tiers. Ma conclusion repose sur les deux observations suivantes à propos de la jurisprudence.

[103] Ma première observation concerne les origines de la règle. Les vieux précédents anglais qui sous-tendent la règle anti-privation canadienne décrivaient systématiquement les ententes en cause comme étant frauduleuses, malhonnêtes ou évasives : voir *Belmont*, par. 74-79, le lord Collins; Ho, p. 151-152; R. J. Wood, « Direct Payment Clauses and the Fraud Upon the Bankruptcy Law Principle : *Re Horizon Earthworks Ltd. (Bankrupt)* » (2014), 52 *Alta. L.R.* 171, p. 175. Dans la décision *Higinbotham c. Holme* (1812), 19 Ves. Jr. 88, 34 E.R. 451, p. 453, le lord chancelier Eldon a conclu qu'une stipulation [TRADUCTION] « adoptée dans le but exprès de soustraire l'affaire à l'application des lois en matière de faillite » constitue « une fraude directe contre les lois en matière de faillite ». Le juge Vaughan Williams a conclu pour sa part, dans la décision *In re Stephenson*, [1897] 1 Q.B. 638, p. 640, qu'une entente selon laquelle l'intérêt d'un débiteur à l'égard d'un bien serait établi au moment de sa faillite est [TRADUCTION] « la preuve d'une intention de commettre une fraude contre [ses] créanciers ». Dans le jugement *Whitmore c. Mason* (1861), 2 J. & H. 204, 70 E.R. 1031, p. 1035, le vice-chancelier Wood a déclaré que [TRADUCTION] « personne ne peut être autorisé à retirer un avantage d'un contrat qui constitue une fraude contre les lois en matière de faillite ». Dans le jugement *Ex parte Mackay* (1873), L.R. 8 Ch. App. 643, p. 647, lord James a décrit le contrat qu'il a annulé comme étant [TRADUCTION] « une tentative évidente d'éviter l'application des lois en matière de faillite » : voir aussi *Voisey*, le lord Brett et *Murphy*, le lord chancelier Redesdale, tous les deux précitées. Les plus vieux précédents canadiens *Hobbs*, *Hoskins* et *Watson* vont dans le même sens.

[104] Le raisonnement adopté par ces tribunaux semble avoir reposé sur une crainte que les ententes en cause aient visé un objectif illégal s'apparentant

purpose which approximated fraud, not on a finding that they were impliedly prohibited by statute. The early common law courts applying the rule needed to analogize the public policy ground upon which they based their decisions to an established category, and the comparatively less sophisticated insolvency legislation in force at the time did not provide a basis for invalidating such contracts. In my view, this is why the jurisprudence is replete with references to "fraud" and similar terminology.

[105] My next observation relates to the mode of reasoning in anti-deprivation rule decisions. If the anti-deprivation rule were based on an implied prohibition in the relevant bankruptcy statute, one would expect both the English and the Canadian authorities to turn on an appreciation of Parliament's legislative intent as embodied in the wording of the relevant statute: see J. D. McCamus, *The Law of Contracts* (2nd ed. 2012), at pp. 457 and 486. However, on my reading of those authorities, courts considering the application of the anti-deprivation rule have routinely recited the principles and policies articulated in prior authorities with little or no regard for the wording of the relevant statute in force. Thus, the rule is more in the nature of a judicially-apprehended public policy than an implied prohibition in the various insolvency statutes which have been enacted and revised throughout the centuries of the rule's trans-Atlantic existence. In this regard, it should be recalled that this Court adopted the early English authorities and then extended their reach to cases outside of the bankruptcy context in *Hobbs*, notwithstanding the fact that there was no bankruptcy legislation in force in Canada at the time. To me, this suggests that the public policy is judicially derived.

[106] My view, based on these two observations, is that the anti-deprivation rule falls under the common law branch of the public policy doctrine, which includes a policy against agreements entered into for the purpose of defrauding or otherwise injuring third parties: see McCamus, at p. 456; *Elford v. Elford* (1922), 64 S.C.R. 125; *Campbell River Lumber Co.*

à de la fraude, et non sur une conclusion qu'elles étaient implicitement interdites par une loi. Les premiers tribunaux de common law ayant appliqué la règle devaient faire une analogie entre l'intérêt public sur lequel ils fondaient leur décision et une catégorie établie, et les lois moins sophistiquées en matière d'insolvabilité en vigueur à l'époque n'offraient pas de fondement permettant d'invalider de tels contrats. À mon avis, c'est pour cette raison que la jurisprudence est empreinte de références à la « fraude » et à des notions similaires.

[105] Ma prochaine observation concerne le mode de raisonnement dans les décisions relatives à la règle anti-privation. Si cette règle était fondée sur une prohibition implicite contenue dans la loi sur la faillite pertinente, on pourrait s'attendre à ce que tant la jurisprudence anglaise que la jurisprudence canadienne examinent l'intention législative du Parlement tel qu'elle ressort du libellé de la loi en cause : voir J. D. McCamus, *The Law of Contracts* (2e éd. 2012), p. 457 et 486. Or, ma revue des décisions en question illustre que les tribunaux qui ont envisagé l'application de la règle anti-privation ont toujours cité les principes et les politiques exposés dans la jurisprudence en accordant peu ou pas d'importance au libellé de la loi pertinente en vigueur. Par conséquent, la règle relève davantage de la nature d'un intérêt public envisagé par les tribunaux que d'une prohibition implicite contenue dans les diverses lois sur l'insolvabilité qui ont été adoptées et révisées à travers les siècles au cours desquels cette règle a existé de part et d'autre de l'Atlantique. À cet égard, il faut se rappeler que la Cour a adopté les vieux précédents anglais et en a ensuite élargi la portée aux affaires ne relevant pas du domaine de la faillite dans l'arrêt *Hobbs*, et ce, malgré le fait qu'à cette époque, il n'existait aucune loi sur la faillite au Canada. À mon avis, cela donne à penser que l'intérêt public émane des tribunaux.

[106] Compte tenu de ces deux observations, je suis d'avis que la règle anti-privation relève du volet de common law de la doctrine de l'intérêt public, qui interdit les ententes conclues dans le but de commettre une fraude ou de causer autrement un préjudice à un tiers : voir McCamus, p. 456; *Elford c. Elford* (1922), 64 R.C.S. 125; *Campbell River*

v. McKinnon (1922), 64 S.C.R. 396; *Zimmermann v. Letkeman*, [1978] 1 S.C.R. 1097.

[107] My colleague appears to take the view that the anti-deprivation rule falls under the statutory branch of the public policy doctrine: Rowe J.'s reasons, at para. 30. With respect, however, the provision on which my colleague relies, s. 71 of the *BIA*, is far from clear in this regard. Under s. 71, a bankrupt ceases to have any capacity to dispose of or otherwise deal with their property only when a bankruptcy order is made or an assignment into bankruptcy is filed. It is not clear from its wording that this provision has any effect on the validity of an agreement entered into before that time. This ambiguity is particularly apparent in relation to agreements which qualify the bankrupt's interest in an asset from the outset, as is the case with Condition Q of the Subcontract. It is a well-established principle that the *BIA* does not grant a trustee any greater interest in a bankrupt's property than that enjoyed by the bankrupt prior to bankruptcy: *Giffen (Re)*, [1998] 1 S.C.R. 91, at para. 50; *Lefebvre (Trustee of)*, 2004 SCC 63, [2004] 3 S.C.R. 326, at para. 37; *Flintoft v. Royal Bank of Canada*, [1964] S.C.R. 631, at p. 634. The trustee "steps into the shoes" of the bankrupt and takes the bankrupt's property "warts and all": *Saulnier v. Royal Bank of Canada*, 2008 SCC 58, [2008] 3 S.C.R. 166, at para. 50. With respect, my colleague breaks with this principle by, in effect, holding that s. 71 converts the bankrupt's qualified interest in an asset into an absolute or unqualified interest in the hands of the trustee. Although the common law may restrict parties' freedom to qualify a party's interest in the event of insolvency, there is nothing in the wording of s. 71 which purports to do so.

[108] Nor is the picture made any clearer when one considers the statutory context, which includes numerous provisions indicating that arm's length *bona fide* commercial transactions — even transfers of assets at an undervalue — are valid as against the trustee of the bankrupt's estate: *BIA*, ss. 95(1), 96(1), 97(1) and 99(1). Thus, it would appear that Parliament's objective of maximizing "global recovery for all creditors" was not intended to be achieved at the expense of all *bona fide* agreements which may stand in the way of that goal: *Alberta (Attorney*

Lumber Co. c. McKinnon (1922), 64 R.C.S. 396; *Zimmermann c. Letkeman*, [1978] 1 R.C.S. 1097.

[107] Mon collègue semble être d'avis que la règle anti-privation relève du volet statutaire de la doctrine de l'intérêt public : motifs du juge Rowe, par. 30. Avec égards, la disposition sur laquelle il se fonde, soit l'art. 71 de la *LFI*, est toutefois loin d'être claire à cet égard. Aux termes de l'art. 71, le failli cesse d'être habile à céder ou à aliéner ses biens uniquement au moment où l'ordonnance de faillite est rendue ou lorsqu'une cession est produite. Il ne ressort pas clairement de ce libellé que cette disposition a un effet quelconque sur la validité d'une entente conclue avant ce moment. Cette ambiguïté est particulièrement apparente pour ce qui est des ententes qui ont qualifié l'intérêt du failli à l'égard d'un bien dès le début, comme c'est le cas de la condition Q du contrat de sous-traitance. Il est un principe bien établi que la *LFI* n'accorde pas au syndic, à l'égard d'un bien du failli, un intérêt supérieur à celui qu'avait le failli avant la faillite : *Giffen (Re)*, [1998] 1 R.C.S. 91, par. 50; *Lefebvre (Syndic de)*, 2004 CSC 63, [2004] 3 R.C.S. 326, par. 37; *Flintoft c. Royal Bank of Canada*, [1964] R.C.S. 631, p. 634. Le syndic « prend simplement la place » du failli et prend possession de l'actif « avec tous ses défauts » : *Saulnier c. Banque Royale du Canada*, 2008 CSC 58, [2008] 3 R.C.S. 166, par. 50. Avec égards, l'approche adoptée par mon collègue s'écarte de ce principe, car, dans les faits, elle conclut que l'art. 71 convertit l'intérêt relatif du failli à l'égard d'un bien en intérêt absolu pour le syndic. Même si la common law peut restreindre la liberté des parties de qualifier l'intérêt d'une partie en cas d'insolvabilité, rien dans le libellé de l'art. 71 ne reflète une telle intention.

[108] Le portrait de la situation n'est pas plus clair si l'on considère le contexte statutaire, qui comprend de nombreuses dispositions prévoyant que les transactions commerciales de bonne foi — même les transferts de biens à un prix sous-évalué — sont valides contre un syndic de faillite : *LFI*, par. 95(1), 96(1), 97(1) et 99(1). Ainsi, il semblerait que l'objectif du Parlement de maximiser « le recouvrement global pour tous les créanciers » n'avait pas pour but d'être réalisé aux dépens de toutes les ententes conclues de bonne foi qui font obstacle à cet objectif :

General) v. Moloney, 2015 SCC 51, [2015] 3 S.C.R. 327, at para. 33. At the very least, then, s. 71 is ambiguous.

[109] Courts applying the statutory branch of the public policy doctrine "should be slow to imply the statutory prohibition of contracts, and should do so only when the implication is quite clear": *St. John Shipping Corp. v. Joseph Rank Ltd.*, [1957] 1 Q.B. 267, at p. 289. To approach the matter otherwise would introduce significant uncertainty into commercial affairs given the enormous body of statute law in force in modern times. Indeed, the modern approach to the statutory branch of the public policy doctrine has been to relax the rigidity of the classical doctrine by permitting the enforcement of contracts in appropriate cases even where they contravene the provisions of a statute: *Still v. M.N.R.*, [1998] 1 F.C. 549 (C.A.), at para. 37; *Transport North American*, at paras. 19-26. Therefore, the better approach, in my opinion, is to treat the anti-deprivation rule as falling under the common law branch of the public policy doctrine rather than adopting a strained interpretation of s. 71 of the *BIA*.

[110] In contrast with s. 71, the *pari passu* provision in the *BIA*, s. 141, establishes a very clear bright-line rule that "all claims proved in a bankruptcy shall be paid rateably": s. 141. This was the provision on which this Court rested its decision in *Gingras*, and it is substantially similar to s. 302 of the *Companies Act, 1948* (U.K.), 11 & 12 Geo. 6, c. 38, on which Lord Cross relied in *British Eagle*. This clear and straightforward statutory language readily supports a conclusion that Parliament intended to prohibit a debtor from contracting with creditors for a different distribution of the debtor's assets in bankruptcy than that provided for in s. 141. Thus, the *pari passu* rule falls under the statutory branch of the public policy doctrine.

[111] In sum, the reason behind the different tests for the *pari passu* rule and the anti-deprivation rule lies in the difference in the juridical character of the

Alberta (Procureur général) c. Moloney, 2015 CSC 51, [2015] 3 R.C.S. 327, par. 33. Donc, à tout le moins, l'art. 71 est ambigu.

[109] Les tribunaux qui appliquent le volet statutaire de la doctrine de l'intérêt public [TRADUCTION] « ne devraient pas s'empresser de considérer qu'un contrat va à l'encontre de la loi, et ne devraient le faire que lorsque l'intention en ce sens est passablement évidente » : *St. John Shipping Corp. c. Joseph Rank Ltd.*, [1957] 1 Q.B. 267, p. 289. Examiner la question sous un autre angle entraînerait une incertitude considérable dans les affaires commerciales étant donné l'énorme quantité de lois en vigueur de nos jours. En effet, l'approche moderne relative au volet statutaire de la doctrine de l'intérêt public consiste à assouplir la doctrine classique en permettant l'exécution de contrats dans les cas appropriés, même lorsqu'ils contreviennent aux dispositions d'une loi : *Still c. M.R.N.*, [1998] 1 C.F. 549 (C.A.), par. 37; *Transport North American*, par. 19-26. Par conséquent, la meilleure approche, à mon avis, consiste à traiter la règle anti-privation comme relevant du volet de common law de la doctrine de l'intérêt public plutôt que d'adopter une interprétation forcée de l'art. 71 de la *LFI*.

[110] Par contraste avec l'art. 71, la disposition *pari passu* de la *LFI*, l'art. 141, établit une règle de démarcation très nette selon laquelle « toutes les réclamations établies dans la faillite sont acquittées au prorata » : art. 141. Il s'agit de la disposition sur laquelle la Cour a fondé sa décision dans l'arrêt *Gingras* et elle est essentiellement semblable à l'art. 302 de la *Companies Act, 1948* (R.-U.), 11 & 12 Geo. 6, c. 38, sur laquelle lord Cross s'est fondé dans l'arrêt *British Eagle*. Ce libellé clair et précis de la loi appuie d'emblée la conclusion selon laquelle le législateur avait pour intention d'interdire à un débiteur de conclure un contrat avec des créanciers en vue de distribuer ses biens en cas de faillite d'une manière autre que celle prévue à l'art. 141. La règle du *pari passu* relève donc du volet statutaire de la doctrine de l'intérêt public.

[111] En somme, la différence entre les tests applicables à la règle du *pari passu* et à la règle anti-privation s'explique par la nature juridique

two rules. The *pari passu* rule is based on an implied prohibition in the *BIA* that operates regardless of the parties' intentions, whereas the anti-deprivation rule has its origins in the common law public policy against agreements entered into for an unlawful purpose: see *Still*, at para. 22. There is therefore a principled legal basis for maintaining different tests for the two rules.

[112] It remains to be considered, however, whether sufficient policy considerations can be mustered to justify departing from the anti-deprivation rule's objective purpose test.

(3) The Weight of Public Policy Considerations Favours the *Bona Fide* Commercial Purpose Test Over the Effects-Based Test

[113] The anti-deprivation rule's common law character does not preclude it from operating in tandem with the *BIA* in support of Parliament's statutory objectives. Although the common law and statutory branches of the public policy doctrine are distinct, they are not watertight compartments. It is prudent for courts applying the common law branch to take into account the policies embodied in legislation as a reflection of society's public policy concerns: Waddams, at para. 566. Therefore, the anti-deprivation rule's common law character does not preclude a court from taking into account Parliament's objective of maximizing global recovery for all creditors when considering how to formulate the anti-deprivation rule. What it does mean, however, is that Parliament's objectives must be weighed against the other policy interests protected by the common law when considering how best to formulate the rule.

[114] It may appear that my colleague and I differ on this point. However, in my view, our differences in approach flow from our disagreement about the legal nature of the anti-deprivation rule: Rowe J.'s reasons, at para. 33. If I shared my colleague's view that the anti-deprivation rule should be understood as

différente des deux règles. La première est fondée sur une prohibition implicite contenue dans la *LFI* qui s'applique indépendamment de l'intention des parties, tandis que la seconde tire son origine du principe d'intérêt public de common law qui interdit les ententes conclues à des fins illégales : voir *Still*, par. 22. Par conséquent, il existe un fondement juridique valable qui justifie le recours à des tests différents pour l'application des deux règles.

[112] Il reste toutefois à examiner s'il existe suffisamment de considérations d'intérêt public pour justifier que l'on s'écarte du test de la finalité commerciale objective applicable à la règle anti-privation.

(3) Le poids des considérations d'intérêt public fait pencher la balance vers le test fondé sur l'objectif commercial véritable plutôt que vers le test fondé sur les effets

[113] Le fait que la règle anti-privation découle de la common law ne l'empêche pas de s'appliquer en même temps que la *LFI* ni de concourir à l'atteinte des objectifs législatifs du Parlement. Bien que le volet de common law et le volet statutaire de la doctrine de l'intérêt public soient distincts, ils ne constituent pas des compartiments étanches. Les tribunaux qui appliquent le volet de common law font preuve de prudence en tenant compte des politiques intégrées dans les lois comme le reflet des préoccupations de la société en matière d'intérêt public : Waddams, par. 566. Par conséquent, le fait que la règle anti-privation soit issue de la common law n'empêche pas un tribunal de tenir compte de l'objectif du Parlement qui est de maximiser le recouvrement global pour tous les créanciers lorsqu'il se penche sur la façon de formuler la règle anti-privation. Cela veut toutefois dire que les objectifs du Parlement doivent être évalués par rapport aux autres intérêts publics protégés par la common law au moment de décider de la meilleure façon de formuler la règle.

[114] Il peut sembler que mon collègue et moi ne soyons pas d'accord sur ce point. Or, à mon avis, les différences dans nos approches découlent de notre désaccord sur la nature juridique de la règle anti-privation : motifs du juge Rowe, par. 33. Si je partageais l'avis de mon collègue selon lequel la

an implied statutory prohibition, then I would have no hesitation in agreeing that the inquiry should be more narrowly focused on selecting the test that best gives effect to Parliament's legislative intent. However, I see the anti-deprivation rule as a judicially derived public policy and, as a result, my approach is informed by Parliament's policy objectives as well as by the other interests and values protected by the common law.

[115] Freedom of contract is the general rule, and it can be displaced only by an "overriding public policy . . . that outweighs the very strong public interest in the enforcement of contracts": *Tercon Contractors Ltd. v. British Columbia (Transportation and Highways)*, 2010 SCC 4, [2010] 1 S.C.R. 69, at para. 123, per Binnie J., dissenting, but not on this point. Therefore, I see the policy issue as being whether the effects-based test put forward by my colleague or the *bona fide* commercial purpose test confirmed, in my view, by the existing jurisprudence most accurately reflects the point at which the public policy furthered by the anti-deprivation rule outweighs the public interest in the enforcement of contracts. In my judgment, that point is reached only where there is no legitimate and objectively ascertainable commercial purpose for the deprivation in bankruptcy.

[116] The common law "places great weight on the freedom of contracting parties to pursue their individual self-interest": *Bhasin v. Hrynew*, 2014 SCC 71, [2014] 3 S.C.R. 494, at para. 70. The common law even accepts that "a party may sometimes cause loss to another . . . in the legitimate pursuit of economic self-interest": para. 70. In my view, a purely effects-based test gives too little weight to freedom of contract, party autonomy, and the "elbow-room" which the common law traditionally accords for the aggressive pursuit of self-interest: see *A.I. Enterprises*, at para. 31, quoting C. Sappideen and P. Vines, eds., *Fleming's The Law of Torts* (10th ed. 2011), at para. 30.120. On the other hand, adopting a purely subjective test may create significant uncertainty by introducing a vague standard which unduly restricts the scope of the anti-deprivation

règle anti-privation devrait être comprise comme une prohibition statutaire implicite, je n'aurais aucune hésitation à convenir que l'enquête devrait être plus étroitement axée sur la sélection du test qui donne le mieux effet à l'intention législative du Parlement. Toutefois, je considère la règle anti-privation comme une règle d'intérêt public émanant des tribunaux et, par conséquent, mon approche est éclairée tant par les objectifs politiques du Parlement que par les autres intérêts et valeurs protégés par la common law.

[115] La règle générale est celle de la liberté contractuelle et elle ne peut être écartée que par « une considération d'ordre public prépondérante [. . .] qui l'emporte sur le très grand intérêt public lié à l'application des contrats » : *Tercon Contractors Ltd. c. Colombie-Britannique (Transports et Voirie)*, 2010 CSC 4, [2010] 1 R.C.S. 69, par. 123, le juge Binnie, dissident, mais pas sur ce point. Par conséquent, j'aborde la question de l'intérêt public comme celle de savoir lequel entre le test fondé sur les effets préconisé par mon collègue et le test fondé sur l'objectif commercial véritable confirmé à mon avis par la jurisprudence reflète le mieux le point où l'intérêt public visé par la règle anti-privation l'emporte sur l'intérêt public à l'égard de l'exécution des contrats. J'estime que ce point est atteint dans les cas où la privation touchant l'actif de la faillite ne répond à aucune finalité commerciale légitime et objectivement vérifiable.

[116] La common law « accorde [. . .] beaucoup de poids à la liberté des parties contractantes dans la poursuite de leur intérêt personnel » : *Bhasin c. Hrynew*, 2014 CSC 71, [2014] 3 R.C.S. 494, par. 70. Elle accepte même qu'« une partie [puisse] parfois causer une perte à une autre partie [. . .] dans la poursuite légitime d'intérêts économiques personnels » : par. 70. À mon avis, un test fondé uniquement sur les effets accorde trop peu de poids à la liberté contractuelle, à l'autonomie des parties et à la liberté d'action que la common law confère traditionnellement en vue de la poursuite agressive d'intérêts personnels : voir *A.I. Enterprises*, par. 31, citant C. Sappideen et P. Vines, dir., *Fleming's The Law of Torts* (10e éd. 2011), par. 30.120. Par contre, l'adoption d'un test purement subjectif pourrait entraîner une incertitude considérable, car on introduirait une

rule. A subjective purpose test would place too little weight on Parliament's objective of maximizing global recovery for all creditors. That is why, in my opinion, the middle path of following the objective *bona fide* commercial purpose test is the best way to balance freedom of contract, the interests of third party creditors, and commercial certainty.

[117] My colleague fears that a purpose-based test would render the anti-deprivation rule ineffective because the rule would apply only in the clearest of cases: Rowe J.'s reasons, at para. 36. However, as I demonstrated in my discussion of the Canadian jurisprudence, there is not a single Canadian decision applying the anti-deprivation rule in which an absence of a *bona fide* commercial purpose could not be discerned from the objective circumstances in the record. Indeed, the majority of the courts applying the rule have, in fact, inquired into the objective purpose behind the transaction or contractual provision in question rather than simply resting their decision on its effects. I therefore do not agree that retaining the objective purpose element would "threaten to undermine the statutory scheme of the *BIA*": Rowe J.'s reasons, at para. 36. Further, this Court's jurisprudence establishes that the public policy doctrine "should be invoked only in clear cases": *In re Estate of Charles Millar, Deceased*, [1938] S.C.R. 1, at p. 7, quoting *Fender v. St. John-Mildmay*, [1938] A.C. 1, at p. 12. A more restricted scope for the anti-deprivation rule is therefore in keeping with this Court's jurisprudence on the public policy doctrine. It is also in line with the modern trend in the English cases, which has been to restrict rather than to broaden the scope of the anti-deprivation rule: *Lomas v. JFB Firth Rixson Inc.*, [2010] EWHC 3372 (Ch.), [2011] 2 B.C.L.C. 120, at para. 96, aff'd [2012] EWCA Civ. 419, [2012] 2 All E.R. (Comm.) 1076.

[118] My colleague also argues that an effects-based test is consistent with the American-style *ipso facto* provisions in the *BIA*: Rowe J.'s reasons, at para. 35. These *ipso facto* provisions state that no one may terminate or amend, or claim an accelerated payment or forfeiture of the term under, any

norme vague qui restreindrait indûment la portée de la règle anti-privation. Un test subjectif fondé sur la finalité accorderait trop peu de poids à l'objectif du Parlement de maximiser le recouvrement global pour tous les créanciers. C'est pourquoi, à mon avis, la meilleure solution pour respecter l'équilibre entre la liberté contractuelle, les intérêts des créanciers tiers et la certitude commerciale consisterait à adopter un test objectif fondé sur la finalité commerciale véritable.

[117] Mon collègue craint qu'un test fondé sur l'objectif ou la finalité rende la règle anti-privation inefficace parce qu'elle ne s'appliquerait que dans les cas les plus évidents : motifs du juge Rowe, par. 36. Pourtant, comme je l'ai démontré dans mon examen de la jurisprudence canadienne, il n'existe aucune décision appliquant la règle anti-privation dans laquelle l'absence d'un objectif commercial véritable n'a pu être dégagée des circonstances objectives du dossier. En effet, la majorité des tribunaux qui ont appliqué la règle ont examiné les fins objectives de la stipulation plutôt que de simplement fonder leur décision sur ses effets. Je ne suis donc pas d'accord pour dire que le fait de retenir la notion de fins objectives « risquerait de nuire au régime législatif de la *LFI* » : motifs du juge Rowe, par. 36. En outre, la jurisprudence de la Cour établit que la doctrine de l'intérêt public [TRADUCTION] « ne doit être invoquée que dans les cas clairs » : *In re Estate of Charles Millar, Deceased*, [1938] R.C.S. 1, p. 7, citant *Fender c. St. John-Mildmay*, [1938] A.C. 1, p. 12. Une portée plus restreinte pour la règle anti-privation est donc compatible avec la jurisprudence de la Cour sur la doctrine de l'intérêt public. Elle va également dans le même sens que la tendance moderne observée dans la jurisprudence anglaise qui consiste à restreindre plutôt qu'à élargir la portée de la règle : *Lomas c. JFB Firth Rixson Inc.*, [2010] EWHC 3372 (Ch.), [2011] 2 B.C.L.C. 120, par. 96, conf. par [2012] EWCA Civ. 419, [2012] 2 All E.R. (Comm.) 1076.

[118] Mon collègue soutient également que le test fondé sur les effets est compatible avec les dispositions *ipso facto* de style américain de la *LFI* : motifs du juge Rowe, par. 35. Ces dispositions *ipso facto* établissent que nul ne peut, au seul motif de l'insolvabilité d'une personne, résilier ou modifier un contrat,

agreement by reason only of a person's insolvency: *BIA*, ss. 84.2 (individual bankruptcies), 65.1 (corporate proposals) and 66.34 (consumer proposals). I do not regard these *ipso facto* provisions as analogous to an effects-based test because they apply to contractual terms that are triggered on insolvency, regardless of the terms' effects. The test applied by these provisions is more aptly characterized as trigger-based, not effects-based. In addition, as Rowe J. observes, the statutory *ipso facto* provisions were enacted for a purpose different than that served by the anti-deprivation rule: Rowe J.'s reasons, at para. 28. The *ipso facto* provisions are aimed at protecting debtors; the anti-deprivation rule, by contrast, protects creditors. I therefore do not view the statutory *ipso facto* provisions as relevant statements of public policy on the matter at hand.

[119] If regard is to be had to Parliament's policies enacted in the *BIA*, then this Court should take notice of Parliament's policy of upholding the validity of arm's length *bona fide* commercial transactions that have the effect of giving one creditor a preference over another or of depriving the bankrupt's estate of value: ss. 95(1)(a), 96(1) and 97(3). In addition, "good faith" continues to play a role in upholding the validity of protected transactions, which occur after the date of the initial bankruptcy event: ss. 97(1) and 99(1). In my view, these provisions reflect Parliament's policy preference for upholding the validity of *bona fide* commercial arrangements, even when they have the effect of reducing the pool of assets available to a debtor's creditors in bankruptcy. Indeed, it would be a "significant departure from [the] bankruptcy principle to void transactions with a valid commercial purpose based on a mechanical application of a broad principle", such as the effects-based test favoured by my colleague: M. Grottenthaler and E. Pillon, "Financial Products and the Anti-Forfeiture Principle" (2012), 1 *J. Insolvency Inst. Can.* 139, at p. 159. In this regard, I agree with my colleague that courts should pay close attention to the policies which Parliament has enacted through legislation and should not develop the common law in a way that would create "new and greater

ni se prévaloir d'une clause de déchéance du terme : *LFI*, art. 84.2 (faillites de personnes physiques), 65.1 (propositions d'entreprises), 66.34 (propositions de débiteurs consommateurs). Je ne considère pas ces dispositions *ipso facto* comme étant analogues à un test fondé sur les effets parce qu'elles s'appliquent aux stipulations dont l'application est déclenchée par l'insolvabilité, quels que soient les effets de ces stipulations. Il est plus exact de décrire le test appliqué par ces dispositions comme un test fondé sur les éléments déclencheurs plutôt qu'un test fondé sur les effets. De plus, comme le juge Rowe l'observe, les dispositions législatives *ipso facto* ont été adoptées à une fin différente de celles visées par la règle anti-privation : motifs du juge Rowe, par. 28. Les dispositions *ipso facto* visent à protéger les débiteurs; la règle anti-privation, à l'inverse, protège les créanciers. Je considère donc que ces dispositions ne sont pas des énoncés d'intérêt public pertinents pour la question en cause en l'espèce.

[119] S'il faut tenir compte des politiques énoncées dans la *LFI*, la Cour devrait aussi tenir compte de la politique du Parlement favorable à la validité des transactions commerciales de bonne foi faites en l'absence d'un lien de dépendance même lorsque celles-ci ont pour effet de procurer à un créancier une préférence sur un autre créancier ou de réduire la valeur de l'actif du failli : al. 95(1)a) et par. 96(1) et 97(3). En outre, la « bonne foi » continue de jouer un rôle dans le maintien de la validité des transactions protégées qui surviennent après l'ouverture de la faillite : par. 97(1) et 99(1). À mon avis, ces dispositions reflètent une préférence du Parlement pour le maintien de la validité des ententes commerciales de bonne foi, même lorsque celles-ci ont pour effet de réduire l'ensemble de biens accessibles aux créanciers en cas de faillite. Effectivement, ce serait [TRADUCTION] « une dérogation importante au principe du droit de la faillite que d'annuler les transactions visant un objectif commercial valide par application mécanique d'un principe général », comme le test fondé sur les effets favorisé par mon collègue : M. Grottenthaler et E. Pillon, « Financial Products and the Anti-Forfeiture Principle » (2012), 1 *J. Insolvency Inst. Can.* 139, p. 159. À cet égard, je conviens avec mon collègue que les tribunaux devraient être très attentifs aux politiques que le

difficulties": Rowe J.'s reasons, at paras. 33 and 39, quoting *Watkins v. Olafson*, [1989] 2 S.C.R. 750, at p. 762. However, it is the adoption of an effects-based test in lieu of the traditional purpose-based test that offends these principles in this appeal.

[120] My colleague also states that a purpose-based test gives rise to uncertainty at the time of contracting because parties cannot know if a court will accept their *bona fide* commercial reasons: Rowe J.'s reasons, at para. 34. However, given that the *bona fide* commercial purpose test is objective, purpose is discernable from the objective circumstances at the time of contract formation and can thus be determined just as readily as effects can under the effects-based test. Therefore, either standard provides the same measure of clarity. In addition, certainty in commercial affairs is typically better served by giving effect to, rather than invalidating, contracts which were freely entered into, particularly when they serve commercial purposes and are not directed at an unlawful objective.

[121] I also do not share my colleague's view that applying a *bona fide* commercial purpose test would require a significantly more onerous analysis of the parties' intentions than that entailed by an effects-based test: Rowe J.'s reasons, at para. 34. An objective assessment of purpose is inescapable on either standard. Like the purpose-based test, ascertaining the effects of a provision when applying an effects-based test would require an interpretation of the impugned contractual arrangement. The interpretation of a contract requires an objective assessment of the parties' intentions: *Sattva*, at para. 49. In addition, a test which requires a court to assess the parties' *bona fides* is not new in the realm of commercial law, especially in light of this Court's recognition of a general organizing principle of good faith performance in the common law of contract: *Bhasin*, at para. 33.

Parlement a adoptées par voie législative et s'abstenir de faire évoluer la common law d'une manière qui créerait « des difficultés nouvelles plus grandes » : motifs du juge Rowe, par. 33 et 39, citant *Watkins c. Olafson*, [1989] 2 R.C.S. 750, p. 762. Toutefois, c'est l'adoption d'un test fondé sur les effets plutôt que le test traditionnel fondé sur l'objectif ou la finalité qui porte atteinte à ces principes dans le présent pourvoi.

[120] Mon collègue est également d'avis qu'un test fondé sur l'objectif ou la finalité crée une incertitude au moment de conclure le contrat, car les parties ne peuvent pas savoir si un tribunal acceptera leurs motifs commerciaux de bonne foi : motifs du juge Rowe, par. 34. Or, comme le test fondé sur la finalité commerciale véritable est un test objectif, la finalité ressort des circonstances objectives qui prévalaient au moment de la conclusion du contrat et peut donc être déterminée aussi facilement que des effets peuvent l'être lors de l'application du test fondé sur les effets. Les deux normes procurent donc le même degré de clarté. Par ailleurs, la certitude dans les affaires commerciales est habituellement mieux servie en donnant effet aux contrats conclus librement plutôt qu'en les invalidant, surtout lorsque les ententes en question poursuivent des fins commerciales et non un objectif illégal.

[121] Je ne suis pas non plus d'accord avec le point de vue de mon collègue selon lequel le fait d'appliquer un test fondé sur la finalité ou l'objectif commercial véritable exigerait une analyse considérablement plus détaillée des intentions des parties que celle associée au test fondé sur les effets : motifs du juge Rowe, par. 34. Une évaluation objective de la finalité est inévitable dans les deux cas. Tout comme c'est le cas en appliquant le test fondé sur l'objectif, l'examen des effets d'une stipulation lors de l'application du test fondé sur les effets exigerait une interprétation de l'entente contractuelle contestée. L'interprétation d'un contrat requiert une évaluation objective de l'intention des parties : *Sattva*, par. 49. De plus, un test qui oblige un tribunal à évaluer la bonne foi des parties n'a rien de nouveau dans le domaine du droit commercial, particulièrement à la lumière de la reconnaissance par la Cour d'un principe directeur général d'exécution de bonne foi des contrats en common law : *Bhasin*, par. 33.

[122] Finally, my colleague argues that the anti-deprivation rule should involve an effects-based test in order to better protect the interests of creditors, because debtors are not properly incentivized to protect their creditors' interests when dealing with third parties: Rowe J.'s reasons, at para. 37. However, one must take into account the full range of options available to creditors to protect their rights. For example, the *Canadian Business Corporations Act*, R.S.C. 1985, c. C-44, includes in s. 241 what this Court has described as a "broad oppression remedy" which provides a "mechanism for creditors to protect their interests from the prejudicial conduct of directors": *Peoples Department Stores Inc. (Trustee of) v. Wise*, 2004 SCC 68, [2004] 3 S.C.R. 461, at para. 51; see also paras. 48-50. I view the oppression remedy, the directors' duty of care, the various anti-avoidance provisions in the *BIA* and in provincial statutes and the ability of creditors to bargain for contractual protections as alleviating any perceived need to extend the reach of the anti-deprivation rule.

[123] In conclusion, I am not persuaded that the policy considerations raised by my colleague are sufficient to override the otherwise strong countervailing public interest in the enforcement of contracts. There is a strong jurisprudential basis for concluding that the anti-deprivation rule has always included a *bona fide* commercial purpose element in Canada, and there is a principled legal basis for maintaining this distinct feature of the anti-deprivation rule as compared to the *pari passu* rule. I would therefore hold that the anti-deprivation rule does not apply to transactions or contractual provisions which serve a legitimate and objectively ascertainable commercial purpose.

B. *Paragraph (d) of Condition Q Furthers a Bona Fide Commercial Purpose*

[124] Nielsen J. found that clause Q(d) was a genuine pre-estimate of damages. He noted that Chandos would incur administration and management costs as a result of Capital Steel's bankruptcy and that it was

[122] Enfin, mon collègue fait valoir que la règle anti-privation devrait entraîner le recours à un test fondé sur les effets afin de mieux protéger les intérêts des créanciers, car les débiteurs ne sont pas motivés à protéger les intérêts de leurs créanciers lorsqu'ils traitent avec des tiers : motifs du juge Rowe, par. 37. Il faut cependant tenir compte de l'ensemble des options qui s'offrent aux créanciers pour protéger leurs droits. Par exemple, la *Loi canadienne sur les sociétés par actions*, L.R.C. 1985, c. C-44, incorpore à l'art. 241 ce que la Cour décrit comme « un recours aussi général en cas d'abus de droit » prévoyant un « mécanisme qui permet aux créanciers d'obtenir la protection de leurs intérêts en cas de conduite préjudiciable des administrateurs » : *Magasins à rayons Peoples inc. (Syndic de) c. Wise*, 2004 CSC 68, [2004] 3 R.C.S. 461, par. 51; voir aussi par. 48-50. Je suis d'avis que le redressement en cas d'abus de droit, l'obligation de diligence des administrateurs, les diverses dispositions anti-évitement de la *LFI* et des lois provinciales ainsi que la capacité des créanciers de négocier des protections contractuelles sont des moyens qui permettent d'atténuer la perception qu'il soit nécessaire d'élargir la portée de la règle anti-privation.

[123] En conclusion, je ne suis pas convaincue que les considérations d'intérêt public soulevées par mon collègue surpassent en importance l'intérêt public opposé dans l'exécution des contrats. Il existe un fondement jurisprudentiel solide pour conclure que la règle anti-privation a toujours compris une notion d'objectif commercial véritable au Canada de même qu'un fondement juridique valable pour maintenir cette caractéristique distincte de la règle anti-privation que ne comporte pas la règle du *pari passu*. Je conclurais donc que la règle anti-privation ne s'applique pas aux transactions ou aux stipulations ayant une finalité commerciale légitime et objectivement vérifiable.

B. *Le paragraphe (d) de la condition Q vise un objectif commercial véritable*

[124] Le juge Nielsen a conclu que la clause Q(d) constituait une véritable estimation anticipée des dommages-intérêts. Il a noté que Chandos aurait à assumer des coûts administratifs et de gestion

at risk for future liabilities of Capital Steel. He added that the clause was not an attempt to contract out of the bankruptcy laws. He thus found that clause Q(d) served a *bona fide* commercial purpose. That finding was not disturbed on appeal, as the Court of Appeal was unanimous in its view that clause Q(d) serves "legitimate commercial interests": paras. 55 and 394-97. The application of the anti-deprivation rule in this appeal could therefore be dealt with on the basis of the standard of review.

en raison de la faillite de Capital Steel et qu'elle courrait des risques en lien avec les dettes futures de Capital Steel. Il a ajouté que la stipulation ne constituait pas une tentative par les parties de se soustraire aux lois en matière de faillite. Il a donc conclu que la clause Q(d) visait un objectif commercial véritable. Cette conclusion n'a pas été infirmée en appel, car la Cour d'appel a jugé à l'unanimité que la clause Q(d) visait bel et bien des [TRADUCTION] « intérêts commerciaux légitimes » : par. 55 et 394-397. L'application de la règle anti-privation dans cet appel pouvait donc être abordée selon la norme de contrôle.

[125] However, Deloitte urges a different interpretation of the Subcontract, which, if persuasive, may call into question Nielsen J.'s finding of fact. Deloitte argues that clause Q(d) grants Chandos a sum which is essentially gratuitous or duplicative because clause Q(b) completely covers all costs to Chandos arising from Capital Steel's bankruptcy. Thus, it argues, the 10 percent fee arising from clause Q(d) is in addition to the full indemnity of Chandos arising from clause Q(b).

[125] Cependant, Deloitte demande instamment une interprétation différente du contrat de sous-traitance qui, si elle est convaincante, pourrait remettre en question la conclusion de fait du juge Nielsen. Deloitte soutient que la clause Q(d) accorde à Chandos une somme offerte essentiellement à titre gratuit ou qui fait du moins double emploi, puisque la clause Q(b) vise tous les coûts qui incombent à Chandos en raison de la faillite de Capital Steel. En conséquence, Deloitte fait valoir que les frais de 10 p. 100 prévus à la clause Q(d) s'ajoutent à l'indemnisation complète de Chandos prévue à la clause Q(b).

[126] One problem Deloitte faces is that the interpretation of a contract is generally considered to be a question of mixed fact and law reviewable on the palpable and overriding error standard: *Sattva*, at para. 50; *Heritage Capital Corp. v. Equitable Trust Co.*, 2016 SCC 19, [2016] 1 S.C.R. 306, at paras. 21-24. There is an exception which permits correctness review where the contract at issue is "a standard form contract, the interpretation at issue is of precedential value, and there is no meaningful factual matrix . . . to assist in the interpretation process": *Ledcor Construction Ltd. v. Northbridge Indemnity Insurance Co.*, 2016 SCC 37, [2016] 2 S.C.R. 23, at para. 24. While we are told that the Subcontract is a standard form contract, it is not suggested that it is widely used throughout the construction industry or that the interpretation of clause VII Q is of precedential value. It is therefore unclear that the interpretation of the Subcontract falls within the *Ledcor* exception. I express no firm conclusion

[126] Un des problèmes auxquels Deloitte fait face est que l'interprétation d'un contrat constitue généralement une question mixte de fait et de droit susceptible de contrôle selon la norme de l'erreur manifeste et déterminante : *Sattva*, par. 50; *Heritage Capital Corp. c. Équitable, Cie de fiducie*, 2016 CSC 19, [2016] 1 R.C.S. 306, par. 21-24. Il existe une exception qui permet d'appliquer la norme de la décision correcte lorsqu'il est question d'un « contrat type, que l'interprétation en litige a valeur de précédent et que l'exercice d'interprétation ne repose sur aucun fondement factuel significatif qui est propre aux parties concernées » : *Ledcor Construction Ltd. c. Société d'assurance d'indemnisation Northbridge*, 2016 CSC 37, [2016] 2 R.C.S. 23, par. 24. Bien que l'on nous ait dit que le contrat de sous-traitance est un contrat type, rien ne donne à penser qu'il soit largement utilisé dans l'industrie de la construction ou que l'interprétation de la clause VII Q ait valeur de précédent. Il n'est donc pas évident que

on the matter, however, because assuming, without deciding, that the interpretation of the Subcontract could be reviewed on the correctness standard, I am not persuaded by the interpretation of clause VII Q urged upon this Court by Deloitte.

(1) Clause VII Q Does Not Permit Double Recovery

[127] The overriding concern when interpreting a contract is to determine the objective intent of the parties and the scope of their understanding. The court must "read the contract as a whole, giving the words used their ordinary and grammatical meaning, consistent with the surrounding circumstances known to the parties at the time of formation of the contract": *Sattva*, at para. 47.

[128] Clause Q(b) provides that Chandos may recover from Capital Steel "any cost . . . arising from the suspension of this Subcontract Agreement or the completion of the Work by the Contractor, plus a reasonable allowance for overhead and profit". On its face, this appears to be a very broad basis for recovery. However, clause Q(d), the clause at issue, adds some ambiguity, because it provides that Capital Steel "shall forfeit 10% of the within Subcontract Agreement price to the Contractor as a fee for the inconvenience of completing the work using alternate means and/or for monitoring the work during the warranty period." It might be assumed that the specific matters mentioned in clause Q(d) would also fall under the general term in clause Q(b). Does Condition Q, then, permit Chandos to, in effect, double recover against Capital Steel? I answer this question in the negative, for three reasons.

[129] First, it is apparent from the ordinary and grammatical meaning of the words that clause Q(b) applies to different matters than clause Q(d). The focus of clause Q(b) is on the cost to Chandos of

l'interprétation du contrat de sous-traitance relève de l'exception *Ledcor*. Je ne tire cependant aucune conclusion ferme sur la question, car, même si je tiens pour acquis, sans en décider, que l'interprétation du contrat de sous-traitance peut être assujettie à la norme de la décision correcte, je ne suis pas convaincue par l'interprétation de la clause VII Q proposée par Deloitte.

(1) La clause VII Q ne permet pas un double recouvrement

[127] La question prédominante en ce qui concerne l'interprétation d'un contrat est de discerner l'intention objective des parties et la portée de leur entente. Le tribunal doit « interpréter le contrat dans son ensemble, en donnant aux mots y figurant le sens ordinaire et grammatical qui s'harmonise avec les circonstances dont les parties avaient connaissance au moment de la conclusion du contrat » : *Sattva*, par. 47.

[128] La clause Q(b) prévoit que Chandos peut recouvrer auprès de Capital Steel [TRADUCTION] « tous les coûts [. . .] découlant de la suspension du présent contrat de sous-traitance ou de l'achèvement des travaux par l'entrepreneur, plus une indemnisation raisonnable pour les frais généraux et le profit ». À première vue, cela semble établir un cadre très général pour le recouvrement. La clause Q(d) ajoute cependant une certaine ambiguïté parce qu'elle prévoit que Capital Steel « renonce à 10 % du prix du présent contrat de sous-traitance en faveur de l'entrepreneur à titre de frais pour les dérangements liés à l'achèvement des travaux par d'autres moyens et/ou pour la surveillance des travaux durant la période de garantie. » On pourrait présumer que les éléments précis mentionnés à la clause Q(d) relèvent également de la condition générale énoncée à la clause Q(b). La condition Q, alors, permet-elle à Chandos le double recouvrement des sommes auprès de Capital Steel? Je réponds par la négative, et ce, pour trois raisons.

[129] Premièrement, il est évident d'après le sens ordinaire et grammatical des mots utilisés à la clause Q(b) que les sujets visés sont différents de ceux visés à la clause Q(d). La clause Q(b) est

completing Capital Steel's unfinished structural steel work. By contrast, clause Q(d) applies after the work is completed as a fee for, among other things, Chandos having to monitor Capital Steel's work during the warranty period. As well, clause Q(b) applies to the cost to Chandos arising from the suspension of the Subcontract, whereas clause Q(d) covers the inconvenience to Chandos specifically of completing the work using alternate means, which would require the reallocation by Chandos of significant administrative and managerial resources as well as the reallocation of the risks assumed under the Subcontract (e.g. Condition G, "Indemnity"). Thus, the matters covered by clause Q(d) may be difficult to quantify in monetary terms, and so the parties agreed beforehand on a figure for them, while leaving clause Q(b) to cover the more direct and quantifiable costs.

axée sur ce qu'il en coûte à Chandos pour terminer la structure en acier commencée par Capital Steel. En revanche, la clause Q(d) s'applique une fois les travaux achevés, et concerne notamment les frais découlant de l'obligation qu'a Chandos de surveiller les travaux de Capital Steel durant la période de garantie. De plus, la clause Q(b) s'applique aux coûts engagés par Chandos à la suite de la suspension du contrat de sous-traitance, tandis que la clause Q(d) vise les dérangements subis par elle lorsque les travaux sont achevés par d'autres moyens, ce qui l'oblige à réaffecter des ressources administratives et de gestion considérables en plus de réattribuer les risques qui étaient assumés dans le cadre du contrat de sous-traitance (p. ex., la condition G, [TRADUCTION] « Indemnisation »). Par conséquent, les sujets visés par la clause Q(d) se quantifient difficilement en termes pécuniaires et les parties se sont donc entendues au préalable sur une évaluation des dommages-intérêts, en laissant la clause Q(b) prévoir les coûts plus directs et quantifiables.

[130] Second, if the grammatical and ordinary meaning does not resolve the matter, then there is an apparent conflict between clause Q(b) and clause Q(d). "[W]here there is apparent conflict between a general term and a specific term, the terms may be reconciled by taking the parties to have intended the scope of the general term to not extend to the subject-matter of the specific term": *BG Checo International Ltd. v. British Columbia Hydro and Power Authority*, [1993] 1 S.C.R. 12, at p. 24; *Douez v. Facebook, Inc.*, 2017 SCC 33, [2017] 1 S.C.R. 751, at para. 46. Thus, the general grounds for recovery listed in clause Q(b) should not be read as extending to the specific matters in clause Q(d), that is, "the inconvenience of completing the work using alternate means" and "monitoring the work during the warranty period".

[130] Deuxièmement, si le sens ordinaire et grammatical ne règle pas la question, il y a un conflit apparent entre la clause Q(b) et la clause Q(d). « [L]orsqu'il y a apparence de conflit entre une condition générale et une condition explicite, elles peuvent être conciliées si l'on considère que les parties ont voulu que la condition générale ne s'applique pas à l'objet de la condition spécifique » : *BG Checo International Ltd. c. British Columbia Hydro and Power Authority*, [1993] 1 R.C.S. 12, p. 24; *Douez c. Facebook, Inc.*, 2017 CSC 33, [2017] 1 R.C.S. 751, par. 46. Ainsi, les motifs généraux du recouvrement prévu à la clause Q(b) ne doivent pas être interprétés comme s'appliquant aux questions spécifiques que sont les [TRADUCTION] « dérangements liés à l'achèvement des travaux par d'autres moyens » et la « surveillance des travaux durant la période de garantie » prévues à la clause Q(d).

[131] Third, a court may deviate from the plain meaning of the words if a literal interpretation of the contractual language would lead to a commercially unrealistic or absurd result: *Consolidated-Bathurst Export Ltd. v. Mutual Boiler and Machinery Insurance Co.*, [1980] 1 S.C.R. 888, at p. 901. In my view, permitting double recovery under clause Q(b)

[131] Troisièmement, un tribunal peut s'écarter du sens ordinaire des mots si une interprétation littérale entraînait un résultat irréaliste ou absurde sur le plan commercial : *Exportations Consolidated Bathurst Ltée c. Mutual Boiler and Machinery Insurance Co.*, [1980] 1 R.C.S. 888, p. 901. À mon avis, permettre un double recouvrement par l'application de

would be commercially impractical and unrealistic. Therefore, clause Q(b) should be read so as to avoid such an absurdity.

[132] For these reasons, I disagree with the interpretation of Condition Q advanced by Deloitte. The 10 percent fee arising under clause Q(d) is not duplicative of the amounts which may accrue under clause Q(b). Nielsen J.'s finding that clause Q(d) furthers a *bona fide* commercial purpose is, as a result, left unimpeached. Nonetheless, it is worth briefly exploring the objective commercial basis for the provision to show why it is important that the law give effect to such a clause.

(2) Paragraph (d) of Condition Q Advances a Legitimate and Objectively Ascertainable Commercial Interest

[133] In my view, it is significant that the Subcontract included ongoing obligations on the part of Capital Steel that were unperformed at the time of its bankruptcy. The bankruptcy of a party with an unperformed or ongoing obligation under a contract is likely to necessitate a commercial rearrangement of rights in order to protect the legitimate interests of the counterparty because the party's bankruptcy is likely to undermine the counterparty's assurance of ongoing performance or to change the risk allocation under the contract: Grottenthaler and Pillon; see also *Lomas* (2010), at paras. 108-10; *Lomas* (2012), at paras. 88-91. There are therefore ample legitimate commercial reasons for rearranging contractual rights in such circumstances.

[134] An important element of the Subcontract is that it created a general contractor-subcontractor relationship between two parties in the construction industry. The construction industry generally operates in a pyramid-like structure, with the owner or developer at the top of the pyramid, a general contractor or contractors one level down, subcontractors under them, and possibly further sub-subcontractors: J. Westeinde, "Construction is 'Risky Business'" (1988), 29 *C.L.R.* 119. Generally, payment flows down the pyramid once the work has been completed.

la clause Q(b) serait irréaliste et impraticable sur le plan commercial. Par conséquent, la clause Q(b) doit être interprétée de manière à éviter une telle absurdité.

[132] Pour ces motifs, je ne partage pas l'interprétation que Deloitte propose pour la condition Q. Les frais de 10 p. 100 prévus à la clause Q(d) ne constituent pas un dédoublement des montants qui peuvent découler de l'application de la clause Q(b). La conclusion du juge Nielsen selon laquelle la clause Q(d) vise un objectif commercial véritable n'est donc pas contestée. Néanmoins, il vaut la peine d'explorer brièvement le fondement commercial objectif de la stipulation afin de démontrer pourquoi il est important que la loi donne effet à une telle clause.

(2) Le paragraphe (d) de la condition Q favorise un intérêt commercial légitime et objectivement vérifiable

[133] À mon avis, le fait que le contrat de sous-traitance prévoyait des obligations continues incombant à Capital Steel qui n'avaient pas été exécutées au moment de sa faillite est important. La faillite d'une partie ayant une obligation non exécutée ou continue au titre d'un contrat est susceptible d'entraîner par la force des choses une réorganisation commerciale des droits afin de protéger les intérêts légitimes de l'autre partie, car la faillite est susceptible de nuire à la garantie dont bénéficie cette dernière quant à la poursuite des travaux, ou encore de modifier la répartition des risques prévue au contrat : Grottenthaler et Pillon; voir aussi *Lomas* (2010), par. 108-110; *Lomas* (2012), par. 88-91. Il y a donc amplement de motifs commerciaux légitimes pour réorganiser les droits contractuels dans de telles circonstances.

[134] Le contrat de sous-traitance a ceci d'important qu'il a créé une relation générale entrepreneur-sous-traitant entre deux parties qui travaillent dans l'industrie de la construction. Cette industrie fonctionne habituellement selon une structure pyramidale où le propriétaire ou promoteur se trouve en haut de la pyramide, l'entrepreneur général ou les entrepreneurs à l'échelon d'en dessous, les sous-traitants encore plus bas et ainsi de suite si les sous-traitants ont eux-mêmes des sous-traitants : J. Westeinde, « Construction is "Risky Business" » (1988), 29

Thus, the insolvency of a subcontractor during the construction of a project can have major ramifications up and down the pyramid structure, causing costly delays and fundamentally altering the allocation of risk created by the web of contractual relationships involved.

[135] Capital Steel had significant unperformed obligations under the Subcontract at the time of its bankruptcy. It had agreed to "repair and make good any defect in its work and all resulting damages that might appear as the result of any improper work or defective materials" it furnished: clause III. The operative period for this guarantee corresponded to the period specified in the Stipulated Price Contract, which was one year from the date of substantial performance: clause GC 12.3.1. However, Capital Steel's bankruptcy occurred before it had even completed its own work under the Subcontract, let alone before the date of substantial performance of the entirety of the project. Therefore, the Subcontract was still executory at the time of its bankruptcy.

[136] In this case, Capital Steel's bankruptcy exposed Chandos to significant risks under the Stipulated Price Contract. In it, Chandos had agreed to be "as fully responsible to the *Owner* for acts and omissions" of Capital Steel, or a replacement subcontractor, as it was for "acts and omissions of persons directly employed by" it: clause GC 3.7.1.3 (emphasis in original). Chandos had also agreed that it would promptly correct defects or deficiencies in the work which appeared during the warranty period at its own expense: clause GC 12.3.4. As well, Chandos was required to correct or pay for damage resulting from such corrections: clause GC 12.3.5. Owing to its bankruptcy, Capital Steel was not available to monitor or correct its work during the warranty period. Chandos therefore had to do so or face liability to the owner under the Stipulated Price Contract. Thus, a fee for monitoring the work during the warranty period is legitimate.

C.L.R. 119. Habituellement, les paiements se font du haut vers le bas de la pyramide une fois que les travaux ont été exécutés. Ainsi, l'insolvabilité d'un sous-traitant durant la construction du projet peut avoir des répercussions importantes dans l'ensemble de la structure, entraîner des retards coûteux et modifier fondamentalement la répartition des risques créés par le réseau de relations contractuelles nécessaires à la réalisation du projet.

[135] Capital Steel avait des obligations importantes en vertu du contrat de sous-traitance qui n'étaient pas encore exécutées au moment de sa faillite. Elle avait accepté de [TRADUCTION] « réparer tout défaut dans ses travaux et tout dommage découlant d'un travail mal fait ou d'un équipement défectueux » qu'elle fournissait : clause III. La durée de cette garantie correspondait à la période mentionnée dans le contrat à forfait, soit un an à compter de la date de l'achèvement substantiel : clause GC 12.3.1. Cependant, Capital Steel a fait faillite avant même d'avoir terminé les travaux qu'elle devait exécuter selon le contrat de sous-traitance, et donc bien avant la date de l'achèvement substantiel de l'ensemble du projet. Le contrat de sous-traitance était donc toujours exécutoire au moment de la faillite de Capital Steel.

[136] En l'espèce, la faillite de Capital Steel exposait Chandos à des risques importants dans le cadre du contrat à forfait. Dans ce dernier, Chandos avait accepté d'être [TRADUCTION] « aussi pleinement responsable à l'égard du *Propriétaire* pour les actes et omissions » de Capital Steel, ou d'un sous-traitant qui remplacerait cette dernière, qu'elle l'était pour les « actes et omissions des personnes qu'elle employait directement » : clause GC 3.7.1.3 (en italique dans l'original). Chandos avait également accepté de corriger rapidement, et à ses frais, les défauts apparaissant dans les travaux durant la période de garantie : clause GC 12.3.4. En outre, elle devait corriger ou payer les dommages découlant de ces corrections : clause GC 12.3.5. En raison de sa faillite, Capital Steel n'a pu surveiller ou corriger ses travaux durant la période de garantie. Chandos a donc dû le faire ou assumer la responsabilité à l'égard du propriétaire conformément au contrat à forfait. Par conséquent, l'imposition de frais pour la surveillance des travaux durant la période de garantie est légitime.

[137] A general contractor's role is essentially to oversee and coordinate the construction of a project by various subcontractors according to a set schedule. It is evident that a subcontractor's bankruptcy during the construction of the project would require the general contractor to redirect significant administrative and management resources in order to respond, for example by seeking a substitute subcontractor willing to complete a job already partially performed by another company. The general contractor would also incur administrative and management costs from mitigating the fallout up and down the pyramid. Undoubtedly, costly delays would ensue as well. Thus, a fee for the inconvenience of completing the work using alternate means is also legitimate.

[138] As to the quantum of the fee, 10 percent of the Subcontract price, Nielsen J. found as a fact that this was a genuine pre-estimate of damages, and I am content to rely on this finding: A.R., at pp. 9-10. In my view, this amount is not extravagant in light of the importance of the structural steel work to the project, the Stipulated Price Contract's total value of $56,852,453.45, and the fact that the risks reallocated to Chandos by Capital Steel's bankruptcy were likely difficult to state in monetary terms. I do not see in clause Q(d) any intent on the part of Chandos or Capital Steel to avoid the operation of bankruptcy laws or to prejudice Capital Steel's creditors. There is, therefore, a *bona fide* commercial purpose behind clause Q(d).

V. Conclusion

[139] As clause Q(d) furthers a *bona fide* commercial purpose, I would dispose of this appeal by holding that provisions of this kind do not offend the anti-deprivation rule. I therefore conclude that clause Q(d) is enforceable against the trustee of Capital Steel's estate in bankruptcy. As a result, I would allow the appeal and restore the original order made at first instance.

[137] Le rôle d'un entrepreneur général consiste essentiellement à superviser et à coordonner la construction d'un projet par différents sous-traitants conformément au calendrier fixé. Il est évident que la faillite d'un sous-traitant durant la construction du projet oblige l'entrepreneur général à réaffecter beaucoup de ressources administratives et de gestion pour réagir à la situation, par exemple en cherchant un autre sous-traitant qui est prêt à terminer les travaux déjà partiellement exécutés par une autre entreprise. L'entrepreneur général a également à assumer des coûts administratifs et de gestion pour atténuer les répercussions dans toute la pyramide. Sans aucun doute, cela entraîne des retards coûteux. Par conséquent, il est aussi légitime de prévoir des frais pour les dérangements liés à l'achèvement des travaux par d'autres moyens.

[138] Quant au montant de ces frais, qui représente 10 p. 100 du prix du contrat de sous-traitance, le juge Nielsen a tiré la conclusion de fait qu'il s'agissait d'une véritable estimation anticipée des dommages-intérêts et je me contenterai de souscrire à sa conclusion : d.a., p. 9-10. À mon avis, il ne s'agit pas d'un montant extravagant compte tenu de l'importance de la charpente d'acier requise pour le projet, de la valeur totale du contrat à forfait qui s'élève à 56 852 453,45 $ et du fait que les risques réattribués à Chandos en raison de la faillite de Capital Steel étaient susceptibles d'être difficiles à définir en termes pécuniaires. Je ne vois dans la clause Q(d) aucune intention de la part de Chandos ou de Capital Steel d'éviter l'application des lois en matière de faillite ou de nuire aux créanciers de Capital Steel. La clause Q(d) poursuit donc un objectif commercial véritable.

V. Conclusion

[139] Comme la clause Q(d) poursuit un objectif commercial véritable, je disposerais du pourvoi en concluant que de telles stipulations n'enfreignent pas la règle anti-privation. Je conclus donc que la clause Q(d) est exécutoire contre le syndic de faillite de Capital Steel. En conséquence, j'accueillerais le pourvoi et je rétablirais l'ordonnance originale rendue en première instance.

Appeal dismissed with costs throughout, CÔTÉ J. *dissenting.*

Solicitors for the appellant: Duncan Craig, Edmonton.

Solicitors for the respondent: Reynolds Mirth Richards & Farmer, Edmonton.

Solicitor for the intervener the Attorney General of Canada: Attorney General of Canada, Ottawa.

Solicitors for the intervener the Canadian Association of Insolvency and Restructuring Professionals: Stikeman Elliott, Toronto.

Solicitors for the intervener the Insolvency Institute of Canada: McCarthy Tétrault, Toronto.

Pourvoi rejeté avec dépens devant toutes les cours, la juge CÔTÉ *est dissidente.*

Procureurs de l'appelante : Duncan Craig, Edmonton.

Procureurs de l'intimée : Reynolds Mirth Richards & Farmer, Edmonton.

Procureur de l'intervenant le procureur général du Canada : Procureur général du Canada, Ottawa.

Procureurs de l'intervenante l'Association canadienne des professionnels de l'insolvabilité et de la réorganisation : Stikeman Elliott, Toronto.

Procureurs de l'intervenant l'Institut d'insolvabilité du Canada : McCarthy Tétrault, Toronto.

TAB 4

Lorna P. Elsley, Executrix of the Estate of Donald Champion Elsley (*Defendant*) *Appellant*;

and

J. G. Collins Insurance Agencies Limited (*Plaintiff*) *Respondent*.

1977: October 31; 1978: March 7.

Present: Laskin C.J. and Martland, Ritchie, Pigeon, Dickson, Beetz and Pratte JJ.

ON APPEAL FROM THE COURT OF APPEAL FOR ONTARIO

Contract — Restrictive covenant — Restraint of trade — Vendor of business subsequently purchaser's employee — Covenant against competition — Term of five years — Fixed sum — Stipulated as liquidated damages — Alternative remedies.

On April 24, 1956, the respondent agreed to purchase the general insurance business of a competitor, D. C. Elsley Limited, owned by Elsley. The agreement contained a covenant on the part of the vendor that it would not for ten years carry on or be engaged in the business of a general insurance agency in the area in question, with liquidated damages stipulated at $1,000 "for each and every breach". By a second agreement Elsley was employed as manager of the respondent's operation subject to a covenant that Elsley not become engaged in the business of a general insurance agent while in the respondent's employ or during a five year period after cessation of his employment. Liquidated damages for the breach of this covenant were simply set at $1,000. After 17 years Elsley resigned and recommenced his own general insurance business. At trial Elsley was ordered restrained from carrying on the business of general insurance agent within the defined area and a reference was directed to assess damages with respect to the business taken, such damages being restricted to the loss of commissions on contracts of insurance with specified former clients for the period from resignation to the date of trial. The Court of Appeal affirmed the trial judgment with one variation, namely that Collins be compensated on the basis of *all* contracts of general insurance sold in the relevant period after taking into account expenses incurred in securing and servicing the contracts. Jessup J.A. dissented on the basis that the covenant was unreasonably wide in not being restricted to solicitation of the employer's particular clients and hence was unenforceable.

Lorna P. Elsley, exécutrice de la succession de Donald Champion Elsley (*Défenderesse*) *Appelante*;

et

J. G. Collins Insurance Agencies Limited (*Demanderesse*) *Intimée*.

1977: 31 octobre; 1978: 7 mars.

Présents: Le juge en chef Laskin et les juges Martland, Ritchie, Pigeon, Dickson, Beetz et Pratte.

EN APPEL DE LA COUR D'APPEL DE L'ONTARIO

Contrat — Clause restrictive — Restriction à la liberté du commerce — Vendeur de l'entreprise employé subséquemment par l'acheteur — Clause restreignant la concurrence — Période de cinq ans — Somme déterminée — Montant stipulé à titre de dommages-intérêts liquidés — Il faut faire un choix quant au recours.

Le 24 avril 1956, l'intimée a acheté l'entreprise d'assurance générale d'une société concurrente, D. C. Elsley Limited, propriété de Elsley. Aux termes du contrat, le vendeur s'engageait à ne pas exploiter d'entreprise d'assurance générale dans la région en cause et à payer $1,000 «pour chaque violation» à titre de dommages-intérêts liquidés. Par une seconde convention, Elsley a été engagé à titre de gérant des entreprises de l'intimée sous réserve de ne pas exploiter une entreprise d'agent d'assurance générale tant qu'il serait à l'emploi de l'intimée ou pendant les cinq ans qui suivront la cessation de son emploi. Les dommages-intérêts liquidés en cas de violation de cette clause étaient simplement fixés à $1,000. Après dix-sept ans, Elsley a démissionné et formé sa propre entreprise d'assurance générale. En première instance, on a ordonné à Elsley de s'abstenir d'exploiter l'entreprise d'agent d'assurance générale dans la zone définie; on a également ordonné un renvoi pour l'évaluation des dommages-intérêts dus en raison des affaires enlevées, à condition que ces dommages-intérêts fussent limités à la perte de commissions entre la démission et la date du procès relativement aux contrats d'assurance d'anciens clients énumérés. La Cour d'appel a confirmé le jugement de première instance, avec une modification, soit que Collins soit indemnisé pour la perte de commissions sur *tous* les contrats d'assurance générale conclus par Elsley au cours de la période pertinente, compte tenu des frais afférents à l'obtention des contrats et aux démarches subséquentes. Le juge Jessup était dissident au motif que la clause était trop large, puisqu'elle n'interdisait pas uniquement la sollicitation des propres clients de l'employeur, et ne pouvait donc pas être imposée.

Held: The appeal should be dismissed.

The principles to be applied in considering restrictive covenants of employment are well established. The test of reasonableness as between the parties and with reference to the public interest, can be applied, however, only in the particular circumstances of the particular case. The distinction made between restrictive covenants in agreements for sale of a business and those in contracts of employment is well-conceived and responsive to practical considerations. In this case the covenant in the sale agreement was exhausted. The restrictive covenant in the employment contract cannot be regarded as fed by the sale agreement and to be enforceable has to stand up to the more rigorous tests applied in the employer/employee context. In an exceptional case such as this, the nature of the employment may justify a covenant prohibiting an employee not only from soliciting customers, but also from establishing his own business or working for others so as to be likely to appropriate the employer's trade connection through his acquaintance with the employer's customers.

With respect to damages, where a fixed sum is stipulated as and for liquidated damages upon a breach of the agreement, the covenantee must elect with respect to that breach between these liquidated damages and an injunction. If he elects to take an injunction and not the liquidated sum stipulated, he may recover damages in equity for the actual loss sustained up to the date of the injunction or, if tardy, up to the date upon which he should have sought the injunction, but in either case not exceeding the amount stipulated as payable upon a breach. Where the stipulated sum is less than the actual loss, the agreed sum represents the maximum amount recoverable whether the sum is a penalty or a valid liquidated damages clause. As a result, the respondent was entitled to an injunction and such damages as he could prove up to the date of the trial, to a maximum of $1,000.

Herbert Morris Limited v. Saxelby, [1916] 1 A.C. 688; *Stenhouse Australia Ltd. v. Phillips*, [1974] 1 All E.R. 117; *Robert W. Maguire v. Northland Drug Company Limited*, [1935] S.C.R. 412; *Nordenfelt v. Maxim Nordenfelt Guns and Ammunition Co. Ltd.* [1894] A.C. 535; *Mason v. Provident Clothing and Supply Co.*, [1913] A.C. 724; *Attwood v. Lamont*, [1920] 3 K.B. 571; *Scorer v. Seymour-John*, [1966] 3 All E.R. 347; *Gledhow Autoparts Ltd. v. Delaney*, [1965] 1 W.L.R. 1366; *Silverman v. Silverman* (1969), 113 Sol. J. 563;

Arrêt: Le pourvoi doit être rejeté.

Les principes applicables lorsqu'on examine les clauses restrictives en matière d'emploi sont bien établis. Le critère du caractère raisonnable vis-à-vis des parties et dans le sens de l'intérêt public ne peut toutefois s'appliquer que dans les circonstances spéciales d'un cas particulier. La distinction faite en jurisprudence entre une clause restrictive contenue dans un contrat de vente d'une entreprise et celle contenue dans un contrat de louage de services est bien conçue et répond à des considérations pratiques. En l'espèce, la clause du contrat de vente avait cessé d'avoir des effets. La clause restrictive du contrat de louage de services ne pouvait être alimentée par le contrat de vente et pour être exécutée, elle devait répondre aux critères plus rigoureux appliqués dans le contexte des relations employeur-employé. Dans des cas exceptionnels comme celui-ci, la nature de l'emploi peut justifier une clause interdisant à un employé, non seulement de solliciter des clients, mais également d'établir son propre commerce ou de travailler pour le compte de tiers de façon à s'approprier éventuellement la clientèle de l'employeur du fait qu'il la connaît.

Relativement aux dommages-intérêts, lorsqu'une somme déterminée est stipulée à titre de dommages-intérêts liquidés en cas de violation, le bénéficiaire doit choisir, à l'occasion de chaque violation, entre ces dommages-intérêts liquidés et une injonction. S'il opte pour l'injonction et non pour le montant liquidé stipulé, il peut obtenir des dommages-intérêts en *equity* pour la perte effectivement subie jusqu'à la date de l'injonction ou, s'il est en retard, jusqu'à la date à laquelle il aurait dû demander l'injonction, mais, dans les deux cas, ces dommages-intérêts ne doivent pas excéder le montant stipulé en cas de violation. Lorsque la somme stipulée est inférieure au préjudice réel, la somme fixée représente le montant maximum qui peut être recouvré, que le montant corresponde à une pénalité ou à une clause valide de dommages-intérêts liquidés. En conséquence, l'intimée a droit à une injonction et aux dommages-intérêts qu'elle peut justifier jusqu'à la date du procès, sans toutefois dépasser $1,000.

Jurisprudence: *Herbert Morris Limited v. Saxelby*, [1916] 1 A.C. 688; *Stenhouse Australia Ltd. v. Phillips*, [1974] 1 All E.R. 117; *Robert W. Maguire c. Northland Drug Company Limited*, [1935] R.C.S. 412; *Nordenfelt v. Maxim Nordenfelt Guns and Ammunition Co. Ltd.*, [1894] A.C. 535; *Mason v. Provident Clothing and Supply Co.*, [1913] A.C. 724; *Attwood v. Lamont*, [1920] 3 K.B. 571; *Scorer v. Seymour-John*, [1966] 3 All E.R. 347; *Gledhow Autoparts Ltd. v. Delaney*, [1965] 1 W.L.R. 1366; *Silverman v. Silverman* (1969),

Fitch v. Dewes, [1921] 2 A.C. 158; *Marion White v. Francis*, [1972] 1 W.L.R. 1423; *P.C.O. Services Ltd. v. Rumleski*, [1963] 2 O.R. 62; *Campbell, Imrie and Shankland v. Park*, [1954] 2 D.L.R. 170; *Putsman v. Taylor*, [1927] 1 K.B. 637; *Jones v. Heavens* (1877), 4 Ch.D. 636; *National Provincial Bank of England v. Marshall* (1888), 40 Ch.D. 112; *Snider v. McKelvey* (1900), 27 O.L.R. 339; *General Accident Assurance Corporation v. Noel*, [1902] 1 K.B. 377; *H. F. Clarke Limited v. Thermidaire Corporation Limited*, [1976] 1 S.C.R. 319; *Cellulose Acetate Silk Company Limited. v. Widnes Foundry (1925) Limited*, [1933] A.C. 20; *Wilbeam v. Ashton* (1807), 1 Camp. 78; *Imperial Tobacco v. Parslay*, [1936] 2 All E.R. 515 referred to.

APPEAL from a judgment of the Court of Appeal for Ontario[1] dismissing an appeal and allowing a cross-appeal from a judgment of Stark J.[2] in favour of the plaintiff in an action to enforce a restrictive covenant. Appeal dismissed, judgment below varied to provide for payment of such damages not to exceed $1,000 as can be established for the period to the date of trial.

G. J. Smith, Q.C., for the appellant.

R. A. O'Donnell and *R. F. L. Rose*, for the respondent.

The judgment of the Court was delivered by

DICKSON J.—The question for decision in this case is whether a restrictive covenant contained in a certain contract of employment, to which I will shortly refer, is valid.

The facts are, to all intents, undisputed. On April 24, 1956, an agreement was entered into for the purchase by the Collins Company of the general insurance business of a competitor, D. C. Elsley Limited. The price was $46,137. The life insurance business and the real estate business conducted by the Elsley Company were not included. The agreement contained a covenant on the part of the vendor that it would not, for a period of ten years, carry on or be engaged in the business of a general insurance agency within the City of Niagara Falls,

[1] (1976), 13 O.R. (2d) 177.
[2] (1974), 18 C.P.R. (2d) 1187.

113 Sol. J. 563; *Fitch v. Dewes*, [1921] 2 A.C. 158; *Marion White v. Francis*, [1972] 1 W.L.R. 1423; *P.C.O. Services Ltd. v. Rumleski*, [1963] 2 O.R. 62; *Campbell, Imrie and Shankland v. Park*, [1954] 2 D.L.R. 170; *Putsman v. Taylor*, [1927] 1 K.B. 637; *Jones v. Heavens* (1877), 4 Ch.D. 636; *National Provincial Bank of England v. Marshall* (1888), 40 Ch.D. 112; *Snider v. McKelvey* (1900), 27 O.L.R. 339; *General Accident Assurance Corporation v. Noel*, [1902] 1 K.B. 377; *H. F. Clarke Limited v. Thermidaire Corporation Limited*, [1976] 1 R.C.S. 319; *Cellulose Acetate Silk Company Limited v. Widnes Foundry (1925) Limited*, [1933] A.C. 20; *Wilbeam v. Ashton* (1807), 1 Camp. 78; *Imperial Tobacco v. Parslay*, [1936] 2 All E.R. 515.

POURVOI à l'encontre d'un arrêt de la Cour d'appel de l'Ontario[1] qui a rejeté l'appel et accueilli le contre-appel d'une décision du juge Stark[2] en faveur du demandeur relativement à une action visant à faire valoir une clause restrictive. Pourvoi rejeté. Le jugement d'instance inférieure est modifié de façon à prévoir le versement de dommages-intérêts, d'au plus $1,000, qui pourront être établis pour la période allant jusqu'à la date du procès.

G. J. Smith, c.r., pour l'appelante.

R. A. O'Donnell et *R. F. L. Rose*, pour l'intimée.

Le jugement de la Cour a été rendu par

LE JUGE DICKSON—La question à trancher en l'espèce est de savoir si une clause restrictive contenue dans un contrat de louage de services, auquel je me référerai brièvement, est valide.

A toutes fins pratiques, les faits ne sont pas contestés. Par contrat en date du 24 avril 1956, la compagnie Collins a acheté l'entreprise d'assurance générale d'une société concurrente, D. C. Elsley Limited, au prix de $46,137. L'assurance-vie et les activités immobilières exploitées par la compagnie Elsley n'étaient pas comprises dans la vente. Aux termes du contrat, le vendeur s'engageait à ne pas exploiter d'entreprise d'assurance générale à Niagara Falls, dans le canton de Stamford et dans le village de Chippawa, tous sis dans

[1] (1976), 13 O.R. (2d) 177.
[2] (1974), 18 C.P.R. (2d) 1187.

the Township of Stamford and the Village of Chippawa, all in the County of Welland, and that the vendor would pay the purchaser $1,000 for each and every breach. The parties entered into a further agreement on May 1, 1956, whereby Elsley was employed as interim manager of the combined general insurance businesses, now owned by Collins, upon terms which included a restrictive covenant almost identical with that contained in the purchase agreement of April 24, 1956.

The interim management agreement was short-lived. It was replaced by an agreement of May 30, 1956 by which Elsley undertook to serve as manager of the Collins Company's general insurance business in the greater Niagara Falls area, devoting all necessary time and attention to such employment, subject to the proviso that he might supervise the Elsley Company in its real estate and life insurance business. The agreement commenced June 1, 1956 and was stated to continue in force from year to year until terminated by either party upon three months' notice. As things developed, it continued until May, 1973.

Clause 3 of the management agreement contains the covenant which gave rise to the present proceedings. It reads:

3. Subject to the restrictive covenants contained in the Agreement made between the Parties dated May 1, 1956, in consideration of the employment, the Manager shall not, while in the employ of the Company or of its successors and assigns, whether in the capacity in which he is now or in any other capacity, or during the period of five years next after he shall, whether by reason of dismissal, retirement or otherwise, have ceased to be so employed, directly or indirectly, and whether as principal, agent, director of a company, traveller, servant or otherwise, carry on or be engaged or concerned or take part in the business of a general insurance agent within the corporate limits of the City of Niagara Falls, the Township of Stamford and the Village of Chippawa, all in the County of Welland; and in the event of his failing to observe or perform the said agreement, he shall pay to the said Company, its successors or assigns, or other the person or persons entitled for the time being to the benefit of the said agreement, the sum of One Thousand Dollars ($1,000.00) as and for liquidated damages, and

le comté de Welland, et le vendeur devait payer à l'acheteur $1,000 pour chaque violation. Par nouvelle convention des parties datée du 1er mai 1956, Elsley a été engagé à titre de gérant provisoire des entreprises combinées d'assurance générale dont Collins était maintenant propriétaire. Les conditions contenaient une clause restrictive presque identique à celle du contrat de vente du 24 avril 1956.

Le contrat de gérance provisoire a été de courte durée. Il a été remplacé par un contrat daté du 30 mai 1956 selon lequel Elsley s'engageait à travailler comme gérant des entreprises d'assurance générale de la compagnie Collins dans l'agglomération de Niagara Falls, à consacrer à cet emploi tout le temps et l'attention nécessaires, sous réserve qu'il puisse superviser les entreprises immobilières et d'assurance-vie de la compagnie Elsley. Le contrat est entré en vigueur le 1er juin 1956 et devait se poursuivre d'année en année jusqu'à ce que l'une des parties le résilie en donnant un préavis de trois mois. En fait, il est demeuré en vigueur jusqu'en mai 1973.

La clause 3 du contrat de gérance contient l'engagement qui a donné lieu à la présente procédure. Elle stipule:

[TRADUCTION] 3. Sous réserve des clauses restrictives contenues au contrat de louage de services intervenu entre parties le 1er mai 1956, le gérant ne doit pas, tant qu'il est à l'emploi de la compagnie ou de ses successeurs et ayants droit, soit en sa qualité actuelle soit en toute autre qualité, ou pendant les cinq ans qui suivront la cessation de son emploi, pour cause de renvoi, de retraite ou autre, directement ou indirectement, à titre de patron, mandataire, administrateur d'une compagnie, voyageur, préposé ou autre, exploiter une entreprise d'agent d'assurance générale, s'engager dans pareille entreprise, s'en occuper ou y participer, dans la municipalité de Niagara Falls, dans le canton de Stamford et le village de Chippawa, tous dans le comté de Welland; et dans le cas où il manquerait d'observer ou d'exécuter ladite convention, il devra payer à la compagnie, ses successeurs ou ayants droit, ou à toute autre personne qui en sera à ce moment titulaire, la somme de mille dollars ($1,000) à titre de dommages-intérêts liquidés et Mme Elsley, épouse du gérant, en signant les présentes,

the said Mrs. Elsley, wife of the Manager, by her signature hereto, agrees to observe and be bound by the aforesaid covenant.

The clause differs substantially from the restrictive covenant contained in each of the two earlier agreements. It is for a five-year period after cessation of the employment. It is made subject to the covenant contained in the sale agreement of May 1, 1956, for the purpose, no doubt, of assuring a minimum restrictive period of ten years and a maximum restrictive period of the term of employment plus five years. The sum of $1,000 was to become payable for failure on the part of Elsley to observe or perform the agreement; each of the earlier agreements made provision for payment of $1,000 "for each and every breach."

At trial, Collins asked for rectification of the agreement by adding the words "for each and every breach." The evidence disclosed, however, that although both parties had agreed that there should be a restrictive clause the drafting and detail had been left to the solicitor of the parties. The solicitor had died prior to date of trial and neither party had any recollection of the discussion as to the terms of the clause. There was no memorandum or other written material. In the absence of evidence of mutual mistake leading to the conclusion that the true agreement of the parties was other than as recorded, the application for rectification was properly refused by the trial judge. Upon such refusal counsel for Collins abandoned any claim for liquidated damages.

To return to the narrative, Elsley managed the combined general insurance businesses for seventeen years, from June 1, 1956 until May 31, 1973, at which time he gave proper notice of termination of employment. During the seventeen-year period Elsley dealt with the customers of the agency to the almost total exclusion of Collins. To them Elsley was the business, Collins little more than a name. Elsley met the customers, telephoned them frequently, placed their insurance policies and answered their queries. Such were the findings of the trial judge. People became accustomed to doing business with him on a personal basis and he looked after their insurance needs. He served not

accepte l'engagement précité et est liée par lui.

La clause diffère substantiellement des clauses restrictives des deux conventions précédentes. Elle stipule une période de cinq ans après la cessation de l'emploi. Elle est assujettie à l'engagement contenu au contrat de vente du 1er mai 1956, dans le but, sans aucun doute, d'assurer une période restrictive minimum de dix ans et une période restrictive maximum équivalant à la durée de l'emploi plus cinq ans. Elsley devait payer la somme de $1,000 à défaut de respecter ou d'exécuter la convention. Les conventions précédentes stipulaient le paiement de $1,000 [TRADUCTION] «pour chaque violation».

Pendant le procès, Collins a demandé que la convention soit rectifiée en y ajoutant les termes «pour chaque violation». La preuve révèle, toutefois, que bien que les deux parties eussent convenu qu'il y aurait une clause restrictive, elles en avaient laissé la rédaction et le détail à leur avocat. Ce dernier est mort avant la date du procès et aucune des parties ne se souvient de la discussion sur les termes de la clause. Il n'y a pas de note à ce sujet ni d'autres documents écrits. La demande de rectification a été à bon droit rejetée par le juge de première instance, en l'absence de preuve d'une erreur mutuelle permettant de conclure que l'accord réel des parties était autre que celui qui avait été mis par écrit. A la suite de ce refus, l'avocat de Collins a abandonné toute réclamation de dommages-intérêts liquidés.

Pour en revenir aux faits, Elsley a dirigé les entreprises combinées d'assurance générale pendant 17 ans, du 1er juin 1956 au 31 mai 1973, date à laquelle il a donné le préavis de cessation d'emploi prévu. Pendant ces dix-sept ans, Elsley a traité avec les clients de l'agence presque sans aucune participation de Collins. Pour eux, Elsley, c'était l'entreprise, Collins, c'était à peine un peu plus qu'un nom. Elsley rencontrait les clients, leur téléphonait fréquemment, plaçait leurs polices d'assurance et répondait à leurs demandes. C'est ce que le juge de première instance a conclu. Les gens se sont habitués à traiter avec Elsley sur une base personnelle et il pourvoyait à leurs besoins en

only customers of the business he formerly owned, but also Collins' customers.

From 1956 to 1973 the business bore the name "Collins & Elsley Insurance Agencies." During that period, as a convenience, many policyholders paid their premiums at the office of D. C. Elsley Limited, the real estate office of Elsley, because a large part of the business purchased by Collins from Elsley came from the area in which this office was located. As general manager of the combined businesses, Elsley, of course, had access to all policyholder records; he was familiar with the nature and extent of coverage and the premium paid by each policyholder. He had knowledge of the insurable assets, financial credit, likes and dislikes and idiosyncrasies of each customer, in a recurring and confidential relationship not unlike that of lawyer/client or doctor/patient. It was only natural that policyholders would follow him if he made a change.

I

Following termination of his employment with Collins, Elsley commenced his own general insurance business under D. C. Elsley Limited. He took with him two insurance salesmen and an insurance clerk formerly employed by the Collins and Elsley agency. A large number of former clients of the agency transferred their business. Exhibit 10 comprised a list of approximately two hundred former clients who had advised Collins they were transferring their insurance business to Elsley. The only factual dispute in the entire case is as to whether Elsley solicited the business of former clients. He denied having done so. Collins could not say that Elsley himself had solicited former clients, but said that Elsley's employees had done so. When asked as to how many former clients he had had dealings with after leaving the employ of Collins, Elsley replied that he had never "stopped to add them up." There is evidence he advertised for general insurance business and that some advertisements referred to him as being "formerly of Collins and

matière d'assurances. Il servait non seulement la clientèle de l'entreprise qui lui avait appartenu, mais également celle de Collins.

De 1956 à 1973, l'entreprise a fait affaire sous la raison sociale «Collins & Elsley Insurance Agencies». Pendant cette période, pour des raisons de commodité, un grand nombre de détenteurs de polices ont payé leurs primes dans les bureaux de D. C. Elsley Limited, l'entreprise immobilière de Elsley, parce qu'une grande partie des affaires achetées par Collins à Elsley provenait de la région dans laquelle ce bureau se trouvait. En tant que gérant général des entreprises combinées, Elsley avait évidemment accès aux dossiers de tous les détenteurs de polices; il était très au courant de la nature et de l'étendue de la couverture ainsi que de la prime payée par chacun. Vu ses relations continues et confidentielles avec sa clientèle, très semblables à celles d'un avocat avec son client ou d'un médecin avec son malade, il connaissait les biens assurables, la solidité financière, les goûts, les aversions et les petites manies de chacun de ses clients. Il n'était que naturel que les détenteurs de polices le suivent s'il changeait de situation.

I

A la suite de la cessation de son emploi auprès de la compagnie Collins, Elsley forma sa propre entreprise d'assurance générale sous la raison sociale D. C. Elsley Limited. Il prit avec lui deux courtiers en assurances et un employé précédemment au service de la compagnie Collins & Elsley. Un grand nombre d'anciens clients de la compagnie transférèrent leurs affaires auprès de Elsley. La pièce 10 comprend une liste d'à peu près 200 anciens clients qui avaient avisé Collins qu'ils transféraient leurs assurances auprès d'Elsley. Dans tout le litige, la seule contestation de fait est de savoir si Elsley a sollicité les anciens clients. Il le conteste. Collins ne pouvait pas dire qu'Elsley lui-même avait sollicité d'anciens clients, mais il a déclaré que les employés d'Elsley l'avaient fait. Quand on lui a demandé avec combien d'anciens clients il avait fait affaire après avoir quitté son emploi auprès de Collins, Elsley a répondu qu'il n'avait jamais [TRADUCTION] «pensé à les compter». Il est prouvé qu'une partie de la publicité qu'il

Elsley Insurance Agencies." In the Ontario Court of Appeal, Mr. Justice Evans (with whom Mr. Justice MacKinnon agreed) found that Elsley had actively solicited former clients. Mr. Justice Jessup took a contrary view. Both courts below considered Collins and Elsley to be successful businessmen, competent and experienced.

a faite au sujet de son entreprise d'assurance générale parle de lui comme étant [TRADUCTION] «précédemment de Collins & Elsley Insurance Agencies». En Cour d'appel de l'Ontario, le juge Evans (avec lequel le juge MacKinnon était d'accord) a conclu qu'Elsley avait activement sollicité d'anciens clients. Le juge Jessup était d'avis contraire. Les deux tribunaux d'instance inférieure ont considéré que Collins et Elsley étaient des hommes d'affaires compétents et expérimentés et qui avaient réussi.

At trial, Mr. Justice Stark ordered Elsley restrained until September 1, 1978 from carrying on the business of general insurance agent within the defined area. He also directed a reference to the Local Master to assess the damages of Collins with respect to the business taken from him by Elsley from June 1, 1973 until the date of trial, subject to such damages being restricted to the loss of the agent's share of the premiums from contracts of insurance detailed in Exhibit 10, to which I have referred.

En première instance, le juge Stark a ordonné à Elsley de s'abstenir, jusqu'au 1er septembre 1978, d'exploiter l'entreprise d'agent d'assurance générale dans la zone définie. Il a également ordonné un renvoi au *Master* local pour l'évaluation des dommages-intérêts dus à Collins en raison des affaires que lui avait enlevées Elsley du 1er juin 1973 jusqu'à la date du procès, à condition que ces dommages-intérêts fussent limités à la perte de la part des primes de l'agent relativement aux contrats d'assurance énumérés à la pièce 10 précitée.

The majority of the Court of Appeal affirmed the judgment at trial, with one variation. The Court directed that Collins be compensated for the loss of commission on *all* contracts of general insurance sold by Elsley from June 1, 1973 to the date of the injunction (not limited to the policies set out in Exhibit 10), after taking into account the expenses incurred in securing and servicing the contracts. Mr. Justice Jessup dissented.

La majorité de la Cour d'appel a confirmé le jugement de première instance, avec une modification. La Cour a ordonné que Collins soit indemnisé pour la perte de commissions sur *tous* les contrats d'assurance générale conclus par Elsley du 1er juin 1973 jusqu'à la date de l'injonction (pas seulement sur les polices énumérées à la pièce 10), compte tenu des frais afférents à l'obtention des contrats et aux démarches subséquentes. Le juge Jessup était dissident.

The point taken by Mr. Justice Jessup is central to the case. It is this. The restrictive covenant, it is contended, does not merely restrain the solicitation by Elsley of clients of the Collins & Elsley agency, it prevents Elsley engaging at all in the general insurance business in a large area and operates, therefore, to eliminate competition *per se* without regard for the public interest and beyond necessary protection of Collins' interest. The argument, in short, is that the covenant would have been valid if it had precluded Elsley from soliciting clients of his former employer but, drawn in more sweeping terms, it is unenforceable as being in restraint of trade and an interference with individual liberty of action. Among the authorities cited in support of

La question soulevée par le juge Jessup est cruciale en l'espèce. La voici. On soutient que la clause restrictive n'empêche pas simplement Elsley de solliciter des clients de la compagnie Collins & Elsley; elle interdirait à ce dernier de se livrer d'une façon quelconque à des activités d'assurance générale dans une zone étendue et aurait pour effet, en conséquence, d'éliminer la concurrence en soi, sans égard à l'intérêt public et par-delà la protection nécessaire des intérêts de Collins. En résumé, l'argument est que la clause aurait été valide si elle avait interdit à Elsley de solliciter les clients de son ancien employeur mais, rédigée en termes trop généraux, elle ne peut être imposée car elle constitue une restriction à la liberté du com-

this are *Herbert Morris Limited v. Saxelby*[3]; *Stenhouse Australia Ltd. v. Phillips*[4] and *Robert W. Maguire v. Northland Drug Company Limited*[5].

II

The principles to be applied in considering restrictive covenants of employment are well-established. They are found in the cases above-mentioned and in such familiar authorities as the *Nordenfelt* case[6], *Mason v. Provident Clothing and Supply Co.*[7] and *Attwood v. Lamont*[8]. Of more recent vintage: *Scorer v. Seymour-John*[9] and *Gledhow Autoparts Ltd. v. Delaney*[10]. A covenant in restraint of trade is enforceable only if it is reasonable between the parties and with reference to the public interest. As in many of the cases which come before the courts, competing demands must be weighed. There is an important public interest in discouraging restraints on trade, and maintaining free and open competition unencumbered by the fetters of restrictive covenants. On the other hand, the courts have been disinclined to restrict the right to contract, particularly when that right has been exercised by knowledgeable persons of equal bargaining power. In assessing the opposing interests the word one finds repeated throughout the cases is the word "reasonable." The test of reasonableness can be applied, however, only in the peculiar circumstances of the particular case. Circumstances are of infinite variety. Other cases may help in enunciating broad general principles but are otherwise of little assistance.

It is important, I think, to resist the inclination to lift a restrictive covenant out of an employment agreement and examine it in a disembodied

[3] [1916] 1 A.C. 688.
[4] [1974] 1 All E.R. 117.
[5] [1935] S.C.R. 412.
[6] [1894] A.C. 535.
[7] [1913] A.C. 724.
[8] [1920] 3 K.B. 571.
[9] [1966] 3 All E.R. 347.
[10] [1965] 1 W.L.R. 1366.

merce et une immixtion dans la liberté d'action individuelle. Parmi les arrêts cités à l'appui de cette théorie, on trouve *Herbert Morris Limited v. Saxelby*[3]; *Stenhouse Australia Ltd. v. Phillips*[4] et *Robert W. Maguire c. Northland Drug Company Limited*[5].

II

Les principes applicables lorsqu'on examine les clauses restrictives en matière d'emploi sont bien établis. On les trouve dans les décisions susmentionnées et dans d'autres arrêts connus comme *Nordenfelt*[6], *Mason v. Provident Clothing and Supply Co.*[7] et *Attwood v. Lamont*[8]. Et plus récemment: *Scorer v. Seymour-John*[9] et *Gledhow Autoparts Ltd. v. Delaney*[10]. Une clause restreignant le commerce ne peut être exécutoire que si elle est raisonnable vis-à-vis des parties et de l'intérêt public. Comme dans beaucoup d'affaires dont les tribunaux ont à connaître, on doit peser des exigences contradictoires. Dans l'intérêt public, il est important de décourager les restrictions à la liberté du commerce et de maintenir une concurrence exempte des entraves que constituent les clauses restrictives. En revanche, les tribunaux n'ont pas été enclins à restreindre le droit de contracter, particulièrement quand ce droit a été exercé par des personnes expérimentées ayant un pouvoir de négociation égal. En évaluant les intérêts opposés, on constate qu'on retrouve dans toutes les affaires le mot «raisonnable». Le critère du caractère raisonnable ne peut toutefois s'appliquer que dans les circonstances spéciales d'un cas particulier. Les circonstances varient à l'infini. Si d'autres affaires peuvent aider à énoncer des principes généraux, elles sont, par ailleurs, de peu d'utilité.

Il est important, je crois, de résister au désir de sortir une clause restrictive d'un contrat de louage de services et de l'examiner hors de son contexte,

[3] [1916] 1 A.C. 688.
[4] [1974] 1 All E.R. 117.
[5] [1935] R.C.S. 412.
[6] [1894] A.C. 535.
[7] [1913] A.C. 724.
[8] [1920] 3 K.B. 571.
[9] [1966] 3 All E.R. 347.
[10] [1965] 1 W.L.R. 1366.

manner, as if it were some strange scientific specimen under microscopic scrutiny. The validity, or otherwise, of a restrictive covenant can be determined only upon an overall assessment, of the clause, the agreement within which it is found, and all of the surrounding circumstances.

The distinction made in the cases between a restrictive covenant contained in an agreement for the sale of a business and one contained in a contract of employment is well-conceived and responsive to practical considerations. A person seeking to sell his business might find himself with an unsaleable commodity if denied the right to assure the purchaser that he, the vendor, would not later enter into competition. Difficulty lies in definition of the time during which, and the area within which, the non-competitive covenant is to operate, but if these are reasonable, the courts will normally give effect to the covenant.

A different situation, at least in theory, obtains in the negotiation of a contract of employment where an imbalance of bargaining power may lead to oppression and a denial of the right of the employee to exploit, following termination of employment, in the public interest and in his own interest, knowledge and skills obtained during employment. Again, a distinction is made. Although blanket restraints on freedom to compete are generally held unenforceable, the courts have recognized and afforded reasonable protection to trade secrets, confidential information, and trade connections of the employer.

The majority of the Court of Appeal considered the present case to be one which did not fit neatly into the category of either sale or employment, being inextricably bound together as in *Silverman v. Silverman*[1]. In a sense that is true, but I do not think the restrictive covenant of the employment agreement can be fed by the sale agreement. The covenant contained in the sale agreement expired, and its force exhausted, seven years before the

[1] (1969), 113 Sol. J. 563.

comme s'il s'agissait de l'examen microscopique d'un spécimen scientifique rare. La validité ou tout autre aspect d'une clause restrictive ne peut être déterminé que par une évaluation générale de cette clause, du contrat où elle est insérée et de toutes les circonstances qui l'entourent.

La distinction faite en jurisprudence entre une clause restrictive contenue dans un contrat de vente d'une entreprise et celle contenue dans un contrat de louage de services est bien conçue et répond à des considérations pratiques. Celui qui cherche à vendre son entreprise peut se retrouver avec une chose invendable si on lui conteste le droit d'assurer l'acheteur que lui, le vendeur, ne lui fera pas concurrence plus tard. La difficulté réside dans la définition de la période au cours de laquelle la clause de non-concurrence doit jouer et la région visée; mais si ces deux éléments sont raisonnables, les tribunaux donneront normalement effet à la clause.

Une situation différente, du moins en théorie, surgit dans la négociation d'un contrat de louage de services où un déséquilibre dans le pouvoir de négociation peut conduire à de l'oppression et à nier à l'employé son droit, à la suite de la cessation de son emploi, d'exploiter dans l'intérêt public et dans son propre intérêt, les connaissances et la compétence qu'il a acquises au cours de son emploi. De nouveau, on fait une distinction. Bien que les tribunaux jugent le plus souvent que les restrictions générales à la liberté de la concurrence ne sont pas exécutoires, ils reconnaissent et accordent une protection raisonnable aux secrets commerciaux, aux renseignements confidentiels et à la clientèle de l'employeur.

La majorité de la Cour d'appel a considéré que la présente affaire n'entre nettement ni dans la catégorie de la vente d'entreprise ni dans celle du louage de services, les deux étant liées d'une façon inextricable comme dans l'affaire *Silverman v. Silverman*[1]. Dans un sens, cela est vrai, mais je ne crois pas que la clause restrictive du contrat de louage de services puisse être alimentée par le contrat de vente. La clause du contrat de vente est

[1] (1969), 113 Sol. J. 563.

restrictive covenant contained in the employment agreement came into operation. The employment agreement was negotiated subsequent to and independent of the sale agreement. The agreement sued upon is the employment agreement. It would be wrong, in my opinion, to test that agreement by the criteria applicable in the case of a vendor/purchaser agreement, or by some hybrid test. The restrictive covenant, if enforceable, must stand up to the more rigorous tests applied in an employer/employee context.

III

The critical question, as I have indicated, is whether the employer, in seeking to protect his trade connection, overreached in the formulation of clause 3 of the agreement of May 30, 1956.

In assessing the reasonableness of the clause with reference to the interests of the parties, several questions must be asked. First, did Collins have a proprietary interest entitled to protection? The answer to this question must surely be in the affirmative. Shortly before the agreement for the employment of Elsley, Collins had paid Elsley some $46,000 for the general insurance trade connection of Elsley. By the agreement Elsley was placed in control, not only of that trade connection, but also the trade connection which Collins enjoyed prior to that time. Second, were the temporal or spatial features of the clause too broad? Some argument was directed to the Court as to those aspects, but I am in entire agreement with the courts below that they are not open to successful challenge. The next and crucial question is whether the covenant is unenforceable as being against competition generally, and not limited to proscribing solicitation of clients of the former employer. In a conventional employer/employee situation the clause might well be held invalid for that reason. The fact that it could have been drafted in narrower terms would not have saved it, for as Viscount Haldane said in *Mason v. Provident Clothing and Supply Co.*, *supra*, p. 732, ". . . the question is not whether they could have made a valid agreement but whether the agreement actu-

expirée et a cessé d'avoir des effets sept ans avant que la clause restrictive du contrat de louage de services n'entre en vigueur. Le contrat de louage de services a été négocié subséquemment à l'acte de vente et indépendamment de ce dernier. La présente action est introduite en vertu du contrat de louage de services. A mon avis, il serait erroné d'utiliser à l'égard de ce contrat les critères applicables à un contrat entre un vendeur et un acheteur ou un critère hybride. Pour être exécutoire, la clause restrictive doit répondre aux critères plus rigoureux appliqués dans le contexte des relations employeur-employé.

III

Comme je l'ai indiqué, la question cruciale est de savoir si l'employeur, en cherchant à protéger sa clientèle, est allé trop loin dans la formulation de la clause 3 du contrat du 30 mai 1956.

On doit peser plusieurs questions quand on évalue le caractère raisonnable de la clause relativement à l'intérêt des parties. Premièrement, est-ce que Collins a un droit de propriété qu'il peut protéger? La réponse à cette question doit certainement être affirmative. Peu de temps avant qu'Elsley ne signe son contrat d'engagement, il avait vendu à Collins sa clientèle dans le domaine de l'assurance générale pour quelque $46,000. Ce contrat donnait à Elsley le contrôle non seulement de cette clientèle, mais également celui de la clientèle dont Collins bénéficiait antérieurement. Deuxièmement, est-ce que les stipulations temporelles et territoriales de la clause sont trop larges? On a plaidé sur ces questions devant la Cour, mais je souscris complètement à l'avis des cours d'instance inférieure selon lequel ces stipulations ne peuvent être attaquées avec succès. La question essentielle qui suit est de savoir si la clause n'est pas inexécutoire parce qu'elle vise la concurrence d'une façon générale et ne se limite pas à interdire la sollicitation des clients de l'ancien employeur. Dans une situation employeur-employé classique, la clause pourrait être jugée invalide pour ce motif. Le fait qu'elle aurait pu être rédigée en termes plus étroits ne l'aurait pas sauvée, car, comme l'a dit le vicomte Haldane dans l'arrêt *Mason v. Provident Clothing and Supply Co.*, précité, à la p.

ally made was valid." Whether a restriction is reasonably required for the protection of the covenantee can only be decided by considering the nature of the covenantee's business and the nature and character of the employment. Admittedly, an employer could not have a proprietary interest in people who were not actual or potential customers. Nevertheless, in exceptional cases, of which I think this is one, the nature of the employment may justify a covenant prohibiting an employee not only from soliciting customers, but also from establishing his own business or working for others so as to be likely to appropriate the employer's trade connection through his acquaintance with the employer's customers. This may indeed be the only effective covenant to protect the proprietary interest of the employer. A simple non-solicitation clause would not suffice.

There are cases which uphold the validity of a covenant prohibiting an employee from engaging in a particular type of work within a specified area, and for an acceptable period of time after the termination of his employment: see e.g. *Fitch v. Dewes*[12]; *Marion White v. Francis*[13]; *P.C.O. Services Ltd. v. Rumleski*[14]; *Campbell, Imrie and Shankland v. Park*[15]. In each of these cases the employee was in a position where he acquired a close personal acquaintance with the clients or customers of the business. Such a restrictive covenant was reasonable, in the words of Lord Birkenhead in *Fitch v. Dewes* at p. 165, in order that the employee "should not be in a position to use the intimacies and knowledge which he had acquired in the course of his employment in order to create a practice of his own in that same place and by doing so undermine the business and the connection of the [employer]." In the present case, when the clause was drafted it was known that Elsley had, or would acquire, a special and intimate knowledge of the customers of his prospective employer and the means of influence over them.

[12] [1921] 2 A.C. 158.
[13] [1972] 1 W.L.R. 1423.
[14] [1963] 2 O.R. 62.
[15] [1954] 2 D.L.R. 170.

732, [TRADUCTION] «... la question n'est pas de savoir s'ils auraient pu conclure un contrat valide, mais si le contrat effectivement conclu était valide». La seule façon de déterminer s'il est raisonnable d'insérer une clause restrictive pour la protection du stipulant est d'examiner la nature de son entreprise, ainsi que la nature et les attributs de l'emploi. Il est admis qu'un employeur ne peut pas avoir de droit à l'égard de personnes qui n'étaient pas ses clients actuels ou potentiels. Néanmoins, dans des cas exceptionnels, et je crois que celui-ci en est un, la nature de l'emploi peut justifier une clause interdisant à un employé, non seulement de solliciter des clients, mais également d'établir son propre commerce ou de travailler pour le compte de tiers de façon à s'approprier éventuellement la clientèle de l'employeur du fait qu'il la connaît. En vérité, c'est peut-être là la seule clause restrictive efficace pour protéger le droit de propriété de l'employeur. Une simple clause de non-sollicitation ne suffirait pas.

Des arrêts ont confirmé la validité d'une clause interdisant à un employé de prendre part à un genre de travail particulier dans une zone déterminée et ce, pendant une période de temps acceptable après la cessation de son emploi: voir par exemple les arrêts *Fitch v. Dewes*[12]; *Marion White v. Francis*[13]; *P.C.O. Services Ltd. v. Rumleski*[14]; *Campbell, Imrie and Shankland v. Park*[15]. Dans chacune de ces affaires, l'employé occupait un poste qui lui avait fait connaître personnellement les clients de l'entreprise. Pour reprendre les termes de lord Birkenhead dans l'arrêt *Fitch v. Dewes*, à la p. 165, pareille clause restrictive était raisonnable pour que l'employé [TRADUCTION] «ne fût pas en mesure d'utiliser les relations étroites et l'expérience qu'il avait acquises au cours de son emploi pour créer sa propre affaire au même endroit et, ce faisant, saper l'entreprise et la clientèle de l'employeur». En l'espèce, lorsque la clause a été rédigée, on savait qu'Elsley avait, ou aurait, une connaissance spéciale et intime de la clientèle de son employeur éventuel et les moyens de l'influencer.

[12] [1921] 2 A.C. 158.
[13] [1972] 1 W.L.R. 1423.
[14] [1963] 2 O.R. 62.
[15] [1954] 2 D.L.R. 170.

In the leading case of *Morris v. Saxelby, supra*, Lord Parker enunciated with clarity the circumstances in which a covenant taken by an employer from an employee or apprentice will be enforceable. He said, at p. 709:

> Wherever such covenants have been upheld it has been on the ground, not that the servant or apprentice would, by reason of his employment or training, obtain the skill and knowledge necessary to equip him as a possible competitor in the trade, but that he might obtain such personal knowledge of and influence over the customers of his employer, or such an acquaintance with his employer's trade secrets as would enable him, if competition were allowed, to take advantage of his employer's trade connection or utilize information confidentially obtained.

Dans l'affaire faisant autorité, *Morris v. Saxelby*, précitée, lord Parker a clairement énoncé les conditions dans lesquelles une clause restrictive imposée par un employeur à son employé ou à son apprenti serait exécutoire. Il a dit à la p. 709:

> [TRADUCTION] Chaque fois que l'on a confirmé pareilles clauses, ce n'était pas pour le motif que le préposé ou l'apprenti, vu son emploi ou son apprentissage, obtiendrait la compétence et la connaissance nécessaires pour devenir un concurrent éventuel dans le commerce, mais parce qu'il pourrait obtenir une connaissance personnelle des clients de son employeur et une influence sur eux, ou une connaissance des secrets commerciaux de son employeur, qui lui permettrait, si la concurrence était autorisée, de tirer profit de la clientèle de son employeur ou d'utiliser les renseignements confidentiels ainsi obtenus.

It is difficult to envisage a factual situation in which an employee would be in a better position than that of Elsley in the present case, to obtain "personal knowledge of and influence over the customers of his employer." Later in his speech, Lord Parker made the point that it is of importance: whether "the defendant ever came into personal contact with the plaintiff's customers." The same point is made in the following passage from Cheshire & Fifoot, *The Law of Contract* (8th ed.), at p. 369:

> A restraint is not valid unless the nature of employment is such that customers will either learn to rely upon the skill or judgment of the servant or will deal with him directly and personally to the virtual exclusion of the master, with the result that he will probably gain their custom if he sets up business on his own account.

Il est difficile d'imaginer une situation de fait dans laquelle un employé serait dans une meilleure position que celle d'Elsley en l'espèce, pour acquérir [TRADUCTION] «une connaissance personnelle des clients de son employeur et une influence sur eux». Plus loin dans son exposé, lord Parker a relevé qu'il était important de savoir si [TRADUCTION] «le défendeur est jamais entré en contact personnel avec les clients du demandeur». On retrouve le même point dans le passage suivant de Cheshire & Fifoot, *The Law of Contract* (8e éd.) à la p. 369:

> [TRADUCTION] Une clause restrictive n'est valide que si la nature de l'emploi est telle que les clients apprendront soit à s'en remettre à l'expérience ou au jugement du préposé ou traiteront avec lui directement et personnellement en excluant virtuellement le patron, de sorte que si le préposé s'établit à son compte, il acquerra probablement leur clientèle.

In the view which I take of this case a covenant against solicitation would not have been adequate to protect the proprietary interest entitled to protection. Exhibit 10 is telling support of that view. Elsley testified that he did not solicit former clients; notwithstanding, two hundred clients switched their custom to him. That is a vivid illustration of what Lord Parker had in mind in speaking of the influence of an employee over the customers of his employer. And it is not suggested that Exhibit 10 was a complete list of all those who took action. It was filed as representative only. Collins estimated that Elsley had taken close to

Vu mon optique en l'espèce, une clause interdisant la sollicitation n'aurait pas été appropriée pour protéger le droit de propriété comme il se doit. La pièce 10 appuie ce point de vue. Elsley a témoigné qu'il n'avait pas sollicité d'anciens clients; malgré cela, deux cents clients lui ont transféré leur clientèle. C'est un exemple vivant de ce que lord Parker avait en vue en parlant de l'influence d'un employé sur les clients de son employeur. Personne n'a prétendu que la pièce 10 est une liste complète de tous ceux qui ont changé d'assureur. On l'a déposée à titre d'exemple seulement. Collins a estimé qu'Elsley a pris près de la

one-half of the business on the books when Elsley left. As Salter J. said in the case of *Putsman v. Taylor*[16] at p. 642, a covenant against solicitation "is difficult to enforce; it is difficult to show breach and difficult to frame an injunction." The difficulty is demonstrated in this case. Does an advertisement which comes to the attention of former clients amount to solicitation? Was there solicitation by Elsley? I need not attempt to answer those questions. The point is that a non-solicitation covenant, in the circumstances here found, would have been meaningless.

Mr. Justice Jessup suggested in his reasons that a simple provision in a non-solicitation agreement would have enabled the plaintiff to examine the defendant's books and records from time to time so that solicitation of clients acquired by the plaintiff could be detected. I do not think any experienced businessman would consent to examination of his books by a competitor, whether a former employer or not. I doubt that clients of the defendant would welcome such intrusion upon their confidential affairs, or permit it if it came to their attention. If the defendant were hired by someone rather than being self-employed, by what right could he open the books of his employer to examination by a former employer? In short, I cannot accept the efficacy of the simple provision Mr. Justice Jessup envisages.

For the foregoing reasons, in my view the impugned covenant is no wider than reasonably required in order to afford adequate protection to Collins.

After the party relying on a restrictive covenant has established its reasonableness as between the parties, the onus of proving that it is contrary to the public interest lies on the party attacking it: *Morris v. Saxelby*, (*supra*). Since in my opinion the respondent has established what is required of him, the matter of the public interest must now be considered.

Unless it can be said that any and every restraint upon competition is bad, I do not think that enforcement of the clause could be considered

[16] [1927] 1 K.B. 637.

moitié du portefeuille quand il est parti. Comme l'a dit le juge Salter dans l'arrêt *Putsman v. Taylor*[16] à la p. 642, une clause de non-sollicitation [TRADUCTION] «est difficile à faire exécuter; il est difficile de prouver la violation et difficile de formuler une injonction». La difficulté est démontrée en l'espèce. Est-ce qu'une annonce qui attire l'attention d'anciens clients équivaut à une sollicitation? Elsley a-t-il sollicité? Je n'ai pas besoin d'essayer de répondre à ces questions. Le fait est qu'une clause de non-sollicitation, dans les circonstances de l'espèce, aurait été dénuée de sens.

Le juge Jessup a suggéré dans ses motifs qu'une simple stipulation dans une convention de non-sollicitation aurait permis au demandeur d'examiner de temps à autre les livres et registres du défendeur de façon à lui permettre de détecter la sollicitation de ses clients acquis. Je ne crois pas qu'un homme d'affaires expérimenté consentirait à faire examiner ses livres par un concurrent, qu'il s'agisse d'un ex-employeur ou non. Je doute que les clients du défendeur verraient d'un bon œil cette intrusion dans leurs affaires confidentielles ou l'autoriseraient s'ils l'apprenaient. Si le défendeur avait été engagé par un tiers au lieu de travailler pour son compte, de quel droit pourrait-il ouvrir les livres de son employeur pour qu'ils puissent être examinés par un ancien employeur? En résumé, je ne puis accepter l'efficacité de la simple stipulation envisagée par le juge Jessup.

Pour les motifs qui précèdent, la clause attaquée n'est pas plus large qu'il est raisonnablement requis pour protéger Collins de façon appropriée.

Après que la partie qui s'appuie sur une clause restrictive a établi son caractère raisonnable entre parties, il incombe à celle qui l'attaque de prouver qu'elle est contraire à l'intérêt public: *Morris v. Saxelby*, précité. Vu qu'à mon avis, l'intimée a établi ce qu'on lui demande, il faut maintenant examiner la question de l'intérêt public.

A moins que l'on puisse dire que toute restriction à la concurrence est néfaste, je ne crois pas que l'on puisse considérer que la mise en vigueur

[16] [1927] 1 K.B. 637.

inimical to the public interest. There were twenty to twenty-two general agents in Niagara Falls according to the evidence as of the date of trial, employing eighty to ninety employees. There was nothing to suggest that the people of Niagara Falls would suffer through the loss, for a limited period, of the services of Elsley in the general insurance business.

I am of opinion that the clause in contention is valid, and enforceable in accordance with its terms.

IV

The only other question is as to damages. The injunction granted at trial and continued by the Court of Appeal ceased to have effect with the death of Elsley, after the judgment of the Court of Appeal. Proceedings in this Court were continued by his widow as executrix of his estate.

The damage issue is one of some importance and difficulty. It subsumes two questions: (i) the right of a plaintiff enforcing a restrictive covenant to claim both an injunction and damages; (ii) whether the quantum is, or is limited to, the amount stipulated as liquidated damages in the covenant. In other words, can Collins claim *any* damages; and if so, is the amount limited to $1,000? I would answer both of these questions in the affirmative.

The Court was referred to a number of authorities. The first, in time, was *Jones v. Heavens*[17]. In that case, the covenant precluded the carrying on of the business of a saddler under penalty of £100 to be paid by way of liquidated damages for each such offence. A motion was made for an injunction. It was argued that the plaintiff's remedy was by action for recovery of the sum named as liquidated damages. An injunction was granted. Thus, even where there is provision for liquidated damages, the plaintiff may elect instead to ask for an

[17] (1877), 4 Ch.D. 636.

de la clause soit contraire à l'intérêt public. Selon la preuve, il y avait à Niagara Falls, à la date du procès, de vingt à vingt-deux agents généraux employant quatre-vingts à quatre-vingt-dix personnes. Rien ne permet de penser que les habitants de Niagara Falls souffriraient de la perte, pendant une période limitée, des services d'Elsley dans l'assurance générale.

Je suis d'avis que la clause litigieuse est valide et exécutoire conformément à ses conditions.

IV

La seule autre question est celle des dommages-intérêts. L'injonction accordée en première instance et confirmée en Cour d'appel a cessé de faire effet avec le décès d'Elsley, après l'arrêt de la Cour d'appel. La procédure devant cette Cour a été reprise par sa veuve, en sa qualité d'exécutrice de la succession.

La question des dommages-intérêts est importante et présente des difficultés. Elle se subdivise en deux points: (i) le droit d'un demandeur qui fait appliquer une clause restrictive de réclamer à la fois une injonction et des dommages-intérêts; (ii) la question de savoir si le quantum des dommages est ou doit être limité au montant stipulé à titre de dommages-intérêts liquidés dans la clause restrictive. En d'autres termes, Collins peut-il demander des dommages-intérêts *quels qu'ils soient*? S'il le peut, le montant en est-il limité à $1,000? Je suis d'avis que la réponse à ces deux questions doit être affirmative.

On a renvoyé la Cour à de nombreux arrêts. Le premier et le plus ancien est l'arrêt *Jones v. Heavens*[17]. La clause interdisait l'exploitation d'une sellerie sous peine d'une somme de £100 due à titre de dommages-intérêts liquidés pour chaque infraction. En défense à la demande d'injonction, le défendeur a plaidé que le demandeur devait recourir à une action en recouvrement de la somme indiquée à titre de dommages-intérêts liquidés. Une injonction a été accordée. Ainsi, même s'il existe une stipulation de dommages-inté-

[17] (1877), 4 Ch.D. 636.

injunction to prevent breach.

In the later case of *National Provincial Bank of England v. Marshall*[18], the defendant, on entering the service of the plaintiffs, a banking company, had executed a bond in the penal sum of £1,000 a condition of which was that he should pay this sum to the plaintiffs as liquidated damages if he should within a limited period after leaving the service of the plaintiffs accept employment in any other bank. The defendant accepted other employment in breach of the bond and the plaintiffs brought an action claiming an injunction. In response to the claim the defendant offered to pay the penal sum of £1,000. The Court held that he could not purchase his liberty to do the proscribed act. Lord Justice Cotton said that if the obligee brings an action at law he can recover damages, but (p. 116) ". . . if he comes into a Court of Equity the agreement will be enforced, if no action for damages has been brought, and an injunction will be granted." This case illustrates the principle that if the plaintiff is entitled to an injunction, the defendant cannot deprive him of this remedy by paying damages. The plaintiff may pursue whatever remedy is his due, even though it clearly affords him wider relief than another remedy open to him. Cotton L.J. added that if the Bank had brought an action they were not obliged to prove the damage they had suffered, but would be entitled without proof of damage to recover £1,000 as liquidated damages. Lindley L.J. in the same case spoke of the plaintiffs having an alternative remedy by way of injunction to enforce the agreement if they do not bring an action.

An early Canadian case, *Snider v. McKelvey*[19] dealt also with the matter. The defendant, who had sold his medical practice, acted in defiance of the sale agreement by which he had bound himself

[18] (1888), 40 Ch.D. 112.
[19] (1900), 27 O.L.R. 339.

rêts liquidés, le demandeur peut choisir de demander une injonction pour empêcher la violation du contrat.

Dans une affaire subséquente, *National Provincial Bank of England v. Marshall*[18], le défendeur, en entrant au service de la demanderesse, une banque, avait signé une garantie contenant une clause pénale de £1,000, montant qu'il devait payer à la demanderesse à titre de dommages-intérêts liquidés, si, après avoir quitté son service, il acceptait, dans un délai déterminé, un emploi auprès d'une autre banque. Le défendeur a accepté un autre emploi, en violation de la garantie, et la demanderesse a présenté une demande d'injonction. En réponse à l'action, le défendeur a offert de payer la somme de £1,000 faisant l'objet de la clause pénale. La Cour a jugé qu'il ne pouvait pas acheter la liberté de faire l'acte interdit. Le lord juge Cotton a dit que si le créancier intente une action en *common law*, il peut obtenir des dommages-intérêts, mais (p. 116) [TRADUCTION] «. . . s'il se présente devant une cour d'*equity* et qu'aucune action en dommages-intérêts n'a été intentée, la convention sera appliquée et une injonction accordée». Cette affaire illustre le principe que si le demandeur a droit à une injonction, le défendeur ne peut pas le priver de ce recours en payant des dommages-intérêts. Le demandeur peut utiliser le recours auquel il a droit quel qu'il soit, même s'il lui accorde clairement un redressement plus étendu qu'un autre recours qui lui est ouvert. Le lord juge Cotton a ajouté que si la banque avait intenté une action, elle n'aurait pas été obligée de prouver le préjudice qu'elle avait subi et aurait eu droit, sans preuve de préjudice, à £1,000 à titre de dommages-intérêts liquidés. Le lord juge Lindley, dans la même affaire, a parlé du recours subsidiaire ouvert à la demanderesse sous forme d'injonction pour faire exécuter la convention si elle n'intentait pas une action.

Une ancienne affaire canadienne, *Snider v. McKelvey*[19] a également traité de cette question. Le défendeur, qui avait vendu son cabinet de médecin, avait contrevenu aux conditions de l'acte

[18] (1888), 40 Ch.D. 112.
[19] (1900), 27 O.L.R. 339.

in the sum of $400 to be paid if he set up in practice within a defined time and area. Robertson J. granted an injunction and awarded damages of $100. On appeal, the Court held that the plaintiff must elect whether to take judgment for the $400 or for the injunction. The plaintiff insisted that the $400 was a penalty and, if such, he could have damages assessed for the breach of the condition as well as the injunction to restrain further breaches. Osler J.A., in the leading judgment, rejected this argument. He declined to recognize any distinction between the case of bond with a penalty and an agreement to pay liquidated damages, because the plaintiff would, if the equitable remedy by injunction were enforced, be obtaining performance of the agreement *in specie* and also what he was only entitled to recover in the case of its non-performance. He was of opinion that the $400 was intended to be payable as liquidated damages. After referring to the passage of *Lord Cairns' Act*, 21-22 Vict. c. 27, the learned judge of appeal had this to say, at p. 344:

> It is clear that the Act did not enable the Court to give the plaintiff a double remedy where before the Act his right was in the alternative—either at law or in equity, but not in both: *Sainter v. Ferguson* (1849), 7 C.B. 716; 1 Mac. & G. 286.

The following passage from the judgment of Osler J.A. is of particular interest because of the distinction made in respect of those cases concerning the sale of goodwill where there was no valid covenant or bond for the breach of which the plaintiff could have sued at law, and therefore no choice available between a suit at law and injunction in equity (at pp. 344-5):

> The learned trial Judge relied upon the case of *Mossop v. Mason* (1869), 16 Gr. 302, (1870), 18 Gr. 360, (1871), 18 Gr. 453 (in appeal), where damages were awarded as well as an injunction. But that case is quite distinguishable. There the defendant had sold to the plaintiff *inter alia* the goodwill of the business of an innkeeper carried on by him, and the bill was filed to restrain him from resuming the business he had sold and for damages sustained in consequence of his having done so. There was, as the Court held, no valid covenant or bond for the breach of which the plaintiff could have sued at law. The plaintiff had, therefore, no alternative

de vente en vertu duquel il s'était engagé à payer la somme de $400 s'il pratiquait pendant une période et dans une zone déterminées. Le juge Robertson a accordé une injonction et des dommages-intérêts de $100. En appel, la Cour a statué que le demandeur devait choisir entre obtenir un jugement pour les $400 et l'injonction. Le demandeur a soutenu que les $400 constituaient une peine et que, cela étant, il pouvait obtenir des dommages-intérêts pour la violation de la condition aussi bien qu'une injonction pour en empêcher d'autres. Le juge d'appel Osler, dans le jugement principal, a rejeté cet argument. Il a refusé de faire une distinction entre une garantie accompagnée d'une peine et un accord de payer des dommages-intérêts liquidés, parce que si l'on avait recours à l'injonction en *equity*, le demandeur obtiendrait l'exécution intégrale du contrat ainsi que ce à quoi il a droit seulement en cas de non-exécution. A son avis, les $400 étaient dus à titre de dommages-intérêts liquidés. Après avoir cité le passage de la *Lord Cairns' Act*, 21-22 Vict. c. 27, le savant juge a dit, à la p. 344:

> [TRADUCTION] Il est clair que la Loi n'a pas permis à la Cour de donner au demandeur un double recours là où, avant la Loi, il devait faire un choix—recours en *common law* ou en *equity*, mais pas les deux: *Sainter v. Ferguson* (1849), 7 C.B. 716; 1 Mac. & G. 286.

Le passage suivant du jugement du juge Osler présente un intérêt particulier parce qu'il distingue les affaires relatives à la vente d'un achalandage lorsqu'il n'y a pas de clause ou de garantie valide dont la violation aurait permis au demandeur d'introduire une action en *common law* et où il n'y avait donc aucun choix possible entre une poursuite en *common law* et une injonction en *equity* (aux pp. 344 et 345):

> [TRADUCTION] Le savant juge de première instance s'est appuyé sur l'arrêt *Mossop v. Mason* (1869), 16 Gr. 302, (1870) 18 Gr. 360, (1871), 18 Gr. 453 (en appel), qui a accordé des dommages-intérêts et une injonction. Toutefois, cette affaire est clairement différente. En l'espèce, le défendeur a notamment vendu au demandeur l'achalandage d'une auberge qu'il exploitait. La déclaration a été déposée pour l'empêcher de poursuivre le commerce qu'il avait vendu et pour le préjudice subi du fait qu'il l'avait poursuivi. Comme la Cour l'a décidé, il n'y avait aucune clause de garantie valide dont la violation aurait permis au demandeur d'introduire une action

remedy, and his right to recover rested solely upon the defendant's equitable obligation, implied in the sale of the goodwill, not to hold out in any way that he was carrying on business in continuation of, or in succession to, the business formerly carried on by him, the goodwill of which he had sold. See *Labouchere v. Dawson* (1872), L.R. 13 Eq. 322; approved in *Trego v. Hunt*, [1896] A.C. 7.

There was, therefore, nothing to prevent the Court from directing a reference to ascertain what damages the plaintiff had sustained consequent upon the breach of the equitable obligation.

We are, of course, not dealing here with a sale of goodwill but with an agreement for employment. McLennan J.A. shared the opinion of Osler J.A. that the $400 was clearly liquidated damages and he regarded it as clearly settled that in the case of liquidated damages the plaintiff must elect between the damages and an injunction. This case emphasizes that the basic principle being applied is the prohibition against double recovery. The agreed liquidated damages sum is to be a complete remedy for the entire breach specified. Once this sum has been awarded, to grant an injunction for even part of the breach would be to have overlapping remedies.

A year later, Wright J. in *General Accident Assurance Corporation v. Noel*[20], concluded that the current of authority in England was such that if the plaintiffs elected to take an injunction they could not have judgment as well for the liquidated damages for which the employment agreement in the case provided.

The British Columbia case of *Campbell, Imrie and Shankland v. Park, supra*, was cited in argument. In that case a restrictive covenant had been given by a chartered accountant engaged to serve as branch manager by a firm of accountants. The agreement was silent as to the payment of a stated amount for breach. The plaintiffs sought both injunction and damages. The defendant, relying on *General Accident Assurance Corporation v. Noel,*

[20] [1902] 1 K.B. 377.

en *common law*. Le demandeur n'avait, en conséquence, aucun autre recours possible et son droit à un redressement s'appuyait uniquement sur l'obligation du défendeur en *equity*, découlant implicitement de la vente de l'achalandage, de ne montrer en aucune façon qu'il exploitait une entreprise en continuation ou à titre de successeur de l'entreprise qu'il exploitait antérieurement et dont il avait vendu l'achalandage. Voir l'arrêt *Labouchere v. Dawson* (1872), L.R. 13 Eq. 322; approuvé dans l'arrêt *Trego v. Hunt*, [1896] A.C. 7.

Par conséquent, il n'y avait rien qui empêchait la Cour d'ordonner un renvoi pour fixer le préjudice que le demandeur avait subi à la suite de la non-exécution de l'obligation en *equity*.

Évidemment, nous ne traitons pas ici de la vente d'un achalandage, mais d'un contrat de louage de services. Le juge d'appel McLennan partageait l'avis du juge d'appel Osler selon lequel les $400 constituaient nettement des dommages-intérêts liquidés et il considérait comme clairement établi qu'en ce cas, le demandeur devait choisir entre dommages-intérêts et injonction. Cette affaire souligne que le principe fondamental appliqué est l'interdiction d'une double indemnisation. Le montant fixé à titre de dommages-intérêts liquidés est le redressement complet si la violation stipulée se réalise. Une fois ce montant alloué, accorder une injonction, même pour une partie de la violation, équivaudrait à utiliser des recours qui chevauchent.

Un an plus tard, le juge Wright dans l'arrêt *General Accident Assurance Corporation v. Noel*[20] a conclu que la tendance de la jurisprudence en Angleterre était telle que, si le demandeur choisissait de recourir à l'injonction, il ne pourrait pas en même temps obtenir un jugement pour les dommages-intérêts liquidés stipulés au contrat de travail.

Au cours des plaidoiries, on a cité une affaire de la Colombie-Britannique, *Campbell, Imrie and Shankland v. Park*, précitée. Dans cette affaire, un comptable agréé engagé à titre de directeur de succursale par une firme de comptables avait consenti à une clause restrictive. Le contrat était muet quant au paiement d'un montant déterminé en cas de violation. Les demandeurs ont requis à la fois une injonction et des dommages-intérêts. Le défen-

[20] [1902] 1 K.B. 377.

supra, said they could not have both. Wilson J., as he then was, had this to say in respect of that contention, at p. 183:

The plaintiffs have asked for an injunction and for damages. The defendant, relying on *Gen'l Accident Ass'ce Corp. v. Noel*, 1902 1 K.B. 377, says they cannot have both, but must elect. The case referred to is one in which the restrictive agreement contained a clause requiring the covenantor, in case of breach, to pay £100 as liquidated damages. Very reasonably, the covenantee was required to elect. The sum of £100 had been agreed to by the parties as being the total amount of damage which the covenantee would suffer by a breach. If he were paid this sum, he could not reasonably ask for an injunction to prohibit the doing of something in respect of which he had already collected full damages. But here the plaintiffs cannot say what their full damage may be i.e. the defendant is allowed to continue to attract their clients, they can only tell me what damage they have suffered to date, and ask me to prevent the defendant from inflicting on them further damage. I have no doubt that it is my right and duty so to do. I refer to *Garbutt Business College Ltd. v. Henderson*, [1939] 4 D.L.R. 151, as a case in which both forms of relief were granted.

The judge fixed damages at $1,000 and granted an injunction.

In the recent case in this Court, *H. F. Clarke Limited v. Thermidaire Corporation Limited*[21], the claim was for damages for breach of a restrictive covenant contained in a distributorship agreement. The question of injunction was not in issue. The agreement provided that the defaulting party would be required to pay as liquidated damages the gross profit realized from the sale of competitive products. The issue was whether the plaintiff could recover this amount or only provable damages. A majority of the Court held in favour of the latter disposition. In the majority judgment the Chief Justice in *obiter dicta* had this to say, at p. 335:

[21] [1976] 1 S.C.R. 319.

deur, se fondant sur l'arrêt *General Accident Assurance Corporation v. Noel*, précité, a dit qu'ils ne pouvaient avoir les deux. Voici ce que le juge Wilson, tel était alors son titre, a dit au sujet de cette prétention, à la p. 183:

[TRADUCTION] La demanderesse a requis une injonction et des dommages-intérêts. Le défendeur s'appuie sur l'arrêt *Gen'l Accident Ass'ce Corp. v. Noel*, 1902 1 K.B. 377, pour dire qu'elle ne peut avoir les deux et doit donc choisir. Dans l'affaire citée, la convention restrictive contenait une clause qui obligeait le débiteur, en cas de violation, à payer £100 à titre de dommages-intérêts liquidés. On a très raisonnablement demandé au stipulant de choisir. Les parties avaient convenu que la somme de £100 était le montant total du préjudice que subirait le stipulant s'il y avait violation. Si on lui paye cette somme, il ne peut raisonnablement pas demander une injonction pour interdire qu'on fasse une chose pour laquelle il a déjà touché des dommages-intérêts complets. Mais, en l'espèce, la demanderesse ne peut pas dire quel peut être son préjudice total, c'est-à-dire que si le défendeur est autorisé à continuer d'attirer les clients de la demanderesse, elle peut seulement me dire quel préjudice elle a subi à ce jour et me demander d'interdire à ce dernier de lui en faire subir davantage. Je ne doute pas que j'ai le droit et le devoir de le faire. Je me reporte à l'arrêt *Garbutt Business College Ltd. v. Henderson*, [1939] 4 D.L.R. 151, une affaire où l'on a accordé les deux formes de redressement.

Le juge a fixé les dommages-intérêts à $1,000 et a accordé une injonction.

Dans l'affaire récemment tranchée par cette Cour, *H. F. Clarke Limited c. Thermidaire Corporation Limited*[21], il s'agissait d'une demande en dommages-intérêts pour violation d'une clause restrictive contenue dans un contrat de distribution. La question de l'injonction n'était pas en litige. Le contrat stipulait que la partie en défaut devrait payer à titre de dommages-intérêts liquidés le profit brut réalisé par la vente des produits concurrents. La question était de savoir si le demandeur pouvait obtenir ce montant ou seulement la réparation du préjudice susceptible d'être prouvé. La majorité de la Cour s'est prononcée en faveur de cette dernière solution. Dans le jugement de la majorité, le Juge en chef a dit en *obiter*, à la p. 335:

[21] [1976] 1 R.C.S. 319.

There is no doubt that a covenantee cannot have both an injunction during the covenant period and damages based on a breach of covenant for the entire period where they are based on a formula. There is case law holding that where a fixed sum is stipulated as the liquidated damages upon a breach, the covenantee cannot have both the damages and an injunction but must elect between the two remedies: see *General Accident Assurance Corp. v. Noel*, [1902] 1 K.B. 377; *Wirth and Hamid Booking Inc. v. Wirth* (1934), 192 N.E. 297. I do not however read these cases as excluding damages for past loss by reason of the breach, but only as precluding recovery of the liquidated amount referable to breach in the future which that amount was designed to cover and against which an injunction has been granted.

Il ne fait pas de doute qu'un créancier ne peut obtenir à la fois une injonction durant la période de la clause et des dommages-intérêts fondés sur une violation toute la période durant lorsque ceux-ci sont basés sur une formule. Il est des arrêts qui ont décidé que lorsqu'une somme fixe est stipulée pour valoir comme montant de dommages liquidés lors d'une violation, le créancier ne peut avoir à la fois les dommages-intérêts et une injonction mais doit choisir entre les deux recours: voir *General Accident Assurance Corp. v. Noel*, [1902] 1 K.B. 377; *Wirth and Hamid Booking Inc. v. Wirth* (1934), 192 N.E. 297. Je n'interprète pas toutefois ces arrêts comme excluant des dommages-intérêts pour une perte passée qui est due à la violation, mais seulement comme empêchant le recouvrement du montant liquidé se rapportant à la violation ultérieure que ce montant était destiné à couvrir et contre laquelle une injonction a été accordée.

The *Campbell, Imrie and Shankland* case, as well as the passages quoted above from *Snider* and *H. F. Clarke*, in my opinion, point up the fact that a plaintiff may have a right to damages in equity in addition to an injunction if he can establish his entitlement under the appropriate equitable considerations. In Ontario, the Court's power to award damages in equity is founded on what is now s. 21 of *The Judicature Act*, R.S.O. 1970, c. 228, which is derived from *Lord Cairns' Act* of 1858. Section 21 provides as follows:

L'arrêt *Campbell, Imrie and Shankland* ainsi que les passages précités des arrêts *Snider* et *H. F. Clarke* soulignent, à mon avis, le fait qu'un demandeur peut avoir droit à des dommages-intérêts en *equity* en plus d'une injonction, s'il peut établir son droit en vertu de considérations d'*equity* pertinentes. En Ontario, le pouvoir des tribunaux d'allouer des dommages-intérêts en *equity* est fondé sur ce qui est maintenant l'art. 21 de *The Judicature Act*, R.S.O. 1970, c. 228, qui dérive de la *Lord Cairns' Act* de 1858. L'article 21 dispose:

21. Where the court has jurisdiction to entertain an application for an injunction against a breach of a covenant, contract or agreement, or against the commission or continuance of a wrongful act, or for the specific performance of a covenant, contract or agreement, the court may award damages to the party injured either in addition to or in substitution for the injunction or specific performance, and the damages may be ascertained in such manner as the court directs, or the court may grant such other relief as is considered just.

[TRADUCTION] 21. Lorsqu'un tribunal est compétent pour connaître d'une demande d'injonction visant la violation d'un engagement, d'un contrat ou d'une convention, ou un acte illicite ou sa continuation, ou l'exécution intégrale d'un engagement, d'un contrat ou d'une convention, le tribunal peut accorder des dommages-intérêts à la partie lésée soit en sus soit à la place de l'injonction ou de l'exécution intégrale et le préjudice peut être constaté de la manière que le tribunal ordonnera, ou le tribunal peut accorder tout autre redressement qu'il considère juste.

It should be remembered that if a plaintiff is entitled to an injunction to restrain breach of a restrictive covenant, he is entitled to prevent the entire breach, not just part of it. Thus, for any part not restrained, he may be entitled to unliquidated damages in equity. There would be no double recovery provided the damages were not referable to any period during which breach was restrained

Il faut se souvenir que si un demandeur a droit à une injonction pour faire interdire la violation d'une clause restrictive, il a le droit d'empêcher la violation totale et pas seulement une partie de cette dernière. Ainsi, pour toute partie non interdite par l'injonction, il peut avoir droit, en *equity*, à des dommages-intérêts non liquidés. Il n'y aura pas double indemnisation, pourvu que les domma-

by the injunction. This right to damages would not be based on the liquidated damages clause, but on the right under s. 21 to damages in equity in substitution for an injunction in respect of the period of breach prior to the granting of the injunction. A plaintiff, of course, cannot delay seeking an injunction in order to inflate his damages. He would not be entitled to damages past the time when he should have sought the injunction.

How then should the measure of such damages be determined? It will generally be appropriate to adopt in equity rules similar to those applicable at law: Spry, *Equitable Remedies* (1971), at pp. 552-4. This is so not because the Court is obliged to apply analogous legal criteria, but because the amount of compensation which would satisfy the loss suffered, and which the Court considers it just and equitable be paid, usually happens to be equivalent to the amount of legal damages which would be appropriate. The award is still governed, however, by general equitable considerations which would not apply if the plaintiff were seeking damages at law rather than in equity. These considerations might serve, for example, to reduce the amount, due to such factors as delay or acquiescence. In addition, if the parties have agreed on a set amount of damages at law, or a maximum amount, it would be unconscionable, in my opinion, to allow recovery of a greater amount of damages in equity.

In the case of a gross underestimate of damages as, presumably, in the present case, the plaintiff may receive an amount equivalent to the liquidated damages sum, plus an injunction, and therefore appear to have double relief. But such is not the case. The injunction relates to the latter part of the period in respect of which the restrictive covenant imposes restraint, the damages (not exceeding the stipulated liquidated damages) relate to the period prior to the granting of the injunction and are in substitution for injunctive relief during that period.

ges-intérêts ne visent pas une période durant laquelle la violation était interdite par l'injonction. Ce droit à des dommages-intérêts ne serait pas fondé sur la clause accordant des dommages-intérêts liquidés, mais sur le droit que donne l'art. 21 à des dommages-intérêts en *equity* à la place d'une injonction pour la période de violation antérieure à celle-ci. Évidemment, un demandeur ne peut pas retarder la demande d'injonction pour gonfler les dommages-intérêts. Il n'y aurait pas droit pour la période suivant le moment où il aurait dû demander l'injonction.

Comment donc déterminer l'importance de ces dommages-intérêts? Il sera généralement approprié d'adopter en *equity* des règles semblables à celles qui sont appliquées en *common law*: Spry, *Equitable Remedies* (1971), aux pp. 552-554. Il en est ainsi non pas parce que la Cour est tenue d'appliquer des critères juridiques similaires, mais parce que le montant de l'indemnité qui répare le préjudice subi, et que la Cour considère approprié en *equity*, est habituellement équivalent aux dommages-intérêts qui seraient appropriés en *common law*. Toutefois l'indemnité est toujours soumise à des considérations générales d'équité qui ne seraient pas applicables si le demandeur actionnait en dommages-intérêts en *common law* plutôt que de le faire en *equity*. Ces considérations peuvent servir, par exemple, à réduire le montant, en raison de facteurs tels que le retard ou l'acquiescement. De plus, si les parties ont convenu d'un montant déterminé de dommages-intérêts en *common law*, ou d'un montant maximum, il serait déraisonnable, à mon avis, d'accorder un montant plus important de dommages-intérêts en *equity*.

Dans le cas d'une sous-évaluation flagrante des dommages-intérêts, comme c'est probablement le cas en l'espèce, le demandeur peut recevoir un montant équivalent aux dommages-intérêts liquidés, ainsi qu'une injonction. Il semble donc ainsi bénéficier d'un redressement double. Mais tel n'est pas le cas. L'injonction se rapporte à la dernière partie de la période d'interdiction visée par la clause restrictive alors que les dommages-intérêts (qui n'excèdent pas les dommages-intérêts liquidés) se rapportent à la période antérieure à l'injonction et remplacent le redressement par injonction pendant cette période.

V

The matter of the right of a plaintiff to recover legal damages for actual loss sustained where a lesser stipulated amount is mentioned was considered in the House of Lords decision in *Cellulose Acetate Silk Company Limited v. Widnes Foundry (1925) Limited*[22]. The amount stipulated was £20 for each week of delay in the erection of an acetone recovery plant. The contractors were thirty weeks late. The actual loss suffered was £5,850. The case is of interest in two respects. First, the recovery was limited to £600, the agreed damages. Second, Lord Atkin, delivering judgment, said that he found it unnecessary to consider what would be the position if the stipulated £20 per week were a penalty, adding, at p. 26:

> It was argued by the appellants that if this were a penalty they would have an option either to sue for the penalty or for damages for breach of the promise as to time of delivery. I desire to leave open the question whether, where a penalty is plainly less in amount than the prospective damages, there is any legal objection to suing on it, or in a suitable case ignoring it and suing for damages.

There is authority indicating that a penalty clause is ineffective even where it is less than the actual loss suffered (see Hals. 4th vol. 12, para. 118, p. 422 and the authorities cited therein). The result would be that actual damages could be recovered which exceeded the amount stipulated as a penalty. To that extent, the proposition appears to me to be contrary to principle and productive of injustice. The foundation of relief in equity against penalties is expressed in Story, *Equity Jurisprudence* (14th ed.) at s. 1728, as follows:

> Where a penalty or forfeiture is designed merely as a security to enforce the principal obligation, it is as much against conscience to allow any party to pervert it to a different and oppressive purpose as it would be to allow him to substitute another for the principal obligation.

[22] [1933] A.C. 20.

V

La question du droit du demandeur d'obtenir des dommages-intérêts pour un préjudice effectivement subi lorsqu'un montant inférieur est stipulé a été examinée dans la décision de la Chambre des lords dans l'affaire *Cellulose Acetate Silk Company Limited v. Widnes Foundry (1925) Limited*[22]. Le montant stipulé était de £20 par semaine de retard dans la construction d'une fabrique de récupération d'acétone. Les entrepreneurs avaient trente semaines de retard. Le préjudice effectivement subi se montait à £5,850. L'affaire est intéressante à deux égards. Premièrement, l'indemnité a été limitée à £600, dommages-intérêts convenus. Deuxièmement, lord Atkin, rendant le jugement, a dit qu'il avait jugé inutile d'examiner quelle serait la situation si les £20 par semaine stipulés constituaient une peine; il ajoute à la p. 26:

> [TRADUCTION] L'appelante a soutenu que, s'il s'agissait d'une peine, elle aurait eu la possibilité d'actionner soit en recouvrement de la peine soit en dommages-intérêts pour violation de l'engagement relatif à la date de livraison. Je ne veux pas me prononcer sur la question de savoir s'il y a une objection juridique à intenter une action en se fondant sur la peine ou, dans un cas pertinent, à y passer outre et à poursuivre en dommages-intérêts, quand la peine est clairement inférieure au montant des dommages-intérêts éventuels.

Selon un courant de jurisprudence, une clause pénale est inefficace même lorsqu'elle est inférieure au préjudice effectivement subi (voir Hals. 4e vol. 12, par. 118, à la p. 422 et la jurisprudence qui y est citée). Il en résulterait que l'on pourrait effectivement obtenir des dommages-intérêts excédant le montant fixé par la clause pénale. Dans cette mesure, cette thèse me paraît contraire aux principes et être injuste. Le fondement du redressement en *equity* par opposition aux clauses pénales est exposé par Story dans *Equity Jurisprudence* (14e éd.), art. 1728, comme suit:

> [TRADUCTION] Lorsqu'une peine ou une déchéance est conçue uniquement à titre de garantie d'exécution de l'obligation principale, il serait tout aussi contraire à la conscience de permettre à une partie de l'utiliser dans un but différent et oppressif que de lui permettre de changer l'obligation principale.

[22] [1933] A.C. 20.

The operation of this relief in the face of contrary agreement by the party is also explained in this section:

> If it be said that it is his own folly to have made such a stipulation, it may equally well be said that the folly of one man cannot authorize gross oppression on the other side.

It is now evident that the power to strike down a penalty clause is a blatant interference with freedom of contract and is designed for the sole purpose of providing relief against oppression for the party having to pay the stipulated sum. It has no place where there is no oppression. If the actual loss turns out to exceed the penalty, the normal rules of enforcement of contract should apply to allow recovery of only the agreed sum. The party imposing the penalty should not be able to obtain the benefit of whatever intimidating force the penalty clause may have in inducing performance, and then ignore the clause when it turns out to be to his advantage to do so. A penalty clause should function as a limitation on the damages recoverable, while still being ineffective to increase damages above the actual loss sustained when such loss is less than the stipulated amount. As expressed by Lord Ellenborough in *Wilbeam v. Ashton*[23]: "Beyond the penalty you shall not go; within it, you are to give the party any compensation which he can prove himself entitled to." Of course, if an agreed sum is a valid liquidated damages clause, the plaintiff is entitled at law to recover this sum regardless of the actual loss sustained.

In the context of the present discussion of the measure of damages, the result is that an agreed sum payable on breach represents the maximum amount recoverable whether the sum is a penalty or a valid liquidated damages clause.

It should be noted that the above principles concern only the situation where there is a single sum specified for breach of the agreement, or a single breach. Where there are different breaches and the agreement provides for a particular sum of

[23] (1807), 1 Camp. 78.

Cet article explique également l'effet du redressement en présence d'une entente en sens contraire entre les parties:

> [TRADUCTION] Si l'on dit que cette stipulation est le fruit de sa propre sottise, on peut tout aussi bien dire que la sottise de l'un ne peut autoriser l'oppression flagrante de l'autre.

Il est maintenant évident que le pouvoir d'annuler une clause pénale constitue une ingérence criante dans la liberté contractuelle et qu'il vise seulement à fournir un redressement contre l'oppression de la partie qui doit payer la somme convenue. Ce pouvoir n'existe pas s'il n'y a pas oppression. S'il s'avère que le préjudice réel excède la peine, les règles normales d'exécution des contrats doivent s'appliquer pour permettre le recouvrement de la somme convenue seulement. La partie qui impose la peine ne doit pas être en mesure de profiter de la force d'intimidation que peut avoir la clause pénale pour forcer l'exécution et ensuite la laisser de côté quand il s'avère avantageux de le faire. Une clause pénale doit servir à limiter les dommages-intérêts recouvrables, tout en restant sans effet pour augmenter les dommages-intérêts au-delà de la perte réelle subie quand cette dernière est inférieure au montant convenu. Comme l'a dit lord Ellenborough dans l'arrêt *Wilbeam v. Ashton*[23]: [TRADUCTION] «N'allez pas au-delà de la peine; dans les limites de cette dernière, accordez à la partie toute l'indemnité qu'elle peut justifier». Évidemment, si une somme fixée est une clause valide de dommages-intérêts liquidés, le demandeur a droit, en *common law*, de recouvrer cette somme indépendamment de la perte effectivement subie.

Dans le contexte de cette discussion sur l'étendue des dommages-intérêts, il ressort qu'une somme fixée, due en cas d'inexécution, représente le montant maximum qu'on peut obtenir qu'il s'agisse d'une clause pénale ou d'une clause valide de dommages-intérêts liquidés.

Il faut souligner que les principes précités s'appliquent uniquement dans les cas où il n'y a qu'une seule somme fixée en cas d'inexécution du contrat, ou d'une seule violation. Lorsqu'il y a plusieurs violations et que le contrat stipule un montant

[23] (1807), 1 Camp. 78.

liquidated damages to be payable for each and every breach, there is no bar to awarding the liquidated damages amount for each breach which has occurred to date of trial, and also awarding an injunction to restrain future breaches. In *Imperial Tobacco v. Parslay*[24] the Court of Appeal held that an agreed sum payable on every breach of a covenant was a recoverable amount of liquidated damages for past breaches, even though an injunction had also been granted to prevent future breaches. In principle, this result is correct. There is no double recovery because the liquidated damages award and the injunction are referable to different breaches.

To summarize:

1. Where a fixed sum is stipulated as and for liquidated damages upon a breach, the covenantee must elect with respect to that breach between these liquidated damages and an injunction.
2. If he elects to take the liquidated damages stipulated he may recover that sum irrespective of his actual loss.
3. Where the stipulated sum is a penalty he may only recover such damages as he can prove, but the amount recoverable may not exceed the sum stipulated.
4. If he elects to take an injunction and not the liquidated sum stipulated, he may recover damages in equity for the actual loss sustained up to the date of the injunction or, if tardy, up to the date upon which he should have sought the injunction, but in either case, not exceeding the amount stipulated as payable upon a breach.
5. Where a liquidated damages sum is stipulated as payable for each and every breach, the covenantee may recover this sum in respect of distinct breaches which have occurred and he may also be granted an injunction to restrain future breaches.

Applying these propositions to the present case, in my view the plaintiff was entitled to an injunc-

[24] [1936] 2 All E. R. 515.

déterminé de dommages-intérêts liquidés pour chacune, rien ne s'oppose à ce qu'on accorde des dommages-intérêts liquidés pour chaque violation jusqu'à la date du procès ainsi qu'une injonction pour prévenir des violations futures. Dans l'arrêt *Imperial Tobacco v. Parslay*[24], la Cour d'appel a jugé qu'un montant fixé, dû à chaque violation d'un engagement, constituait un montant de dommages-intérêts liquidés recouvrable pour des violations passées, quoiqu'une injonction eût également été accordée pour prévenir des violations futures. En principe, ce résultat est approprié. Il n'y a pas double redressement, parce que le versement des dommages-intérêts liquidés et l'injonction se rapportent à des violations différentes.

En résumé:

1. Lorsqu'une somme déterminée est stipulée à titre de dommages-intérêts liquidés en cas de violation, le bénéficiaire doit choisir, à l'occasion de chaque violation, entre ces dommages-intérêts liquidés et une injonction.
2. S'il opte en faveur des dommages-intérêts liquidés convenus, il peut les obtenir indépendamment de la perte réelle qu'il a subie.
3. Quand la somme stipulée est une peine, il peut seulement recouvrer les dommages qu'il peut justifier, mais le montant attribué ne peut pas dépasser la somme stipulée.
4. S'il opte pour l'injonction et non pour le montant liquidé stipulé, il peut obtenir des dommages-intérêts en *equity* pour la perte effectivement subie jusqu'à la date de l'injonction ou, s'il est en retard, jusqu'à la date à laquelle il aurait dû demander l'injonction, mais, dans les deux cas, ces dommages-intérêts ne doivent pas excéder le montant stipulé en cas de violation.
5. Lorsqu'un montant de dommages-intérêts liquidés est stipulé pour chaque violation, le stipulant peut obtenir cette somme relativement à chacune et il peut également obtenir une injonction pour empêcher des violations futures.

Si j'applique ces principes en l'espèce, le demandeur a droit à une injonction et aux dommages-

[24] [1936] 2 All E.R. 515.

tion and such damages as he could prove to date of trial but not to exceed the sum of $1,000.

I would accordingly dismiss the appeal and direct the payment of such damages, not to exceed $1,000, as the respondent can establish in respect of the period from June 1, 1973 to date of trial, for the loss of commission on all contracts of general insurance sold by Elsley during that period, after taking into account expenses incurred in securing and servicing the contracts.

Success has been divided. The respondent sustained the validity of the covenant; the appellant succeeded in limiting damages to the stipulated amount. I would not award costs to either party.

Judgment accordingly.

Solicitors for the appellant: Weir & Faulds, Toronto.

Solicitors for the respondent: Fitzpatrick, O'Donnell & Poss, Toronto.

intérêts qu'il peut justifier jusqu'à la date du procès, sans toutefois dépasser $1,000.

En conséquence, je suis d'avis de rejeter le pourvoi et d'ordonner le paiement des dommages-intérêts que l'intimée pourra établir, mais ne dépassant pas $1,000, pour la période du 1er juin 1973 à la date du procès, au titre des commissions perdues sur tous les contrats d'assurance générale conclus par Elsley au cours de cette période, compte tenu des frais afférents à l'obtention des contrats et aux démarches subséquentes.

Les deux parties ont partiellement gain de cause en l'espèce. L'intimée a fait reconnaître la validité de la clause; l'appelante a réussi à faire limiter les dommages-intérêts au montant stipulé. Je n'adjuge donc les dépens à aucune des parties.

Jugement en conséquence.

Procureurs de l'appelante: Weir & Faulds, Toronto.

Procureurs de l'intimée: Fitzpatrick, O'Donnell & Poss, Toronto.

TAB 5

COURT FILE NO.: 07-29117
DATE: 20070314

ONTARIO

SUPERIOR COURT OF JUSTICE

B E T W E E N:	)	
	)	
FRENCHMEN'S CREEK ESTATES INC., 550075 ONTARIO INC. and JOSEPH ZAWADZKI	)	**George Gligoric, counsel on behalf of the Applicants**
	)	
Applicants	)	
	)	
- and -	)	
	)	
	)	
TUCKERNUCK MORTGAGE ADMINISTRATION INC., TUCKERNUCK MORTGAGE ADMINISTRATION INC., IN TRUST, MATHEWS SOUTHWEST DEVELOPMENTS LIMITED, MSW DALLAS LIMITED and BRUCE BENT	)	**Mark A. Klaiman, counsel on behalf of the Respondents Tuckernuck Mortgage Administration Inc. and Tuckernuck Mortgage Administration Inc., In Trust**
	)	
Respondents	)	**Edwin G. Upenieks, counsel on behalf of the Respondents, Mathews Southwest Developments Limited, MSW Dallas Limited and Bruce Bent**
	)	
	)	
	)	
	)	
	)	**HEARD: March 8 & 9, 2007 (at Hamilton)**

LOFCHIK J.

[1] This is an application for relief from foreclosure judgments obtained against the applicant by the respondent, Tuckernuck Mortgage Investment Inc., In Trust. Each of the

corporate applicants is mortgagor of a separate piece of property and the individual applicant is a guarantor of such mortgages. The lands which are the subject of the mortgages are vacant development lands in the Town of Fort Erie.

FACTS

[2] In or about the year 2001, Joseph Zawadzki had discussions with the respondents, other than Tuckernuck, with respect to development of the subject lands. These discussions never came to fruition. Zawadzki sought financing from the respondents, other than Tuckernuck, who were not prepared to provide the $2,000,000 financing required. The said respondents approached Tuckernuck on behalf of Zawadzki, in order to seek mortgage financing and after investigating the potential mortgage investment, Tuckernuck sourced funds from two individual investors, namely Ruth Kerbel and Michael Finkelstein, and agreed to advance the sum of $2,000,000, which loan was secured by mortgages in that amount on three properties referred to hereinafter as the *“Frenchmen’s Creek property”*, the *“550075 property”*, and the *“Old Willoughby Realty Limited property”*.

[3] The mortgages were registered in favour of Tuckernuck Mortgage Administration Inc., In Trust.

[4] The Frenchmen’s Creek property and the 550075 property were subject to a first mortgage in favour of Yolles Realty Ltd.

[5] When the first mortgages went into default, actions were commenced on the mortgages by Yolles Realty Ltd. in September 2003. In order to secure its position as second mortgagee, Tuckernuck took an Assignment of each first mortgage in December of 2003 upon payment of $340,574.62 with respect to the mortgage on the Frenchmen’s Creek property and $283,658.38 with respect to the mortgage on the 550075 property, and continued with the foreclosure actions.

[6] After Tuckernuck brought motions for judgment in each of the foreclosure actions, negotiations ensued between the parties whereby Minutes of Settlement dated October 4, 2004 were entered into.

[7] The Minutes of Settlement set out terms of payment. The Minutes of Settlement also provided that upon default, Zawadzki, Frenchmen’s and 550075 were provided with a 10-day cure period. Consents to judgment were provided to Tuckernuck to be held in escrow and not to be relied upon unless default

occurred. Tuckernuck specifically agreed that it would not rely upon the consent to judgment for a period of 10 days following default. In consideration for a promise of payment pursuant to the terms of the Minutes of Settlement, the two mortgage actions were stayed and the motions for judgment were adjourned *sine die*.

[8] The Minutes of Settlement dated October 4, 2004 were amended by a letter of agreement dated June 29, 2005. Under the terms of that amendment, Zawadzki had an obligation to make payments at various points in time, more particularly set out in the letter of June 29, 2005. In addition, the parties agreed that the mortgages were to be paid in full by November 27, 2005. The letter of agreement was executed by counsel acting on behalf of Zawadzki, Frenchmen’s Creek Estates and 550075.

[9] Default in payment occurred under the Minutes of Settlement and the appropriate 10 day notice was provided to Zawadzki. Default continued to occur after the 10-day grace period.

[10] On December 1, 2005 solicitors for Tuckernuck wrote to the applicants’ solicitor advising of the default and advising that unless $150,000 was received no later than Monday, December

5, 2005, Tuckernuck would enforce its rights under the Minutes of Settlement. The $150,000 requested was not paid.

[11] On February 15, 2006 Tuckernuck's lawyers wrote to the lawyers for the applicants advising that their clients had been having discussions with Joseph Zawadzki with respect to Zawadzki's attempt to cure the default under the Minutes of Settlement. In that letter the solicitors for Tuckernuck confirmed that such discussions were without prejudice to Tuckernuck's rights under the Minutes of Settlement and that Tuckernuck reserved prior rights to enforce the Minutes of Settlement including reliance on the consents to judgment.

[12] There is a further letter from Tuckernuck's solicitors, dated February 21, 2006 to the applicants' solicitors referring to direct communication between their clients and advising that Zawadzki was advised that Tuckernuck must receive a significant payment on account of the settlement in the amount of $250,000 by February 24, 2006. The letter also advised that Tuckernuck reserved all of its rights under the Minutes of Settlement including the right to rely on the consents to judgment. The $250,000 was not paid by February 24, 2006.

[13] On March 10, 2006 a cheque in the amount of $150,000 payable to Joseph Zawadzki was endorsed over to Tuckernuck with the following endorsement:

> *Payable to Tuckernuck Mortgage Administration Inc. for agreement Frenchmen's Creek, 550075 Ontario Inc., Old Willoughby Realty Ltd.*

[14] There was correspondence from Joseph Zawadzki to Martin Bernholtz on April 27, 2006 and May 5, 2006 concerning the expiry of an Offer to Purchase the Frenchmen's Creek property which had been received but which had expired because of the failure to reach an agreement between the vendor and the purchaser as to the discharge of the Tuckernuck mortgage.

[15] In June of 2006 the solicitor for the applicants wrote to the solicitors for Tuckernuck requesting status statements with respect to the mortgages in question. A further letter with the same request was sent August 15, 2006. On August 15, 2006 Tuckernuck's solicitors sent a mortgage statement with respect to the second mortgages showing a balance due of $2,879,333.12. On September 29, 2006 they forwarded a statement with respect to the two first mortgages on the Frenchmen's Creek and 550075 lands showing a total owing of $890,120.00.

[16] On October 4, Joseph Zawadzki wrote to Tuckernuck advising that the applicants had received an unconditional offer on the Frenchmen's Creek land and advising that the property had been included in the urban boundary of the Town of Fort Erie, zoned residential, and this was being processed by the Region. The letters also raised some issue with respect to the accounting under the mortgages.

[17] On October 17, 2006 Tuckernuck took out the consent judgments for foreclosure on the Frenchmen's Creek property and the 550075 property which it was holding pursuant to the Minutes of Settlement as the mortgages remained unpaid. Copies of these judgments were provided to the solicitor for the applicants under cover of letter dated December 4, 2006. The judgments had been registered on title prior to that letter.

[18] Subsequently this Application was brought and Certificates of Pending Litigation were registered against the subject properties by the applicants.

DISPOSITION

[19] The respondents object to this Application and the venue arguing that the relief sought should be in the foreclosure actions which were commenced in Toronto. Counsel for the applicants argues that there is an outstanding Agreement for Sale on the Frenchmen's Creek property dated June 2006 which will allow for redemption of the mortgages. This Agreement was scheduled to close October 2006 but has been extended to March 14, 2007. The Application could not be heard in Toronto until some time in April 2007 so this Application was brought in Hamilton on the basis of urgency.

[20] In my view, a claim to set aside the foreclosure judgments need not necessarily take place in the context of the foreclosure application. (See ***Lawyers' Professional Indemnity et al v. Geto*** 54 O.R. (3d) 795, para. 16). Alternatively, given the urgency, it is appropriate that leave be granted to deal with this Application in Hamilton.

[21] The applicants seek to set aside the foreclosure judgments on the basis that they had reached an agreement with Bruce Bent, director and officer of Mathews Southwest Developments Limited *("Mathews Southwest")* and MSW Dallas Limited (*"MSW"*) that action would be withheld on the mortgages

until April 27, 2007 in order to allow the sale to close and the mortgages to be redeemed.

[22] The applicants argue that Tuckernuck Mortgage Administration Inc. held the mortgages as trustee for Mathews Southwest and MSW and Bruce Bent had the authority to bind Tuckernuck.

[23] Bruce Bent denies any connection between Tuckernuck and the other respondents and specifically denies that there was any trust relationship or that he made any agreement with respect to the mortgages or that he had any authority to bind Tuckernuck.

[24] Martin Bernholz, in his affidavit, denies any connection between Tuckernuck and the other respondents and denies any agreement not to take action on the mortgages and consent judgments for foreclosure.

[25] Apart from the bald allegations of Joseph Zawadzki there is no evidence of any trust relationship between Tuckernuck and the other respondents, nor is there any evidence

of any agreement to withhold action on the mortgages or consent judgments or that Bruce Bent had authority to bind Tuckernuck.

[26] The evidence before me is to the contrary. I am satisfied that Tuckernuck held the mortgages in trust for Ruth Kerbel and Michael Finklestein to the extent of fifty per cent each. The exhibits to Joseph Zawadzki's affidavit indicate that he was writing to Bruce Bent in September of 2005 requesting that he speak to Tuckernuck and request them not to act on the mortgage and to Martin Bernholz at Tuckernuck with respect to asking him to withhold action on the mortgages. Joseph Zawadzki's correspondence of May 5, 2006 to Martin Bernholz of Tuckernuck and of May 10, 2006 to Bruce Bent, with a copy to Martin Bernholz, causes me to conclude that he was aware that it was Martin Bernholz who had the authority to deal with the Tuckernuck mortgages.

[27] I also conclude that there was no agreement to postpone action on the mortgages. All previous dealings with respect to the mortgages were confirmed in writing. In the case of the agreement being alleged by Joseph Zawadzki, there is nothing in writing between the parties. Nor is there any

contemporaneous writing from either Joseph Zawadzki or his counsel, confirming any agreement.

[28] For these reasons the applicants' argument for relief on the basis of an agreement not to act on the consent judgments, which is binding on Tuckernuck, fails.

[29] The applicants argue that they were entitled to reasonable notice in order to remedy their default before Tuckernuck could take action and utilize the consent judgments and rely on the decision in ***Murano v. Bank of Montreal***, 41 O.R. (3d) 222 (C.A.). This case can be distinguished on its facts from ***Murano***. Here the creditor was acting under the terms of Minutes of Settlement in which the respondents specifically waive notice of default as they were aware of the due dates for payments referred to in the Minutes and that failure to make payment constituted default. In any event, the correspondence from Tuckernuck's counsel to the applicants' counsel referred to above, indicated that Tuckernuck was reserving its rights to rely on the Minutes of Settlement and consent judgments and the applicants continued in default under the terms of the Minutes of Settlement. The applicants' arguments in this regard must fail.

[30] The applicants also seek to set aside the foreclosure on equitable grounds and argue that they were in a position to satisfy the requirements set out in ***Royal Bank of Canada v. Swan*** [1979] 2 A.C.W.S. 159 (Ont. S.C.) aff'd. (1980), 3 A.C.W.S. (2d) 341 (Div. Ct.).

[31] In my view the applicants in this case meet three of the four requirements, in that they acted with reasonable promptness once they became aware of the foreclosure judgment, there had been activity on the part of the applicants to raise money necessary to redeem on time and the applicants have a substantial interest in the mortgaged property. However, I am not satisfied that they meet the fourth condition, that is that they had a reasonable prospect of paying the amount due under the mortgage at once or in a short period of time after the judgment was taken out. Even at this point in time, given that there is a sale of the property in question, there would not be sufficient cash generated from the sale to pay out the mortgages when the sale closes. The applicants argue that they can raise money to pay out the mortgages by borrowing on the strength of the take back mortgage which they are to obtain on the closing of the sale. The only thing they have to support this argument is a three-line letter dated February 23, 2007 conditional upon

the lender's solicitor being satisfied with title. In my view this is too little, too late and does not meet the requirements of the ***Swan*** case set out above as the relevant question is whether the mortgagors were in a position to redeem at the time of judgment. It appears clear in this case that they were not.

[32] In any event the relevant issue here, in my view, is not equitable discretion to redeem after foreclosure, but an issue of breach of contract. A consent order is, in effect, a contract which can only be set aside or varied by subsequent consent, upon grounds of common mistake, misrepresentation or fraud or on any other ground that would invalidate a contract. (see ***Chaitel v. Rothbart*** [1984] 40 2 C.P.C. 217 aff'd. [1985] 2 C.P.C. (3d) para. 25; ***McCowan v. McCowan*** [1995] 24 O.R. (3d) 707 paras. 16-18). Those grounds do not exist here.

[33] In this case the parties came to settlement arrangements with respect to the mortgage claims and recorded that arrangement in Minutes of Settlement. It would be contrary to the orderly administration of justice for this Court not to enforce the Minutes of Settlement. The simple fact is that the applicants entered into Minutes of Settlement and have almost continuously been in default under the terms of such Minutes. It

appears evident that entering into the Minutes of Settlement was an unsuccessful attempt to buy more time. It follows that the respondent, Tuckernuck, should be allowed the remedies that the parties agreed to in such Minutes. The consent foreclosure judgments will not be set aside.

[34] As there is no factual basis for the other heads of relief sought in the Notice of Application, the Application is dismissed in its entirety. The Certificates of Pending Litigation registered against the Frenchmen's Creek Property and the 550075 Property are hereby set aside.

[35] The respondents are entitled to their costs. If the parties cannot agree on costs, I will entertain a motion to fix costs at a mutually convenient time.

_____

LOFCHIK J.

Released: March 14, 2007

COURT FILE NO.: 07-29117
DATE: 20070314

ONTARIO

SUPERIOR COURT OF JUSTICE

B E T W E E N:

FRENCHMEN'S CREEK ESTATES INC., 550075 ONTARIO INC. and JOSEPH ZAWADZKI

Applicants

- and –

TUCKERNUCK MORTGAGE ADMINISTRATION INC., TUCKERNUCK MORTGAGE ADMINISTRATION INC., IN TRUST, MATHEWS SOUTHWEST DEVELOPMENTS LIMITED, MSW DALLAS LIMITED and BRUCE BENT

Respondents

REASONS FOR JUDGMENT

LOFCHIK J.

TRL/sh

Released: March 14, 2007

TAB 6

CITATION: Frenchmen's Creek Estates Inc. v. Tuckernuck Mortgage Administration Inc., 2008 ONCA 107

DATE: 20080214
DOCKET: C46994

COURT OF APPEAL FOR ONTARIO

FELDMAN, MacFARLAND and WATT JJ.A.

BETWEEN:

FRENCHMEN'S CREEK ESTATES INC., 550075 ONTARIO INC. and JOSEPH ZAWADZKI

Applicants (Appellants)

and

TUCKERNUCK MORTGAGE ADMINISTRATION INC., TUCKERNUCK MORTGAGE ADMINISTRATION INC., IN TRUST, MATHEWS SOUTHWEST DEVELOPMENTS LIMITED, MSW DALLAS LIMITED and BRUCE BENT

Respondents (Respondents in Appeal)

John F. Evans, Q.C. and Andrea M. Hill for the appellants

Diana M. Edmonds for the respondents Tuckernuck Mortgage Administration Inc.

Edwin G. Upenieks for the respondent Mathews Southwest Developments Limited

Heard and released orally: February 6, 2008

On appeal from the order of Justice Thomas R. Lofchik of the Superior Court of Justice, dated March 14, 2007

ENDORSEMENT

[1] The appellants' appeal is from an order of Justice Lofchik refusing to give relief from the foreclosure judgments obtained *ex-parte* by the respondents.

[2] On the appeal, it became clear that Justice Lofchik did not have before him the record that was placed before Justice Echlin to obtain the *ex-parte* orders. That record is before us on the appeal and discloses that on the first attempt to obtain the *ex-parte* orders from Justice Rouleau (as he then was), Justice Rouleau required disclosure of the calculation and justification of the amount of the consent judgments, the form of which was signed in blank by the appellants as part of the Minutes of Settlement.

[3] The respondents then re-filed the *ex-parte* foreclosure motions with affidavits from Mr. Bernholtz which included an accounting that showed no monies had been paid on the Yolles first mortgages. Those affidavits failed to properly account for monies paid by the appellants which under paragraph 2 and 3 of the Minutes of Settlement had to be credited to the Yolles first mortgages. Because the material before Justice Echlin did not constitute full, fair and frank disclosure as required on an *ex-parte* motion, those orders should have been set aside by Justice Lofchik and we are satisfied they would have been had he been aware of this problem.

[4] We therefore allow the appeal from Justice Lofchik, set aside his order and set aside the *ex-parte* foreclosure orders of Justice Echlin. The record before us does disclose an ongoing financial default by the appellants. The respondents are entitled to seek appropriate remedies, as advised, on proper notice to the appellants.

[5] In the result, the appeal is allowed and the portion of the judgment of Justice Lofchik that refused to set aside the foreclosures is set aside. The portion of the judgment of Justice Lofchik that dismissed the application in respect of Matthews and Bent is not set aside by this court.

Costs

[6] Costs of the appeal to the appellants paid by the Tuckernuck respondents are in the amount of $20,000 inclusive of disbursements and G.S.T. on the partial indemnity scale. The Matthews respondents are entitled to their costs of the appeal from the appellants on the partial indemnity scale fixed at $12,000 inclusive of disbursements and G.S.T. The costs order of Justice Lofchik as between the appellants and Tuckernuck respondents is set aside. If the parties cannot agree on the amount to be paid to the appellants for such costs, they shall be fixed by the application judge.

Signed: "K. Feldman J.A."

"J. MacFarland J.A."

"David Watt J.A."

TAB 7

CITATION: Goodfellow v. CUMIS General Insurance Company, 2021 ONSC 3604
COURT FILE NOS.: CV-21-00658241-00CL
CV-21-00658643-00CL
CV-21-00655599-00CL
CV-21-00656590-00CL
CV-21-00655627-00CL
DATE: 20210518

SUPERIOR COURT OF JUSTICE - ONTARIO

RE: **CV-21-00658241-00CL**

IAN GOODFELLOW, WENDY MITCHELL, NEIL WILLIAMSON, PAULINE WAINWRIGHT, DEBORAH BAKER, BRENT BAILEY, JIM TINDALL, PETER REBELLATI, AL JONES, AND GEIRGE POHLE, Applicants

AND:

CUMIS GENERAL INSURANCE COMPANY, Respondent

AND:

FINANCIAL SERVICES REGULATORY AUTHORITY OF ONTARIO, in its capacity as the Administrator of PACE SAVINGS & CREDIT UNION INC., Intervenor

CV-21-00658643-00CL

FRANK KLEES and KLEES and ASSOCIATES, Applicants

AND:

CUMIS GENERAL INSURANCE COMPANY, Respondent

CV- 21-00655599-00CL

LARRY SMITH, Applicant

AND:

CUMIS GENERAL INSURANCE COMPANY, Respondent

CV-21-00656590-00CL

PHILLIP SMITH, Applicant

AND:

CUMIS GENERAL INSURANCE COMPANY, Respondent

CV-21-00655627-00CL

BRIAN HOGAN, Applicant

AND:

CUMIS GENERAL INSURANCE COMPANY, Respondent

BEFORE: Cavanagh J.

COUNSEL: *Steven Stieber*, for the Goodfellow Applicants

Michael A. Cohen, for the Applicants, Frank Klees and Klees and Associates

Alistair Crawley and *Clarke Tedesco*, for the Applicant, Larry Smith

Steven Weisz and *Pat Corney*, for the Applicant, Phillip Smith

Victor L. Vandergust, for the Applicant, Brian Hogan

Thomas J. Donnelly and *Joyce Tam*, for the Respondent, CUMIS General Insurance Company

Jason Wadden and *Michael Wilson*, for the Intervenor in Goodfellow application, Financial Services Regulatory Authority of Ontario, in its capacity as the Administrator of PACE Savings & Credit Union Ltd.

HEARD: April 20, 2021

ENDORSEMENT

Introduction

[1] There are five applications before me. The applicants are former directors of PACE Savings & Credit Union Limited ("PACE"), a credit union. An action has been brought against the applicants in the name of PACE by its regulator and administrator, the Financial Services Regulatory Authority ("FSRA").

[2] In these applications, the applicants seek a declaration that CUMIS General Insurance Company ("CUMIS") is obligated to defend the applicants in this underlying claim pursuant to a Directors' and Officers' Liability Policy (the "D&O Policy") issued by CUMIS.

[3] For the following reasons, I conclude that CUMIS is obligated under the D&O Policy to defend the applicants in the underlying claim.

Factual background

[4] The FSRA is the regulator of credit unions in Ontario pursuant to the *Credit Unions and Caisses Populaire Act, 1994* (the "Act"). On June 8, 2019, the FSRA amalgamated with the Deposit Insurance Corporation of Ontario, the former entity that carried out the regulation of credit unions in Ontario under the Act. For ease of reference, I refer to the regulator as FSRA, regardless of whether the event described took place before or after June 8, 2019.

[5] The FSRA administers deposit insurance to members of Ontario's credit unions. It is the regulatory supervisor and, where required, the administrator and liquidator of credit unions (as those terms are defined in the Act).

[6] PACE is a credit union incorporated under the Act and is regulated by the FSRA. As a credit union, PACE is owned and controlled by its members.

[7] The Applicants are each former members of the Board of Directors of PACE.

[8] CUMIS is an Ontario-based insurance company which provides, among other things, insurance products and services to credit unions, caisses populaires, and their members in Canada.

[9] CUMIS issued the D&O Policy for the policy period January 1, 2018 through January 1, 2019. Capitalized words in the D&O Policy have the meanings in the "Definitions" section of the policy.

[10] The D & O Policy provides the following coverage to the applicants:

> Subject to the terms and conditions of this Policy, the Insurer will pay on behalf of:
>
> For a DIRECTOR OR OFFICER, any of the following:
>
> 1. All LOSS arising from any CLAIM first made against such DIRECTOR OR OFFICER during the POLICY PERIOD, for which the DIRECTOR OR OFFICER is not indemnified by the CORPORATION.
> 2. All LOSS arising from any CLAIM first made against such DIRECTOR OR OFFICER during the POLICY PERIOD, and for which they become legally obligated to pay solely as a result of INSOLVENCY of the CORPORATION.

[11] The D & O Policy provides that it shall not apply to loss based upon, arising out of, or attributable to:

> A CLAIM by or on behalf of the CORPORATION or a DIRECTOR OR OFFICER except for a CLAIM:
>
> a. that is a derivative action brought or maintained on behalf of the CORPORATION by a person who is not a DIRECTOR OR OFFICER without the cooperation, solicitation, assistance or active participation of the CORPORATION or any DIRECTOR OR OFFICER; ...
>
> ...
>
> e. brought or maintained by a liquidator, receiver, or trustee in bankruptcy and made directly against a DIRECTOR of the CORPORATION and then only for DEFENCE COSTS, to the extent that they are covered under this policy.

[12] Following an investigation into various transactions and conduct that had occurred or were occurring at PACE, the FSRA issued an Administration Order dated September 28, 2018 and took control of PACE as administrator. This ultimately resulted in the Board of Directors of PACE being rendered functus and the employment of the former CEO and former president being terminated for cause. Pursuant to the Administration Order, the FSRA as administrator took control of PACE and now exercises the powers of the Board of Directors and controls the management of PACE.

[13] By Notice of Action issued on March 18, 2019, a claim was commenced by the FSRA as administrator for PACE. In the Fresh as Amended Statement of Claim dated October 11, 2019 (the "Underlying Claim"), the plaintiff is identified as "PACE Savings & Credit Union Limited, by its administrator, Financial Services Regulatory Authority". In the Underlying Claim, the plaintiff makes claims for damages suffered by PACE caused by wrongful conduct allegedly engaged in by the defendants against PACE including breaches of duties owed to PACE.

[14] CUMIS was provided with notice of the Underlying Claim and the applicants requested coverage under the D&O Policy.

[15] On October 25, 2019, CUMIS denied coverage for the Underlying Claim on the basis of the "Insured vs. Insured" exclusion in the D&O Policy.

Analysis

[16] CUMIS acknowledges that the Underlying Claim against the Applicants falls within the insuring agreement of the CUMIS policy, for purposes of the duty to defend.

[17] The issues to be decided on these applications are:

a. whether the "Insured vs. Insured" exclusion applies to the claim brought in the name of PACE by the FSRA against PACE's officers and directors;

b. whether the "derivative action" exception to the "insured vs. insured" exclusion restores coverage for the claim;

c. whether the "liquidator" exception to the "insured vs. insured" exclusion restores coverage for the claim; and

d. whether, if there is coverage for the defence of the Underlying Claim, the applicants are entitled to retain and instruct counsel of their choice without the need to report to or take instructions from CUMIS.

Legal principles applicable to interpretation of policies of insurance

[18] An insurer is required to defend an action in which the pleadings allege facts which, if true, could possibly require the insured to indemnify the insured on a claim. The mere possibility that a claim within the policy may succeed is sufficient to trigger the insured's duty to defend: *Progressive Homes v. Lombard General Insurance Co. of Canada*, 2010 SCC 33, at para. 19.

[19] In *Progressive*, at paras. 22-28, the Supreme Court of Canada reviewed the following principles to be applied to the interpretation of insurance policies (in that case, a comprehensive general liability policy):

a. The primary interpretive principle is that when the language of the policy is unambiguous, the court should give effect to clear language, reading the contract as a whole.

b. Where the language of the insurance policy is ambiguous, the courts rely on general rules of contract construction. For example, courts should prefer interpretations that are consistent with the reasonable expectations of the parties, so long as such an interpretation can be supported by the text of the policy.

c. Courts should avoid interpretations that would give rise to an unrealistic result or that would not have been in the contemplation of the parties at the time the policy was concluded.

d. Courts should also strive to ensure that similar insurance policies are construed consistently.

e. When these rules of construction fail to resolve an ambiguity, courts will construe the policy contract *contra proferentem* - against the insurer. One corollary of the *contra proferentem* rule is that coverage provisions are interpreted broadly, and exclusion clauses narrowly.

f. Exceptions to exclusions do not create coverage - they bring an otherwise excluded claim back within coverage, where the claim fell within the initial grant of coverage in the first place.

g. Because of this alternating structure, it is generally advisable to interpret the policy in the order of coverage, exclusions and then exceptions.

[20] In *Sabean v. Portage La Prairie*, [2017] 1 S.C.R. 121, the Supreme Court of Canada confirmed, at para. 12, that the overriding principle is that where the language of the disputed clause is unambiguous, reading the contract as a whole, effect should be given to that clear language. Only where the disputed language in the policy is found to be ambiguous should general rules of contract construction be employed to resolve that ambiguity. If these general rules of construction fail to resolve the ambiguity, courts will construe the contract *contra proferentem*, and interpret coverage provisions broadly and exclusion clauses narrowly.

[21] In *Markham v. AIG Insurance Company of Canada*, 2020 ONCA 239, the Court of Appeal, at para. 45, confirmed that the language of the policy is construed in accordance with the usual rules of construction rather than inferred "expectations" not apparent on a fair reading of the document. The Court of Appeal held that this is particularly so in the case of commercial insurance policies involving sophisticated parties. The insurer must explicitly state the basis on which coverage may be limited.

Does the Insured vs. Insured exclusion apply?

[22] The D&O Policy expressly provides that it shall not apply to loss based upon, arising out of, or attributable to a claim "by or on behalf of" of PACE, except for claims specified.

[23] The applicants submit that this exclusion was intended to provide protection for insurance companies against collusive suits between insured corporations and their insured officers and directors. They submit that when the plaintiff is not the insured corporation, but a representative acting as a genuinely adverse party to the defendant officers and directors, there is no threat of collusion and the underlying rationale for the exclusion does not apply. The applicants contend that to interpret the D&O Policy such that the Underlying Claim is excluded from coverage would result in the virtual nullification of the coverage provided by the D&O Policy and would be contrary to the reasonable expectations of the ordinary person as to the coverage afforded.

[24] In *Stuart v. Hutchins*, 1998 CarswellOnt 3540, the insured argued that to construe the notice provision in the policy as the insurer submitted it should be read would contravene the spirit of s. 129 of the *Insurance Act* providing for relief against forfeiture. The Court of Appeal, at paras. 28-30, did not accept that the language of the policy should be interpreted to avoid this outcome:

> On a more fundamental level, the position advanced by RE/MAX is one which leads inexorably to the discarding of basic principles that

> have long governed the interpretation and construction of contracts of insurance.
>
> To the extent that the wording in a contract of insurance is found to be ambiguous, it is accepted that the ambiguity will generally be resolved in favour of the insured. This rule, however, has no application where the wording of the policy is plain on its face and capable of only one meaning.
>
> Trite though it may be, an insurer has the right to limit coverage in a policy issued by it and when it does so, the plain language of the limitation must be respected.

[25] I observe that the question of collusion is not implicated by the language of the exclusion itself. The question of collusion between the insured corporation and officers or directors is addressed in the D&O Policy by the language of an exception to the exclusion, where the claim is a derivative action brought or maintained on behalf of the insured corporation by a person who is not a director or officer, "without the cooperation, solicitation, assistance or active participation of the CORPORATION or any DIRECTOR or OFFICER".

[26] The language of the exclusion, when the D&O Policy is read as a whole, is not ambiguous. The "Insured vs. Insured" exclusion applies because the Underlying Claim is brought by FSRA on behalf of PACE.

Does the exception to the exclusion relating to a "derivative action" apply so as to restore coverage?

[27] The Applicants argue that if coverage is excluded by the Insured vs. Insured exclusion, the exception to the exclusion relating to a claim that is a "derivative action" applies such that coverage is restored.

[28] This exception in the D&O Policy to the "Insured vs. Insured" exclusion reads:

> ... except for a CLAIM:
>
> a. that is a derivative action brought or maintained on behalf of the CORPORATION by a person who is not a DIRECTOR OR OFFICER, without the cooperation, solicitation, assistance or active participation of the CORPORATION or any DIRECTOR OR OFFICER;

[29] CUMIS submits that this exception does not apply for two reasons. First, CUMIS submits that the exception only applies where a derivative action is brought or maintained on behalf of the insured by a "person", and that neither FSRA nor CUMIS is a "person" as that word

should be interpreted when used in the D&O Policy. Second, CUMIS submits that the Underlying Claim is not a "derivative action". I address each of these arguments in turn.

[30] The word "person" is not defined in the D&O Policy. In the absence of a definition, it is necessary to give meaning to this word following the application of principles of interpretation of insurance policies. Where the language in an exception is unambiguous, I must give effect to the clear language, reading the policy as a whole. Where the language is not unambiguous, I must rely on general rules of contract construction. If the ambiguity is not then resolved, I am to construe the D&O Policy against CUMIS according to the doctrine of *contra proferentem* and, in so doing, interpret the exception broadly and the exclusion narrowly.

[31] The *Financial Services Regulatory Authority of Ontario Act, 2016*, S.O. 2016, c. 37, Sch. 8 provides in s. 2(1) that "the predecessor Authority and DICO [Deposit Insurance Corporation of Ontario] are amalgamated and shall continue as one corporation without share capital under the name Financial Services Regulatory Authority of Ontario ...". Section 6(1) of this statute provides that FSRA "has the capacity, rights, powers and privileges of a natural person for carrying out its objects, subject to the limitations of this Act". It is clear that the FSRA is a corporation which has the capacity, rights, powers and privileges of a natural person for carrying out its objects.

[32] Apart from the statutory power of FSRA to bring an action, a corporation, generally, is capable of making a "CLAIM" (as this word is defined in the D&O Policy) and bringing an action. A corporation is a creature of statute and a legal "person" when this word is used in the context of a corporation making a claim or bringing an action. In this context, the ordinary meaning of the word "person" would generally include a corporation.

[33] The *Legislation Act, 2006*, R.S.O. 2006, c. C-21, Sch F provides in s. 87 that in every Act and regulation, "person" includes a corporation. The D&O Policy includes a condition which states that "[t]erms of this Policy which are in conflict with any statute of the province or territory in which it is issued are amended to conform to such statute". Although I do not hold that to interpret the word "person" as used in the D&O Policy to mean only a human being would conflict with the *Legislation Act, 2006* (which does not apply to contracts such as insurance policies), I find support in this statutory provision for my conclusion that the ordinary meaning of the word "person", when used in a contractual provision in reference to a "person" who brings an action, includes a corporation.

[34] CUMIS contends, however, that the D&O Policy, read as a whole, makes a clear distinction between "persons" and "entities", and that "persons" is used to refer to human beings and "entities" is used to refer to corporations or other entities which are not human beings. CUMIS submits that different words used in an insurance policy are presumed to have different meanings and that PACE and FSRA are "entities", and not "persons". Therefore, CUMIS submits, the derivative action exception does not apply.

[35] CUMIS points to several terms in the D&O Policy which refer to a "person or entity" (the definitions of "Change of Control", "Co-operation", and "Subrogation"). CUMIS points to

other terms which refer to "the entity", "an entity", or "any entity" (the definitions of "Corporation", "Predecessor", and "Subsidiary"; and the condition with respect to an "entity" which has undergone a change of control), without also referring to a "person". CUMIS points to other policy terms which refer only to "any person" (the Bodily Injury and Property damage exclusion) or to "a person" (definition of "Employee"), without also referring to an "entity".

[36] In those paragraphs in the D&O Policy in which the word "entity" is used, and not the words "person or entity", the context of the policy term indicates that the word "entity" does not refer to a human being. In these policy terms, the context does not require more than the use of the word "entity" to give it the meaning that is intended.

[37] In other policy terms, where the words "person or entity" are used, these words apply broadly to capture any person or entity, human, corporate, or other. A human or a non-human person or entity is able to acquire ownership of securities. A human or a non-human person or entity is able to execute documents or render assistance to the insurer. The insurer may have rights of subrogation against a human or a non-human person or entity, including a corporation, a partnership, an unincorporated association, or any legal entity capable of being sued.

[38] In other terms of the D&O Policy, the word "person" is used in a context that indicates that the word refers to a human person and not a corporation where, for example, the policy refers to "bodily injury, sickness, disease, mental anguish or death of any person".

[39] It does not follow, however, that because the word "entity" is used in the D&O Policy in contexts where the word does not refer to a human being, and the word "person" is used elsewhere in the policy in contexts where the word does not refer to a corporation or other non-human entity, the word "person" must be given a narrower meaning than its ordinary meaning where the context does not so require. In the exception to the Insured vs. Insured exclusion, the context in which the word "person" is used does not require that the "person" making the "CLAIM" that is a derivative action ..." must be a human being. An individual member of a credit union could make a claim that is a derivative action as could a member of a credit union that is a corporation.

[40] CUMIS argues that the reference in the exception itself to a "person who is not a DIRECTOR OR OFFICER" can only refer to a human being. I disagree. A derivative action may be brought or maintained by an individual who is not an officer or director or by a corporation which is not, and cannot be, an officer or director. In either case, if the meaning of the word "person" includes a corporation, the exception would apply.

[41] CUMIS also relies on the definition of the capitalized word "CORPORATION" in the D&O Policy to mean "[t]he entity named as the Insured in the Declarations or Certificate ..." in support of its submission that a corporation is an "entity" as that word is used in the D&O Policy but not a "person". I disagree that this definition assists CUMIS. The word "CORPORATION" is a defined term in the D&O Policy that means the insured, PACE, which is a corporation described as an "entity". It does not follow, however, that where the

word “person” is used in other terms of the D&O Policy, the meaning to be given to this word must exclude a corporation where the context does not so require.

[42] I observe that the D&O Policy does not consistently use the word “person” to refer to a human being. In the exclusion dealing with “Outside Directorship”, the D&O Policy refers to “[a]ny act of an individual while serving as a director ...” CUMIS submits that the word “individual” has the same meaning as “person”, and both refer to a human being. I agree that the word “individual” as used in this policy term means a human being. I do not agree, however, that the meaning of the word “person” where it is used elsewhere in the D&O Policy is limited to a human being, unless the context so requires. The ordinary meaning of the word “person” is broader than the ordinary meaning of the word “individual”. Because these two words are each used in the D&O Policy, I presume that, depending on the context in which each is used, the words do not necessarily have the same meaning.

[43] When I consider the language of the exception in the context of the D&O Policy as a whole, I do not agree that the word “person” should be given a meaning other than its ordinary meaning, which, in the context of a person making a claim or bringing an action, includes both an individual and a corporation. It is not necessary to give this word a narrower and more limited meaning. The purpose of the exception applies to both individuals and corporations. If CUMIS wished to limit its risk and exclude coverage for a person bringing a derivative action which is a corporation, it could have done so using clear language. I conclude that the language of the exception is not ambiguous and the word “person”, as used in the exception, includes a person that is a corporation.

[44] If I had concluded that the meaning of the word “person” as used in the exception is ambiguous, I would consider the reasonable expectations of the parties to give meaning to this word. The D&O Policy provides coverage to a director or officer for a loss arising from any claim first made against such director or officer for which the director or officer is not indemnified by PACE. The exception to the exclusion for a claim by or on behalf of PACE that is a derivative action does not expressly limit its application to a claim that is a derivative action brought by an individual. The stated purpose of the D&O Policy is to ensure PACE’s officers and directors against loss from claims made for breach of duty. This purpose would be severely restricted if suits initiated by the FSRA, the regulator of PACE, were not covered.

[45] Given the stated purpose of the D&O Policy, to give the word “person” the narrow meaning advanced by CUMIS would be contrary to the reasonable expectations of an ordinary person as to the coverage purchased. See *Zurich Insurance Co. v. 686234 Ontario Ltd*., [2002] O.J. No. 4496 (ONCA), at para. 28.

[46] The interpretation of “person” as used in the exception to include a corporation is consistent with the reasonable expectations of the parties and supported by the text of the D&O Policy. To give the word “person” the restrictive meaning advanced by CUMIS would lead to unreasonably restrictive coverage because it would exclude coverage for claims by FSRA, the regulator of PACE, one of the most significant risks faced by directors of a credit union. If I had concluded that the language of the exception is ambiguous, I would conclude that

after applying these rules of construction, the D&O Policy should not be given the restrictive interpretation advanced by CUMIS.

[47] If, after applying rules of construction to resolve ambiguity, I had held that the meaning of the word "person" in the exception remained ambiguous, I would apply the *contra preferentem* rule and interpret the D&O Policy against CUMIS by giving the language of the exception a broad interpretation which includes a corporation within the meaning of the word "person".

[48] The second submission made by CUMIS is that the Underlying Claim is not a "derivative action" within the meaning of this phrase in the exception.

[49] CUMIS submits that the term "derivative action" is a term of art which has a meaning recognized under Ontario law and that the Underlying Claim does not fall within any of the types of derivative actions so recognized. In support of this submission, CUMIS contends:

a. The Underlying Claim is not a derivative action under s. 246 of the Ontario *Business Corporations Act* ("OBCA") because that statute does not apply to corporations to which the Act applies.

b. Prior to the enactment of statutory provisions like s. 246 of the *OBCA*, a common law derivative action for shareholders existed through exceptions to the rule in *Foss v. Harbottle*. The Underlying Claim does not qualify as a common law derivative action because the conditions precedent to such an action have not been fulfilled. The action is not brought by minority shareholders on behalf of the credit union.

c. The PACE action is not a derivative action under s. 50 (1) of the *Act* which, CUMIS contends, is the only derivative action available in Ontario in the credit union context and, given this, the "derivative action" exception to the "insured versus insured" exclusion can only refer to the s. 50 derivative action.

[50] In *Rea v. Wildeboer*, 2015 ONCA 373, the question before the Court was whether a complainant may assert by way of an oppression remedy proceeding a claim that is by nature a derivative action for a wrong done to the corporation, thereby circumventing the statutory requirement to obtain leave to commence such an action. In its analysis, the Court of Appeal for Ontario described, at para. 18, the nature of a "derivative action" under the OBCA:

> The derivative action was designed to counteract the impact of *Foss v. Harbottle* by providing a "complainant" - broadly defined to include more than minority shareholders - with the right to apply to the court for leave to bring an action "in the name of or on behalf of the corporation ... for the purpose of prosecuting, defending or discontinuing the action on behalf of the body corporate": *Business Corporations Act*, RSO 1990, c. B. 16, s. 246 ("OBCA"). It is an action for "corporate" relief, in the sense that the goal is to recover

> for wrongs done to the company itself. As Professor Welling has colourfully put it in his text, *Corporate Law in Canada: The Governing Principles,* 3rd ed. (Mudgeeraba: Scribblers Publishing, 2006), at p. 509, "[a] statutory representative action is the minority shareholder's sword to the majority's twin shields of corporate personality and majority rule."

[51] Although in *Rea v. Wildeboer* the legal basis for the derivative action was the OBCA, the nature of a derivative action, as described by the Court of Appeal, is one brought by a person in the name of or on behalf of a corporation to recover for wrongs done to the corporation itself. The term "derivative action" describes such an action. This meaning of the term "derivative action" is consistent with the language of the exception in the D&O Policy which refers to a "derivative action brought or maintained on behalf of the CORPORATION by a person who is not a DIRECTOR OR OFFICER ...".

[52] CUMIS also maintains that s. 50 of the Act does not apply to the Underlying Claim because it was not brought by a credit union member, and no leave was obtained from the court permitting the start of the action. CUMIS contends that there is no other type of "derivative action" known to law which could possibly apply to the Underlying Claim.

[53] Subsections 50(1) and (2) of the Act provide:

> Members may maintain representative actions
>
> 50(1) Subject to subsection (2), a member of a credit union may maintain an action in a court of competent jurisdiction in a representative capacity for the member and all other members of the credit union suing for and on behalf of the credit union to enforce any right, duty or obligation owed to the credit union under this Act or under any other statute or rule of law or equity that could be enforced by the credit union itself, or to obtain damages for any breach of any such right, duty or obligation.
>
> (2) An action under subsection (1) shall not be started until the member has obtained an order of the court permitting the start of the action.

[54] The D&O Policy, in the exception to the "Insured v. Insured" exclusion, does not limit the words "derivative action" to a derivative action brought under s. 50 of the Act. As I have noted, the term "derivative action" is not defined in the D&O Policy, although many other words are defined. If CUMIS had intended to give particular meaning to the term "derivative action", or to limit it to an action brought under s. 50 of the Act, it could have done so using clear language. In the absence of a meaning assigned to this term through a definition in the D&O Policy, the term "derivative action" must be given a meaning having regard to the context in which it is used in the D&O Policy, reading the policy as a whole.

[55] I do not accept the submission by CUMIS that a derivative action is a term of art limited to a common law derivative action by a minority shareholder of a corporation, a statutory derivative action under the OBCA or the federal corporate statute, or an action brought under s. 50 of the Act. In making this submissions, CUMIS conflates the common law or statutory requirements for a person to bring an action in the name of or on behalf of a corporation with the action itself. At common law, and under the federal and provincial corporate statutes, a shareholder of a company may only bring an action in a representative capacity on behalf of a company for remedies available to the company in respect of a wrong done to it if certain requirements are satisfied. Under s. 50 of the *CUCP Act*, a member of a credit union may maintain an action described in this provision in a representative capacity provided that the member has obtained a court order permitting the start of such an action. These requirements are legal rules that, where they apply, specify who may bring such an action and when it may be brought. They do not, however, change the nature of the action.

[56] The nature of the Underlying Claim is clear from the Fresh as Amended Statement of Claim in which PACE, by its administrator, FSRA, sues for wrongful acts by the defendants against PACE. In the Fresh as Amended Statement of Claim, the plaintiff claims remedies for losses suffered by PACE, as pleaded in paragraph 26:

> Through the Investigation, the Administrator and the Credit Union learned that the conduct of the Defendants, individually and collectively, had resulted in the Credit Union suffering material losses which in some instances, are continuing. The basis of each of the claims against the Defendants is outlined in detail below.

[57] In paragraph 146 of the Fresh as Amended Statement of Claim, the plaintiff pleads that each of the defendants has engaged in wrongful conduct against PACE:

> Each of the Defendants has engaged in wrongful conduct against the Credit Union. Such wrongful conduct includes, but is not limited to, fraud, deceit, breach of fiduciary duties, breach of employment duties, negligence, conversion, unjust enrichment, breach of trust, knowing assistance of breach of fiduciary duty and breach of trust, knowing receipt of the proceeds from breach of fiduciary duty and breach of trust, and breach of contract, all as set out above. The Defendants are liable to compensate and pay damages to the Credit Union on a joint and several basis for the losses suffered by the Credit Union with respect to the wrongful conduct they were involved with, and to disgorge any amounts that they received on account of such wrongful conduct.

[58] The Underlying Claim is one brought by FSRA in the name of and on behalf of PACE for wrongs allegedly done to the corporation itself. This is, by its nature, a derivative action.

[59] When I give the words used in the exception their plain meaning, I conclude that the Underlying Claim is "a derivative action brought or maintained by or on behalf of the "CORPORATION by a person who is not a DIRECTOR OR OFFICER, without the cooperation, solicitation, assistance or active participation of the CORPORATION or any DIRECTOR OR OFFICER".

[60] The exception to the "Insured vs. Insured" exclusion applies to restore coverage under the D&O Policy.

Does the exception for a claim brought or maintained by a liquidator, receiver, or trustee in bankruptcy and made directly against a Director of the Corporation apply?

[61] The applicants Larry Smith and Phillip Smith submit that if the "derivative action" exception does not apply, the Underlying Claim is, nonetheless, excepted from the exclusion because the Underlying Claim is, in substance, one "brought or maintained by a liquidator, receiver, or trustee in bankruptcy". This exception applies only for "DEFENCE COSTS", as defined in the D&O Policy. These applicants contend that although FSRA has authority over PACE as an "Administrator" under the Act, its powers are functionally equivalent to a liquidator, receiver, or trustee in bankruptcy, such that the exception should apply.

[62] Because I have concluded that the "derivative action" exception applies, it is not necessary for me to decide whether this exception applies.

Are the applicants entitled to appoint and instruct counsel of their choice in the Underlying Claim?

[63] CUMIS acknowledges that if it is held that the Underlying Claim is not excluded from coverage, Larry Smith, Philip Smith, Frank Klees and Brian Hogan are entitled to choose and instruct defence counsel. This is so because the claims of fraud and other similar conduct against them potentially trigger exclusions in the policy which would create a conflict of interest and entitle them to independent counsel.

[64] The applicants in the Goodfellow application contend that they are also entitled to appoint and instruct counsel of their choice to defend them in the Underlying Claim, which counsel is to be paid for by CUMIS without needing to report to or take instructions from CUMIS. CUMIS disagrees on the basis that the claims against them are in negligence and there is no conflict of interest.

[65] And insurer who has a duty to defend an action also has a *prima facie* to choose and instruct counsel and to control the defence. This right to defend and control the defence of the litigation is lost only where there is a reasonable apprehension of conflict of interest on the part of counsel appointed by the insurer. See *Markham (City) v. AIG Insurance Company of Canada*, 2020 ONCA 239, at paras. 88-89.

[66] The Goodfellow applicants argue that (i) CUMIS denied coverage for defence obligations without a reservation of rights with respect to coverage and thereby repudiated the D&O

Policy, and (ii) the actions have been ongoing for some time, and these applicants have retained and instructed counsel who are closely involved in the litigation, such that a change on representation will be prejudicial. The Goodfellow applicants submit that in these circumstances, CUMIS has lost the right under the D&O Policy to retain and instruct counsel.

[67] In support of their submission, the Goodfellow applicants rely on *Ontario v. Kansa General Insurance* 1991 CanLII 7318 (ONSC). In that case, the insured argued that the insurer had repudiated the contract of insurance by refusing to defend the claim, with the result that the insurer lost its right to appoint and instruct counsel. The application judge examined the correspondence exchanged between the insurer and the insured and concluded that the conduct of the insurer did not entitle the insured to treat the policy as having been repudiated. The request by the insured that it be given the right to appoint counsel and control the defence of the claim was denied.

[68] On the evidence before me, the Goodfellow applicants did not elect to accept the repudiation and treat the D&O Policy as having been terminated. As a result, the D&O Policy remains in full force and effect.

[69] There is no reasonable apprehension of conflict of interest on the part of counsel to be appointed by CUMIS. The right of CUMIS under the D&O Policy to appoint and instruct counsel for the Goodfellow applicants has not been lost.

Disposition

[70] For these reasons, I make the following declarations:

a. A declaration that CUMIS is obligated to defend the applicants in the Underlying Claim pursuant to the D&O Policy.

b. A declaration that the applicants Larry Smith, Phillip Smith, Frank Klees, and Brian Hogan are entitled to appoint counsel of their choosing at CUMIS' sole expense who need not report to or take instructions from CUMIS.

c. A declaration that CUMIS is required to reimburse the applicants on a full indemnity basis for all past legal and administrative expenses incurred in defending the Underlying Claim and pursuing coverage.

[71] If the parties are unable to resolve costs, the applicants may make written submissions (not exceeding 3 pages for each application excluding costs outlines) within 10 days. CUMIS may make written responding submissions within 10 days thereafter. The applicants may make brief reply submissions (not exceeding one page) if so advised, within 5 days thereafter.

Cavanagh J.

Date: May 18, 2021

TAB 8

COURT OF APPEAL FOR BRITISH COLUMBIA

Citation: ***Group Eight Investments Ltd. v. Taddei,***
2005 BCCA 489

Date: 20051012
Docket: CA032197

Between:

Group Eight Investments Ltd.

Respondent
(Plaintiff)

And

Giovanni John Taddei, Adrian Crawford Ansell, and Taddei Development & Management Group Inc.

Appellants
(Defendants)

Before: The Honourable Chief Justice Finch
The Honourable Madam Justice Levine
The Honourable Madam Justice Kirkpatrick

G.K. Macintosh, Q.C. and S.B. Horne	Counsel for the Appellants
T.G. Keast	Counsel for the Respondent
Place and Date of Hearing:	Vancouver, British Columbia September 20, 2005
Place and Date of Judgment:	Vancouver, British Columbia October 12, 2005

Written Reasons by:
The Honourable Madam Justice Kirkpatrick

Concurred in by:
The Honourable Chief Justice Finch
The Honourable Madam Justice Levine

Reasons for Judgment of the Honourable Madam Justice Kirkpatrick:

[1] This appeal concerns the correct interpretation of the phrase "other permitted project costs" contained in a promissory note that secured the balance of the purchase price under an agreement of sale between the respondent as vendor and appellants as purchasers. The practical result of the appeal will determine whether the personal appellants are liable to the respondent under an indemnity agreement that limits their liability to $300,000. The parties agree that the judgment against the insolvent corporate appellant is unrecoverable.

[2] On a summary trial under Rule 18A of the ***Rules of Court***, the chambers judge interpreted the words "permitted project costs" to have a restricted meaning that meant "agreed to by the parties". Because there was no evidence that the respondent vendor had agreed to costs beyond additional financing, the chambers judge found that the vendor was entitled to judgment against the appellant company for the full amount owing of $706,715.53 and against the personal appellants for the sum of $300,000. The order further entitled the respondent to proceed pursuant to a hypothecation agreement over 200 shares in the capital of Taddei Developments Ltd.

Background

[3] The circumstances giving rise to this litigation are set out in the reasons of the chambers judge, 2004 BCSC 947, [2004] B.C.J. No. 1448 (Q.L.). The facts as found by the chambers judge may be summarized as follows.

[4] In 1995, the respondent ("Group Eight") purchased property in Vancouver intending to build a 31-unit strata title development. The purchase price was $1,570,000, $1 million of which was financed by a mortgage to the Bank of Montreal. At the time Group Eight purchased the property, it was zoned for single-family use with a permitted floor-space ratio of 0.8.

[5] In co-operation with the Vancouver Resource Society for the Physically Disabled ("VRS"), Group Eight made an unsuccessful application to the City for rezoning. The personal appellants, Mr. Ansell and Mr. Taddei, were active in the land development business in Vancouver. They learned of the respondent's interest in developing the property. They began negotiations to become involved in the project through a company that would develop the land and construct the building. They believed that the value of the land was $1.6 million, and if the property were rezoned to a floor-space ratio of 1.68, it would increase in value to $2.3 million.

[6] Group Eight, VRS and the appellant company signed a letter of intent in December 1995, following which Mr. Ansell and Mr. Taddei proceeded with a rezoning application and the preparation of architectural plans.

[7] On June 27, 1996, the City approved a conditional rezoning to a floor-space ratio of 1.55. Between June and October 1996, after spending approximately $300,000 of their own funds, Mr. Ansell and Mr. Taddei completed a presentation centre for the project and commenced marketing pre-sales of the strata units.

[8] On October 30, 1996, the respondent, VRS, and the appellants executed an agreement of sale, pursuant to which Group Eight agreed to sell the property to the

appellants for a purchase price of $2.3 million. Under clause 3.1 of the agreement, $1 million of the purchase price was to be paid in cash to permit Group Eight to retire its mortgage to the Bank of Montreal. The balance of the purchase price was secured by the promissory note.

[9] Under the terms of the promissory note, Group Eight was entitled to be paid only from the sale of strata lots and only after the project financing and "any other permitted project costs" had been paid. As the chambers judge noted, "other permitted project costs" is not defined in either the promissory note or the agreement of sale.

[10] A further term of the agreement permitted the purchasers to include the $1 million cash purchase price in the initial $5.4 million financing for the development of the project that would be secured by a mortgage. Group Eight continued to hold legal title as bare trustee for the purchasers and was thus able to control the financing of the property.

[11] Richmond Savings Credit Union advanced a $5.4 million construction loan. Construction of the project began in early January 1997. In November 1997, the purchasers negotiated a refinancing of the construction loan with another lender on terms approved by Group Eight. The Canadian Imperial Bank of Commerce ("CIBC") took a first mortgage against 10 unsold units upon which $2,156,505 was advanced and from which Group Eight was paid $717,184. Mandate National Mortgage Corporation ("Mandate") took a mortgage on four unsold units upon which $797,500 was advanced.

[12] In April 1998, a second mortgage of $300,000 was placed against the units mortgaged to CIBC to pay out a list of project costs supplied by the appellants. Group Eight approved the placement of this mortgage.

[13] Sales in the project slowed, evidently resulting in non-payment of the project debt. The second mortgagee commenced foreclosure proceedings and obtained an order nisi in the spring of 1999. Group Eight took an assignment of the mortgagee's claim upon payment of $272,102.

[14] Group Eight commenced its action on June 2, 2000. The summary trial commenced on June 11, 2001. The chambers judge referred to the Registrar an inquiry of an accounting between the parties. The Registrar issued his decision on November 7, 2003, and certified the amounts expended by the appellants on the project ($5,878,142.11); the amounts received by the appellants from the mortgages charging the property (net $5,964,646.68); and the net sale proceeds from the sale of the strata lots ($6,962,880.77). The parties agree that the Registrar omitted to include $160,000 that was expended on the project (raising the amount expended to $6,038,142.11).

Promissory Note

[15] The note reads:

> RE: Agreement of Sale between Group Eight and 523573 B.C. Ltd. ("523573") (the "Agreement")
>
> For value received, 523573 promises to pay to the order of Group Eight the total of the following sums:

- $1,300,000.00 (*the principal amount*), together with
- an amount equal to interest, from Closing Date, calculated annually at a rate equal to the prime rate per annum as determined by Bank of Montreal (the "Bank") from time to time at its head office in Vancouver and recorded as such by the Bank from time to time upon the sum of $1,265,000.00, such interest to commence from July 28, 1996.

Payment of the principal sum shall be made at the office of Group Eight as set out above upon demand by Group Eight, which demand may be made only after the later of:

- the completion of the sale of any strata lots in the Development;
- receipt of sales proceeds by 523573; and
- payment out of the financing obtained by 523573 to complete and purchase the Development and any other permitted project costs

all as set out in the Agreement. Whether demand is made or not by Group Eight, net proceeds of the sale of any strata lots in the Development shall be paid to Group Eight until the amounts owing under this Promissory Note are paid in full.

AND PROVIDED interest as aforesaid shall be paid on the first day of each month commencing on the first day of the month after the first mortgage draw is made under the financing taken out bo [*sic*] complete the Development as set out in the Agreement.

Defined terms in this Promissory Note shall have the meaning given to them in the Agreement.

[16] At trial, the purchasers argued that no amount was owed under the promissory note because, although all of the strata lots had been sold, all of the sale proceeds were applied to the payment of financing and "other permitted costs". The purchasers contended that "permitted project costs" must refer to actual costs incurred. Group Eight argued that it was entitled to be paid the amounts due to it

after payment of the $5.4 million mortgage plus additional financing of $297,200 and the $300,000 second mortgage. The chambers judge made his essential finding at para. 31 of his reasons:

> I interpret the words "permitted costs" in the Promissory Note to have a restricted meaning in the sense that there would be no purpose to using the word “permitted” if it was contemplated that any and all costs related to the project took priority to any payment to Group Eight. In that context, the only sense I can make of the word “permitted” is that it means agreed to by the parties. In this case, there is no evidence that Group Eight agreed to costs as “permitted costs” beyond the additional financing it agreed to in order to pay project costs. I find, therefore, that Group Eight is entitled to judgment for the amount owing to it under the Promissory Note, after deducting payments made to date, up to the amount by which the net sales and rentals of this project exceed the amount required to pay the mortgages agreed upon and put in place by the parties. According to the numbers I have in evidence, the total amount of financing agreed to was $5,997,200 which is close to the total of costs certified by the Registrar plus the $160,000 omitted, namely, $6,038,142.11 (which includes the initial $990,000 paid by the Defendant company on the land purchase). The Registrar has certified that there were proceeds from sales in the amount of $6,962,880.77.

[17] On appeal, the appellants argue that the chambers judge erred in restricting the meaning of "permitted project costs" to agreed financing. The appellants say that such an interpretation is inconsistent with the express wording of the agreement and with the profit-sharing objective of what the appellants contend was a joint venture arrangement.

[18] The respondent argues that the repayment scheme set out in the promissory note, together with certain provisions in the agreement of sale, were designed to protect the $1.3 million portion of the purchase price carried by the respondent. The respondent contends that the agreement constituted an absorption of risk by the

appellants with a concomitant fixing of the price to be paid to the respondent. The respondent says that the chambers judge's interpretation of "permitted project costs" reflects the ordinary meaning of the language of the note and the surrounding circumstances prevalent at the time the parties entered into the agreement. The respondent says that the appellants' post-contract conduct, in particular the absence of any reference to costs other than financing costs in the negotiations leading up to the refinancing in early January 1998, confirms that "permitted project costs" meant only additional financing costs.

Discussion

[19] Both the appellants and the respondent presented evidence and argument about conduct of the parties during the negotiation of the contract and after its execution, both before this Court and in the chambers application. It is settled law that a court must, in interpreting a contract, determine the intention of the parties from the words of the contract and not interpret the words of the contract based on the intentions of the parties: G.H.L. Fridman, *The Law of Contract in Canada*, 4th ed. (Scarborough: Carswell, 1999) at 482.

[20] The plain and ordinary meaning must be given to words in a contract unless to do so would result in an absurdity: ***Ex parte Walton. In re Levy*** (1881), 17 Ch.D. 746 (C.A.). Words must be interpreted in light of the whole of the contract and the intention of the parties expressed therein. In construing contracts, the court assumes that the words in the contract are there for a purpose and "reject an

interpretation that would render one of [the contract's] terms ineffective" (***National Trust Co. v. Mead*** (1990), 71 D.L.R. (4th) 488 at 499).

[21] A helpful review of the principles of contract interpretation in the commercial context is found in the decision of ***Scanlon v. Castlepoint Development Corp.*** (1992), 99 D.L.R. (4th) 153 (Ont. C.A.); leave to appeal to S.C.C. refused (1993), 102 D.L.R. (4th) vii. Robins J.A. stated at 179:

> The agreement with which we are concerned is a negotiated commercial document which should be construed in accordance with sound commercial principles and good business sense. To the extent that it is possible to do so, it should be construed as a whole and effect should be given to all of its provisions. The provisions should be read, not as standing alone, but in light of the agreement as a whole and the other provisions thereof: *Hillis Oil & Sales Ltd. v. Wynn's Canada Ltd.* (1986), 25 D.L.R. (4th) 649 at p. 655, [1986] 1 S.C.R. 57, 71 N.S.R. (2d) 353.

[22] More recently, this Court summarized the principles of contract interpretation in ***Gilchrist v. Western Star Trucks Inc.*** (2000), 73 B.C.L.R. (3d) 102, at paras. 17-18:

> The goal in interpreting an agreement is to discover, objectively, the parties' intention at the time the contract was made. The most significant tool is the language of the agreement itself. This language must be read in the context of the surrounding circumstances prevalent at the time of contracting. Only when the words, viewed objectively, bear two or more reasonable interpretations, may the court consider other matters such as the post-contracting conduct of the parties: *Delisle v. Bulman Group Ltd.* (1991), 54 B.C.L.R. (2d) 343 (B.C.S.C.), approved by Chief Justice McEachern in *Bramalea Ltd. v. Vancouver School Board No. 39* (1992), 65 B.C.L.R. (2d) 334 (B.C.C.A.); *Prenn v. Simmonds*, [1971] 3 All E.R. 237 (U.K.H.L.); *Eli Lilly and Co. v. Novopharm Ltd.* (1998), 161 D.L.R. (4th) 1, (S.C.C.).
>
> The first inquiry, then, is to determine whether there is only one reasonable meaning to the words in the contract, or more than one. In

> this search one must look to the surrounding circumstances and the whole of the contract. The words of the contract must be looked at in their ordinary and natural sense and cannot be distorted beyond their actual meaning: *MacMillan Bloedel Ltd. v. British Columbia Hydro & Power Authority* (1992), 72 B.C.L.R. (2d) 273 (B.C.C.A.); *Melanesian Mission Trust Board v. Australian Mutual Provident Society*, [1997] 1 N.Z.L.R. 391 (New Zealand P.C.).

[23] It is not contested that Group Eight could only demand payment under the promissory note after:

(a) the completion of the sale of any strata lots in the development;

(b) the appellants had received the sale proceeds; and

(c) the financing obtained by the appellants had been repaid.

The contentious aspect raised on appeal is whether, as argued by the respondent, only financing costs had to be repaid before Group Eight could be paid; or whether, as argued by the appellants, a second class of costs, namely "any other permitted project costs" had also to be paid before Group Eight was entitled to be paid.

[24] Although the appellants argued that the agreement between the parties was, or was in the nature of, a joint venture, I do not think the words of the agreement support such a conclusion. Nor is such a finding necessary for the purpose of construing the contract.

[25] It is important to note that the entire phrase in dispute reads:

> payment out of the financing obtained by 523573 [the appellant company] to complete and purchase the Development and any other permitted project costs

all as set out in the Agreement.

[26] The financing of the project is specifically referenced at clause 16.2(e) of the agreement of sale:

> arrange construction or other financing in an amount up to $5,400,000.00 (the "Development Loan") for the purposes of raising the Cash Purchase Price and creating the Development secured against the Lands subject to paragraphs 8.2 and 8.3 hereof, and the form and content of any documentation relating to any such borrowing subject to compliance with paragraphs 8.2 and 8.3 hereof and provided that the Purchaser cannot, and shall not, draw down funds from such financing except as follows:
>
> (i) no funds shall be advanced under such financing except for payment of the costs of the Development and before each advance Davidson and Company shall provide details of the use to which each advance will be put to VRS and the Vendor;
>
> (ii) no funds shall be advanced under such financing in respect of project management or similar or related fees or disbursements which are in excess of $12,000.00 per month commencing on the date of the construction of the Development and continuing only so long as construction continues, up to a maximum total of $96,000.00; and
>
> (iii) the cumulative aggregate total of the advances under such financing shall never exceed an amount equal to the total costs incurred in respect of the Development at any time less $200,000.00 until after the date that the VRS Lots are transferred to VRS and the total amount owing to the Vendor under this Agreement has been paid (so that the Purchaser's expenditure of $200,000.00 for plans or other soft costs related to the Development will remain outstanding until that date);

[27] The respondent submits that clause 16.2 limited the appellants' ability to obtain financing to an amount not to exceed $5.4 million. However, the respondent subsequently agreed to the refinancing in early 1998 and the placement of additional security in the form of the second mortgage. The chambers judge found that the second mortgage was to pay a list of project costs supplied by the appellants. In my opinion, the respondent's assertion that the development financing was limited to

$5.4 million cannot be sustained given the subsequent financings to which the respondent gave its express consent.

[28] As the chambers judge noted, "permitted project costs" is not a defined term of either the promissory note or the agreement of sale. This class of costs is more general and potentially ambiguous and required the court to apply the rules of construction referred to above.

[29] The first tenet of contract construction is to give words in a contract their plain and ordinary meaning unless to do so would result in an absurdity. The *Concise Oxford Dictionary* defines "permit (permitted, permitting)" as "give permission or consent to; authorize." Applying that definition to the entire phrase "other permitted project costs all as set out in the agreement" leads to the ineluctable interpretation that the phrase means project costs authorized or allowed under the agreement. There does not appear to be an alternative reasonable interpretation which would render this provision ambiguous in light of the plain and ordinary meaning of the words. All that is left is to determine what, if any, additional costs are authorized or allowed under the agreement.

[30] Clause 16.2 of the agreement of sale, in addition to laying out the specifics of financing terms, also provides:

> Without limiting the foregoing, the Purchaser shall have the right to, from and after the date of this Agreement, and covenants that it shall diligently perform the following activities relating to the Development, and the Vendor and VRS shall execute any documents or perform any acts required by the Purchaser to complete the Development and without limitation to perform the following activities; . .

(b) do media advertising relating to the Development;

. . .

(h) place in a form, content and amount acceptable to the Purchaser a policy of insurance regarding the Lands;

(i) obtain all licences and permits as are necessary to permit the Development to proceed, including, without any limitations, building permits;

(j) procure any necessary municipal or statutory approvals for the Development;

. . .

(l) prepare and arrange for filing all Subdivision Plans, Strata Plans, Disclosure Statements and other documents required to raise title to individual strata lots in the Development and prepare those strata lots for resale;

(m) obtain occupancy permits for the Strata Lots as required by the City of Vancouver;

(n) **such other activities as are normally carried out by a developer in connection with the development of a residential real estate development of the size, type and location [of] the Development.**

[Emphasis added.]

The words in sub-clause (n) are particularly broad and provide the purchaser with considerable latitude to undertake "normal" activities that would realistically incur costs. This was, as in ***Scanlon***, a negotiated commercial document that "should be construed in accordance with sound commercial principles and good business sense." The purchaser was bound to diligently perform the referenced activities. It cannot be realistically accepted that if in complying with that covenant the purchaser incurred costs, such costs could be denied by the vendor. Furthermore, the

purchaser's ability to incur costs was not completely unfettered. Clause 9.2 of the agreement of sale provided:

> A representative of the Vendor and of VRS will meet with the Purchaser or Davidson and Company to review tenders before contracts are let by the Purchaser and will review the proposals of the Purchaser to let contracts. The Vendor or VRS must object within one business day or the Purchaser may assume the Vendor and VRS approve all such contracts. Davidson and Company will provide the Vendor and VRS with project updates whenever such an update is prepared. In addition, the Purchaser will provide such information regarding the Development as may be reasonably requested by the Vendor or VRS from time to time. In the event of any dispute regarding the letting of contracts, the quantity surveyor of the lender for the project will arbitrate.

Thus, this clause limited "permitted project costs", at least in relation to those associated with the letting of contracts. The fact that the respondent evidently never exercised its rights under clause 9.2 is of no moment.

[31] Thus, it will be seen from the foregoing that I am of the opinion that the plain and obvious meaning of the phrase "other permitted project costs" means costs in addition to financing costs. This interpretation is consistent with the words of the contract taken as a whole and with commercial sense. The scheme of the agreement was that the vendor agreed that it would receive payment of $1.3 million of its $2.3 million investment if the sales of the strata lots exceeded the costs of the development and construction of the project. I conclude that the chambers judge erred in interpreting the word "permitted" in a restrictive manner to mean "agreed to by the parties" and thereby limiting the phrase "other permitted project costs" to additional financing costs. It follows that I would allow the appeal.

[32] There remains to be determined what are the legitimate costs of the development project. Based on the evidence before the chambers judge and bearing in mind the prolonged time this litigation has consumed, the costs are:

(a) the project costs certified by the Registrar of $5,878,142.11 plus $160,000; and

(b) the costs associated with securing the financing from CIBC and Mandate not accounted for in the Registrar's decision. Specifically, $717,184.62 was paid to the respondent as a condition of approving the refinancing and was a legitimate cost of the project.

[33] The appellants also seek to add other claimed expenses totalling $562,265. This amount was referred to in the Registrar's decision as "outstanding amounts owed for GST, amounts owed to CCRA/Revenue Canada, and for outstanding bills relating to the project." The Registrar declined to allow those amounts because the terms of reference from the chambers judge required that he certify the amounts expended. The Registrar concluded that a debt incurred but not paid cannot be money expended. The personal appellants say that GST in the amount of $311,932.65 was received by the development project and is owed to Revenue Canada. The Registrar did allow certain amounts for GST that had been paid as monies expended on the project and were included in item (a) project costs. The respondent concedes that GST must be paid on the sale of the strata units. GST owing but not yet paid is obviously an item that must be taken into account.

[34] Because of the interpretation placed on the contract by the chambers judge, he did not address the claim of additional expenses totalling $562,265. In March 2004, after the Registrar's hearing and decision but before the continued summary trial, Mr. Ansell deposed that part of the $562,265 claim comprised interest on loans that he and Mr. Taddei took out to pay for expenses to complete the project. The accounting of those amounts is incomplete and it is impossible for me to say with any confidence whether they are properly allowable as "other permitted costs". However, accepting that $311,932.65 in GST expense is a proper permitted cost, this would nevertheless leave approximately $250,265 to potentially be taken into account. In the usual course, I would refer the determination of these amounts back to the Supreme Court.

[35] The respondent also challenges the appellants' right to have the second mortgage taken into account because of alleged misuse of the funds. The misuse is denied by the appellants. However, the chambers judge found that the second mortgage was to be included in the total amount of agreed financing. In my view, the time is long past to address the alleged misuse of the second mortgage proceeds.

[36] Lastly, the respondent also seeks to introduce evidence of notional rents available, said to total $75,000, which would increase the revenue to the project (and increase the appellants' exposure to liability). However, this was an issue that, if it was to be addressed, should have been raised with the chambers judge. As with the alleged misuse of the second mortgage proceeds, it is simply too late in this protracted litigation to argue the issue now. According to my calculations, the

difference between the net proceeds of sale ($6,962,880.77), less the certain project costs ($5,878,142.11 + $160,000 + $717,184.62 = $6,755,326.73) is $207,554.04. In my opinion, this approximate $208,000 difference could be easily applied to "other permitted project costs", most notably the $312,000 owed for GST, as contemplated by the promissory note. The net effect is to reduce the appellants' exposure under their indemnity to the respondent to nil. This renders it unnecessary to refer the issue of the $250,265 amount back to the Supreme Court for determination.

[37] I would allow the appeal and set aside the judgments against the personal appellants, including the respondent's right to proceed under the hypothecation agreement over the shares in Taddei Developments Ltd.

"The Honourable Madam Justice Kirkpatrick"

I Agree:

"The Honourable Chief Justice Finch"

I Agree:

"The Honourable Madam Justice Levine"

TAB 9

H. F. Clarke Limited *Appellant;*

and

Thermidaire Corporation Limited *Respondent.*

1974: January 28, 29, 30; 1974: October 1.

Present: Laskin C.J. and Martland, Judson, Spence and Dickson JJ.

ON APPEAL FROM THE COURT OF APPEAL FOR ONTARIO

Contract—Restrictive covenant—Measure of liquidated damages—Whether formula reasonable or penalty—Construction of covenant in restraint of trade—Scope of covenant—Limitation of operation of covenant by construction or rectification.

In January 1966, the parties entered into a written contract constituting the appellant as from January 1, 1966, the exclusive distributor of the respondent's products (as defined) in a specified area of Canada comprising the larger part of the country. This contract which replaced an earlier one under which there were two restrictive covenants, one respecting competition during the currency of the contract and the second respecting competition during the three year period after termination or cancellation, showed one marked variation in the successor covenants in that the 1966 covenant dealing with sale of competitive products omitted the references to the three year period and to the territory. The covenant dealing with Termination of Agreement by Clarke in neither case made reference to territory but provided for liquidated damages payable by Clarke to Thermidaire of an amount equal to the gross trading profit realised through the sale of competitive products. The contract was terminated by Thermidaire and it was the appellant which initiated suit claiming damages for wrongful termination of the contract. Thermidaire counter-claimed for damages under the covenants against competition. The appellant discontinued its action and the trial of the counter-claim began well after the expiry of the three-year period within which the post-contract covenant was effective. The appellant had continued to sell competitive products contrary to the terms of the covenant and put itself at risk of having to account under the formula for post-contract damages. The respondent however did not seek an interim injunction and while the prayer for relief in the counter-claim did ask for an injunction by the time the action came on for trial there was no longer any basis for one.

H. F. Clarke Limited *Appelante;*

et

Thermidaire Corporation Limited *Intimée.*

1974: les 28, 29 et 30 janvier; 1974: le 1er octobre.

Présents: Le juge en chef Laskin et les juges Martland, Judson, Spence et Dickson.

EN APPEL DE LA COUR D'APPEL DE L'ONTARIO

Contrat—Clause restrictive—Mesure des dommages liquidés—S'agit-il d'une formule raisonnable ou d'une pénalité?—Interprétation de la clause restrictive de commerce—Portée de la clause—Limitation d'application de la clause par interprétation ou par rectification.

En janvier 1966, les parties ont passé un contrat qui faisait de l'appelante, à compter du 1er janvier 1966, le distributeur exclusif des produits de l'intimée (tels que définis) dans une région spécifiée du Canada qui comprenait la plus grande partie du pays. Ce contrat qui remplaçait un contrat antérieur en vertu duquel les deux clauses restrictives, dont une avait trait à la concurrence pendant la période d'application du contrat et l'autre à la concurrence durant les trois années suivant la résiliation ou l'annulation du contrat, révélaient une différence marquée en regard des clauses qui ont suivi en ce que la clause de 1966 portant sur la vente des produits concurrents ne faisait aucune mention de la période de trois ans et du territoire. La clause portant sur la «Résiliation de l'accord par Clarke» ne mentionnait pas, dans les deux cas, la question du territoire mais elle prévoyait le paiement par Clarke, en dommages-intérêts liquidés, d'un montant égal aux bénéfices bruts d'exploitation réalisés par la vente des produits concurrents. Le contrat a été résilié par Thermidaire et c'est l'appelante qui a commencé les poursuites, réclamant des dommages-intérêts pour la résiliation illicite du contrat. Thermidaire fit une demande reconventionnelle en dommages-intérêts en vertu des clauses de non-concurrence. L'appelante discontinua son action et l'instruction de la demande reconventionnelle commença bien après l'expiration de la période de trois ans durant laquelle la clause post-contractuelle était en vigueur. L'appelante avait continué à vendre des produits concurrents après la résiliation du contrat et s'était placée dans une situation où elle risquait d'avoir à rendre compte sous le régime de la formule concernant les dommages post-contractuels. Cependant, l'intimée n'a pas cherché à obtenir une injonction provisoire et même si les conclusions de la demande reconventionnelle demandaient une injonction, celle-ci n'avait plus raison d'être lorsque le procès a eu lieu.

Both the trial judge and the Court of Appeal found the contracts, either as rectified or as limited by construction as to territory, reasonable *inter partes* and consonant with the public interest. The trial judge also found and the Court of Appeal affirmed that Clarke had broken the contract during its currency by selling competitive products (other than those of the respondent) and had also broken the covenant against post-contract competition. These findings and the finding that the respondent was entitled to terminate the contract were not contested thereafter.

Le juge de première instance et la Cour d'appel ont tous deux statué que les contrats, tels que rectifiés ou tels que limités par interprétation quant au territoire, étaient raisonnables *inter partes* et en accord avec l'intérêt public soit tels que rectifiés soit tels que limités par l'interprétation relative au territoire. Le juge de première instance a conclu, et la Cour d'appel confirmé, que Clarke avait brisé le contrat durant sa période d'application en vendant des produits concurrents (autres que ceux de l'intimée), et avait également violé la clause interdisant la concurrence post-contractuelle. Ces conclusions et la conclusion selon laquelle l'intimée avait le droit de résilier le contrat n'on pas été contestées par la suite.

As to damages, the trial judge found that the contractual formula of gross trading profit as a measure was business-like and reasonable, as did the Court of Appeal, despite the fact that it was accepted in the Court of Appeal that the damages would reach $200,000.

«Quant aux dommage-intérêts, le juge de première instance a conclu que la formule de bénéfices bruts d'exploitation comme mesure était propre aux affaires et raisonnable comme l'a fait la Cour d'appel malgré qu'il ait été accepté en Cour d'appel que les dommages-intérêts s'élèveraient à $200,000.

Held (Martland and Dickson JJ. dissenting): The appeal should be allowed with costs.

Arrêt (les juges Martland et Dickson étant dissidents): Le pourvoi doit être accueilli avec dépens.

Per Laskin C.J. and Judson and Spence JJ.: Three points were in issue, first, the validity of the convenants by reason of their alleged unlimited scope, second, the main issue of whether the formula fixing damages for breach of covenant in the post-contract period establishes a measure of liquidated damages or is a penalty against which relief must be given, and, third, whether certain products should not be taken into account in assessing damages.

Le juge en chef Laskin et *les* juges Judson et Spence: Trois points étaient en litige, premièrement, la validité des clauses en regard de ce qu'on allègue être leur portée illimitée, deuxièmement, la principale question en litige, de savoir si la formule fixant les dommages-intérêts pour violation de la clause durant la période post-contractuelle établit une mesure des dommages liquidés ou constitue une pénalité contre laquelle un recours doit être octroyé, et, troisièmement, de savoir si certains produits ne devraient pas être pris en ligne de compte dans l'évaluation des dommages-intérêts.

Neither of the covenants against competition referred to a territorial limitation and rectification was sought on the ground of mutual mistake, and, while the trial judge found them enforcable without granting rectification, the Court of Appeal allowed the cross-appeal as to rectification and qualified their operation by including therein the words "in the territory". Without interfering with the view taken by the Court of Appeal, reasonable construction of the covenants would, in the absence of indication to the contrary, have limited them to that territory in any event. The covenants having been by construction or rectification limited as to territory the appellants failed also in any challenge to the covenants as being in unreasonable restraint of trade.

Ni l'une ni l'autre des clauses de non-concurrence ne faisaient mention d'une limitation territoriale et la rectification a été demandée pour motif d'erreur mutuelle, et, alors que le juge de première instance les jugeaient exécutoires sans rectification, la Cour d'appel accueillait l'appel incident relatif à la rectification et atténuait leur application par l'inclusion des mots «dans le Territoire». Sans modifier la position prise par la Cour d'appel, une interprétation raisonnable des clauses aurait restreint, en l'absence d'indications contraires, leur application à ce territoire-là de toute façon. Les clauses ayant été restreintes territorialement par interprétation ou par rectification, l'appelante a également échoué dans toute contestation des clauses pour motif de restriction déraisonnable du commerce.

As to whether the formula fixing damages was in the circumstances a penalty, while it is always open to parties to make such a pre-determination of damages or their measure this must yield to judicial appraisal of its reasonableness. The doctrine that a sum will be held to be a penalty if extravagant and unconscionable in amount in comparison with the greatest loss that could conceivably be proved to have followed from the breach is well established and does not lose its force in cases where exact calculation or pre-estimation is difficult. In the present case the stipulation for liquidated damages (of which the estimated loss of net profits of respondent is only 40 per cent) was disproportionate and unreasonable. The respondent was however entitled to recover its provable damages for breach of convenant.

The submission by the appellant that sales of certain products ought not to be taken into account should be rejected as it was in the courts below.

Per Martland and Dickson JJ. *dissenting*: The appeal should be dismissed with costs for the unanimous reasons given by the Court of Appeal.

[*Dunlop Pneumatic Tyre Co. Ltd. v. New Garage and Motor Co. Ltd.*, [1915] A.C. 79; *Clydebank Engineering & Shipbuilding Co. Ltd. et al. v. Don José Ramos Yzquierdo y Castaneda et al.*, [1905] A.C. 6 appld.]

APPEAL from a judgment of the Court of Appeal for Ontario[1], dismissing an appeal from a judgment of Wilson J. at trial. Appeal allowed with costs, Martland and Dickson JJ. dissenting.

J. J. Fitzpatrick, Q.C., and *H. Ross*, for the appellant.

C. E. Woollcombe, Q.C., and *D. H. Sandler*, for the respondent.

The judgment of Laskin C.J. and Judson and Spence JJ. was delivered by

THE CHIEF JUSTICE—There are three points in this appeal, which concerns the enforceability, under an exclusive distributorship contract, of covenants against competition during the currency of the contract and for three years after its lawful

[1] [1973] 2 O.R. 57.

Quant à savoir si la formule fixant les dommages-intérêts constituait dans les circonstances une pénalité, alors que les parties peuvent toujours préétablir les dommages ou la mesure de ceux-ci, cela ne peut se soustraire au pouvoir des tribunaux d'en apprécier le caractère raisonnable. La théorie voulant que la somme sera jugée être une pénalité si elle est extravagante et exorbitante en comparaison de la plus grande perte qui pourrait concevablement être prouvée comme conséquence de la violation est bien établie et ne perd pas sa force dans des affaires où un calcul exact, ou une estimation anticipée, s'avèrent difficiles. En l'espèce, la stipulation prévoyant des dommages liquidés (desquels la perte de bénéfices nets estimative de l'intimée n'est que d'environ 40 pour cent) était disproportionnée et déraisonnable. Cependant, l'intimée a eu le droit de recouvrer ses dommages prouvables découlant de la violation de la clause.

La prétention de l'appelante que les ventes de certains produits ne devraient pas être prises en ligne de compte doit être rejetée comme elle l'a été par les cours d'instance inférieure.

Les juges Martland et Dickson, *dissidents*: L'appel devrait être rejeté avec dépens pour les motifs unanimes de la Cour d'appel.

[Arrêts appliqués: *Dunlop Pneumatic tyre Co. Ltd. v. New Garage and Motor Co. Ltd.*, [1915] A.C. 79; *Clydebank Engineering & Shipbuilding Co. Ltd. et al v. Don José Ramos Yzquierdo y Castaneda et al.*, [1905] A.C. 6.]

POURVOI à l'encontre d'un arrêt de la Cour d'appel de l'Ontario[1], rejetant un appel interjeté à l'encontre d'un jugement de première instance prononcé par le juge Wilson. Pourvoi accueilli avec dépens, les juges Martland et Dickson étant dissidents.

J. J. Fitzpatrick c.r., et *H. Ross*, pour l'appelante.

C. E. Woollcombe c.r., et *D. H. Sandler*, pour l'intimée.

Le jugement du juge en chef Laskin et des juges Judson et Spence a été rendu par

LE JUGE EN CHEF—Trois points se trouvent soulevés en ce pourvoi, qui porte sur le caractère exécutoire, sous le régime d'un contrat de concession exclusive de distribution, de clauses interdisant la concurrence pour la période d'application

[1] [1973] 2 O.R. 57.

termination. The first point relates to the validity of the covenants by reason of their alleged unlimited scope. Secondly, there is an important issue, which in my opinion is the main issue, whether the formula fixing damages for breach of the covenant in the specified post-contract period establishes the measure of liquidated damages or is in reality a penalty against which relief must be given. The third point relates to certain products which, on the appellant's contention, should not be taken into account in assessing damages. Although the appellant also questioned the reference as to damages, directed by the trial judge and affirmed by the Court of Appeal, it being its contention that the assessment should be by a judge of the Supreme Court of Ontario, I would not interfere with this direction if the right to damages should be confirmed by this Court.

du contrat et pour trois ans après sa résiliation licite. Le premier point a trait à la validité des clauses en regard de ce que l'on allègue être leur portée illimitée. Deuxièmement, une importante question se pose, qui à mon avis est la principale question en litige, de savoir si la formule fixant les dommages-intérêts pour violation de la clause durant la période post-contractuelle spécifiée établit la mesure des dommages liquidés ou constitue en réalité une pénalité contre laquelle un recours doit être octroyé. Le troisième point a trait à certains produits qui, d'après la prétention de l'appelante, ne devraient pas être pris en ligne de compte dans l'évaluation des dommages-intérêts. Bien que l'appelante ait aussi mis en cause le renvoi relatif aux dommages-intérêts, prescrit par le juge de première instance et confirmé par la Cour d'appel, la prétention de l'appelante étant que l'évaluation doit être faite par un juge de la Cour suprême de l'Ontario, je ne modifierais pas cette prescription si le droit aux dommages-intérêts devait être confirmé par cette Cour.

The contract which is the subject of this litigation was dated January 14, 1966, and as amended shortly thereafter, it constituted the appellant, as from January 1, 1966, the exclusive distributor of the respondent's products (as defined) in a specified area of Canada, embracing the larger part of Canada from Ontario to the west coast and including the North West Territories and part of Quebec but excluding the eastern part of Quebec and the four Atlantic provinces. This contract replaced an earlier one under which the two covenants against competition, one respecting competition during the currency of the contract, and the second respecting competition during the three year period after termination or cancellation of the contract showed one marked variation from the successor covenants. Article 7 of the first contract of January 20, 1964, provided as follows:

Le contrat qui fait l'objet du litige est daté du 14 janvier 1966, et tel que modifié peu de temps après cette date il fait de l'appelante, à compter du 1er janvier 1966, le distributeur exclusif des produits de l'intimée (tels que définis) dans une région spécifiée du Canada, comprenant la plus grande partie du Canada de l'Ontario jusqu'à la côte ouest et incluant les territoires du Nord-Ouest et une partie du Québec mais excluant la partie est du Québec et les quatre provinces de l'Atlantique. Ce contrat remplaçait un contrat antérieur en vertu duquel les deux clauses interdisant la concurrence, dont une avait trait à la concurrence pendant la période d'application du contrat et l'autre à la concurrence durant les trois années suivant la résiliation ou l'annulation du contrat, révélaient ce qui se trouvait être une différence marquée en regard des clauses qui ont suivi. L'article 7 du premier contrat du 20 janvier 1964 prévoyait ce qui suit:

7. *Sale of Competitive Products*

Distributor undertakes and agrees that during the currency of this Agreement and for a period of three (3) years after the termination hereof, as herein provided, neither it nor any company

[TRADUCTION]

7. *Vente de produits concurrents*

Le distributeur accepte et convient que durant la période d'application du présent accord et pour une période de trois (3) années après sa résiliation, tel que prévu aux présentes, le distributeur ni aucune

affiliated or associated with it shall sell competitive products in the Territory.

In the contract out of which this litigation arises, the references to the three year period and to the territory were left out, and the paragraph, numbered 7 as before, was in these words:

7. *Sale of Competitive Products*

Clarke undertakes and agrees that during the currency of this Agreement, neither it nor any company associated or affiliated with it shall manufacture, sell, cause to be manufactured or sold, products competitive to Thermidaire products.

Neither Article 14 of the first contract nor its successor Article 15 of the second contract, in restraining competition for three years after termination or cancellation made any reference to its operation in the territory of the distributorship. The two articles were substantially the same in their relevant particulars, and it is enough to reproduce the one that is in issue here. It reads as follows:

15. *Termination of Agreement by Clarke*: In the event of the termination or cancellation of this Agreement by, or caused by, Clarke, either by reason of its non-renewal by Clarke or by reason of any default on the part of Clarke or by reason of any violation or non-fulfilment of the conditions of this contract by Clarke and not remedied by Clarke as laid down in Section 12, including the grounds for termination specified in paragraph 19 hereof, Clarke further undertakes and agrees that neither it nor any company affiliated or associated with it will produce, sell or cause to be produced or sold, directly or indirectly, products competitive with Thermidaire Products for a period of three (3) years after the date of termination or cancellation. In the event of breach by Clarke of this convenant pertaining to competitive products, Clarke shall pay to Thermidaire by way of liquidated damages an amount equal to the gross trading profit realized through the sale of such competitive products.

Although neither of the covenants against competition referred to a territorial limitation on their ambit and rectification was sought on the ground of mutual mistake, the trial judge found them enforceable without granting rectification, it being

compagnie qui lui est affiliée ou associée ne vendront des produits concurrents dans le Territoire.

Dans le contrat dont découle le présent litige, les mentions de la période de trois ans et du territoire ont été omises, et le paragraphe, qui garde toujours le numéro 7, est dans les termes suivants:

[TRADUCTION]

7. *Vente de produits concurrents*

Clarke accepte et convient que durant la période d'application du présent accord, Clarke ni aucune compagnie qui lui est associée ou affiliée ne fabriqueront, vendront, feront fabriquer ou vendre, des produits faisant concurrence aux produits de Thermidaire.

Ni l'article 14 du premier contrat ni l'article 15 qui le remplace dans le second contrat ne font mention, en interdisant la concurrence pour les trois années suivant la résiliation ou l'annulation, de son application dans le territoire de distribution. Les deux articles sont substantiellement les mêmes dans leurs dispositions pertinentes, et il suffit de reproduire celui qui est présentement en litige. Il se lit comme suit:

[TRADUCTION] 15. *Résiliation de l'accord par Clarke*: Advenant la résiliation ou l'annulation du présent accord par Clarke ou à cause de Clarke, du fait du non-renouvellement de l'accord par Clarke ou du fait d'un manquement de la part de Clarke ou du fait d'une violation ou inexécution des conditions du présent contrat par Clarke qui n'a pas été réparée par Clarke comme prévu à l'Article 12, y compris des motifs de résiliation spécifiés au paragraphe 19 des présentes, Clarke accepte et convient en outre que Clarke ni aucune compagnie qui lui est affiliée ou associée ne produiront, vendront ou feront produire ou vendre, directement ou indirectement, pendant une période de trois (3) années après la date de la résiliation ou de l'annulation, des produits faisant concurrence aux produits de Thermidaire. Advenant violation par Clarke de la présente clause relative aux produits concurrents, Clarke devra payer à Thermidaire en dommages-intérêts liquidés un montant égal aux bénéfices bruts d'exploitation réalisés par la vente de tels produits concurrents.

Bien que ni l'une ni l'autre des clauses de non-concurrence ne font mention d'une limitation territoriale de leur portée, et qu'on ait demandé la rectification pour motif d'erreur mutuelle, le juge de première instance les a jugées exécutoires sans

his view that there was no mutual mistake. In the Court of Appeal, whose reasons were delivered by Brooke J.A., the cross-appeal as to rectification was allowed and the operation of the two covenants was qualified by including therein the words "in the Territory".

I am not disposed to interfere with the view on rectification taken by the Court of Appeal, but I do not think that the relief was necessary in view of the definition in the contract of the territory within which the distributorship was to operate. It seems to me that, in the absence of any indications in the convenants against competition that they were to operate outside the distributorship territory, reasonable construction would limit them to that territory. I do not find it compelling today to view the covenants against competition as if they were detached provisions and to seek thereby a basis of invalidation, especially when no claim was made by the covenantee for a wider application than the distributorship territory.

I need not embark here on any discussion of whether the two convenants, either as rectified or as limited by construction to operation only in the distributorship territory, are invalid as in unreasonable restraint of trade. Both the trial judge and the Court of Appeal found them to be reasonable *inter partes* and consonant with the public interest, and this conclusion was not questioned by the appellant save by reading the convenants as being unlimited in territorial ambit. In failing on this point they fail also in any challenge to the covenants as being in unreasonable restraint of trade.

This brings me to the second and, as I said, the main point in the appeal. The trial judge found, and the Court of Appeal confirmed, that the appellant Clarke had broken the contract during its currency by selling competitive products other than those of the respondent and that it had also broken the covenant against post-contract competition. These findings, and as well a finding that

accorder la rectification, étant d'avis qu'il n'y avait pas eu erreur mutuelle. En la Cour d'appel, dont les motifs ont été rédigés par le juge d'appel Brooke, l'appel incident relatif à la rectification a été accueilli et l'application des deux clauses a été atténuée par inclusion des mots «dans le Territoire».

Je ne suis pas prêt à modifier la position qu'a prise la Cour d'appel sur la rectification, mais je ne crois pas que le recours était nécessaire étant donné la définition dans le contrat du territoire dans lequel la distribution devait avoir lieu. Il me paraît que, en l'absence d'indications dans les clauses de non-concurrence qu'elles devaient s'appliquer en dehors du territoire de distribution, une interprétation raisonnable devrait restreindre leur application à ce territoire-là. Je n'estime pas qu'il faille aujourd'hui considérer les clauses de non-concurrence comme si elles étaient des dispositions détachées et chercher par là un fondement d'annulation, spécialement quand aucune réclamation n'a été faite par le créancier aux fins de leur donner une application plus vaste que le territoire de distribution.

Je n'ai pas à me lancer ici dans une discussion de la question de savoir si les deux clauses, soit telles que rectifiées soit telles que limitées par interprétation à l'application dans le territoire de distribution seulement, sont nulles pour motif de restriction déraisonnable du commerce. Le juge de première instance et la Cour d'appel ont tous deux statué qu'elles étaient raisonnables *inter partes* et en accord avec l'intérêt public, et cette conclusion n'a pas été mise en doute par l'appelante sauf qu'elle a interprété les clauses comme étant illimitées sur le plan territorial. En échouant sur ce point l'appelante échoue également dans toute contestation des clauses pour motif de restriction déraisonnable du commerce.

Cela m'amène au deuxième et, je l'ai dit, principal point du pourvoi. Le juge de première instance a conclu, et la Cour d'appel confirmé, que l'appelante Clarke avait brisé le contrat durant sa période d'application en vendant des produits concurrents autres que ceux de l'intimée, et qu'elle avait également violé la clause interdisant la concurrence post-contractuelle. Ces conclusions, de

the respondent was entitled to terminate the contract before it had run its five-year period, were not contested in this Court by the appellant.

At the time the parties hereto commenced their business relationship the appellant was in the business of selling boilers in western Canada. The respondent from 1958 on concentrated on the manufacture and sale of water treatment products; and in agreeing to give the appellant the exclusive distributorship of its products in the defined territory it necessarily excluded itself from sales therein and thus depended on the appellant to keep its name and its reputation before the public in the territory. The appellant was not only precluded by the contract between the parties from selling products in the territory competitive to those of the respondent but was also subject to other supporting contractual obligations, such as being required to give the respondent upon request its list of customers, and various provisions respecting advertising and packaging.

It was the appellant which initiated suit, claiming damages for wrongful termination of the contract on January 19, 1967, by the respondent and the latter counterclaimed for damages under the covenants against competition. The action was brought on March 9, 1967, the statement of claim was delivered on April 10, 1967, and the defence and counterclaim on April 25, 1967. The appellant discontinued its action on April 29, 1968, and the trial of the counterclaim began on September 19, 1971, well after the expiry of the three-year period within which the post-contract covenant against competition was effective. The respondent did not seek an interim or interlocutory injunction, which it might have done promptly and thus avoided the running of some of the damages which it claimed in its suit. Its explanation, which is far from satisfactory, was that there was a serious question whether there was a breach of the agreement by the appellant and, even if there was a breach, whether it was not remedied. The prayer for relief in the counterclaim did ask for an injunction but, of course, by the time the action came on for trial

même qu'une conclusion selon laquelle l'intimée avait le droit de résilier le contrat avant que sa durée de cinq ans ne se fût écoulée, n'ont pas été contestées en cette Cour par l'appelante.

Au moment où les parties au pourvoi ont commencé leurs relations d'affaires, l'appelante était dans le commerce de la vente de chaudières et elle faisait affaires dans l'ouest du pays. L'intimée à partir de 1958 a concentré ses activités sur la fabrication et la vente de produits de traitement d'eau; et en convenant d'octroyer à l'appelante la concession exclusive de distribution de ses produits dans le territoire défini elle s'interdisait nécessairement le droit d'y faire des ventes et comptait ainsi sur l'appelante pour garder son nom et sa réputation devant le public dans le territoire. L'appelante n'était pas seulement empêchée par le contrat intervenu entre les parties de vendre dans le territoire des produits faisant concurrence à ceux de l'intimée mais aussi elle était liée par d'autres obligations contractuelles accessoires, comme par exemple l'obligation de donner à l'intimée sur demande sa liste de clients, et diverses dispositions concernant la réclame et l'emballage.

C'est l'appelante qui a commencé les poursuites, réclamant des dommages-intérêts pour résiliation illicite du contrat par l'intimée le 19 janvier 1967, et cette dernière a fait une demande reconventionnelle en dommages-intérêts en vertu des clauses de non-concurrence. L'action a été intentée le 9 mars 1967, la déclaration écrite a été déposée le 10 avril 1967 et la défense et demande reconventionnelle le 25 avril 1967. L'appelante a discontinué son action le 29 avril 1968, et l'instruction de la demande reconventionnelle a commencé le 19 septembre 1971, bien après l'expiration de la période de trois ans durant laquelle la clause de non-concurrence post-contractuelle était en vigueur. L'intimée n'a pas cherché à obtenir une injonction provisoire ou interlocutoire, ce qu'elle aurait pu faire promptement évitant ainsi la continuation de certains des dommages qu'elle réclamait dans sa demande. Son explication, qui est loin d'être satisfaisante, a été qu'on se demandait sérieusement s'il y avait eu violation de l'accord par l'appelante et, même s'il y avait eu violation, si elle n'avait été réparée. Les conclusions de la demande reconventionnelle

there was no longer any basis for one. Nonetheless, it was obvious from the record that the appellant continued to sell competitive products other than those of the respondent after the contract was terminated and thus put itself at the risk, which indeed materialized, of being called to account under the formula for post-contract damages. Notwithstanding this, no interlocutory injunction was sought by the respondent.

demandent une injonction mais, bien entendu, lorsque le procès a eu lieu une injonction n'avait plus de raison d'être. Néanmoins, il apparaissait clairement au dossier que l'appelante avait continué à vendre des produits concurrents autres que ceux de l'intimée après la résiliation du contrat et s'était ainsi placée dans une situation où elle risquait d'être appelée, ce qui s'est effectivement produit, à rendre des comptes sous le régime de la formule concernant les dommages post-contractuels. Nonobstant cela, l'intimée n'a cherché à obtenir aucune injonction interlocutoire.

No question arises here as to the entitlement of the respondent to damages for breach of the covenant against competition during the currency of the contract (the covenant in this respect being enforceable), such damages being the loss suffered by the respondent by reason of sales by the appellant of products competitive with those of the respondent and not purchased from the respondent. The formula for assessing damages for breach of Article 15, the post-contract covenant, was however attacked as constituting a penalty rather than a measure of liquidated damages. It was accepted by counsel for the respective parties that the damages under the prescribed formula, namely, the gross trading profit realized by the covenantor on the sale of competitive products, would be about $200,000. Counsel for the appellant pointed to the very modest, almost inconsequential, profits of the respondent for the ten-year period 1961 to 1970 inclusive. Indeed, it was contended that were it not for an interest free loan to the respondent by its president, there would have been a loss over the ten-year period of some $86,000 if a realistic rate of interest had to be paid for the loan. To support its contention of the extravagance of the formula as a measure of liquidated damages, counsel for the appellant noted (although not accepting the sum as properly based) that the respondent had, in the alternative, claimed some $92,000 as the amount of its actual loss of net profit over the three-year post-contract period.

Aucune question ne se pose ici relativement au droit de l'intimée à des dommages-intérêts pour violation de la clause de non-concurrence durant la période d'application du contrat (la clause à cet égard étant exécutoire), les dommages étant la perte subie par l'intimée par suite de ventes par l'appelante de produits faisant concurrence à ceux de l'intimée et ne lui ayant pas été achetés. La formule d'évaluation des dommages pour violation de l'article 15, la clause post-contractuelle, a cependant été contestée comme étant une pénalité plutôt qu'une mesure servant à liquider les dommages. Il a été concédé par les avocats des parties que les dommages sous le régime de la formule prescrite, soit les bénéfices bruts d'exploitation réalisés par le débiteur lors de la vente de produits concurrents, s'élèveraient à environ $200,000. L'avocat de l'appelante a souligné les bénéfices très modestes, presque insignifiants, de l'intimée pour la période de dix ans allant de 1961 à 1970 inclusivement. On a même prétendu que si ce n'avait été d'un prêt sans intérêt fait à l'intimée par son président, il y aurait eu au cours de la période de dix ans une perte d'environ $86,000 si un taux d'intérêt réaliste avait dû être payé pour le prêt. Pour appuyer sa prétention d'extravagance de la formule comme mesure de dommages liquidés, l'avocat de l'appelante a noté (bien que n'acceptant pas la somme comme régulièrement fondée) que l'intimée avait, comme conclusion de remplacement, réclamé environ $92,000 comme montant de sa perte véritable de bénéfices nets au cours de la période post-contractuelle de trois ans.

The trial judge concluded that the formula of gross trading profit as the measure of liquidated

Le juge de première instance a conclu que la formule de bénéfices bruts d'exploitation adoptée

damages was a business-like and reasonable one, but this conclusion was associated with an apparent belief that the damages according to this formula would be small. The Court of Appeal accepted, as did counsel, that they would reach $200,000, but it held nonetheless that the formula, in the circumstances, was "one designed for the determination of liquidated damages in the truest sense and . . . therefore enforceable".

Although there was only brief consideration in the reasons of the trial judge of the issue whether the provision for liquidated damages (so termed by the parties in their contract) was not in substance a penalty and hence unenforceable, the Court of Appeal addressed itself to this issue at some length. I think it important to appreciate that we are dealing here with a not very usual case (so far as reported decisions go) where the pre-estimate of damages was not a fixed sum (as was the situation in the leading English case of *Dunlop Pneumatic Tyre Co. Ltd. v. New Garage and Motor Co. Ltd.*[2]) but was based upon a formula which when applied necessarily yielded a result far in excess of loss of net profits. Gross trading profit, in the words of the trial judge, "means the difference between the net selling prices of the goods and their laid down cost", the laid down cost being the seller's invoice price plus transportation charges to put the goods on the purchaser's shelves. In the words of the Court of Appeal, "the term 'gross trading profit' is profit after cost of sales but before costs customarily deducted to determine net profit".

The contract in this case was lawfully terminated by the respondent on January 19, 1967, and the three-year post-contract covenant against competition ran from that date. The appellant admitted in a letter from its president, dated January 16, 1967,

[2] [1915] A.C. 79.

comme mesure des dommages liquidés était propre aux affaires et raisonnable, mais cette conclusion est associée à une croyance apparente que les dommages-intérêts fixés suivant cette formule seraient peu élevés. La Cour d'appel a accepté, comme l'ont fait les avocats, qu'ils s'élèveraient à $200,000, mais elle a néanmoins statué que la formule, dans les circonstances, était [TRADUCTION] «une formule conçue pour la fixation de dommages liquidés dans le sens le plus véritable de l'expression et ... par conséquent susceptible d'exécution».

Bien que les motifs du juge de première instance ne parlent que brièvement de la question de savoir si la disposition prévoyant des dommages-intérêts liquidés (ainsi appelée par les parties dans leur contrat) n'était pas essentiellement une pénalité et donc non exécutoire, la Cour d'appel s'est penchée sur cette question plus longuement. Je crois qu'il est important de comprendre que nous sommes ici en présence d'un cas très habituel (si on s'en tient aux décisions publiées) où l'estimation anticipée des dommages-intérêts n'était pas une somme fixe (comme c'était le cas dans l'arrêt de principe rendu en Angleterre dans l'affaire *Dunlop Pneumatic Tyre Co. Ltd. v. New Garage and Motor Co. Ltd.*[2]) mais était basée sur une formule dont l'application devait nécessairement produire un résultat dépassant de beaucoup la perte de bénéfices nets. Les bénéfices bruts d'exploitation, d'après les termes utilisés par le juge de première instance, [TRADUCTION] «désignent la différence entre les prix de vente nets des produits et leurs prix de revient énoncés», le prix de revient énoncé étant le prix facturé par le vendeur plus les frais de transport requis pour placer les produits sur les étalages de l'acheteur. D'après les termes employés par la Cour d'appel, [TRADUCTION] «l'expression bénéfices bruts d'exploitation est le profit après le coût des ventes mais avant les coûts habituellement déduits pour déterminer les bénéfices nets».

Le contrat en l'espèce a été licitement résilié par l'intimée le 19 janvier 1967 et la clause interdisant la concurrence post-contractuelle pour trois ans est entrée en vigueur à compter de cette date-là. L'appelante a reconnu dans une lettre adressée par son

[2] [1915] A. C. 79.

that as late as June, 1966, it had sold competitive products covered by the agreement and not purchased from the respondent, and it promised to desist from this "hereafter". The trial judge, obviously by inadvertent error, referred to June 30, 1967 (instead of to June, 1966) as the end period to which the admission referred. In fact, the appellant did not desist after termination of the contract, and there is evidence that from January 1, 1967, to January 31, 1969, the gross trading profit of the appellant was $177,161.20, consisting of $78,739.80 for 1967, $93,609.25 for 1968 and $4,812.15 for the one month of 1969, the appellant having in 1969 changed its year end from December 31 to January 31.

I take the judgment of the Ontario Court of Appeal to be based on the fact that the parties had fixed the formula of gross trading profit after a mutual consideration of the difficulty of establishing compensation for a probably substantial loss, having regard to the factors to be considered, if there was a breach of the post-contract covenant not to compete. The extent of the loss, by reason of the formula, would vary directly with the length of time, up to the three year limit, over which the breach would continue. In his reasons in the Court of Appeal, Brooke J.A. assessed the matter as follows:

The disproportion of gross trading profit and net profit and financial position of Thermidaire were known by the parties when this agreement was struck. No doubt net profit was considered inappropriate as a measure of damage or loss since its application would involve charging all the costs of advertising, promotion and administration used to put down Thermidaire in a prohibited competitive venture. As to the true object of the provision, Mr. Deeks stated that the formula was used because of the serious difficulties involved in calculating not only simple loss of profit through the prohibited competition, but also the loss of things of value, of real value, which the parties well understood. This included such matters as the loss of the past value of previous years of advertising by Clarke of the Thermidaire products, the loss of present and future worth of advertising by Thermidaire by reason of Clarke's active competition

président, en date du 16 janvier 1967, qu'aussi récemment qu'en juin 1966 elle avait vendu des produits concurrents visés par l'accord et non achetés de l'intimée, ce à quoi elle a promis de renoncer «à partir de maintenant». Le juge de première instance, de toute évidence par suite d'une erreur commise par inadvertance, a mentionné le 30 juin 1967 (au lieu de juin 1966) comme étant la fin de la période que mentionnait l'aveu. En fait, l'appelante n'a pas renoncé après la résiliation du contrat, et il y a preuve que du 1er janvier 1967 au 31 janvier 1969 les bénéfices bruts d'exploitation de l'appelante ont été de $117,-161.20, consistant dans une somme de $78,739.80 pour 1967, de $93,609.25 pour 1968 et $4,812.15 pour l'unique mois de 1969, l'appelante ayant en 1969 changé sa fin d'exercice du 31 décembre au 31 janvier.

Je considère le jugement de la Cour d'appel de l'Ontario comme basé sur le fait que les parties avaient fixé la formule relative aux bénéfices bruts d'exploitation après examen conjoint de la difficulté d'établir une indemnisation pour une perte probablement substantielle, eu égard aux facteurs à considérer, advenant une violation de la clause de non-concurrence post-contractuelle. L'étendue de la perte, par suite de la formule, devait varier directement en fonction de la durée au cours de laquelle la violation se poursuivrait, jusqu'à la limite de trois ans. Dans ses motifs en Cour d'appel, le juge d'appel Brooke a vu la question comme suit:

[TRADUCTION] La disproportion entre les bénéfices bruts d'exploitation et les bénéfices nets, ainsi que la situation financière de Thermidaire, étaient connues par les parties lorsque l'accord a été conclu. Il ne fait pas de doute que les bénéfices nets ont été considérés comme non appropriés comme mesure de dommages ou de pertes du fait que leur application comporterait la déduction de tous les coûts de réclame, de promotion et d'administration consacrés à l'écrasement de Thermidaire dans une initiative de concurrence prohibée. Quant à l'objet véritable de la disposition, M. Deeks a dit que la formule avait été utilisée à cause des difficultés sérieuses que comporte le calcul non seulement de la simple perte de bénéfices due à la concurrence prohibée, mais également de la perte de choses de valeur, de valeurs réelles, que les parties comprenaient bien. Cela comprenait des choses comme la perte de la valeur

and, of course, the loss of the value of product identification, product integrity and the loss of customers and, of importance, the name and reputation of the product in the marketplace. If the effect in terms of loss of present and future sales because of adverse advertising and competitive sales suffered by a company which had placed its entire reliance upon the conduct of its exclusive agent was properly a part of the parties' consideration, perhaps the difficulty encountered by the witness Anderson in his attempt to establish the loss limited to Thermidaire's net profit reflects the difficulties which the parties foresaw in any effort to assess the real loss which would be sustained by Thermidaire in the event of a breach. It is clear to me that the learned trial judge accepted the evidence of Mr. Deeks as worthy of belief and entirely reasonable in these circumstances.

passée de la réclame faite par Clarke au sujet des produits de Thermidaire durant les années antérieures, la perte de la valeur présente et future de la réclame de Thermidaire par suite de la concurrence active de Clarke et, bien entendu, la perte de la valeur d'identification du produit, d'intégrité du produit et la perte de clients et, chose importante, du renom et de la réputation du produit sur le marché. Si l'effet en termes de perte de ventes présentes et futures pour cause de réclame concurrente et de ventes préjudiciables à une compagnie qui avait placé sa pleine confiance dans la conduite de son concessionnaire exclusif, faisait régulièrement partie des préoccupations des parties, peut-être la difficulté qu'a éprouvée le témoin Anderson dans sa tentative d'établir la perte limitée aux bénéfices nets de Thermidaire reflète-t-elle les difficultés que les parties prévoyaient dans toute tentative d'évaluer la perte réelle que subirait Thermidaire advenant une violation. Il est clair selon moi que le savant juge de première instance a accepté le témoignage de M. Deeks comme digne de foi et entièrement raisonnable dans ces circonstances.

Does the formula represent a genuine attempt by the parties to pre-estimate the loss as best they could within their special knowledge of the circumstances? It is true that the amount that may eventually be assessed may be large, but this was foreseeable when the contract was entered upon. Equally clear was the fact that the loss in terms of both profits and value, as above-mentioned, would also be large. Indeed, the longer the competition was carried on within the prohibited period the greater would be the loss, and the more successful the competition, the greater was the probability that Thermidaire would suffer substantial and permanent damage in the light of the various factors above-mentioned. Losses such as loss of product identification, loss of the benefits of advertising through the operations of its exclusive agent throughout a large territory are among the imponderables for the appraisal which this clause was intended to provide. To have fixed a lump sum as a measure of Thermidaire's damages would have been a haphazard measure at best and, in all the circumstances, the employment of a formula geared to sales of competitive products during the prohibited period was adopted by two keen business firms as the best method of determining the loss resulting from a breach of the covenant—a covenant into which they entered with their eyes open.

La formule représente-t-elle une tentative authentique des parties d'estimer à l'avance la perte du mieux qu'elles le pouvaient selon leur connaissance spéciale des circonstances? Il est vrai que le montant qui pourra éventuellement être fixé peut s'avérer élevé, mais cela était prévisible quand le contrat a été conclu. Il était également clair que la perte en termes à la fois de bénéfices et de valeur, comme mentionné ci-dessus, serait élevée aussi. En effet, plus la durée de la concurrence serait longue à l'intérieur de la période prohibée, plus la perte serait grande, et, de même, plus la concurrence faite aurait du succès, plus il était probable que Thermidaire subisse des dommages substantiels et permanents à la lumière des divers facteurs ci-dessus. Des pertes telles que perte d'identification de produit, perte des avantages de la réclame par le truchement des activités de sa concessionnaire exclusive à la grandeur d'un vaste territoire sont parmi les impondérables que cette clause était destinée à évaluer. Fixer une somme globale comme mesure des dommages de Thermidaire aurait été au mieux une disposition prise au petit bonheur et, dans toutes les circonstances, l'emploi d'une formule axée sur les ventes de produits concurrents durant la période prohibée a été adoptée par deux entreprises averties comme la meilleure méthode de déterminer la perte résultant d'une violation de la clause—clause qu'elles ont arrêtée en pleine connaissance de cause.

When is the amount of recovery in such circumstances extravagant as opposed to actual probable loss? The fact that the estimated loss of net profit,

Quand le montant de recouvrement est-il dans de telles circonstances extravagant en regard de la perte probable réelle? Le fait que la perte prévue de bénéfices

$92,000.00, is something a little less than half of the possible recovery of $200,000.00 in circumstances like these is not by itself proof of extravagance. The figures may be large, but I am not persuaded that they are unrealistic or extravagant. The parties knew and appreciated these factors and chose this method to establish compensation for a loss, the amount of which was difficult to determine and, no doubt, very costly to establish. I am convinced that they agreed upon a method which they both regarded as one which would lead to a fair and just determination of Thermidaire's damages and losses in the event of a breach of the covenant.

If all that was involved in determining whether the parties had agreed on a measure of liquidated damages or on a penalty was the intention of those parties, there could be no quarrel with the result reached at trial and on appeal. Indeed, if that was the case it is difficult to conceive how any penalty conclusion could ever be reached when business men or business corporations, with relatively equal bargaining power, entered into a contract which provided for payment of a fixed sum or for payment pursuant to a formula for determining damages, in case of a breach of specified covenants, including a covenant not to compete. The law has not, however, developed in this way in common law jurisdictions; and the power to relieve against what a court may decide is a penalty is a recognized head of equity jurisdiction. Of course, the court will begin by construing the contract in which the parties have objectively manifested their intentions, and will consider the surrounding circumstances so far as they can illuminate the contract and thus aid in its construction. It seems to me, however, that if, in the face of the parties' assertion in their contract that they were fixing liquidated damages, the court concludes that a penalty was provided, it would be patently absurd to say that the court was giving effect to the real intention of the parties when the court's conclusion was in disregard of that intention as expressed by the parties.

What the court does in this class of case, as it does in other contract situations, is to refuse to

nets, $92,000, soit quelque chose d'un peu moins que la moitié du recouvrement possible de $200,000 dans des circonstances comme celles-ci, n'est pas en soi une preuve d'extravagance. Les chiffres peuvent être élevés, mais je ne suis pas convaincu qu'ils ne sont pas réalistes ou qu'ils sont extravagants. Les parties connaissaient et comprenaient ces facteurs et elles ont choisi cette méthode pour établir l'indemnité qui serait octroyée pour une perte, dont le montant était difficile à déterminer et, sans doute, d'estimation coûteuse. Je suis convaincu qu'elles sont tombées d'accord sur une méthode qu'elles considéraient toutes deux comme une méthode qui permettrait l'évaluation équitable et juste des dommages et des pertes advenant une violation de la clause.

Si la question de savoir si les parties avaient convenu d'une mesure de dommages liquidés ou d'une pénalité reposait uniquement sur l'intention de ces parties, on ne pouvait rien objecter au résultat auquel on a conclu en première instance et en appel. Voire, si tel était le cas il est difficile de concevoir comment on pourrait jamais conclure qu'une pénalité a été stipulée quand des hommes d'affaires ou corporations commerciales, dotés d'un pouvoir de marchandage relativement égal, ont conclu un contrat prévoyant le paiement d'une somme fixe ou le paiement d'une somme conformément à une formule de détermination des dommages, advenant la violation de clauses précises, y compris d'une clause de non-concurrence. Le droit ne s'est pas, toutefois, développé de cette façon dans les ressorts de *Common Law*; et le pouvoir d'alléger ce qu'un tribunal peut juger constituer une pénalité est un chef reconnu de la compétence d'*equity*. Bien entendu, le tribunal interprétera d'abord le contrat dans lequel les parties ont objectivement manifesté leurs intentions, et considérera les circonstances du contrat dans la mesure où elles peuvent illuminer celui-ci et ainsi aider à son interprétation. Il me semble, cependant, que si, devant l'assertion des parties dans leur contrat, selon laquelle elles fixaient des dommages liquidés, le tribunal conclut qu'une pénalité se trouvait stipulée, il serait manifestement absurde de dire que le tribunal s'est trouvé à donner effet à l'intention réelle des parties quand la conclusion du tribunal est tirée au mépris de cette intention telle qu'elle a été exprimée par les parties.

Ce que fait le tribunal dans cette catégorie de cas, comme dans d'autres situations contractuelles,

enforce a promise in strict conformity with its terms. The court exercises a dispensing power (which is unknown to the civil law of Quebec) because the parties' intentions, directed at the time to the performance of their contract, will not alone be allowed to determine how the prescribed sum or the loss formula will be characterized. The primary concern in breach of contract cases (as it is in tort cases, albeit in a different context) is compensation, and judicial interference with the enforcement of what the courts regard as penalty clauses is simply a manifestation of a concern for fairness and reasonableness, rising above contractual stipulation, whenever the parties seek to remove from the courts their ordinary authority to determine not only whether there has been a breach but what damages may be recovered as a result thereof.

est de refuser d'exécuter une promesse d'une façon strictement conforme avec ses termes. Le tribunal exerce un pouvoir de dispense (que ne connaît pas le droit civil du Québec) pour le motif qu'on ne permettra pas aux intentions des parties, concentrées à l'époque sur l'accomplissement de leur contrat, de décider à elles seules comment la somme prescrite ou la formule compensatoire seront caractérisées. La préoccupation première dans les affaires de violation de contrat (comme c'est le cas dans les affaires de délit civil, bien que dans un contexte différent) est l'indemnisation, et l'intervention judiciaire dans l'exécution de ce que les tribunaux considèrent être des clauses pénales est simplement une manifestation d'une préoccupation d'équité et de raison, s'élevant au-dessus des stipulations contractuelles, chaque fois que les parties tentent de retirer aux tribunaux leur pouvoir ordinaire de déterminer non seulement si il y a eu violation mais quels dommages-intérêts peuvent être recouvrés par suite de la violation.

The courts may be quite content to have the parties fix the damages in advance and relieve the courts of this burden in cases where the nature of the obligation upon the breach of which damages will arise, the losses that may reasonably be expected to flow from a breach and their unsusceptibility to ready determination upon the occurrence of a breach provide a base upon which a pre-estimation may be made. But this is only the lesser half of the problem. The interference of the courts does not follow because they conclude that no attempt should have been made to predetermine the damages or their measure. It is always open to the parties to make the predetermination, but it must yield to judicial appraisal of its reasonableness in the circumstances. This becomes a difficult question of judgment, especially in a case like the present one involving a covenant not to compete which engages the reputation and the vicarious presence of the covenantee in the territorial area of the covenant as well as the products which are the subject of the covenant.

Les tribunaux peuvent fort bien s'accommoder de voir les parties fixer à l'avance les dommages et décharger les tribunaux de cette tâche dans des affaires où la nature de l'obligation dont la violation entraînera des dommages-intérêts, les pertes qu'on peut raisonnablement s'attendre de voir découler d'une violation, et l'incapacité de les évaluer rapidement lorsque survient une violation, fournissent une base sur laquelle préétablir le montant des dommages. Mais cela n'est que la moitié la moins importante de la difficulté. Ce n'est pas parce qu'ils concluent qu'aucune tentative n'aurait dû être faite de préétablir les dommages ou la mesure de ceux-ci, que les tribunaux interviennent. Les parties peuvent toujours préétablir les dommages, mais ce qu'ils ont établi ne peut être soustrait au pouvoir des tribunaux d'en apprécier le caractère raisonnable eu égard aux circonstances. Cela devient une question de jugement difficile, spécialement dans un cas comme le cas présent où une clause de non-concurrence engage dans les limites de son champ territorial la réputation du créancier et sa présence par délégation aussi bien que les produits qui font l'objet de la clause.

In the present case the formula of gross trading profit was not defined, but in the general under-

Dans l'affaire présente la formule des bénéfices bruts d'exploitation n'a pas été définie, mais sui-

standing of the term as adopted by the courts below it departs markedly from any reasonable approach to recoverable loss or actual loss since all the elements of costs and expenses which would be taken into account to arrive at net profit are excluded from consideration. It is of considerable significance on this aspect of the matter to note how the respondent, in putting its best foot forward to show its actual loss, made up its estimated loss of net profits of $92,017, which is less than half of the sum, in fact about 40 per cent, which would be its recoverable damages under the contract formula of gross trading profits.

Evidence of the estimated loss of net profits over the three-year period in question was given on behalf of the respondent by one Anderson, a chartered accountant and member of a firm which was auditor for the respondent. His calculations are set out in an exhibit, Exhibit 72, which shows sales for each of the three years 1967 to 1969 inclusive and cost of sales. The difference between these sums was the gross profit in an amount of $110,270 from which were deducted expenses of warehousing (a minor expense), commissions, office and travel expenses, leaving a net of $92,017 as the loss of profit. Anderson agreed, when cross-examined on his calculations, that they were based on four assumptions put to him by counsel for the appellant, as follows:

> Q. Then the validity of your figures as estimates depends on four assumptions: the first, that Thermidaire would have sold all that Clarke did; the second, that Clarke's sales figures for water chemical treatment material are the correct sales figures; that your figures for Thermidaire's cost of sales are correct; and that your estimate as to how selling and administrative expenses would have increased with the increased sales.
>
> A. That is correct.

Anderson's evidence was that Clarke's gross trading profit for the three-year period amounted to $239,449.05, consisting of $78,739.80 in 1967,

vant ce que les cours d'instance inférieure ont jugé être le sens généralement accordé à l'expression elle s'écarte de façon marquée de toute approche raisonnable servant à déterminer la perte recouvrable ou la perte réelle puisque tous les éléments de coût et de dépense dont il serait tenu compte pour calculer les bénéfices nets n'entrent plus du tout en ligne de compte. Sur cet aspect de l'affaire il est éminemment significatif de noter comment l'intimée, en montrant sa perte réelle de la façon la plus persuasive, a établi sa perte de bénéfices nets estimative de $92,017, ce qui est moins de la moitié, en fait environ 40 pour cent, de ce que seraient ses dommages-intérêts recouvrables sous le régime de la formule contractuelle des bénéfices bruts d'exploitation.

Un témoignage donnant la perte estimative de bénéfices nets pour les trois années en cause a été fourni au nom de l'intimée par un nommé Anderson, un comptable agréé qui faisait partie de la maison qui faisait la vérification des livres de l'intimée. Ces calculs sont exposés dans une pièce, la pièce 72, qui montre les ventes pour chacune des trois années 1967 à 1969 inclusivement ainsi que le coût des ventes. La différence entre ces sommes a été le bénéfice brut d'un montant de $110,270, duquel ont été déduits des frais d'entreposage (une dépense mineure), commissions, frais de bureau et de déplacement, laissant un montant net de $92,017 comme perte de bénéfices. Anderson a convenu, lorsqu'on l'a contre-interrogé sur ses calculs, qu'ils étaient basés sur quatre postulats que l'avocat de l'appelante lui a exposés comme suit:

> [TRADUCTION] Q. Donc la validité de vos chiffres en tant que chiffres estimatifs repose sur quatres postulats: le premier, que Thermidaire aurait vendu tout ce que Clarke a vendu; le second, que les chiffres de vente de Clarke relativement aux produits de traitement chimique de l'eau sont exacts; que vos chiffres relativement au coût des ventes de Thermidaire sont exacts; et que votre estimation de la façon dont les frais de vente et d'administration auraient augmenté avec l'augmentation des ventes.
>
> R. C'est juste.

Le témoignage d'Anderson a été que les bénéfices bruts d'exploitation de Clarke pour la période de trois ans s'étaient élevés à $239,449.05, consis-

$93,609.25 in 1968 and $67,100 in 1969. By contrast, the appellant's net profit for the three-year period in respect of sales of competitive products appears to have been insignificant, if indeed there was any at all. There was a net loss of over $17,000 in 1967 and a net gain of some $18,000 in 1968. There was no net gain figure for 1969, but taking $67,100 as the gross trading profit for that year (as Anderson's evidence showed) the net profit, on any reasonable assessment of deductible expenses, could not have been very large. The respondent Thermidaire's gross trading profit during this period, if it had sold the units or products that Clarke had sold in the same period would have been $110,270, and this is the sum shown on Exhibit 72. The reason for the disparity between the gross trading profits of the appellant and of the respondent, referable to the same and to the same number of items, was that the respondent was a wholesaler selling through a distributor, the appellant, which sold direct to the consumer at retail prices. There could be no affinity between the respective profits of the two firms in respect of products which the appellant did in fact sell and those that the respondent might have sold in the same market during the three-year period because the respondent would be selling at wholesale prices and the appellant at retail prices which would involve a considerable distributor's or resale mark-up, as, for example, a 47 per cent mark-up in 1968 as noted by Anderson in his evidence. (The mark-ups for 1967 and 1969, estimated by Anderson, were 52 per cent and 45 per cent respectively, and he regarded the mark-ups for the three years as reasonable.) Thus, their respective costs were different and their respective selling and administrative expenses were different.

Anderson's figures for Thermidaire's projected sales for 1967 to 1969 inclusive were the figures for Clarke's actual retail sales in that period less the resale mark-up. To take 1967 by way of illustration, Clarke's retail sales in that year of Thermidaire products had a value of $159,667.83,

tant en des sommes de $78,739.80 en 1967, $93,609.25 en 1968 et $67,100 en 1969. Par contraste, les bénéfices nets de l'appelante pour les trois années en ce qui concerne les ventes de produits concurrents semblent avoir été insignifiants, si tant est qu'il y en a eu. Il y a eu une perte nette de plus de $17,000 en 1967 et des gains nets de quelque 18,000 dollars en 1968. Aucun chiffre de gain net n'a été donné pour 1969, mais prenant le chiffre de $67,100 comme bénéfices bruts d'exploitation pour cette année-là (comme l'a montré le témoignage d'Anderson) les bénéfices nets, calculés d'après toute évaluation raisonnable de frais déductibles, n'ont pu être très élevés. Les bénéfices bruts d'exploitation de l'intimée Thermidaire durant cette période, si elle avait vendu les unités ou produits que Clarke avait vendus au cours de la même période, auraient été de $110,270, et c'est là la somme que montre la pièce 72. La raison de la disparité entre les bénéfices bruts d'exploitation de l'appelante et de l'intimée, par référence aux mêmes produits et aux mêmes quantités de produits, était que l'intimée était un grossiste vendant par l'entremise d'un distributeur, l'appelante, qui vendait directement aux consommateurs aux prix du détail. Il ne pouvait y avoir d'affinité entre les bénéfices respectifs des deux firmes relativement à des produits que l'appelante a effectivement vendus et à ceux que l'intimée aurait pu vendre sur le même marché durant la période de trois ans car l'intimée vend au prix du gros et l'appelante, elle, vend à des prix de détail comportant une majoration de distributeur ou détaillant considérable, comme, par exemple, une majoration de 47 pour cent en 1968 comme l'a noté Anderson dans son témoignage. (Les majorations de 1967 et 1969, selon l'estimation d'Anderson, étaient de 52 pour cent et 45 pour cent respectivement, et il a considéré les majorations des trois années comme des majorations raisonnables.) Ainsi, leurs coûts respectifs étaient différents et leurs frais de vente et d'administration étaient différents.

Les chiffres d'Anderson pour les ventes projetées de Thermidaire pour 1967 à 1969 inclusivement étaient les chiffres afférents aux ventes au détail réelles de Clarke au cours de cette période moins la majoration de revente. Pour prendre 1967 comme exemple, les ventes au détail de Clarke

which less the mark-up left the sum of $102,154. From this sum Anderson deducted Thermidaire's cost of sales to arrive at gross profit and then deducted expenses to arrive at net profit for the year. His formula for determining cost of sales was based on an examination of the respondent's financial statements for the years 1967 to 1969 and a finding that the cost was a certain percentage of the selling price, namely 30.37 per cent for 1967 and until September 1968 and 24.65 per cent for the remainder of 1968 and for all of 1969. The lower percentage was because the respondent began to sell its own manufactured products in October 1968. The percentages were applied to the retail sale figures of the appellant's sales (not deducting the resale mark-up) and thus a figure was obtained of the estimated cost of sales.

durant cette année-là en ce qui a trait aux produits de Thermidaire avaient une valeur de $159,667.83, ce qui, une fois la majoration déduite, laissait la somme de $102,154. De cette somme Anderson a déduit le coût des ventes de Thermidaire pour arriver aux bénéfices bruts et ensuite il a déduit les frais pour arriver aux bénéfices nets de l'année. Sa formule pour déterminer le coût des ventes était basée sur un examen des états financiers de l'intimée pour les années 1967 à 1969 et une constatation selon laquelle le coût représentait un certain pourcentage du prix de vente, soit 30.37 pour cent pour 1967 et jusqu'à septembre 1968 et 24.65 pour cent pour le reste de 1968 et pour toute l'année de 1969. Le pourcentage inférieur est dû au fait que l'intimée a commencé à vendre ses propres produits manufacturés en octobre 1968. Les pourcentages ont été appliqués aux chiffres de ventes au détail de l'appelante (majoration de revente non déduite) et ainsi il en est arrivé à un coût des ventes estimatif.

The estimated net profit loss of $92,017 was vigorously attacked by the appellant, and with some justification. For example, there appears to have been some dispute as to whether Anderson's calculations were based solely on so-called competitive products or included others that were not differentiated in the appellant's financial statements. I need say no more about it here other than that it represented an estimate that was as favourable as such an exercise could be to the party that commissioned it. Because of the views of the courts below that gross trading profits were recoverable it was unnecessary for them to inquire into the merit of the sum put forward as the estimated loss of net profits.

La perte de bénéfices nets estimative au montant de $92,017 a été vigoureusement contestée par l'appelante, et avec quelque justification. Par exemple, il semble qu'il y ait eu quelque dispute quant à savoir si les calculs d'Anderson étaient basés uniquement sur les produits qu'on a appelés les produits concurrents ou s'ils en incluaient d'autres qui n'étaient pas différenciés dans les états financiers de l'appelante. Je n'ai pas ici à en dire davantage sur ce chiffre si ce n'est qu'il représentait une estimation qui était aussi favorable qu'une telle enquête pouvait l'être pour la partie qu'il l'avait commandée. A cause des vues des cours d'instance inférieure selon lesquelles les bénéfices bruts d'exploitation étaient recouvrables il ne leur a pas été nécessaire de rechercher le bien-fondé de la somme avancée comme perte estimative de bénéfices nets.

I think it well to emphasize that the estimated actual loss of $92,017 and the estimated loss of gross trading profits of $239,449.05 are sums which relate to the entire three-year post-contract period during which the covenant not to compete was operative. Had the court been called upon to deal with the question of liquidated damages or penalty at or shortly after the time that the con-

Je crois qu'il est bon de souligner que la perte réelle estimative de $92,017, ainsi que le chiffre estimatif de $239,449.05 pour la perte de bénéfices bruts d'exploitation, sont des sommes qui se rapportent à la totalité des trois années post-contractuelles durant lesquelles s'est appliqué la clause de non-concurrence. Si le tribunal avait été appelé à trancher la question des dommages liquidés ou de

tract was lawfully terminated neither the actual loss nor the gross trading profits would have been in any substantial figure, a result that would be fortified, and indeed secured, if an interlocutory injunction had been sought and granted. No such injunction was, however, even sought, and hence the continuation of the breach to the end of the post-contract covenant period yielded the high figures to which reference has been made.

Had a single sum been fixed as a pre-estimate in the amount of some $200,000, it is impossible to think that the court would not have concluded that an *in terrorem* penalty had been fixed at the time of the contract. Moreover, to regard that sum as being equally claimable for a breach that lasted for a short time as well as for a breach which continued over the entire covenant period would be an unreasonable conclusion. The question that arises here however is whether the same appreciation should prevail in a case where the quantum of damages, actually suffered or claimable, depends on the length of time over which the covenantor continues to be in breach of its covenant.

Should the respondent here be faulted then because it did not seek an interim injunction when it filed its counterclaim on April 25, 1967, some three months after it terminated the contract, or because it did not thereafter seek an interlocutory injunction until trial through which to stanch the flow of damages measured by gross trading profits? There is no doubt that a covenantee cannot have both an injunction during the covenant period and damages based on a breach of covenant for the entire period where they are based on a formula. There is case law holding that where a fixed sum is stipulated as the liquidated damages upon a breach, the covenantee cannot have both the damages and an injunction but must elect between the two remedies: see *General Accident Assurance Corp. v. Noel*[3]; *Wirth and Hamid Booking Inc. v. Wirth*[4]. I do not however read these cases as excluding damages for past loss by reason of the breach, but only as precluding recovery of the

[3] [1902] 1 K.B. 377.
[4] (1934), 192 N.E. 297.

la pénalité à l'époque où le contrat a été licitement résilié ou peu de temps après, ni la perte réelle ni les bénéfices bruts d'exploitation n'auraient été d'un chiffre élevé, un résultat qui serait renforcé, voir assuré, si une injonction interlocutoire avait été demandée et obtenue. Aucune semblable injonction n'a, cependant, été même demandée, et par conséquent la continuation de la violation jusqu'à la fin de la période de la clause post-contractuelle a produit les chiffres élevés déjà mentionnés.

Si une estimation préétablie avait été fixée à une somme unique d'un montant d'environ $200,000, il est impossible de penser que le tribunal n'aurait pas conclu qu'une pénalité *in terrorem* avait été fixée au moment du contrat. De plus, considérer cette somme comme étant exigible de façon égale tant pour une violation de courte durée que pour une violation qui s'est poursuivie durant toute la période de la clause serait une conclusion déraisonnable. La question qui se pose ici cependant est de savoir si la même appréciation devrait prévaloir dans un cas où le montant des dommages, effectivement subis ou pour lesquels on peut réclamer, dépend de la durée pendant laquelle le débiteur continue de violer son engagement.

Faudrait-il donc ici tenir rigueur à l'intimée de n'avoir pas cherché à obtenir une injonction provisoire lorsqu'elle a déposé sa demande reconventionnelle le 25 avril 1967, quelque trois mois après qu'elle eut résilié le contrat, ou de n'avoir pas ensuite cherché à obtenir une injonction interlocutoire jusqu'au procès de façon à arrêter le flux des dommages mesurés par les bénéfices bruts d'exploitation? Il ne fait pas de doute qu'un créancier ne peut obtenir à la fois une injonction durant la période de la clause et des dommages-intérêts fondés sur une violation toute la période durant lorsque ceux-ci sont basés sur une formule. Il est des arrêts qui ont décidé que lorsqu'une somme fixe est stipulée pour valoir comme montant de dommages liquidés lors d'une violation, le créancier ne peut avoir à la fois les dommages-intérêts et une injonction mais doit choisir entre les deux recours: voir *General Accident Assurance Corp. v. Noel*[3]; *Wirth and Hamid Booking Inc. v. Wirth*[4].

[3] [1902] 1 K.B. 377.
[4] (1934), 192, N.E. 297.

liquidated amount referable to breach in the future which that amount was designed to cover and against which an injunction has been granted. By not seeking an interim or interlocutory injunction, the respondent gives some support to the proposition that it was more profitable to it to let the default of the appellant continue. On the other hand, the appellant accepted the risk of being held liable for gross trading profits by continuing to be in breach for the entire post-contract period of the covenant's operation.

Je n'interprète pas toutefois ces arrêts comme excluant des dommages-intérêts pour une perte passée qui est due à la violation, mais seulement comme empêchant le recouvrement du montant liquidé se rapportant à la violation ultérieure que ce montant était destiné à couvrir et contre laquelle une injonction a été accordée. En ne cherchant pas à obtenir une injonction provisoire ou interlocutoire, l'intimée donne un certain appui à la proposition selon laquelle il était plus profitable pour elle de laisser continuer le manquement de l'appelante. D'un autre côté, l'appelante a accepté le risque d'être tenue responsable des bénéfices bruts d'exploitation en continuant la violation pour toute la période post-contractuelle durant laquelle s'est appliquée la clause.

In this state of affairs, I think the proper course is to look at the situation (as in fact it was at the time of the trial) as one where each party was content to have the issue of liquidated damages or penalty determined according to the consequences of a breach over the entire period of the covenant. The appellant cannot, of course, escape liability for at least the damages which a court would fix if called upon to do so. Should it be so called upon in this case by a holding that to allow recovery of gross trading profits would be to impose a penalty and not to give compensation in a situation where calculation of damages is difficult and incapable of precise determination? I would answer this question (and I do it after anxious consideration) in the affirmative.

Devant cet état de choses, je pense que la façon régulière de procéder est de voir la situation (ainsi qu'elle était effectivement au moment du procès) comme une situation où chaque partie était satisfaite de faire décider la question des dommages liquidés ou de la pénalité en conformité des conséquences qui interviennent lorsqu'une violation se poursuit toute la période durant. L'appelante ne peut, bien entendu, éviter d'être responsable d'au moins les dommages-intérêts que fixerait un tribunal s'il était appelé à le faire. Celui-ci devait-il être ainsi appelé à le faire en l'espèce par suite d'une décision statuant que permettre le recouvrement des bénéfices bruts d'exploitation serait imposer une pénalité et non octroyer une indemnisation quand le calcul des dommages-intérêts est difficile et non susceptible d'évaluation précise? Je répondrais à cette question (et je le fais après mûre réflexion) par l'affirmative.

I do not ignore a factor or factors in connection with breach of a covenant not to compete that are not as easily measured in dollars as are gross trading profits and net profits but which nonetheless have a value. These entered into the consideration of the Ontario Court of Appeal, and they were mentioned in Anderson's evidence, as follows:

Q. Now I want you to make two assumptions before answering the question I am going to put to you. The first assumption is, assume that Thermidaire

Je n'oublie pas les facteurs qui relativement aux violations de clauses de non-concurrence ne sont pas aussi facilement mesurables en dollars que le sont les bénéfices bruts d'exploitation et les bénéfices nets mais n'en n'ont pas moins une valeur. Ce facteur ou ces facteurs ont été étudiés par la Cour d'appel de l'Ontario, et ils ont été mentionnés dans le témoignage d'Anderson, comme suit:

[TRADUCTION] Q. Maintenant je veux que vous fassiez deux hypothèses avant de répondre à la question que je vais vous poser. La première, supposez

properly terminated Exhibit 3 for cause, and secondly, assume that Clarke sold products competitive with Thermidaire products during the three year period. In your opinion what harm would Thermidaire suffer as a result of Clarke's competition during that three year period, assuming he did compete?

A. During the three year period he would suffer lost profits, because without that competition presumably he would have had more sales, with very few additional costs, inasmuch as he would have had access to an established market, that had been vacated. Now after the three year period the loss would continue because he doesn't have a group of customers that he might otherwise have had, and this loss is virtually incalculable—it would be very, very difficult to calculate without having more information.

Q. Well, what additional information would assist you in making such a calculation?

A. Information out of the books of H. F. Clarke Co. Ltd., product analysis, customer analysis—this type of information—so that we would know perhaps where we would be selling where we are not now, or where Thermidaire would be selling where it is not now—so that profit margin and so on could be actually computed; these factors would help.

Q. Well, with this information, even with this information, how would you describe the task of calculating the dollar value of the harm done as you have described it?

A. Very, very difficult.

Q. Are there any intangibles in such a calculation?

A. Yes, there are. The basic intangibles are, what harm has been done to Thermidaire for the lack of its name being before the public, its stature in the market place—this type of injury. I would say it would be an exceedingly difficult task to arrive with any degree of certainty at a figure.

que Thermidaire a régulièrement résilié la pièce numéro 3 pour cause, et la deuxième, supposez que Clarke a vendu des produits faisant concurrence aux produits de Thermidaire au cours de la période de trois ans. A votre avis quel préjudice Thermidaire souffrirait-elle par suite de la concurrence de Clarke durant cette période de trois ans, en supposant que Clarke ait fait concurrence?

R. Durant la période de trois ans elle perdrait des bénéfices, parce que sans cette concurrence il est à présumer qu'elle aurait fait plus de ventes, avec beaucoup moins de frais additionnels, dans la mesure où elle aurait eu accès à un marché établi, qui avait été laissé vacant. Maintenant, après la période de trois ans la perte continuerait parce qu'elle n'a pas la clientèle qu'elle aurait pu avoir, et cette perte est pratiquement incalculable—elle serait très, très difficile à calculer sans posséder plus de détails.

Q. Eh bien, quels détails additionnels seraient susceptibles de vous aider dans un tel calcul?

R. Des données provenant des livres de H.F. Clarke Co. Ltd., analyse de produits, analyse de clientèle—ce genre de données—de sorte que nous saurions peut-être où des ventes seraient possibles là où il n'y en a pas actuellement, ou à quel endroit Thermidaire ferait des ventes là où elle n'en fait pas actuellement—de sorte que la marge de profit et le reste pourrait être effectivement calculé; ces facteurs aideraient.

Q. Eh bien, avec ces données, même avec ces données, comment décririez-vous la tâche de calculer la valeur en dollars du préjudice causé tel que vous l'avez décrit?

R. Très, très difficile.

Q. Y a-t-il des éléments intangibles dans un tel calcul?

R. Oui, il y en a. Les éléments intangibles fondamentaux sont, quel préjudice a été causé à Thermidaire par suite du fait que son nom n'a pas été connu du public, sa stature sur le marché—ce genre de dommage. Je dirais qu'il serait excessivement difficile d'arriver à un chiffre avec un degré quelconque de certitude.

When regard is had, on the one hand, to the market situation with which the respondent had to contend before the appellant became its distributor, and, on the other hand, to the position of the

Lorsqu'on tient compte, d'un côté, de la situation de marché avec laquelle l'intimée avait à se débattre avant que l'appelante ne devienne son distributeur, et, de l'autre côté, de la position du distribu-

distributor as itself an already known firm in that market, the respondent is undoubtedly entitled to an allowance for what it has termed loss of product identification and goodwill and for depreciation of its customer and trade relations during the three-year period of unlawful competition by the appellant. This allowance cannot, however, be assessed on the basis that ignores completely the existence of the appellant. Whatever it may turn out to be, as related to and as in addition to the estimated net profit loss of $92,017, in my opinion it cannot, because of the difficulty of putting a figure on it, lend the necessary support to make the gross trading profits of $239,449.05 an acceptable measure of liquidated damages.

I regard the exaction of gross trading profits as a penalty in this case because it is, in my opinion, a grossly excessive and punitive response to the problem to which it was addressed; and the fact that the appellant subscribed to it, and may have been foolish to do so, does not mean that it should be left to rue its unwisdom. *Snell's Principles of Equity* (27th ed. 1973), at p. 535 states the applicable doctrine as follows:

> The sum will be held to be a penalty if it is extravagant and unconscionable in amount in comparison with the greatest loss that could conceivably be proved to have followed from the breach.

This proposition comes from a statement by Lord Halsbury in the House of Lords in *Clydebank Engineering and Shipbuilding Co. Ltd. v. Don*[6] *José Ramos Yzquierdo y Castaneda*[5], at p. 10, and was reiterated by Lord Dunedin in *Dunlop Pneumatic Tyre Co. Ltd. v. New Garage and Motor Co. Ltd.*[6], at p. 87. I do not think that it loses its force in cases where there is difficulty of exact calculation or pre-estimation when the stipulation for liquidated damages, as in this case, is disproportionate and unreasonable when compared with the damages sustained or which would be recoverable through an action in the courts for breach of the covenant in question; see 25 *Corpus*

[5] [1905] A.C. 6.
[6] [1915] A.C. 79.

teur en tant qu'entreprise elle-même déjà connue sur ce marché, l'intimée a sans aucun doute droit à quelque chose pour ce qu'elle a appelé perte d'identification du produit et de clientèle et pour la dépréciation de ses relations auprès des clients et dans le commerce durant les trois années de la concurrence illicite de l'appelante. Ce quelque chose ne peut, cependant, être évalué en prenant une base qui méconnaît complètement l'existence de l'appelante. Quoi qu'il s'avère être, en tant qu'élément relié et additionné à la perte de bénéfices nets estimative de $92,017, à mon avis il ne peut, à cause de la difficulté de lui attribuer un chiffre, prêter l'appui nécessaire pour que les bénéfices bruts d'exploitation de $239,449.05 deviennent une mesure acceptable de dommages liquidés.

Je considère l'exaction de bénéfices bruts d'exploitation comme une pénalité en l'espèce parce qu'elle est, à mon avis, une réponse grossièrement excessive et punitive à la difficulté à laquelle elle se réfère; et le fait que l'appelante y ait souscrit, et puisse avoir été très mal avisée de le faire, ne veut pas dire qu'elle devrait n'avoir d'autre recours que de s'en prendre à son manque de sagesse. L'ouvrage *Snell's Principles of Equity* (27e ed. 1973), à la p. 535, énonce la théorie applicable comme suit:

> [TRADUCTION] La somme sera jugée être une pénalité si elle est extravagante et exorbitante en comparaison de la plus grande perte qui pourrait concevablement être prouvée comme conséquence de la violation.

Ce principe provient de l'énoncé qu'a fait Lord Halsbury dans la Chambre des Lords dans l'arrêt *Clydebank Engineering and Shipbuilding Co. Ltd. v. Don José Ramos Yzquierdo y Castaneda*[5], à la p. 10, et a été réitéré par Lord Dunedin dans l'arrêt *Dunlop Pneumatic Tyre Co. Ltd. v. New Garage and Motor Co. Ltd.*[6], à la p. 87. Je ne pense pas qu'il perde de sa force dans des affaires où un calcul exact, ou une estimation anticipée, s'avèrent difficiles, quand la stipulation prévoyant des dommages liquidés est, comme c'est le cas ici, disproportionnée et déraisonnable en comparaison des dommages subis ou qui seraient recouvrables en justice pour violation de la clause en question:

[5] [1905] A.C. 6.
[6] [1915] A.C. 79.

Juris Secundum, s. 108, pp. 1051ff. The fact that the highest amount put forward by the respondent as its actual loss was $92,017 is plainly indicative of the disproportion that resides in the exaction of gross trading profits of $239,449.05.

I would characterize the exaction of gross trading profits for a three-year period as a penalty and not as giving rise to a sum claimable as compensation by way of liquidated damages. The respondent is, however, entitled to recover its provable damages for the breach of covenant, and I would direct a reference to the Master at Toronto, Ontario to enable it to make its proof of all elements entering into such damages.

The appellant urged in this Court, as it did below, that sales of certain products ought not to be taken into account because they were not Thermidaire products within the terms of the contract. On this point I am in agreement with the courts below which rejected this submission.

In the result, I would allow the appeal on what I have called the main issue, set aside the judgments below and in their place I would direct judgment for the respondent for damages for breach of the covenants not to compete with a reference to the Master at Toronto, Ontario, to ascertain the damages. The appellant should have its costs in this Court and in the Ontario Court of Appeal. The respondent should have the costs of the trial and of the reference as ordered by the trial judge.

The judgment of Martland and Dickson JJ. was delivered by

MARTLAND J. (*dissenting*)—I am in agreement with the unanimous reasons of the Court of Appeal for Ontario delivered by Brooke J.A. and, accordingly, I would dismiss the appeal with costs.

Appeal allowed with costs, MARTLAND *and* DICKSON J.J. *dissenting*.

voir 25 *Corpus Juris Secundum*, art. 108, pp. 1051 et suiv. Le fait que le plus haut montant que l'intimée ait avancé à titre de perte réelle soit de $92,017 est un indice clair de la disproportion qui réside dans l'exaction de bénéfices bruts d'exploitation de $239,449.05.

Je dirais que l'exaction de bénéfices bruts d'exploitation pour une période de trois ans constitue une pénalité et non pas une somme qu'on peut réclamer comme indemnité à titre de dommages-intérêts liquidés. L'intimée a, cependant, le droit de recouvrer ses dommages prouvables découlant de la violation de la clause, et je suis d'avis d'ordonner qu'il y ait renvoi au Master à Toronto, Ontario, afin qu'elle puisse faire sa preuve de tous les éléments qui sont inclus dans de tels dommages.

L'appelante a fait valoir devant cette Cour, comme elle l'a fait en instance inférieure, que les ventes de certains produits ne devraient pas être prises en ligne de compte parce qu'il ne s'agissait pas de produits de Thermidaire au sens des termes du contrat. Sur ce point je suis d'accord avec les cours d'instance inférieure, lesquelles ont rejeté cette prétention.

En définitive, je suis d'avis d'accueillir le pourvoi sur ce que j'ai appelé la question principale, d'infirmer les jugements des cours d'instance inférieure et en remplacement d'iceux d'ordonner que jugement soit rendu en faveur de l'intimée pour les dommages-intérêts imputables à la violation des clauses de non-concurrence, avec renvoi au Master à Toronto, Ontario, pour appréciation des dommages. L'appelante a droit à ses dépens en cette Cour et en Cour d'appel de l'Ontario. L'intimée a droit aux dépens du procès et du renvoi comme l'a ordonné le juge de première instance.

Le jugement des juges Martland et Dickson a été rendu par

LE JUGE MARTLAND (*dissident*)—Je souscris aux motifs unanimes de la Cour d'appel de l'Ontario rédigés par le juge Brooke et, par conséquent, je rejetterais l'appel avec dépens.

Appel accueilli avec dépens, les juges MARTLAND *et* DICKSON *étaient dissidents*.

Solicitors for the appellant: Gardiner, Roberts, Toronto.

Solicitors for the respondent: Day, Wilson, Campbell, Toronto.

1974: December 16; 1975: January 28.

Present: Laskin C.J. and Martland, Judson, Ritchie, and Spence JJ.

MOTION ON COSTS

The judgment of the Court was delivered by

SPENCE J.—I am in favour of granting the applicant's, Thermidaire's, motion to provide that there should be no costs to either party in this Court or in the Court of Appeal for Ontario.

Application allowed.

NOTE: A motion to vary the order as to costs and the reference as to damages was subsequently allowed by the Court (coram: Laskin C.J. and Martland, Judson, Ritchie and Spence JJ.) on March 26, 1975. The order of the Court was as follows:

The motion to vary the order as to costs of the trial and costs of the reference as to damages is allowed without costs, and there will be an order directing that if the damages of the respondent are assessed at more than the amount paid in by the appellant in satisfaction thereof the respondent shall have the costs of the trial but if the damages are assessed at no more than the payment in the respondent shall have the costs of the trial to the date of payment in and the appellant shall have the costs of the trial thereafter. The costs of the reference as to damages shall be in the discretion of the Master.

David H. Sandler, for the motion.

John J. Fitzpatrick, Q.C., contra.

Procureurs de l'appelante: Gardiner, Roberts, Toronto.

Procureurs de l'intimée: Day, Wilson, Campbell, Toronto.

1974: le 16 décembre; 1975: le 28 janvier.

Présents: Le juge en chef Laskin et les juges Martland, Judson, Ritchie et Spence.

REQUÊTE POUR ADJUDICATION DE DEPENS

Le jugement de la Cour a été rendu par

LE JUGE SPENCE—Je suis d'accord pour faire droit à la requête de Thermidaire. Il n'y aura pas d'adjudication de dépens à l'une ou l'autre des parties en cette Cour et en Cour d'appel de l'Ontario.

Demande accueillie.

NOTE: La Cour a par la suite accueilli une requête en modification de l'ordonnance concernant les dépens et du renvoi sur les dommages-intérêts (coram: le juge en chef Laskin et les juges Martland, Judson, Ritchie et Spence.) le 26 mars 1975. Voici l'ordonnance de la Cour:

La requête en modification de l'ordonnance concernant les dépens de première instance et les dépens du renvoi sur les dommages, est accueillie sans dépens, et il sera ordonné que si les dommages de l'intimée sont évalués à plus que le montant payé par l'appelante en acquittement de ces derniers l'intimée aura droit aux dépens de première instance mais que si les dommages sont évalués à pas plus que le paiement effectué l'intimée aura droit aux dépens de première instance à la date du paiement et l'appelante aux dépens de première instance depuis le paiement. Les dépens du renvoi sur les dommages sont laissés à la discrétion du Master.

David H. Sandler, pour la requête.

John J. Fitzpatrick, c.r., contra.

TAB 10

Citation: Hnatiuk et al. v. Court et al., 2010 MBCA 20 Date: 20100303
Docket: AI 09-30-07212

IN THE COURT OF APPEAL OF MANITOBA

Coram: Madam Justice Freda M. Steel
Mr. Justice Martin H. Freedman
Mr. Justice Alan D. MacInnes

B E T W E E N:

BRIAN HNATIUK and 5239886 MANITOBA LTD.	)	
	)	***R. J. Handlon*** *and*
	)	***K. Poetker***
(Applicants) Appellants	)	*for the Appellants*
	)	
- and -	)	***M. G. Finlayson***
	)	*for the Respondents*
JAMES E. COURT, CHRISTOS FILOPOULOS, COURT FILOPOULOS HNATIUK CERTIFIED MANAGEMENT ACCOUNTANTS LTD., 4507241 MANITOBA INC. and 4511034 MANITOBA INC.	)	*Appeal heard:*
	)	***December 16, 2009***
	)	
	)	*Judgment delivered:*
	)	***March 3, 2010***
	)	
(Respondents) Respondents	)	

FREEDMAN J.A.

INTRODUCTION

1 This appeal involves a unanimous shareholders' agreement (USA) among shareholders in a closely held Manitoba corporation (the Corporation).

Appeal from 2009 MBQB 8, 235 Man.R. (2d) 71
See 2009 MBQB 114

2 When two of the three shareholders terminated the agreement, as they were entitled to do, they also exercised a right, which they asserted they had, to purchase the shares of the third shareholder. He resisted, and applied for liquidation and dissolution of the Corporation. The other two shareholders sought a stay of that application, and a referral to arbitration, relying on the arbitration clause in the USA. The motion judge granted their request.

3 It is my opinion that, while the matter in dispute between the parties was mischaracterized by the judge, nevertheless the stay and referral to arbitration, with the dispute properly characterized, should not be disturbed. I would allow the appeal only for the purpose of properly describing the nature of the dispute being referred to arbitration.

BACKGROUND

a) The Parties/The Partnership

4 James Court (Court), Christos Filopoulos (Filopoulos) and Larry Scarth (Scarth) are certified management accountants (CMA). They carried on their profession in partnership under the name "Court Scarth Filopoulos Certified Management Accountants." The practice appears to have been carried on (either initially or at some time later) either wholly or partially through the Corporation, which was then known as CSF Consulting Group Inc. Its shareholders were corporations owned by the three individuals.

5 Brian Hnatiuk (Hnatiuk) is also a CMA. On March 1, 2006, he acquired Scarth's interest in the professional practice for $30,000. Concurrently, his corporation acquired the interest that Scarth or his corporation held in the Corporation for $160,000. Then Court, Filopoulos

and Hnatiuk entered into a partnership agreement (the PA) and they and their corporations (and the Corporation) entered into the USA.

6 In October 2006 the accounting practice carried on by the partnership and the Corporation was reorganized by rolling the partnership goodwill into the Corporation and establishing the Corporation as a "professional corporation" under *The Certified Management Accountants Act*, C.C.S.M., c. C46.1. The name of the Corporation was changed to Court Filopoulos Hnatiuk Certified Management Accountants Ltd. The partnership continued to exist, but the business was carried on entirely by the Corporation. The interests that Hnatiuk and his corporation hold in the Corporation and the partnership are collectively called the "Hnatiuk interests."

7 Although the new partnership had only come into existence on March 1, 2006, relations among the partners deteriorated quickly. For reasons which are not relevant here, Court and Filopoulos decided to terminate the relationship. On March 1, 2007, they served notices on Hnatiuk under each of the PA and the USA, bringing the relationship to an end.

b) <u>The USA</u>

8 The USA is expressed to be a "unanimous shareholders' agreement" pursuant to s. 140(2) of *The Corporations Act*, C.C.S.M., c. C225. It contains provisions common to such agreements, such as restrictions on share transfers, designation of directors, selection of officers, management-related provisions on remuneration and vacation entitlement, and operational provisions on several matters.

9 It also contains the following provisions relevant to this appeal:

11. VALUATION

11.1 The parties agree to hold an annual meeting for the purpose of establishing a share value of the Corporation for purposes of this Agreement. Said valuation will be agreed to unanimously and confirmed by a Directors' resolution of the Corporation.

11.2 In the event that this resolution is not agreed to unanimously or the parties fail to fulfill this obligation then the last valuation so established shall remain in force.

. . . . .

13. DISABILITY

13.1 In the event either of the parties (hereinafter referred to as the disabled party) through bonafide illness, physical or mental, shall be unable to devote his full time and attention to the affairs of the business, the disabled party shall be entitled to:

. . . . .

13.3 Should the disability become permanent or prolonged for a period in excess of 6 months, the remaining shareholders agree to purchase the disabled shareholder's shares for the agreed upon annual valuation amount. The Remaining shareholders agree to purchase the shares in proportion to their existing shareholdings of the capital stock of the Corporation;

a. The said value shall be payable in 36 equal installments of principal plus interest at The Toronto-Dominion Bank prime rate of interest from time to time. Payment to be made in full within 3 years of the determination of the amount, however, the entire amount may be prepaid at any time without notice, penalty or bonus.

. . . . .

15. PURCHASE OF SHARES

15.1 In the event that any of the conditions as hereinafter described in subsection 16.1 of this Agreement happen then it is agreed that the Directors may elect to repurchase the shares of a third in accordance to the provisions contained in subsection 13.3 of this Agreement. In the event that the remaining directors fail to elect to repurchase the shares, the Corporation shall be dissolved in accordance to section 16 of this Agreement.

. . . . .

16. DISSOLUTION OF AGREEMENT

16.1 It is agreed that this Agreement may be terminated upon the occurrence of any of the following events:

. . . . .

b. Upon 30 days advance written notice of termination from any party to this Agreement;

. . . . .

16.3 In the event of dissolution, either voluntary or involuntary each shareholder shall be entitled to receive their one-third respective share of the net assets of the Corporation either in cash or kind.

16.4 All of the clients of the Corporation shall be valued at an amount equal to the previous year's fee subject to a deduction for non-recurring services performed in the prior year. The clients will then be divided between the Directors of the Corporation, with each Director of the Corporation being charged for the value of the client as previously determined. The net difference will then be paid ….

. . . . .

18. ARBITRATION

18.1 If at any time during the continuance of this Agreement any dispute, difference, or question shall arise between the parties

> hereto, or any one of them, touching the business or accounts, or transactions of the Corporation or the construction, meaning, or effect of this Agreement or anything herein contained, or the rights or liabilities of the parties hereto, under these presents, or otherwise in relation thereto, or if any dispute, difference of [*sic*] question cannot be settled or determined by the parties hereto, and [*sic*] every such dispute, difference, question or deadlock shall be referred to a single arbitrator if the parties can agree upon such single arbitrator, or otherwise to a Board consisting of three arbitrators to be appointed in keeping with the provisions of the Arbitration Act of the Province of Manitoba, and any finding made by such arbitrators shall be absolutely final, conclusive and binding upon the parties and their respective heirs, executors, administrators, successors and assigns. The arbitrators shall have the full power and authority to hear and determine any and all such matters brought to them and to award costs and direct such steps to be taken as they may see fit.

c) <u>The PA</u>

10 The PA contains provisions roughly parallel to those in the USA, so I will not recite them here. Nevertheless, I note that the PA provides, under the heading "Dissolution of Agreement," that it (the PA) may be terminated on 30-days' notice by any partner, and that on dissolution each partner is entitled to receive one-third of the goodwill (undefined) as determined in para. 17 of the PA. That paragraph, one of four under the heading "Survivorship Arrangements," states:

> 17. The purchase price for the Partnership interest shall be predetermined in writing signed by the partners within 90 days of the fiscal year end of the Partnership and said document shall be appended to this Agreement as Schedule A annually, and this price will remain in force until changed.

11 The PA also contains an arbitration clause that is identical to that in the USA (apart from two insubstantial wording changes, to "Partnership" and "Partners" from "Corporation" and "parties"). The PA does not give a right to any partner to buy the interests of any other partner (other than on the death of a partner). This may not have any practical significance if the value of the business is in the Corporation. The argument of the parties before us focussed on the USA, and these reasons will similarly concentrate on the USA.

d) The Termination Notices

12 The notice given by Court and Filopoulos in relation to the USA went beyond termination of the USA. It reads:

> **To: Brian Hnatiuk CMA**
>
> **NOTICE OF INTENTION TO PURCHASE SHARES**
>
> Pursuant to section 16.1 of the unanimous shareholder agreement between James Court, Chris Filopoulos & Brian Hnatiuk and their respective corporations, the below directors are giving 30 days notice of the termination of this agreement and are exercising the right to have the corporation repurchase the shares held by Brian Hnatiuk and his respective corporation pursuant to section 15.1 of the agreement.
>
> Dated this 1st day of March 2007.

13 They also gave a notice to Hnatiuk dissolving the partnership effective April 1, 2007. That notice was silent on any other matter.

14 The USA (section 11.1) required the parties annually to establish a "share value" for purposes of the USA, but that did not occur. Section 11.2

states that if the parties fail to "fulfill this obligation" then the last established valuation would apply, but no valuation was ever established by the parties.

15 Concurrently with the two termination notices, Court and Filopoulos gave Hnatiuk an offer to purchase the Hnatiuk interests. The offer was based on a dollar amount adjusted by a number of variables, and had some non-financial terms as well. Hnatiuk rejected the offer or it may have been withdrawn.

e) The Application for Liquidation and Dissolution

16 Soon after the events just described, Hnatiuk and his corporation applied for liquidation and dissolution of the Corporation. They sought a declaration that they were entitled, pursuant to the USA, to a one-third share of the net assets of the Corporation and that the valuation and accounting procedures spelled out in s. 16 of the USA had to be followed. Among other matters they sought, as an alternative to liquidation, an order that Court, Filopoulos and their corporations buy the Hnatiuk interests for the greater of the price they had paid to Scarth or the present value of those interests. Other relief was sought including an order that bi-weekly draws continue to be paid until liquidation or further order.

f) The Stay

17 The respondents moved to stay the application for liquidation, on the basis that s. 7(1) of *The Arbitration Act*, C.C.S.M., c. A120, applied:

> **Stay**
> **7(1)** Subject to subsection (2), if a party to an arbitration agreement commences a proceeding in a court in respect of a matter in dispute to be submitted to arbitration under the agreement, the court shall, on the motion of another party to the arbitration agreement, stay the proceeding.

18 In their notice of motion, the respondents said that the "only real issue between the parties is the amount of the applicants' entitlement." It was their position that the arbitration clause governed and the dispute had to be arbitrated, thus the application should be stayed.

19 Some time after the filing of the stay motion a consent order was made by a judge requiring the payment of draws to the appellants, until further order, and imposing certain other requirements on the respondents. Several months later a further order was made by a second judge. That judge ordered that the respondents immediately pay the appellants certain draws which they had not paid, and that they pay into court certain other draws and all future draws, until further order. The second judge also set a peremptory date for the stay motion to be heard.

g) <u>The Decision Staying the Application</u>

20 The motion judge said that the overriding issue was the valuation of the Hnatiuk interests and the payment for them by the respondents, but that the issue then before him was whether to grant the stay. He referred to the USA and the PA, and to *The Arbitration Act*. He noted the considerations applicable in the case before him, found in the decision of the House of Lords in *Heyman v. Darwins Ltd.*, [1942] A.C. 356 (H.L.), where the court said that the judge must (at para. 19):

. . . . .

> (a) ascertain the precise nature of the dispute that has arisen;
>
> (b) ascertain whether the dispute is one that falls within the terms of the arbitration clause;
>
> (c) ascertain whether the arbitration clause is still effective or whether something has happened to render it no longer operative; and
>
> (d) ascertain whether there is any sufficient reason why the matter in dispute should not be referred to arbitration.

21 See also *Injector Wrap Corp. Ltd. v. Agrico Canada Ltd.* (1990), 67 Man.R. (2d) 158 (C.A.), and *Bloomer Hotel Corp. et al. v. Boehm Hotel Corp. et al.*, 2009 MBCA 68, 240 Man.R. (2d) 69.

22 The motion judge's analysis followed that set out in *Heyman*. The respondents had argued, as they did here, that the only issue was the valuation of the Hnatiuk interests. Hnatiuk said there were several issues including a potential claim by the respondents against him. The judge said that the valuation was "precisely the matter in dispute" (at para. 21) and that the respondents had clearly defined the issue as being valuation, so that they could "exercise their rights" (at para. 23) to purchase the interest.

23 He held that the arbitration clause was "sufficiently broad to include the issue in dispute" (at para. 24).

24 The judge found that the dispute arose prior to the date of termination of the USA/partnership, and that there was no reason not to refer the matter to arbitration. He granted the stay.

25 Subsequently, there was difficulty about the contents of the order to be taken out, and the parties appeared before the judge again. As noted, the second judge had ordered that certain payments be made, until further order. The motion judge ordered that such payment order was stayed as of the date he referred the matter to arbitration, but he did not expressly include the issue of such payments in the referral to arbitration. He directed that, the precise nature of the dispute being the valuation of the Hnatiuk interests, "identification of [any other] issues to be resolved and of the method of resolving those issues" (2009 MBQB 114 at para. 16) would be left to the arbitrator. He said that the dispute did not include issues relating to Hnatiuk's performance.

DECISION

1. Section 7(6) of *The Arbitration Act*

26 Section 7(6) of *The Arbitration Act* states: "There is no appeal from the court's decision under this section."

27 At first blush, this section would appear to mean that this court cannot hear and decide any appeal whatsoever from a judge's decision under s. 7 of *The Arbitration Act*. But some decisions of other appellate courts suggest the issue is not so straightforward. There appear to be no decisions of this court on s. 7(6).

28 In *Brown v. Murphy* (2002), 59 O.R. (3d) 404, the Court of Appeal considered the similar section in the Ontario legislation. It referred to its earlier decision in *Huras v. Primerica Financial Services Ltd.* (2000), 137 O.A.C. 79. In *Huras*, the court had held that where the motion court

determined that the arbitration clause has no application, the dispute lies beyond the scope of s. 7, and thus the prohibition on appeals was inapplicable. In *Brown* the motion judge found that part of the subject matter of the action could fall within the scope of the arbitration agreement, but he refused a stay. On appeal, the court said (at paras. 8, 12):

> … [W]e concluded, on the authority of *Huras*, that the bar under s. 7(6) applied to any decision by the motions court under s. 7 to grant or refuse a stay of "*a proceeding in respect of a matter to be submitted to arbitration under the agreement*" within the meaning of s. 7(1). However, a decision by the motions court that a matter was *not* subject to arbitration under the terms of the arbitration agreement fell outside the scope of s. 7 and a right of appeal lay to this court from that decision.
>
> …. In this case, the motions judge refused to grant … a partial stay, on the basis that the matters that did not fall within the scope of the parties' agreement could not easily be dealt with alone. This decision falls within the scope of his discretion under s. 7(5), and no appeal lies to this court.

29 In *Mantini v. Smith Lyons LLP* (2003), 64 O.R. (3d) 505 (C.A.), the same court said (at para. 15) that where a motion judge decides that a matter is not subject to arbitration, such a decision falls outside the scope of s. 7 and an appeal from that decision is not barred.

30 The cases suggest that a decision by a motion judge on whether a dispute comes within the arbitration agreement is akin to a question of jurisdiction. In *Brown*, the court said (at para. 5):

> …. It is only after the court has interpreted the arbitration agreement and determined whether the subject-matter of the action comes within the scope of the agreement that the court can address the issue of a stay. ….

31 The appellants argued before us that s. 7(6) is intended to protect a motion judge's exercise of discretion under s. 7, and that it is not intended to shield from review a decision made without jurisdiction because, for example, the necessary preconditions to the granting of a stay were not satisfied. The appellants further argued that the judge erred in a preliminary matter, namely, in properly defining the precise nature of the dispute, and that such error was not barred from review by this court by virtue of s. 7(6).

32 They also argued that, although the Ontario cases involved appeals of decisions denying a stay and referral, there was no principled reason to insulate from review a decision where the motion judge found the dispute to fall within the scope of the arbitration agreement.

33 In *Lamb v. AlanRidge Homes Ltd.*, 2009 ABCA 343, 464 A.R. 46, the Court of Appeal said (at para. 14):

> In our view, s. 7(6) reflects an equally important policy consideration, namely that the process of determining whether the parties should proceed with arbitration, or legal proceedings, should not become bogged down by resort to the appeal process. The legislature obviously intended that the decision of the Court of Queen's Bench should be final, so as to promote an expeditious determination of the forum to hear the disputes of the parties.

34 *Bloomer* is a decision of this court where an appeal was taken from a stay order under s. 7. Subsection (6) was not discussed. The court said (at para. 14) that the court could interfere with the motion judge's discretionary order granting a stay where the judge misdirected him or herself or where the decision was so clearly wrong as to amount to an injustice.

35 In the present case, as will be seen, my view is that the judge misdirected himself on the nature of the dispute. It follows that appellate intervention for the purpose of properly characterizing the dispute is not barred by s. 7(6). Failure to intervene, by construing s. 7(6) too literally, would result in an ineffective arbitration process. The arbitrator would have to focus on a subsidiary question only, while the fundamental dispute remained outside his or her purview. That cannot be what was intended by the legislature in enacting s. 7(6). A discretionary order which stays a court proceeding and refers a dispute to arbitration cannot be immune from appellate review if failure to review would send a wrongly described dispute to arbitration, with the likely result that the process would be futile.

2. The Precise Nature of the Dispute

36 The difficulty with the judgment under review is that it is based on the premise, assumed but never explained, that in the present circumstances Court and Filopoulos and their corporations have the right to preempt dissolution and to buy the Hnatiuk interests, and that Hnatiuk and his corporation are obliged to sell. That may be a flawed premise and it is, in effect, disputed by the appellants by virtue of their application for dissolution.

37 As I will explain more fully, the dispute between the two sides stems from the failure of the parties to follow the process they set out in the USA for agreeing on a value for their respective interests. The respondents say that notwithstanding that no price has been agreed upon, they have the right forcibly to acquire the Hnatiuk interests. Hnatiuk says that any such right has been negated by the failure of the parties to have agreed on a price, so

the Corporation must be dissolved pursuant to the USA. That is the essence of the fundamental dispute. Valuation is secondary; it only becomes an issue if the respondents are correct in their position.

38 The USA contains a very specific provision relating to valuation. The fact that the parties failed to adhere to its requirements does not mean that such provision and its implications are irrelevant. Rather, that provision is essential to a proper understanding of the agreement the parties had reached, and expressed in the USA.

39 There are several arrangements employed in unanimous shareholder agreements to effect the future separation of the shareholders from each other. See, for example, Stuart Bollefer & Aird & Berlis LLP, *Shareholders' Agreements: A Tax and Legal Guide*, 3rd ed. (Toronto: CCH Canadian Limited, 2009) and Kevin McGuinness, *Canadian Forms & Precedents: Corporations*, looseleaf (Markham: LexisNexis Canada Inc., 2006) c. 3. Common to all such arrangements is the necessity of stipulating a method for determining the price to be paid by the remaining shareholder(s) to the departing shareholder(s).

40 There are many options for price-determination methods. For example, in a typical buy-sell agreement between two equal shareholders, the shareholder initiating the transaction will establish the price unilaterally, and the other shareholder has the choice to buy or sell at that price.

41 As another example, shareholders may agree that if one (or more) has the right in certain stipulated circumstances to buy and therefore the other(s) is obliged to sell, the price will be determined by a third party employing a particular approach or following certain guidelines.

42 Another method sometimes used, when one or more shareholders is to have the right to buy and the other(s) will be obliged to sell, is for the parties to agree upon the price either in the unanimous shareholder agreement itself or, as intended here, by a separate agreement of the parties made from time to time, such as annually. Use of this particular method means the parties should be diligent in keeping the price relatively current to avoid what Ricky W. Ewasiuk, *Drafting Shareholders' Agreements: A Guide* (Scarborough: Thomson Canada Ltd., 1998) at 49, refers to as "potentially disastrous consequences for someone."

43 This USA must be construed in its entirety in order to give it proper meaning. "It is a fundamental precept that contractual interpretation requires an examination of a contract as a whole, not just a consideration of the specific words in dispute" (Geoff R. Hall, *Canadian Contractual Interpretation Law*, 1st ed. (Markham: LexisNexis Canada, 2007) at 11).

44 In explaining why I have concluded that the dispute was mischaracterized, I will set out my understanding of the arrangement upon which the parties agreed in the USA, as related to the present subject. In so doing, and in the analysis which follows, I am mindful that the dispute between the parties is being remitted to arbitration. My comments should not be taken as conclusive findings. Such findings are for the arbitrator to make.

45 The USA provides:

1. At any time, upon 30-days' notice, any party can terminate the USA (s. 16.1b). Subject to what is described in subpara. 4

below, in such event the Corporation is to be dissolved (s. 15.1).

2. In the event of dissolution of the Corporation, each of the three parties has full access to all the Corporation's books and records (s. 16.2) and each receives a one-third share of the net assets of the Corporation (s. 16.3).

3. On dissolution, the clients of the Corporation will be ascribed a value and they will be allocated among the three "Directors" (the individual CMA's), and payment will be made for their value according to a formula (s. 16.4).

4. However, if the USA is terminated under s. 16.1, "the Directors may elect to repurchase the shares of a third in accordance to the provisions contained in subsection 13.3" of the USA (s. 15.1). This means, in my opinion, and subject to what follows, that on termination of the USA any two of the individuals (they were designated as "Directors") may elect to acquire the shares of the third in the Corporation and if they do so he is obliged to sell the shares to them. If that does not occur, there will be a dissolution of the Corporation (s. 15.1) but if it does occur there is no dissolution.

5. If two of the individuals elect to acquire the shares of the third, the price to be paid to the selling party by the purchasing parties is "the agreed upon annual valuation amount," which is payable over three years (s. 13.3).

6. Each year the parties will meet and agree on a value of the shares in the Corporation, for purchase and sale purposes (s. 11.1). The last agreed valuation is the value in force at any time (s. 11.2), and is the value applicable to purchases and sales of shares under the USA.

46 Reading the above as a summary of the relevant provisions of the USA in their entirety, and of their effect, one might rationally conclude that the agreement of one party to the USA that he could be forced to sell to the other two, at their unilateral election, on termination of the USA, is premised on the selling party already knowing and having agreed to the price he will receive (the "agreed upon annual valuation amount"). The purchasing parties would also know and have agreed to the price they will have to pay. If they are prepared to pay that price, already known to them, rather than see the Corporation dissolved, they can achieve that result, and the third shareholder, having already agreed to the price, will be obliged to sell to them. If they are not prepared to pay that price, and the election is theirs, then the Corporation will be dissolved.

47 Of course, it would have been possible for the parties to have foreseen that a valuation might never be agreed upon, or perhaps that it might be entirely overlooked, and they could have expressly provided for an alternative price-determining mechanism (see Bollefer at pp. 20-21). They did not do so. The respondents argue that such mechanism does exist in the arbitration clause. But that argument may not properly take into account the essence of the agreement reached by them in the USA.

48 The USA provides, in effect, that the respondents have the right to trigger a purchase of the Hnatiuk interests, and that he is required to sell to them, at an "agreed upon annual valuation amount." It confers no right to buy, and imposes no obligation to sell, at an amount determined at arbitration. At least, it does not do so explicitly. As noted, the parties could have so stipulated, but that would appear to be a different arrangement than the one now found in the USA. If that was to be the arrangement, which could expose to considerable risk any shareholder forced out, one might have expected that the parties would have expressly so stated.

49 The fact that there has never been an "agreed upon annual valuation amount," in these circumstances may mean that on termination of the USA there is no effective right of two shareholders to elect to purchase the shares of the third, and no obligation on the part of the third to sell them. The possibility of such a forced sale may have been eliminated by the failure of the parties to adhere to the process they chose that would permit a forced sale, and by their failure to build into the USA an alternative price-determination mechanism.

50 Nevertheless, it is possible that an arbitrator might find, for example, that the USA is ambiguous. An arbitrator might then attempt to ascertain if the parties intended the purchase right to exist even when no price was ever agreed upon.

51 Thus, in my respectful opinion, the fundamental nature of the dispute has been incorrectly characterized. The issue, at this stage, cannot be, what is the value of the Hnatiuk interests. That issue would only arise if it was decided (by either an arbitrator or a judge, i.e., by whoever was the proper

person to make such decision) that Hnatiuk was bound by the USA to sell the Hnatiuk interests at a price determined by some method other than that expressly provided for in the USA.

52 Based on the USA in its entirety, and bearing in mind the application for dissolution filed by Hnatiuk and his corporation, the real dispute is that Hnatiuk says he is not obliged to sell at an unknown (and "un-agreed-to") price, and the respondents say that he is. His application for dissolution is premised on the theory that as a matter of interpretation of this particular contract the absence of an agreed price has removed the right of the respondents forcibly to acquire the Hnatiuk interests. Their motion for a stay, in effect, challenges that theory. He says that in the absence of an "agreed upon annual valuation amount" the USA requires that the Corporation be dissolved. The respondents say that is not the effect of the USA. Again, that is the fundamental dispute.

53 Dealing with the first element in *Heyman* (see para. 20), in my opinion the precise nature of the present dispute is whether the respondents, having terminated the USA and the PA, have an enforceable right under the USA to purchase the Hnatiuk interests and whether Hnatiuk and his corporation are obliged to sell, in the absence of an "agreed upon annual valuation amount," or whether the Corporation is to be dissolved.

54 A consequential issue to be decided, but arising only if it is found that the respondents do have the right they assert, is the determination of the price to be paid for the Hnatiuk interests.

55 As to the second element in *Heyman*, the arbitration clause in the USA is broad enough, in my view, to encompass this dispute, which is a

"dispute, difference, or question … touching … the construction, meaning or effect of [the USA] … or the rights or liabilities of the parties [t]hereto." The dispute must, therefore, be decided, as the judge found, by an arbitrator or a board of arbitrators under the USA.

56 I agree with the judge that the third and fourth elements in the *Heyman* criteria are satisfied here.

57 The referral to arbitration must also include the related issue of the payments made, as well as those not made, by the respondents, pursuant to the order of the second judge, as discussed above. Failure to include that matter, which is also within the scope of the arbitration clause, would require either that such issue proceed in court, resulting in parallel and costly proceedings, or that the matter sit in limbo until the arbitration is concluded, which would be both inefficient and unfair (and which is the result of the order below). Therefore, I would confirm that the order made by the second judge is stayed, but would add as a further matter in dispute to be referred to arbitration, resolution of the outstanding issues relating to all such payments made and not made. If the arbitrator concludes on the fundamental issue that the respondents do not have the right to purchase which they assert they do, then this further matter would not be arbitrated, but would be dealt with in the normal court process.

58 Accordingly, while the description of the dispute being referred to arbitration must change to conform to the description set out above in para. 53 (including the two further issues described in paras. 54 and 57) the judge's exercise of discretion to refer the dispute to arbitration must stand. As my colleague Monnin J.A. said in *Bloomer* (at para. 19):

> When the parties entered into their agreements, they purposefully included the arbitration clause. Courts should be reluctant to interfere with the clear intention of the parties, which was certainly in part to protect the privacy of their business affairs. In as much as possible, courts should give effect to the fact that the parties chose their forum to settle disputes.

59 Success is divided, in my opinion, and I would direct that each side pay their own costs in this court.

_____ J.A.

I agree:

_____ J.A.

I agree:

_____ J.A.

TAB 11

DATE: 20010117
DOCKET: C32470

COURT OF APPEAL FOR ONTARIO

FINLAYSON, LABROSSE and WEILER JJ.A.

BETWEEN:

INFINITE MAINTENANCE SYSTEMS LTD. Appellant (Plaintiff)	)	Martin G. Banach, for the appellant (plaintiff)
–and–	)	
ORC MANAGEMENT LIMITED Respondent (Defendant)	)	Inga B. Andriessen, for the respondent (defendant)
	)	Heard: November 2, 2000

On appeal from the judgment of Justice John D. Ground dated May 12, 1999 and June 14, 1999.

WEILER J.A.:

Overview

[1] The issue on this appeal is the enforceability of a clause in a contract that provided for compensation to the appellant in the event that personnel it supplied its customer was hired directly by the customer. For the reasons that follow, I would allow the appeal and award the appellants $12,600 in damages.

Facts

[2] The appellant company is engaged in the provision of maintenance and janitorial services. The respondent is a multi-purpose health club for squash,

tennis, fitness, aerobics and swimming. The respondent had been encountering a high staff turnover and a problem with supervision of staff. There were complaints about the cleanliness of the facilities. After speaking with the appellant's representative, the respondent entered into a seven-day-a-week cleaning contract with the appellant on May 1, 1997. Pursuant to the contract, the appellant provided cleaning services seven days a week at a rate of $5,600 a month.

[3] The contract also contained a clause, hereinafter referred to as the compensation clause. It stated as follows:

> TERMINATION OF CONTRACT
>
> This contract may be terminated by either party by the giving of thirty (30) days notice in advance thereof in writing by one to the other by registered mail.
>
> In the event of the services herein provided for being continued beyond the period of this contract, then all the terms and conditions of this contract including the hereinafter set out provisions for termination shall apply and the contract shall continue on a basis or yearly service.
>
> The contractor reserves the right to terminate this contract, in the event of non-payment of the account for more than thirty days by the Contractor giving to the other party not less than five days' notice in writing, and on any such termination, all accounts between the parties shall be settled and paid.
>
> The customer covenants and agrees that it will not either directly or indirectly employ, engage or become associate with any **team member** or employee of Infinite Maintenance Systems Ltd. employed by the contractor on the customer's premises directly or indirectly at any time either during the term hereof or during a period of twelve months following the termination hereof. If engages in any manner, will be subject to the one year payment of compensation. [Emphasis in original.]

[4] The duration of the contract was not specified. However, a clause in the contract stated that, in the event services continued "beyond the period of this contract", the contract would continue on a basis of yearly service and the

termination provisions would apply. The termination provision enabled the contract to be terminated by either party at any time on thirty days notice in writing.

[5] On September 30,1997, the respondent gave notice of termination of the contract effective October 31, 1997. On November 1,1997, the respondent hired two of the "team members" that had been supplied by the appellant to the respondent (Deborah and Martin).

[6] When the appellant learned that the respondent had hired two of its team members, it sued the respondent for damages for breach of the compensation clause. The word "compensation" is not defined in the contract. The amount claimed by the appellant was the gross amount of the contract for one year.

[7] The trial judge found that the contract was entered into by two business organizations represented by sophisticated business persons. He further found that the respondent breached the covenant that it would not engage a person who was part of the team supplied by the appellant to work at the club for a period of one year by immediately hiring Deborah and Martin. The trial judge then correctly delineated the issue before him as being whether the clause in question was a penalty clause or liquidated damages. He observed:

> The plaintiff (appellant) does not allege that a payment equal to one year's payments under the contract was a genuine pre-estimate of the damages which Infinite would incur as a result of the breach of contract by ORC and in fact the evidence of Mr. Charles of Infinite is that Infinite incurred no damages as a result of such breach of contract. The Compensation clause is therefore in my view clearly a penalty clause and may be struck down by the Court on such terms as to compensation or otherwise as are considered just; see Section 98 *Courts of Justice Act*, R.S.O. 1990, C. c-43.
>
> …
>
> It seems to me that the case law supports the proposition that, if a clause cannot be regarded as in any sense a genuine pre-estimate of damages and the amount payable bears no relation to the damages incurred by the non-defaulting party, the clause should be struck down as a penalty. In view of the fact that Infinite incurred no damages as a result of the breach

> of contract by ORC and that the purpose of the clause was, according to the evidence, to discourage customers of Infinite from hiring employees of Infinite, it does not appear to me that any terms as to compensation or otherwise ought to be imposed on the striking of the Compensation Clause. The action is accordingly dismissed.

[8] Mr. Charles, who gave evidence on behalf of the appellant, testified that he had suffered no "damages". The contract with ORC was terminated with the requisite one month's notice. The appellant did not lose any contracts because it did not have enough employees. Restricting the damage analysis to this evidence alone, the trial judge dismissed the appellant's action.

Analysis

[9] Although I substantially agree with the trial judge, I would not restrict the inquiry into damages in the same manner. While the appellant did not suffer losses relating to lost income or lost contracts, it nonetheless did suffer a loss as a result of the respondent's actions. After the appellant received notice its contract with the respondent would be terminated, Deborah and Martin agreed to work as part of the team supplied by the appellant on a new contract with Novotel. Just before the Novotel job was to commence, Deborah and Martin told the appellant they had changed their minds. After one-and-a-half to two weeks of interviewing, the appellant found two people to replace Deborah and Martin for the Novotel job. Mr. Charles testified that, after finding two persons to replace Deborah and Martin, he had to go through the same training process he went though with them. The compensation clause was intended to compensate the company for the "value-added" to the experience and skills the company had given its team members or employees through its training program. The process relating to the hiring and training of Deborah and Martin is described in the evidence:

- The back record of the various applicants was checked and an inquiry was undertaken to ascertain whether they were capable of being bonded.

- After interviewing about forty people, six to eight people were chosen. Eventually, a couple, Deborah and Martin were selected for training. The others were not punctual; did not have the right appearance in terms of cleanliness; or could not follow instructions respecting cleaning. Deborah had a very good attitude.

- There is a big difference between house cleaning, which Deborah had done, and commercial cleaning. Specific training is required for commercial cleaning. For example, when you hit a squash ball it leaves a black mark on the wall. In order to remove it, you have to know what product to use. If you do not do it properly you damage the wall and the glass around. Toilet bowl cleaning requires the use of an acid bowl cleaner and you have to make sure you do not leave a spot of it on the seat or it will burn.

- Deborah and Martin were asked to do certain areas of the club the first night they came. When they were finished, Mr. Charles pointed out to them what was "wrong" and how to properly clean and noted other things that were not done. Mr. Charles uses an itemized inspection sheet as a check list.

- The second day, Deborah and Martin came to the appellant's office and watched videos on safety instruction as well as handling hazardous material.

- They had to be taken at least three days in the morning for recycling training in addition to their work on the site.
- The appellant provided extra people who were experienced to work with Deborah and Martin and who could train them on the job. These people taught Deborah and Martin how to do the grout cleaning every day in the shower area; how to clean the washrooms so there was no soap line; how to properly clean a toilet and check to see it is clean under the rim with a mirror; how to clean the whirlpool area and make sure none of the cleaning chemicals fall into the whirlpool; how to sanitize the lockers; how to use the commercial laundry machines; how to do minor repairs on the machines. They were shown how to clean the windows using a squeegee in a certain direction. They were also shown that different flooring material requires different chemicals to clean the floor. Deborah and Martin were taught how to use the machines to scrub the floors, how to buff the floors, how to run the tennis court machine, as well as how to clean the carpets.

- For the first two to three weeks, Mr. Charles was at the job site in addition to a site supervisor. Thereafter, he attended two or three times a week. A log book was placed on site and the appellant's personnel were trained to write notes if they had a request or if something broke down so it could be fixed.

- Training is an ongoing matter. You don't have a person trained after two or three weeks. After a period of four to six months, Deborah and Martin were fully trained as professional cleaners.

[10] The evidence of Mr. Charles as to the length of time and effort required to train a person to do commercial cleaning is supported by the description of the

training program that was part of the contract booklet given to the respondent. Under the heading “Skills” respecting heavy duty cleaners, that is, persons who clean floors and empty garbage etc., the contract states: “To become fully competent in the execution of the job about three months on the job training is required.” In the case of light duty cleaners, two weeks on the job training is required after hiring.

[11] The appellant was aware that a team member might form a personal relationship with persons in the organization where the team member worked. The appellant’s position is that the non-solicitation clause was drafted because it is not a personnel agency and it tries to avoid having a high turnover. That is the reason for the compensation clause.

[12] Although the appellant testified that it had not suffered “damages”, the appellant did give evidence that it suffered a loss as a result of the respondent hiring Deborah and Martin. It is difficult to quantify the cost of interviewing, doing a background check and training a person to do professional cleaning.

[13] The trial judge recognized that the compensation clause which was intended to discourage solicitation of its personnel was *prima facie* enforceable. The onus of establishing that the clause is a penalty is on the respondent as the person seeking to set it aside: *Canadian General Electric Co. v. Canadian Rubber Co. of Montreal* (1915), 52 S.C.R. 349. Although the clause contains no definition of compensation, the trial judge held that the clause was not so vague as to render it void for uncertainty. He held that it must be given a commercially reasonable interpretation. I agree. To allow the appellant’s claim for its gross contract price would not be a commercially reasonable interpretation. Nor would it be commercially reasonable to construe the clause as a genuine pre-estimate of damages. In claiming the gross amount of the contract as damages in its statement of claim, the appellant was overreaching. Before us, the appellant acknowledged that its profit was $2,100 a month on the contract. This amount would be the highest potential pre-estimate of loss.

[14] In determining whether a clause is a pre-estimate of damages or a penalty, the most important factor a court will consider is quantum. As stated by Lord Justice Dunedin in *Dunlop Pneumatic Tyre Co. v. New Garage & Motor Co.*, [1915] A.C. 79 at 87:

> It [a “liquidated damage” clause] will be held to be a penalty if the sum stipulated for is extravagant and unconscionable in amount in comparison with the greatest loss that could conceivably be proved to have followed from the breach.

[15] When a court characterizes a provision as a penalty clause, it will nevertheless award the damages that have been proved. For example, in *H.F. Clarke Ltd. v. Thermidair Corp*, [1976] 1 S.C.R. 319, the Court found the clause which provided for payment of $200,000 was a penalty but awarded the plaintiff its provable damages of $90,000. On the view I take of the case, had the respondent not hired Deborah and Martin, the appellant would have had the benefit of their services and would not have had to incur the expense and effort to find, hire, and retrain two other team members. The loss of Deborah and Martin as members of the appellant's team meant that the appellant lost the future profit it would have made from the value it added to their skills that took place over a period of approximately six months. It had to expend time, effort and expense to train two new team members. I would quantify this loss by taking the time required to train two persons and multiplying it by the profit the appellant earned during the training period ($2,100 a month). The result is that the appellant is entitled to $12,600 as its loss.

[16] I appreciate that a case can be made to reduce this amount as damages. Deborah and Martin were largely trained on the job and they were not the only personnel the appellant supplied to the respondent.

[17] Although the actual quantum of damages is difficult to quantify, as was stated by Masten J.A. in *Carson v. Willitts*, [1930] 4 D.L.R. 977 (Ont. Sup. Ct. (A.D.) at 980: "… the difficulty in estimating the quantum is no reason for refusing to award damages." The respondent's breach was a flagrant one and, accordingly, I do not think it necessary to make any adjustment to the damages.

Additional Issue

[18] During oral argument, the respondent asserted that the termination clause applied only to "employees" and not "team members". The appellant company has a different working relationship with its team members than it does with its employees

[19] A team member is a person who does piece work for the appellant. The appellant provides Workers Compensation for its team members but does not make any source deductions for them. The appellant also provides semi-private hospital insurance, a prescription plan, life insurance, short and long-term disability and uniforms to its personnel. Team members are entitled to come in to work when they want and to leave when they want provided that the job or area they are assigned to clean has been done. The appellant provides the cleaning equipment and supplies to the team members.

[20] The respondent's submission in oral argument that the clause did not apply because the persons hired by the respondent were not employees clearly must fail. It is abundantly clear upon reading the plain wording of the clause that it refers to both "team players" and "employees". To the extent that the submission may have been an indirect attempt to suggest that the appellant had no proprietary interest worthy of protection respecting its team members, I would disagree. As these reasons indicate, the appellant expended considerable time and effort in order to recruit and train suitable personnel for commercial cleaning. These efforts resulted in "value-added" to the skills of its team members. In my opinion, this can and does qualify as a proprietary interest capable of protection similar to goodwill or business association: See e.g. *Lyons v. Multari* (2000), 3 C.C.E.L. (3d) 34 (Ont. C.A.).

Conclusion

[21] I would allow the appeal, set aside the judgment at first instance, and substitute an award in favour of the appellant of $12,600. If the parties wish to do so, they make submissions in writing with respect to costs within fourteen days of today's date. In the absence of submissions as to costs, I would award the appellant its costs of the appeal and at trial.

Released: JAN 17 2001 Signed: "Karen M. Weiler J.A."
GDF "I agree G.D. Finlayson J.A."

LABROSSE J.A. (dissenting):

[22] I have read the reasons of my colleague Weiler J.A. I agree with her that the trial judge correctly concluded that there was a breach of contract by the respondent ("ORC") and that the Compensation Clause was a penalty clause that ought to be struck down "on such terms as to compensation or otherwise as are considered just" (s 98, *Courts of Justice Act.*) Clearly, the Compensation Clause is not a genuine pre-estimate of the damages and the amount payable bears no relation to the damages which the appellant ("Infinite") would have incurred as a result of the breach of contract by ORC.

[23] However, I am unable to agree with my colleague's assessment of the damages.

[24] Infinite claimed a one-year payment of compensation for the breach of the Compensation Clause (for our purpose, $5,600 X 12 months = $67,200). My colleague agrees that Infinite did not suffer any damages relating to lost income or lost contracts. Nevertheless, she maintains that it suffered a loss as a result of ORC's actions.

[25] In order to structure an assessment of damages, she relies on the evidence of Mr. Charles of Infinite that he had to go through the same hiring and training process with the new replacement cleaners for the Novotel job that he had gone through with ORC's cleaners, Deborah and Martin. She notes that to allow Infinite its contracted one-year payment would not be a commercially reasonable interpretation of the contract, but it would be valid to allow its acknowledged profit of $2,100 a month. In so finding my colleague takes the monthly profit of $2,100 ($5,600 minus the $3,500 paid to the cleaners), which she terms as the highest potential pre-estimate of loss, multiplies this amount by 6 (representing the training period of six months), and arrives at a total "loss" of $12,600. Although she acknowledges that this amount would be subject to a reduction because "Deborah and Martin were largely trained on the job and were not the only personnel the appellant supplied to the respondent", she refrains from making any adjustment. In sum, the "loss" is derived from a profit that was never lost.

[26] I agree with my colleague that to allow Infinite its gross contract price would not be a commercially reasonable interpretation. It has already been determined that the amount bears no relation to the loss.

[27] I further agree, as my colleague states and restates, that the loss is difficult to quantify. However, in my view this is solely because there is no evidence of

such loss. It was Mr. Charles' testimony that Infinite had suffered no damages. On the evidence, Infinite made the same profit with Novotel that it would have made, irrespective of ORC's actions. Although it was open to Infinite to attempt to prove how many hours and the rate per hour related to the finding, hiring and training of the new cleaners, there is no evidence submitted of the expenses and costs attributable to that purpose. The "loss" structured by my colleague bears no relation to the time, effort and expense to train the two new cleaners. It bears no more relation to the loss than the Compensation Clause, except that it is for a lesser amount.

[28] My colleague makes a calculation of damages based on the assumption that Infinite's intention was to protect itself from the loss for the "value added" to the experience and skills the company had invested in its cleaners and to compensate for any loss or expense in hiring and training workers. Yet, the contract does not express this intention and there is no definition of compensation in the contract prepared by Infinite. The contract neither explicitly nor implicitly states that the compensation of one year's payment is to protect the value-added investments of training. This assumption is being read into the contract.

[29] Further, there was no evidence submitted at trial to indicate that the damages sought were calculated on this intent and thus, no evidence to support the assessment of damages. As stated earlier, the evidence given at trial was that Infinite did not suffer any loss because Deborah and Martin ceased to work for it. In his evidence, Mr. Charles stated:

> No. I'm not asking for any damages or anything. What I'm asking for is my fee, my 20 years' experience, know how put into those people. That's the reason this clause is put in here that everyone who is there not to hire our people… This is what I'm asking for is merely a fee, fee for people not to engage directly and indirectly with our people.

While this statement is evidence that there was a value-added investment, there is nonetheless no evidence of a loss of the value added. Without any evidence of a loss there was no evidence to either quantify nor justify the payment of a fee in the form of damages.

[30] My colleague based her assessment of damages on assumptions that are outside the realm of surrounding circumstances that the court can consider in the construction of the contract. (See *Thermidaire*, supra at p. 331.) It is not the function of this court to rewrite the contract.

[31] The contract provided for a one-year payment of compensation. Infinite never claimed anything else. The loss of profit is not claimed in the pleadings, nor was it argued before the trial judge or considered in his reasons. It was raised for the first time during the appeal and promptly endorsed by counsel for Infinite.

[32] Infinite, as plaintiff, was entitled to present its case as it wished and it was incumbent upon it to prove its damages. ORC defended the case that was presented. As the loss of profit issue was not raised at trial ORC never had the chance to dispute it.

[33] Further, this issue evolved out of a bare statement made by Mr. Charles without any supporting evidence. On his evidence, Infinite was responsible for providing all cleaning and sanitizing supplies and all necessary equipment. There is no evidence as to these costs nor as to the costs associated with supervision. The word “profit”, as used by Mr. Charles, referred to gross profit and was subject to numerous expenses. In light of this, its adoption by my colleague as the basis for the assessment of damages is seriously flawed.

[34] In the end, it is my view that the assessment of damages structured by my colleague is not supported by the evidence.

[35] In any event, it was reasonable for the trial judge to find that Infinite suffered no damages. This finding is clearly supported by the evidence and there is no basis for interference by this court.

[36] Accordingly, I would dismiss the appeal with costs.

Signed: “J.M. Labrosse J.A.”

TAB 12

In the Court of Appeal of Alberta

Citation: Jinnah v Alberta Dental Association and College, 2022 ABCA 336

Date: 20221013
Docket: 2003-0217AC
Registry: Edmonton

Between:

Dr. Nimet Jinnah

Appellant

- and -

Alberta Dental Association and College and the Appeal Panel of Council of the Alberta Dental Association and College

Respondents

Corrected judgment: A corrigendum was issued on October 18, 2022; the corrections have been made to the text and the corrigendum is appended to this judgment.

The Court:

The Honourable Justice Jack Watson
The Honourable Justice Thomas W. Wakeling
The Honourable Justice Kevin P. Feehan

Memorandum of Judgment

Appeal from the Decision of the Appeal Panel of the Council of the Alberta Dental Association and College
Dated the 10th day of November, 2020

Memorandum of Judgment

The Court:

I. Introduction

[1] Nimet Jinnah, a dentist regulated by the Alberta Dental Association and College,[1] appeals[2] a decision[3] by the College's appeal panel. It reprimanded her for unprofessional conduct and ordered her to complete a philosophy course on ethics and to pay hearing tribunal costs of $37,500 and one-quarter of the appeal panel costs.

II. Questions Presented

[2] Does "unprofessional conduct", as defined by section 1(1)(pp)(xii) of the *Health Professions Act*,[4] capture a dentist's business practices?

[3] If so, did Dr. Jinnah engage in "unprofessional conduct"?

[4] Did her use of "office charge" instead of "interest" on four accounts to indicate a charge for interest on an outstanding account in accordance with her agreement with a patient constitute unprofessional conduct?

[5] Did Dr. Jinnah's accounts provide her patient with an adequate explanation of the dental services for which she was asked to pay?

[6] Did Dr. Jinnah's collection efforts constitute unprofessional conduct?

[7] Did Dr. Jinnah commit unprofessional conduct when she asked her patient to agree to a term that increased the amount outstanding by fifty percent if the patient did not pay the amount due within a stipulated period and Dr. Jinnah retained a collection agency to collect the outstanding account?

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[1] There was a name change effective June 1, 2022. The new name is the College of Dental Surgeons of Alberta.

[2] *Health Professions Act*, R.S.A. 2000, c. H-7, s. 90(1). See *Law Society of Saskatchewan v. Abrametz*, 2022 SCC 29, ¶ 29 per Rowe, J. ("This case is a statutory appeal pursuant to *The Legal Profession Act, 1990*. Therefore, the standard of review is correctness for questions of law and palpable and overriding error for questions of fact and of mixed fact and law").

[3] Decision of the Appeal Panel of Council of the Alberta Dental Association and College dated November 10, 2020 [hereinafter cited as Appeal Panel Decision], ¶¶ 118, 119 & 164, Appeal Record 87 & 95.

[4] R.S.A. 2000, c. H-7, s. 1(1)(pp)(xii) ("In this Act ... (pp) 'unprofessional conduct' means one or more of the following, whether or not it is disgraceful or dishonourable: ... (xii) conduct that harms the integrity of the regulated profession").

[8] Did Dr. Jinnah's statement to her patient that she would sue if the patient defamed her in the course of making or advancing a complaint with the College constitute unprofessional conduct?

[9] If the College did not err in finding Dr. Jinnah guilty of unprofessional conduct, did it impose reasonable sanctions?

[10] The appeal panel reprimanded Dr. Jinnah and ordered her to take a philosophy course on ethics and to pay $37,500 to cover twenty percent of the costs the College incurred in a two-day hearing before the hearing tribunal and one-quarter of the costs before the appeal panel. Is this a reversible error?

III. Brief Answers

[11] A dentist's billing and collections practices may be "conduct that harms the integrity of the regulated profession" and properly classified as "unprofessional conduct" under the *Health Professions Act*.[5]

[12] The appeal panel committed a reversible error in upholding the hearing tribunal's finding that Dr. Jinnah's use of "office charge" instead of "interest" in four accounts constituted unprofessional conduct. The patient knew that the words "office charge" were the interest charges she had agreed to pay if she failed to pay on a timely basis. She said so in writing.[6]

[13] The appeal panel also erred in upholding the hearing tribunal's decision that Dr. Jinnah's accounts failed to provide her patient with an adequate explanation for the dental services for which Dr. Jinnah billed. The patient admitted in direct[7] and cross-examination[8] that she may have received an invoice prior to the November 28, 2014 invoice[9] about which she complains that referred to a "Balance Forward" of $444.46 and provided no information about the dental services Dr. Jinnah performed. The missing invoice could only have been the May 12, 2014 invoice that Dr. Jinnah's office printed[10] and that Dr. Jinnah claimed in her April 22, 2015 email to have sent

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[5] R.S.A. 2000, c. H-7, s. 1(1)(pp)(xii). See Part V. of this judgment for the text of the provision.

[6] Respondent's Extracts of Key Evidence 8, 53 & 56.

[7] Transcript of Proceedings Before the Hearing Tribunal [hereinafter cited as Transcript] 30:26-31:2, Appeal Record 131-32.

[8] Transcript 37:20-22, Appeal Record 138.

[9] Hearing Tribunal Decision ¶ 31, Appeal Record 17 & Respondent's Extracts of Key Evidence 54.

[10] Respondent's Extracts of Key Evidence 35.

to her patient.[11] The May 12, 2014 statement provided a detailed explanation of dental services covered by the bill.[12]

[14] Taking into account the undisputed fact that Dr. Jinnah's office printed the May 12, 2014[13] invoice that Dr. Jinnah stated she forwarded to her patient in her April 22, 2015 email to her patient,[14] the patient's admission that she does not recall whether she received a prior statement,[15] and the fact that the five other accounts Dr. Jinnah's office printed made their way to the patient, the College has not proved on a balance of probabilities that Dr. Jinnah's patient did not receive the May 12, 2014 invoice.

[15] Although some may describe the steps Dr. Jinnah undertook to collect her patients' unpaid accounts – including her April 1, 2015 "Final Notice"[16] – as aggressive, they did not constitute unprofessional conduct.

[16] The appeal panel failed to apply the proper test in holding that Dr. Jinnah acted improperly in asking her patient to agree that the outstanding balance be adjusted upward by fifty percent if her patient failed to pay an outstanding account within the agreed period and Dr. Jinnah retained a collection agency to pursue a delinquent account. It should have asked whether the contested provision was "so manifestly grossly one-sided that its enforcement would bring the administration of justice into disrepute".[17] The term does not display these features. It was not oppressive. It is enforceable. A dentist that asks a patient to agree to a term that the law will enforce has not committed unprofessional conduct.

[17] It is regrettable that Dr. Jinnah stated in her April 1, 2015 "Final Notice" that the upward adjustment was 100 percent and not fifty percent, which was the contract amount. But this error is attributable to carelessness, and carelessness in this context is not unprofessional conduct.

[18] The appeal panel correctly held that Dr. Jinnah engaged in conduct that harmed the integrity of the profession by informing her patient that she would sue if the patient defamed her in pursuing a complaint. Her conduct, objectively assessed, would cause a patient with backbone

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[11] See Respondent's Extracts of Key Evidence 16.

[12] Id. 22 & 35.

[13] Id. 35.

[14] Id. 16.

[15] Transcript 30: 26-31:2 & 37: 20-22, Appeal Record 131-32 & 138.

[16] Respondent's Extracts of Key Evidence 13. The "Final Notice" is reproduced verbatim in paragraph 32 of this judgment.

[17] *Capital Steel Inc. v. Chandos Construction Ltd*., 2019 ABCA 32, ¶ 106; 438 D.L.R. 4th 195, 241, majority aff'd, 2020 SCC 25, per Wakeling, J.A.

– more than ordinary resolve – to consider withdrawing a complaint already filed or not filing a complaint that he or she is contemplating filing.

[19] Dr. Jinnah has no legitimate basis to complain about the reprimand the appeal panel imposed. This is not a severe sanction and it matches her moderate degree of blameworthiness. There was no evidence that Dr. Jinnah intended her April 22, 2015 email to her patient to interfere with the complaints process and her lack of knowledge was not *per se* culpable. The Code of Ethics does not address the issue. The *Health Professions Act*[18] is silent on the point and no appeal panel or Court of Appeal decision has tackled the question.

[20] The appeal panel should not have ordered Dr. Jinnah to complete a philosophy course in ethics. There is no reason to believe that Dr. Jinnah would benefit from taking this course. She will acquire the information she needs about the best way to deal with a patient who has filed a complaint by reading the decisions of the appeal panel[19] and this Court.

[21] We set aside the appeal panel's decision to order Dr. Jinnah to pay $37,500 in hearing tribunal costs and one quarter of the expenses incurred before the appeal panel and refer the costs issue back to the appeal panel for reconsideration in accordance with the costs principles set out in this judgment. The College should bear the costs associated with the privilege and responsibility of self-regulation unless a member has committed serious unprofessional conduct, is a serial offender, has failed to cooperate with investigators, or has engaged in hearing misconduct. It would appear that Dr. Jinnah may be a serial offender.

IV. Statement of Facts

A. Dr. Jinnah Took Steps To Collect a Patient's Unpaid Account

[22] Dr. Jinnah, after securing the patient's written agreement to pay interest on outstanding accounts[20], provided dental services to a patient on a number of occasions early in 2014.[21] According to the patient, Dr. Jinnah's staff told her that they would contact her if the insurer did not cover the full costs.[22]

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[18] R.S.A. 2000, c. H-7.

[19] Appeal Panel Decision ¶ 88, Appeal Record 81.

[20] Respondent's Extracts of Key Evidence 33 ("If the amount due is not paid in full in 30 days you will be charged interest on the outstanding amount at the rate of 2% per month, compounded monthly: 26.28% annually. If your account remains unpaid after three months it will be turned over to a collection agency including outstanding interest, plus an additional charge of 50% (administration fee for being sent to the collection agency) which will be added to your balance") & Transcript 23:18-23, Appeal Record 124.

[21] Hearing Tribunal Decision ¶ 12, Appeal Record 14.

[22] Respondent's Extracts of Key Evidence 8. See Transcript 14:19-24, Appeal Record 115.

[23] The patient received a statement from Dr. Jinnah's office dated November 28, 2014 for $444.46.[23] It provided no details. It described the amount due as "Balance Forward". This suggests that Dr. Jinnah issued a previous statement that related to the dental services provided and that the patient had not paid, as of November 28, 2014, the amount billed and it remained outstanding.

[24] The patient admitted in direct[24] and cross-examination[25] that she did not remember if she received any invoices prior to November 28, 2014.

[25] The patient testified that she contacted Dr. Jinnah's office several times after she received the November 28, 2014 account asking for details about the bill.[26] The staff members she spoke to promised to investigate and report to her. The patient claimed this did not happen soon enough.[27] It was not until April 10, 2015 that Dr. Jinnah's office provided the detailed written explanation the patient sought.[28]

[26] According to Dr. Jinnah's records, the patient called her office on January 8, 2015 inquiring about the November 28, 2014 account.[29] Her staff promised to obtain the requested information. The patient said she would call back and did so on February 3, 2015. A staff member made a file entry stating that she provided the patient on the phone with the information she requested.[30]

[27] Dr. Jinnah's office sent out accounts in December 2014 and January 2015 that were identical to the November 2014 account.[31]

[28] Dr. Jinnah's office sent out a fourth account dated March 2, 2015.[32] It sought payment of $444.46, the sum listed in the November 2014 account, and three amounts of $9.63, $9.84 and $10.06, each designated "office charge", for a total of $473.98.

[29] On March 9, 2015 the patient, frustrated by her perceived inability to secure the information she requested from Dr. Jinnah's office, wrote the College seeking assistance in

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[23] Hearing Tribunal Decision ¶ 31, Appeal Record 17 & Respondent's Extracts of Key Evidence 54.

[24] Transcript 30: 26-31:2, Appeal Record 131-32.

[25] Id. 37: 20-22, Appeal Record 138.

[26] Hearing Tribunal Decision ¶ 15, Appeal Record 14.

[27] Id. ¶¶ 16-20, Appeal Record 14-15.

[28] Id. ¶ 23, Appeal Record 15 &16.

[29] Respondent's Extracts of Key Evidence 37& 42.

[30] Id. 24.

[31] Hearing Tribunal Decision ¶¶ 16 & 17, Appeal Record 14.

[32] Id. ¶ 19, Appeal Record 15 & Respondent's Extracts of Key Evidence 9 & 56.

resolving this problem. It is important to note that, objectively assessed, this letter was not a complaint. It was a request for assistance.[33] Part of her letter reads as follows:[34]

> 1 am seeking assistance to resolve matters with Dr. Nimet Jinnah who works out of SMILEMAKERS DENTAL CENTRE ...
>
> ...
>
> Prior to any work being completed I gave permission for her office staff … to seek pre-authorization from the two companies I have dental insurance with. This done, … [the office staff] contacted me to set up an appointment for the crown to be done. At that time I asked … what, if any monies would be owing. She said there would be no or very minimal additional charges and she would be able to verify the amount when I came in for my appointment. I came in for prep work … and asked again if there were any additional charges …, and was told there was no money owing, all was covered [by insurance]. At the end of March 2014, I had my final appointment for the permanent crown to be cemented into place. I asked once again if I owed any additional monies, and was told no. …
>
> In November 2014, I received an invoice for $444.46 … . I contacted SMILEMAKERS DENTAL CENTRE to inquire what the invoice was for … . I was told someone would get back to me. I have since that time contacted their office five times and have been told each time, that someone would get back to me. The last time I called was February 03, 2015, … [when staff] … assured me someone would look into the matter and get back to me by Friday, February 06, 2015. I still have not heard from anyone.
>
> I continue to receive invoices and …, am also accruing *interest*. … Please *provide direction* on how I can resolve this matter. I will not pay for work that was not completed and feel completely frustrated by the lack of professionalism being demonstrated by this dental office. I am also not prepared for this situation to affect my credit rating adversely. Thank you for your anticipated assistance in this matter.

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[33] Transcript 10:2-6, Appeal Record 111 ("[My March 9, 2015 letter to the College] was the original letter I sent to the College seeking their assistance to get information from Dr. Jinnah's office regarding an invoice I had received."); Transcript 15:26-27, Appeal Record 116 ("What I was seeking was information in terms of what the fee was for"); Transcript 16:10, Appeal Record 117 ("I was only seeking information"); Transcript 21:25-26, Appeal Record 122 ("I was simply asking to know what the bill was for in detail"). It is only after Dr. Jinnah sends her patient on April 1, 2015 a final notice, that the patient refers to her March 9, 2015 letter as a complaint. Respondent's Extracts of Key Evidence 11, 12 & 17.

[34] Respondent's Extracts of Key Evidence 8 (emphasis added).

[30] This letter makes it clear that the patient understood Dr. Jinnah charged interest on outstanding amounts.

[31] Almost a month – April 8, 2015 – passed before the complaints director forwarded the patient's March 9, 2015 letter to Dr. Jinnah and encouraged Dr. Jinnah to attempt to talk to her patient and respond to her patient's concerns.[35]

[32] On April 1, 2015, before Dr. Jinnah learned that her patient had written to the College asking for help in securing information about the dental services to which the charges related, Dr. Jinnah's office sent a "Final Notice"[36] and a fifth account to the patient[37]. The account was identical to the March 2, 2015 statement with the exception of an April 1, 2015 "office charge" for $10.27.[38] Dr. Jinnah signed this "Final Notice". Because of its importance, we set it out in full:[39]

> This is your final notice concerning your past due account. Because you have not contacted Smilemakers Dental Centre to discuss options for payment or to set up a payment plan, we must take further action.
>
> A great deal of time, effort and cost in attempting to work out arrangements for payment of your account has been invested. At this time, we must, therefore, insist that payment or contact be made immediately to discuss acceptable options available to you if you are having difficulty paying off your balance.
>
> Please accept responsibility for this obligation. Smilemakers Dental Centre would prefer not to resort to a professional agency to collect what you owe, however, it is prepared to do so. I know this will damage your credit rating. Please do not force us to take extreme measures to obtain payment.
>
> In addition, you will be liable for *interest* incurred as well as all costs associated with the collection proceedings, which is 100% of the FULL balance (including fees) as well as associated legal costs which may be incurred. The collection fee/administration fee has been added to your account. Please contact our office by April 17, 2015 for us to be able to remove this fee for you.

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[35] Id. 102-03.

[36] Id. 13 & 57. Dr. Jinnah explained that the administrative charge listed as 100% instead of 50% as outlined in the Financial Policy was an administrative error, and this error was corrected in Dr. Jinnah's email to the patient on April 22, 2015. Hearing Tribunal Decision, ¶ 60, Appeal Record 23.

[37] Respondent's Extracts of Key Evidence 20.

[38] Id. 36.

[39] Id. 13 (emphasis added).

> This being your final notice, before initiating third party collection procedures please govern yourself accordingly and immediately begin steps to repay your entire outstanding balance. Please call our office immediately to resolve this matter. Thank you for your prompt consideration.
>
> *Possible actions by the collection agency include credit reporting and legal pursuit of payment.

[33] The reference in this letter to "interest" demonstrates that Dr. Jinnah did not intend to conceal the fact that she charged interest on outstanding accounts. The fact that the patient signed an agreement that obliged her to pay interest on unpaid amounts makes this finding incontestable.[40]

[34] On April 10, 2015, the date the patient received the final notice, she phoned Dr. Jinnah's office.[41] A staff member informed the patient that the file would not be forwarded to a collection agency, provided the patient with a detailed explanation of the dental services Dr. Jinnah performed, and promised to promptly mail her a complete statement of services provided.[42] The patient told the staff member that she would pay $444.46[43] after she received a statement describing in detail the dental services Dr. Jinnah provided. She also made it clear to the staff member that she would not pay interest that accrued after she called Dr. Jinnah's office in November 2014. She asserted that if Dr. Jinnah's office had responded in a timely manner to her November request for information, she would have paid the account at that time and no interest would have accrued.[44]

[35] On April 20, 2015 the patient received in the mail the detailed statement of account Dr. Jinnah's office promised to deliver to her.[45]

[36] Dr. Jinnah's next step – an April 22, 2015 email to her patient sent after Dr. Jinnah received notice from the College of her patient's March 9, 2015 letter to the College – was ill-advised, to

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[40] The patient promised to pay interest on an overdue account and an "administration fee" of 50% of the outstanding account if she failed to pay her account within three months and Dr. Jinnah retained a collection agency to collect the outstanding account. Respondent's Extracts of Key Evidence 33.

[41] Hearing Tribunal Decision, ¶¶ 23 & 110, Appeal Record 15 & 32-33.

[42] Id. ¶ 23, Appeal Record 15 & 16.

[43] Transcript 45:20-21, Appeal Record 146 & Respondent's Extracts of Key Evidence 11.

[44] See Respondent's Extracts of Key Evidence 17-18 ("If you or your office staff had responded to my initial call in November 2014 I would never had to contact the ... [College]. AT NO TIME did I indicate that I would not pay for services rendered. I only asked someone to explain to me what the charges were for ... . Now that I have it, I will pay the $444.46 in full. I will not pay for any late charges or any interest as the onus is on you for this matter not being handled in a timely manner").

[45] Hearing Tribunal Decision, ¶ 24, Appeal Record 16. See Respondent's Extracts of Key Evidence 21-22.

say the least. It was not conciliatory in nature and it needlessly exacerbated a problem that probably would have disappeared if it had never been sent:[46]

> It has been brought to my attention that there is a balance outstanding for dental treatment completed April 1st, 2014, which is over a year old. You had originally booked your appointment with Sheila who had explained to you that your approximate portion would be $300+ depending on the exact amount of the crown (see attachment which was scanned on March 20th/14 and is noted in our system). She told you this on March 20/14 and proceeded to book your appointment at 2:06 pm the same day, for March 26th. On the 26th of March 2014, you were told to please pay your portion. You stated, as you can see notes on your statement (attached) that you would pay the day we inserted the crown, however, you did not. You were then sent statements May 12/14, Nov 28/14, Dec 9/14, Jan 28/15, Mar 2/15 and April 1/15, as can be … [seen] on the statements. When Sharrie spoke with you on April 10th/2015 you asked for yet another copy of your statement, which she mailed to you. Now, over 2 weeks later, we still have not received payment.
>
> …
>
> Having said all of the above, I would be willing to make a professional courtesy adjustment of $100 to your account, which currently sits at $454.09, for payment made before this Friday, April 24 if we can close this off and let the dental association know that the complaint has been resolved. This ... is purely a professional courtesy and in no way is an acceptance of any wrongdoing on my part. If however, you feel you do not wish to pay the balance or feel that there are other outstanding issues, the full account without any deductions will be sent to a collection agency as mentioned with the addition of administration fees, as per the signed financial policy. Any costs incurred in retaining a lawyer in a situation where it is deemed that the accusations are false or there is any concern of defamation of character will then rest with yourself. I trust the above clearly outlines the options currently available to you.

[37] The email strongly suggests that Dr. Jinnah had no idea a staff member had spoken with her patient on April 10 and that the patient promised to pay the outstanding account on receipt of the detailed statement of services provided.

[46] Respondent's Extracts of Key Evidence 16.

[38] The patient replied the next day.[47] Her email stated that she now knew, as a result of her April 10, 2015 conversation with a staff member and receipt of a detailed statement of account, "what the charge was for; which is all I have been trying to obtain since November 2014,"[48] and "would pay the $444.46 in full". She stated that "I will not pay ... any interest as the onus is on you for this matter."[49]

[39] On May 1, 2015 the patient paid as promised.[50]

[40] Dr. Jinnah provided her version of the key events in a May 9, 2015 letter to the College, parts of which follow:[51]

> There are notes in our system stating she [the patient] called January 8, 2015 and spoke to Brittney asking about her bill. Brittney said she would look into it as the balance was from our previous software system, which was changed over in July 2014. [The patient] stated as per the notes in our computer system that she would call back the following month. We have a documented call on February 3, 2015 where [the patient] spoke to Brittney who explained all of the charges to her. We still did not receive payment.

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[47] Id. 17-18.

[48] Id. 17.

[49] Id. 18. See also Transcript 26:8-14, Appeal Book 127 ("I also said that ... I would not be paying for any later outstanding charges because ... it wasn't my issue in terms of her inability to navigate things appropriately").

[50] Hearing Tribunal Decision ¶ 110, Appeal Record 33 & Respondent's Extracts of Key Evidence 53.

[51] Respondent's Extracts of Key Evidence 24. See also id. 44-46.

B. The College Charged Dr. Jinnah with Unprofessional Conduct

[41] On September 28, 2017, more than 2.5 years after the patient first contacted the College on March 9, 2014,[52] the College issued a notice of hearing,[53] charging Dr. Jinnah with unprofessional conduct in relation to her billing and collections practices. A subsequent amendment to the notice of hearing produced a final charge that Dr. Jinnah[54]

> between on or about February 2014 and April 2015 … engaged in conduct that displayed a lack of knowledge of, or a lack of skill or judgment in the provision of professional services, that contravened the Code of Ethics (one or more of Principle 5, Articles B5, B.5.1), or that harmed the integrity of the regulated profession, with respect to patient SM, particulars of which include one or more of the following:
>
> a. failing to provide clear and transparent information regarding billing and/ or collection of fees owing;

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[52] This delay is troubling. The important facts were not in dispute and the issues were not complicated. In *The Queen v. Chief Constable of the Merseyside Police, ex p. Calveley*, [1986] 1 Q.B. 424, 435 per Sir John Donaldson, M.R. (C.A. 1985) the Court, in a judicial review application, set aside an order of the Chief Constable convicting the officers of misconduct because "the applicants had no formal notice of the complaints for well over two years. This is so serious a departure from the police disciplinary procedure that, in my judgment, the court should, in the exercise of its discretion, grant judicial review, and set aside the determination of the Chief Constable". It is not in anyone's best interests – not the complainant's, the dentist's, the public's, or the College's – for years to pass before unprofessional conduct cases are resolved. If a dentist needs to alter his or her business practices, this fact should be brought to the dentist's attention promptly, not years later. If the College regularly takes this much time to process complaints, it should search for ways to streamline its procedure. See *Blencoe v. British Columbia Human Rights Comm'n*, 2000 SCC 44, ¶¶ 140 & 144; [2000] 2 S.C.R. 307, 384 & 386 per Lebel, J. ("Unnecessary delay in ... administrative proceedings ... [is] a problem that must be brought under control if we are to maintain an effective system of justice, worthy of the confidence of Canadians. .... When we ask whether there has been an administrative law abuse of process, we ask the same fundamental question: has an administrative agency treated people inordinately badly?") & *Law Society of Saskatchewan v. Abrametz*, 2022 SCC 29, ¶ 46 per Rowe, J. ("Inordinate delay in administrative proceedings ... is contrary to the interests of society. Decisions by administrative decision makers need to be rendered promptly and efficiently. Administrative delay undermines a key purpose for which such decision-making authority was delegated – expeditious and efficient decision-making"). Is it not an abuse of process for the College to wait more than 2.5 years after the patient first contacted the College to issue a notice of hearing and then convene a hearing more than two years after the issuance of a notice of hearing? See D. Jones, Q.C. & A. de Villars, Q.C., Principles of Administrative Law 271-72 (7th ed. 2020) ("The Supreme Court's decision in *Blencoe* did not leave much room for the direct application of section 7 of the *Charter* to the practices and procedures adopted by statutory delegates. However, the case did open the door to the argument that a serious delay may, in rare cares, render administrative proceedings an abuse of process and contrary to the interests of justice and justify the granting of a stay of proceedings").

[53] Appeal Record 4.

[54] Revised Notice of Hearing and Notice to Attend and Produce dated September 5, 2019, Appeal Record 7-8.

b. engaging in inappropriate collection practices;

c. failing to engage in usual and customary business practices to collect payment owing by the patient.

[42] It is not clear to us what specific acts of Dr. Jinnah the College claims constitute unprofessional conduct.[55] The notice of hearing does not particularize the conduct it asserts displays the deficiencies highlighted in it. Did the College claim that the "balance forward" entry in Dr. Jinnah's November 28, 2014, December 9, 2014, January 28, 2015, March 2, 2015 and April 1, 2015 accounts failed to provide "clear and transparent information" about dental services provided? Did the College claim that Dr. Jinnah failed to adequately respond to her patient's request for more information about the November 28, 2014 account? Did the College claim that either Dr. Jinnah's final notice or April 22, 2015 email to her patient or both were contrary to customary business practices and constituted unprofessional conduct? Did the College claim that the "office charge" entries in Dr. Jinnah's accounts were misleading? Did the College assert that Dr. Jinnah interfered with the complaint process?[56]

C. The Hearing Tribunal Held that Dr. Jinnah Engaged in Unprofessional Conduct and Imposed Onerous Sanctions

1. The Merits Decision

[43] The hearing tribunal convened on November 26, 2019.[57] This was more than two years after the College issued a notice of hearing.[58] And, as already noted, the College issued the notice of hearing more than two and a half years after the conduct identified in the notice of hearing was alleged to have occurred.

[44] On March 2, 2020, almost five years after the patient first contacted the College asking for its assistance so that she could determine what she owed Dr. Jinnah, the hearing tribunal concluded that Dr. Jinnah engaged in unprofessional conduct in five ways.

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[55] See *Morris v. Royal College of Dental Surgeons of Ontario*, 127 O.A.C. 282, 283 & 284 (Div. Ct. 1999) per Lane, J. ("The second charge is entirely devoid of particulars apart from confining the act or acts to the year 1997. …. [T]he second charge is quashed for want of particularity").

[56] If so, has the College in its notice of hearing charged Dr. Jinnah with obstruction of the complaints process? Does a charge that relates to billing and collection practices cover an allegation that Dr. Jinnah obstructed the complaints process?

[57] Hearing Tribunal Decision, Appeal Record 11.

[58] This delay is also troubling. See *Veterinary Professions Act*, R.S.A. 2000, c. V-2, s. 42(2) ("Within 30 days after the date on which the chair refers a complaint or conduct to the Committee, the Committee shall hold a hearing on the complaint or conduct") & 42(3) ("The Council may, on the written request of the chair of a review panel, extend the period mentioned in subsection (2) for one or more additional periods, each not exceeding 30 days").

[45] First, it held that four statements – November 28, 2014, December 9, 2014, January 28, 2015 and March 2, 2015 – "lacked clarity and transparency".[59] It criticized Dr. Jinnah for not providing more information than she did in the November 28, 2014 account.[60] This account contained only the "Balance Forward" entry for $444.46.

[46] Unfortunately, the hearing tribunal did not determine whether Dr. Jinnah's office forwarded to the patient the May 12, 2014 statement that contained a detailed explanation of the dental services Dr. Jinnah performed and that her office printed. The patient's evidence was that she could not recall if she had received a statement prior to the November 28, 2014 statement.[61] She has, in effect, acknowledged that she may have received a prior statement. This was an important fact. It is likely that she did given that the sole entry in the November 28, 2014 statement was "Balance Forward". Dr. Jinnah's records indicated that an account was printed on May 12, 2014.[62] The fact that the five other accounts Dr. Jinnah's office printed made it into the patient's hands, and the fact that Dr. Jinnah's April 22, 2015 email expressly claimed that "[y]ou were sent statements May 12/14, Nov 28/14, Dec 9/14, Jan 28/15, Mar 2/15 and Apr 1/15,"[63] strongly support the inference that the patient received the May 12, 2014 account.

[47] Second, the hearing tribunal found that the "office charge" entries were misleading. It was satisfied Dr. Jinnah should have used "interest charge"[64] to describe the interest due.

[48] Third, it determined that Dr. Jinnah engaged in inappropriate collection practices:[65] "The Hearing Tribunal finds that Dr. Jinnah's collection practices with [her] patient ... was conduct that harmed the integrity of the profession and breached Principle 5 of the Code of Ethics such that it amounted to unprofessional conduct under section 1(1)(pp)(ii) and 1(1)(pp)(xii) of the *Health Professions Act*."

[49] Fourth, the hearing tribunal also criticized the provision in Dr. Jinnah's financial agreement that resulted in the outstanding balance being increased by fifty percent if Dr. Jinnah retained a collection agency to chase a debtor patient for an outstanding debt:[66]

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[59] Hearing Tribunal Decision ¶ 112, Appeal Record 33.

[60] Id. ¶ 113, Appeal Record 34.

[61] Transcript 30:26-31:2& 37:20-22, Appeal Record 131-32 & 138.

[62] Respondent's Extracts of Key Evidence 35.

[63] Id. 16.

[64] Hearing Tribunal Decision, ¶¶ 115 & 120, Appeal Record 35 & 37.

[65] Id. ¶ 126, Appeal Record 39.

[66] Id. ¶ 130, Appeal Record 39-40.

> [A]lthough the Hearing Tribunal believes it is acceptable for dentists to use the services of a collection agency to collect on outstanding accounts, the Hearing Tribunal finds Dr. Jinnah's 50% administration fee carries with it an implied threat that is incongruent with a dentist-patient relationship. Dr. Jinnah's collection techniques included her threatening to act on the Financial Policy of 50% … and threatening to affect a patient's credit score. These are collection practices that go beyond what the Hearing Tribunal finds acceptable.

[50] The hearing tribunal concluded that Dr. Jinnah "displayed a lack of knowledge, skill and judgment in the provision of professional services that contravened Principle 5, Veracity of the *Code of Ethics*".[67] It was satisfied "Dr. Jinnah's practice of billing and collecting fees from … [her patient] was not truthful and forthright".[68]

[51] Fifth, the hearing tribunal also concluded that Dr. Jinnah's final notice and her April 22, 2015 email constituted unprofessional conduct.[69] It held that the "tone" of the final notice was unprofessional,[70] and that Dr. Jinnah should not have "threatened legal action for defamation based on comments made by … [the patient] in her letter of complaint"[71] or stated that the patient's credit rating would be harmed if Dr. Jinnah retained a collection agency to collect the patient's outstanding debt.[72]

[52] Of interest, the hearing tribunal urged the College to provide dentists with more guidance on how to collect outstanding accounts:[73] "[T]here is no direction to the profession about what the … [College] expects of dentists and their collection practices. … [T]his case is illustrative of a greater need for clarity for the profession by … [the College]. There should be more guidance for dentists in this area."

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[67] Id. ¶ 118, Appeal Record 36. See Alberta Dental Association and College, Code of Ethics (October 2007) ("The dentist must be truthful and forthright in all professional matters. This means fully disclosing and not misrepresenting information in dealings with patients, the public at large on dental matters, other professionals, and the Alberta Dental Association and College").

[68] Id. ¶ 120, Appeal Record 37.

[69] Id. ¶ 126, Appeal Record 39.

[70] Id. ¶ 124, Appeal Record 38-39.

[71] Id.

[72] Id.

[73] Id. ¶ 132, Appeal Record 40.

2. Sanction Decision

[53] The hearing tribunal's sanction decision[74] prohibited Dr. Jinnah from practicing for one month, ordered her to complete a philosophy course in ethics, and imposed costs of $50,000.[75] The hearing tribunal declined to issue a caution or a reprimand because "the proven conduct in this case was far too serious to justify a caution or a reprimand as the sole order under section 82 of the *Health Professions Act*".[76] A part of its sanction decision follows:[77]

> The conduct was serious and harmed the integrity of the profession. The billing and collection practices were unprofessional and went beyond what the Hearing Tribunal considered acceptable. Dr. Jinnah's financial information to the patient was not transparent or truthful. The interest charges were *disguised* as office charges, and when the patient paid the outstanding invoice, the patient did pay interest charges that she was not aware of. Dr. Jinnah threatened legal action and caused a patient to feel bullied, upset and threatened. A patient should not be made to feel this way. Dr. Jinnah was disrespectful to her patient and made personal threats against her patient over the collection of an account.

[54] Given the fact that the patient agreed in writing before Dr. Jinnah provided any dental services to pay interest on outstanding amounts[78] and stated in her June 25, 2015 letter to the College that "office charges" were interest charges and she refused to pay them,[79] it is difficult to understand on what basis the hearing tribunal could find that "[t]he interest charges were disguised". They were not – plain and simple. Both the patient and Dr. Jinnah understood that an "office charge" was an interest charge.[80]

[55] The hearing tribunal also ordered Dr. Jinnah to take a philosophy course in ethics. It did so because "Dr. Jinnah did not appear to understand or have the knowledge, skill and judgment that her written communications with the patient were unprofessional and inappropriate".[81] The hearing tribunal did not explain how enrolling in a philosophy course in ethics would assist Dr. Jinnah acquire this knowledge.

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[74] Hearing Tribunal Decision on Sanctions, Appeal Record 41.

[75] Id. ¶ 50, Appeal Record 55-56.

[76] Id. ¶ 51, Appeal Record 56.

[77] Id. ¶ 55, Appeal Record 56 & 57 (emphasis added).

[78] Respondent's Extracts of Key Evidence 33.

[79] Id. 53 & 56.

[80] Id.

[81] Hearing Tribunal Decision on Sanctions, ¶ 52, Appeal Record 56.

D. The Appeal Panel Upheld Parts of the Hearing Tribunal's Decision

[56] Dr. Jinnah, relying on section 87(1) of the *Health Professions Act*,[82] appealed[83] both the hearing tribunal's merits and sanctions decisions to the council of the College.

[57] Although the appeal panel identified two errors on the part of the hearing tribunal – the hearing tribunal should not have heard evidence from a forensic accountant[84] relating to criminal interest rates under the *Criminal Code*[85] and it placed insufficient weight on records created by Dr. Jinnah's staff[86] – it substantially upheld the hearing tribunal's factual determinations and its conclusion that Dr. Jinnah had engaged in unprofessional conduct.[87]

[58] The appeal panel upheld as reasonable the hearing tribunal's decision that Dr. Jinnah's accounts failed to provide sufficient details about the dental services for which she billed and that the accounts should have identified interests charges as such and not as "office charges".[88]

[59] The appeal panel concluded that the hearing tribunal's critical assessment of the final notice and Dr. Jinnah's April 22, 2015 email to her patient was reasonable:[89]

> In the opinion of the Appeal Panel, it was open to the Hearing Tribunal to conclude that the tone and content of the Final Notice to a patient was unprofessional and this conclusion was not unreasonable in the circumstances. This was an account of less than $500 on which the patient had called a number of times requesting detailed information on how the outstanding amount was calculated. The Final Notice letter was sent to … [the patient] before any attempt was made to provide the detailed information. The Appeal Panel notes that once this detailed information was provided on April 10, 2015, the patient paid the outstanding amount.
>
> ….
>
> In the opinion of the Appeal Panel, the concern of the Hearing Tribunal regarding Dr. Jinnah threatening an action in defamation against a patient for making a complaint to the … [College] was valid. The right of patients to file a complaint

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[82] R.S.A. 2000, c. H-7. See Part V. of this judgment for the text of the provisions.

[83] Appeal Record 9.

[84] Appeal Panel Decision, ¶ 39, Appeal Record 71.

[85] R.S.C. 1985, c. C-46.

[86] Appeal Panel Decision, ¶¶ 59 & 118, Appeal Record 75 & 87.

[87] Id. ¶¶ 54, 66 & 110, Appeal Record 74, 77 & 87.

[88] Id. ¶¶ 51 & 54, Appeal Record 73 & 74.

[89] Id. ¶¶ 80 & 88, Appeal Record 80 & 81.

> against a dentist that is then investigated by the … [College] is a fundamental aspect of the role of the … [College] as part of a self-regulating profession that acts to protect the public interest. All dentists must respect this right of a patient and conduct that attempts to discourage or threaten a patient for … [filing] a complaint breaches the conduct required of a dentist.

[60] The appeal panel also upheld the hearing tribunal's critical assessment of a provision in Dr. Jinnah's financial agreement with her patient that she pay an additional sum if Dr. Jinnah retains a collection agency:[90]

> What the Hearing Tribunal found unprofessional was the manner in which this claim for a 50% … administration fee was used … as "an implied threat" to obtain payment and part of a further threat to affect the patient's credit score. The Hearing Tribunal found that these actions were "incongruent with a dentist-patient relationship" and "collection practices that go beyond what the Hearing Tribunal finds acceptable."
>
> In the opinion of the Appeal Panel, it was not unreasonable for the Hearing Tribunal to determine that the manner in which the 50% and 100% administration fee was used by Dr. Jinnah was unprofessional for the reasons set out in … [its] decision.
>
> The Hearing Tribunal noted … that Mr. Thoman stated that he had never come across a collection practice like Dr. Jinnah's where the account is doubled before being sent to a collection agency. It is clear in the decision that the professional members of the Hearing Tribunal had not seen such a practice and found that it was not a usual and customary practice used in the dental profession to collect outstanding accounts. In the opinion … of the Appeal Panel it was reasonable for the Hearing Tribunal to reach this conclusion.

[61] The appeal panel quashed the one-month suspension and substituted a reprimand,[91] finding that a suspension was disproportionate,[92] and reduced the hearing tribunal costs to $37,500 because the forensic accountant's evidence on the *Criminal Code* was unnecessary and irrelevant.[93] The appeal panel found that the hearing tribunal's sanction of requiring Dr. Jinnah to take an ethics

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[90] Id. ¶¶ 114-16, Appeal Record 86-87.

[91] Id. ¶¶ 146 & 160, Appeal Record 92 & 95.

[92] Id. ¶¶ 145-46, Appeal Record 91-92.

[93] Id. ¶¶ 149-151, Appeal Record 93.

course was reasonable.[94] It also ordered Dr. Jinnah to pay costs equal to one-quarter of the appeal panel costs.[95]

[62] Dr. Jinnah filed a civil notice of appeal[96] and asks this Court to quash the appeal panel's decision.[97]

V. Statutory and Code of Ethics Provisions

A. *Health Professions Act*

[63] The important parts of the *Health Professions Act*[98] are set out below.

> 1(1) In this Act,
>
> …
>
> (t) "investigated person" means a person with respect to whom
>
> (i) a complaint has been made under Part 4,
>
> (ii) information has been treated as a complaint in accordance with section 56, or
>
> (iii) a notice has been given under section 57(1),
>
> and the proceedings with respect to the complaint, information or notice have not been concluded;
>
> …
>
> (z) "practice" means the practice of a regulated profession within the meaning of section 3 of a schedule to this Act;
>
> …
>
> (ff) "professional service" means a service that comes within the practice of a regulated profession;
>
> …

[94] Id. ¶¶ 147-148.

[95] Id. ¶ 157, Appeal Record 94.

[96] Appeal Record 96.

[97] *Health Professions Act*, R.S.A. 2000, c. H-7, s. 92(1)(b).

[98] R.S.A. 2000, c. H-7.

(pp) "unprofessional conduct" means one or more of the following, whether or not it is disgraceful or dishonourable:

(i) displaying a lack of knowledge of or lack of skill or judgment in the provision of professional services;

(ii) contravention of this Act, a code of ethics or standards of practice;

…

(xii) conduct that harms the integrity of the regulated profession;

…

3(1) A college

(a) must carry out its activities and govern its regulated members in a manner that protects and serves the public interest,

(b) must provide direction to and regulate the practice of the regulated profession by its regulated members,

(c) must establish, maintain and enforce standards for registration and of continuing competence and standards of practice of the regulated profession, … .

…

55(2) The complaints director

(a) subject to subsection (2.1) and (2.2), may encourage the complainant and the investigated person to communicate with each other and resolve the complaint,

(a.1) may, with the consent of the complainant and the investigated person, attempt to resolve the complaint,

(b) subject to subsection (2.1) and (2.2), may make a referral to an alternative complaint resolution process under Division 2,

(c) may request an expert to assess and provide a written report on the subject-matter of the complaint,

(d) may conduct, or appoint an investigator to conduct, an investigation,

(e) if satisfied that the complaint is trivial or vexatious, may dismiss the complaint,

(f) if satisfied that there is insufficient or no evidence of unprofessional conduct, may dismiss the complaint, and

(g) may make a direction under section 118.

…

82(1) If the hearing tribunal decides that the conduct of an investigated person constitutes unprofessional conduct, the hearing tribunal may make one or more of the following orders:

(a) caution the investigated person;

(b) reprimand the investigated person;

…

(d) direct the investigated person to satisfy the hearing tribunal, committee or individual specified in the order that the investigated person is not incapacitated and suspend the investigated person's practice permit until the hearing tribunal, committee or individual is so satisfied;

(e) require the investigated person to undertake counselling or a treatment program that in its opinion is appropriate;

(f) direct that within the time set by the order the investigated person must pass a specific course of study, obtain supervised practical experience of a type described in the order or satisfy the hearing tribunal, committee or individual specified in the order as to the investigated person's competence generally or in an area of the practice of the regulated profession;

…

(j) direct, subject to any regulations under section 134(a), that the investigated person pay within the time set in the order all or part of the expenses of, costs of and fees related to the investigation or hearing or both, including but not restricted to

(i) the expenses of an expert who assessed and provided a written report on the subject-matter of the complaint,

(ii) legal expenses and legal fees for legal services provided to the college, complaints director and hearing tribunal,

(iii) travelling expenses and a daily allowance, as determined by the council, for the complaints director, the investigator and the members of the hearing tribunal who are not public members,

(iv) witness fees, expert witness fees and expenses of witnesses and expert witnesses,

(v) the costs of creating a record of the proceedings and transcripts and of serving notices and documents, and

(vi) any other expenses of the college directly attributable to the investigation or hearing or both;

(k) direct that the investigated person pay to the college within the time set in the order a fine not exceeding the amount set out in the column of the unprofessional conduct fines table that is specified for the college in a schedule to this Act for each finding of unprofessional conduct or the aggregate amount set out in that column for all of the findings arising out of the hearing;

(l) any order that the hearing tribunal considers appropriate for the protection of the public.

…

(4) A fine or expenses ordered to be paid under this section and section 89 are a debt due to the college and may be recovered by the college by an action in debt.

…

89(6) Subject to any regulations under section 134(a), the council may direct the investigated person to pay, within the time set by the council, in addition to expenses, costs and fees referred to in section 82(1)(j), all or part of the expenses of, costs of and fees related to the appeal, including

(a) legal expenses and legal fees for legal services provided to the college, complaints director and council,

(b) travelling expenses and a daily allowance, as determined by the council, for the complaints director and the members of the council who are not public members,

(c) the costs of creating a record of the proceedings and transcripts and of serving notices and documents, and

(d) any other expenses of the college directly attributable to the appeal.

(7) A fine or expenses ordered or directed to be paid under this section are a debt due to the college and may be recovered by the college by an action in debt.

[64] Section 3 in Schedule 7 of the *Health Professions Act*[99] defines a dentist's "practice" as doing "one or more of the following":

> (a) evaluate, diagnose and treat, surgically or non-surgically, diseases, disorders and conditions of
>
> (i) the mouth, which includes teeth, gums and other supporting structures,
>
> (ii) the maxillofacial area, which includes upper and lower jaws and joints, and
>
> (iii) the adjacent and associated structures of the head and neck, to maintain and improve a person's physical, psychological and social health,
>
> (b) provide restricted activities authorized by the regulations, and
>
> (c) teach, manage and conduct research in the science, techniques and practice of dentistry.

B. Alberta Dental Association and College's Code of Ethics

[65] The relevant passages from the Alberta Dental Association and College's Code of Ethics[100] follow:

> Purpose, Authority, Accountability
>
> …
>
> The Code of Ethics is an important part of the way in which the Alberta Dental Association and College fulfills its obligation to promote and protect the public interest.
>
> Principles
>
> …
>
> 5. Veracity
>
> … The dentist must be truthful and forthright in all professional matters. This means fully disclosing and not misrepresenting information in dealings with patients, the public at large on dental matters, other professionals, and the Alberta Dental Association and College.

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[99] R.S.A. 2000, c. H-7.

[100] (October 2007). Factum of the Appellant Appendix A.

…

Article B5: Fees and Compensation for Service

A dentist is responsible for establishing fees for professional services performed for his or her own practice.

…

Article B5.1: Dental Plans and Third Party Carriers

If the patient's third party carrier plan specifies a co-payment from the patient, the dentist providing the services for the patient must, under the conditions of the plan, engage in usual and customary business practices to collect such co-payments from the patient.

VI. Analysis

A. A Dentist's Billing and Collection Practices Are Subject to Regulation by the Alberta Dental Association and College

[66] Section 3(1)(a) of the *Health Professions Act*[101] imposes on the Alberta Dental Association and College the responsibility to "govern its regulated members in a manner that protects and serves the public interest".

[67] Section 3(1), when read with section 1(1)(pp) of the *Health Professions Act*, which is set out below, conclusively determines that "unprofessional conduct" captures a dentist's dental knowledge and skills and business practices:[102]

1(1) In this Act,

…

(pp) "unprofessional conduct" means one or more of the following, whether or not it is disgraceful or dishonourable …

…

(xii) conduct that *harms the integrity* of the regulated profession … .

[101] R.S.A. 2000, c. H-7. See Part V. of this judgment for the full text.

[102] Emphasis added.

[68] In this context, "integrity" means "[s]teadfast adherence to a strict moral or ethical code"[103] or "[s]oundness of moral principle, the character of uncorrupted virtue, esp. in relation to truth and fair dealing: uprightness, honesty, sincerity".[104]

[69] The College must be able to regulate the business practices of dentists to ensure that dentists are ethical, honest, and beyond reproach. Persons who deal with dentists expect them to be persons of good moral character who abide by a code of ethics that promotes sound business practices.

[70] Suppose a dentist has top-level abilities to diagnose dental problems and to identify appropriate remedial treatment, the physical skills needed to execute the requisite steps and best-in class interpersonal skills. But the dentist routinely knowingly charges patients for services not provided. The College must have the ability to sanction this dentist. If it did not, the integrity of the profession would be imperiled. The public expects all dentists to be ethical and honest.

[71] In order to protect the public interest, the College must have the authority to regulate the knowledge and skills dentists possess – to protect consumers of dental services from unskilled practitioners – and the business side of the dental practice – to ensure that patients are informed in plain English of the dental services that their dentists have performed and the cost of these services, have their questions about their bills answered politely, promptly and accurately, and are, in general, treated fairly and with respect.

[72] Twenty years ago this Court said so in *Brown v. Alberta Dental Association*:[105]

> The paramount objective of any professional act is the protection of the public, which is achieved through the establishment of a self-regulating profession charged with that responsibility. It is possible for the public to be adversely impacted by the business practices adopted by a dentist. Furthermore, in order to meet the objective of public protection, it is essential to maintain the honour and dignity of the profession. *To meet these objectives, the legislative scheme must allow for controls on a dentist's business.* For example, the Association might feel compelled to regulate aggressive collection or marketing practices that could jeopardize the

[103] The American Heritage Dictionary of the English Language 911 (5th ed. 2016).

[104] 7 Oxford English Dictionary 1066 (2d ed. 1989).

[105] 2002 ABCA 24, ¶ 30; [2002] 5 W.W.R. 221, 230 per Russell, J.A. (emphasis added). See also *Yee v. Chartered Professional Accountants of Alberta*, 2020 ABCA 98, ¶ 23 per Slatter, J.A. ("The ultimate objective of professional regulation is protection of the public") & *Bishop v. Alberta College of Optometrists*, 2009 ABCA 175, ¶¶ 27-30; 96 Admin. L.R. 4th 1, 7-8 (the Court upheld a decision of the College of Optometrists that a regulated member's billing practice could be a ground of unprofessional conduct).

> standing of the profession. If "practice of dentistry" were given a narrow interpretation, the capacity for this control would be significantly reduced.

[73] The fact that dentists invariably delegate business tasks – scheduling and billing, for example – to others in their offices does not insulate the dentist from the responsibility for the manner in which these workers discharge these assignments. It simply means that dentists must provide their staff with the training and supervision needed to reduce to a sufficiently low degree the risk that their behavior will adversely affect the dentist's reputation.

[74] We accept Dr. Jinnah's argument that other parts of the *Health Professions Act*[106] and the *Dental Profession Regulation*[107] define "practice" and "professional service" narrowly so as to exclude the business side of the practice of dentistry. For example, section 3 of Schedule 7 to the *Health Professions Act*[108] reads as follows:

> Practice
>
> 3 In their practice, dentists do one or more of the following:
>
> (a) evaluate, diagnose and treat, surgically or non-surgically, diseases, disorders and conditions of
>
> (i) the mouth, which includes teeth, gums and other supporting structures,
> (ii) the maxillofacial area, which includes upper and lower jaws and joints, and
> (iii) the adjacent and associated structures of the head and neck,
>
> to maintain and improve a person's physical, psychological and social health ... .

[75] We also agree that section 1(1)(pp)(i) of the *Health Professions Act* – part of the definition of "unprofessional conduct" – applies only to professional competence in the provision of dental services, such as diagnosis and treatment, and does not sweep in the business component of the practice of dentistry.

[76] But, as noted above, section 1(1)(pp)(xii)of the *Health Professions Act*[109] strongly supports the conclusion that a dentist's billing and collections practices can amount to unprofessional

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[106] R.S.A. 2000, c. H-7, s. 1(1)(z), 1(1)(ff) & Sch. 7, s. 3.

[107] Alta. Reg. 254/2001, s. 12.

[108] R.S.A. 2000, c. H-7.

[109] R.S.A. 2000, c. H-7.

conduct within the *Health Professions Act*. It is a basic principle of statutory interpretation that an adjudicator must read the entire statute,[110] and not just the part most obviously engaged by the fact pattern.

[77] In summary, the College has the statutory authority to regulate the billings and collection practices of dentists.[111]

B. The Appeal Panel Erred in Holding that Dr. Jinnah's Statement of Account Failed to Clearly Identify Interest Charges and Provide a Detailed Explanation of the Dental Services to Which the Bill Related and Constituted Unprofessional Conduct

[78] This Court may set aside the appeal panel's decision[112] that Dr. Jinnah was guilty of unprofessional conduct – a question of mixed fact and law – if we are satisfied it is clearly wrong

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[110] *Re Rizzo & Rizzo Shoes Ltd*., [1998] 1 S.C.R. 27, 41 per Iacobucci, J. ("The words of an Act are to be read in their entire context"); *Estate of Hicklin v. Hicklin*, 2019 ABCA 136, ¶ 49; [2019] 6 W.W.R. 238, 255 ("an adjudicator interpreting a ... statute must read the whole ... statute"); *Attorney General v. Prince Ernest Augustus of Hanover*, [1957] A.C. 436, 463 (H.L.) per Viscount Simonds ("no one should profess to understand any part of a statute ... before he had read the whole of it"); *K & S Lake City Freighters Pty. Ltd. v. Gordon & Gotch Ltd*., [1985] HCA 48, ¶ 4; 157 C.L.R. 309, 315 per Mason, J. ("to read the section in isolation from the enactment of which it forms a part is to offend against the cardinal rule of statutory interpretation that requires the words of a statute to be read in their context"); *K Mart Corp. v. Cartier Inc*., 486 U.S. 281, 291 (1988) per Kennedy, J. ("In ascertaining the plain meaning of the statute, the court must look to the particular statutory language at issue, as well as the language and design of the statute as a whole") & *Panama Ref. Co. v. Ryan*, 293 U.S. 388, 439 (1935) per Cardozo, J. ("the meaning of a statute is to be looked for, not in any single section, but in all the parts together and in their relation to the end in view"). See also A. Scalia & B. Garner, Reading Law: The Interpretation of Legal Texts 167 (2012) ("Context is a primary determinant of meaning. A legal instrument typically contains many interrelated parts that make up the whole. The entirety of the document thus provides the context for each of its parts"); R. Sullivan, The Construction of Statutes 393 (7th ed. 2022) ("The context of a legislative provision includes both the whole of the Act in which the provision appears and also any related legislation that may cast light on the meaning or effect of the provision") & D. Pearce, Statutory Interpretation in Australia 136-37 (9th ed. 2019) ("The starting point to the understanding of any document is that it must be read in its entirety. ... It is often tempting to look only at the section that seems immediately applicable to the problem in hand. However, this is as likely to lead to a misconception of the total effect of the provision as is the reading of a passage of a novel out of context").

[111] See *Al-Ghamdi v. College of Physicians and Surgeons of Alberta*, 2020 ABCA 71, ¶ 17; 6 Alta. L.R. 7th 42, 51-52, leave to appeal ref'd, [2020] S.C.C.A. No. 272 ("The appellant is correct in arguing that 'unprofessional conduct' must be situated within the definition in the *Health Professions Act*. That definition, however, is cast at a conceptual level; it does not purport to list in detail all acts or omissions that would constitute unprofessional conduct... the reference to harm to the integrity of the profession is intended to be very wide-ranging") & *Zuk v. Alberta Dental Ass'n and College*, 2018 ABCA 270, ¶ 125; 426 D.L.R. 4th 496, 534, leave to appeal ref'd, [2018] S.C.C.A. No. 439 ("conduct 'that harms the integrity of the regulated profession', should...be read broadly enough to ensure conduct that contravenes ethical standards and professionalism is disciplinable, even if the conduct is not caught under other definitions of 'unprofessional conduct'").

[112] The role of a statutory delegate in a structure featuring more than one delegate is determined by the architecture adopted in the enactment creating the structure. This is a question of statutory interpretation. *Moffat v. Edmonton*

– a palpable and overriding error – or a product of an error of law or a finding of fact that is clearly wrong.[113]

[79] We are satisfied that the appeal panel erred when it held that Dr. Jinnah's failure to generate bills that expressly described the charges for $9.63, $9.84, $10.06 and $10.27 as interest instead of "office charges" constituted unprofessional conduct.[114]

Police Service, 2021 ABCA 183, ¶ 128 per Wakeling, J.A. ("A legislature that creates more than one statutory delegate may establish in whatever detail it considers appropriate the role each statutory delegate plays, including the degree of autonomy of the appeal tribunal. For example, the *Health Professions Act* contains a comprehensive code setting out the precise responsibilities of three statutory delegates – the complaint review committee, the hearing tribunal, and the council of the college – relating to questions of fact, law, and mixed fact and law. In essence, each statutory delegate is authorized to independently determine the facts and answer questions of law and mixed fact and law, as it sees fit. Under this structure, standard of review is not a controversial question"). Other acts adopt a similar structure. See *Harelkin v. University of Regina*, [1979] 2 S.C.R. 561, 590-91 per Beetz, J. ("One should ... expect that ... an appeal [from a university council committee to the senate committee] is more likely to take a form resembling that of a trial *de novo* than that of a 'pure' appeal. There are three main reasons for this. First, nothing in the Act nor in the new by-laws indicates that the council committee's record shall be transferred to the senate committee on an appeal from a council committee decision. Second, university bodies like the Faculty of Social Studies and the council are not courts of records. Such records as they keep ... ordinarily consist of terse minutes, bare resolutions and concise documents. ... The third reason why an 'appeal' within a university should not be given a restricted or technical meaning flows from the fact that the members of a university appeal committee are not usually trained in the law. ... [T]hey would be almost irresistibly inclined to 're-try' the case ... . This inclination is so strong that professional appellate courts sometimes find it difficult to resist. It would be more realistic to expect that a body of laymen would abide by technically less strict standards than a professional court of appeal"). Some statutes do not. See *Newton v. Criminal Trial Lawyers' Ass'n*, 2010 ABCA 399, ¶ 84; 14 Admin. L.R. 5th 181, 210, per Slatter, J.A. ("The [Law Enforcement Review] Board should proceed primarily from the record created by the hearing before the presiding officer. It should extend deference to the decision of the presiding officer on questions of fact, credibility, and technical policing issues") & *Moffat v. Edmonton Police Service*, 2019 ABLERB 29, ¶ 37 ("as the Presiding Officer was the decision maker of first instance, we owe deference to his assessment of each witness's testimony and credibility").

[113] *Law Society of Saskatchewan v. Abrametz*, 2022 SCC 29, ¶ 29 per Rowe, J. ("This case is a statutory appeal pursuant to *The Legal Profession Act, 1990*. Therefore, the standard of review is correctness for questions of law and palpable and overriding error for questions of fact and of mixed fact and law") & *Minister of Citizenship and Immigration v. Vavilov*, 2019 SCC 65, ¶ 37; [2019] 4 S.C.R. 653, 703 per Wagner C.J., Moldaver, Gascon, Côté, Brown, Rowe & Martin, JJ. ("where the legislature has provided for an appeal from an administrative decision to a court, a court hearing such an appeal is to apply appellate standards of review ... . Where, for example, a court is hearing an appeal from an administrative decision, it would, in considering questions of law, including questions of statutory interpretation and those concerning the scope of a decision maker's authority, apply the standard of correctness in accordance with *Housen v. Nikolaisen* ... . Where the scope of the statutory appeal includes questions of fact, the appellate standard of review for those questions is palpable and overriding error (as it is for questions of mixed fact and law where the legal principle is not readily extricable)").

[114] Appeal Panel Decision, ¶¶ 51 & 54, Appeal Record 73-74.

[80] The patient knew that these were interest charges. This is incontestable. She said as much in her March 9, 2015 letter to the College.[115] It must not be forgotten that the patient signed an agreement that obliged her to pay interest on unpaid accounts.[116] When the patient spoke with a staff member in Dr. Jinnah's office on April 10, 2015 she clearly stated that she would not pay interest that accrued after the November 28, 2014 account.[117] She asserted that if Dr. Jinnah's office had responded in a timely manner to her November 2014 request for information, she would have promptly paid the account and no more interest would have accrued. And the patient expressly acknowledged in her June 25, 2015 letter to the College that the "office charge" represents "charges for interest"[118].

[81] We are also satisfied that the College has failed to prove on a balance of probabilities that Dr. Jinnah's patient did not receive the May 12, 2014 invoice that Dr. Jinnah referred to in her April 22, 2015 email to her patient.[119] It is likely that she did given that the sole entry in the November 28, 2014 statement was "Balance Forward". The patient, in effect, admitted that she may have received a prior statement from Dr. Jinnah's office. If she had, it must have been the May 12, 2014 invoice. Dr. Jinnah's records indicates that her office printed the May 12, 2014 invoice.[120] Also relevant is the fact that the five other accounts Dr. Jinnah's office printed made it into the patient's hands. So is the fact that Dr. Jinnah's April 22, 2015 email expressly claimed that "[y]ou were ... sent statements May 12/14, Nov 28/14, Dec 9/14, Jan 28/15, Mar 2/15 and Apr 1/15".[121] Given that the patient received five other invoices that Dr. Jinnah's office printed the likelihood Dr. Jinnah's office did not forward the May 12, 2014 invoice to her is extremely low.

[82] This means that the "Balance Forward" entry in the November 28, 2014 account must be read with the information in the earlier account. And when it is, the charge of inadequate information is met head on. The May 12, 2014 account provides a detailed explanation of the dental services for which Dr. Jinnah seeks payment.

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[115] Respondent's Extracts of Key Evidence 8.

[116] The patient promised to pay interest on an overdue account and an "administration fee" of 50% of the outstanding account if she failed to pay her account within three months and Dr. Jinnah retained a collection agency to collect the outstanding account. Respondent's Extracts of Key Evidence 33.

[117] Transcript 45: 20-25, Appeal Record 146 & Respondent's Extracts of Key Evidence 11.

[118] Respondent's Extracts of Key Evidence 53 & 56.

[119] Id. 16.

[120] Id. 35.

[121] Id. 16.

[83] As a result, we find it is more likely than not that Dr. Jinnah provided her patient with an adequate explanation of the dental services for which Dr. Jinnah billed her – the May 12, 2014 invoice.[122]

C. The Appeal Panel Erred in Holding that the Tone and Content of the April 1, 2015 Final Notice Constituted Unprofessional Conduct

[84] We have reviewed Dr. Jinnah's April 1, 2015 "Final Notice" line by line and see no basis for the criticism that both the hearing tribunal and the appeal panel have directed at it.

[85] Informing a patient whose account is outstanding that the patient must either pay the sum due or contact Dr. Jinnah's office to discuss payment options is appropriate.

[86] So is a clear message from the creditor that failure to take either of these two steps may cause Dr. Jinnah to retain a collection agency to collect the amount due. This should not be a surprise to the patient. She signed a financial agreement that contained this provision:[123] "If your account remains unpaid after three months, it will be turned over to a collection agency including outstanding interest, plus an additional charge of 50% (administration fee for being sent to the collection agency) which will be added to your balance". And informing the patient that a collection agency is the next step is in line with the College's own guidance to its members for collecting overdue accounts[124] of which the hearing tribunal appears to have been unaware.[125]

[87] There is nothing objectionable about informing the patient that Dr. Jinnah's use of a collection agency may damage the patient's credit rating. This is true. And if it is information that a patient does not know, it is a fact the patient needs to know in deciding how to deal with a debt. These observations are sound even though some patients may find information of this nature threatening.

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[122] Id. 22 & 35.

[123] Id. 33.

[124] Alberta Dental Association and College, Practice Management Manual 64-65 (2003) ("Step 6: Follow up with a final letter as shown in Figure 15. This letter informs the patient of their extreme delinquency and of the action that you plan to take. ... Figure 15: '... On the advice of our attorney, we intend to turn this account over for collection unless we have payment in full by _____.' ... Step 7: Follow up with a collection agency or legal action") (emphasis omitted).

[125] Transcript 262:23-263:2 ("Ms. Brook [Hearing Tribunal Member]: Ms. Gagnon, [d]oes the College have any standards for collection activities? Now, that may have been mentioned in passing. I just want to make sure that I understand this. Ms. Gagnon [legal counsel for the Alberta Dental Association and College]: No, there are no standards in place for collections"). Appeal Record 363-64.

[88] Nor is there anything improper about informing the patient that if Dr. Jinnah is forced to sue to collect the unpaid account, the patient may be on the hook for Dr. Jinnah's legal costs.

[89] In any case, neither the Complaints Director,[126] the hearing tribunal,[127] nor the appeal panel[128] took issue with a dentist sending an account to a collection agency – rather, it seems that what they considered problematic was the tone of Dr. Jinnah's communications informing the patient of this fact. But Dr. Jinnah's April 1, 2015 "Final Notice" is not so different from the sample letter included in the College's draft final-notice letter in its Practice Manual.[129]

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[126] Hearing Tribunal Decision, ¶¶ 82-83, Appeal Record 28 ("Ms. Gagnon clarified that the Complaints Director does not take issue with a dentist sending an account to collections. However, dentistry is a health care profession, so collection practices must be reviewed in the context of members of the dental profession providing services for a fee and members of the public receiving services from a health care professional on the basis that a professional fee will be recovered. The collection practices of banks and payday loans should not be considered. There are four appropriate collection practices: (1) attempting to internally collect an account (e.g. reminders to a patient, phone calls); (2) starting legal action; (3) sending the account to a collection agency; and (4) writing it off, but only after attempting to collect the amount in accordance with a dentist's obligations under Article B5.1 Dental Plans and Third Party Carriers of the Code of Ethics. The tone of those communications has to be scrutinized, but certainty a dental practice is entitled to take steps to have their accounts paid").

[127] Id. ¶ 127-28, Appeal Record 39 ("Dentistry is a health care profession and as health care professionals, dentists must not be seen to threaten patients or be confrontational in written communications to patients. ... Dr. Jinnah's written communication to S.M. (Final Notice letter and email of April 22, 2015) used threatening language such that the patient felt bullied, upset, threatened by legal action and threated that her credit rating would be discredited. S.M. also thought she would be responsible for Dr. Jinnah's legal costs and the administration fees. This is not how a patient should be made to feel when they are making inquiries to get more information to have their account balance resolved and there are delays in the patient getting this information. Moreover, the Hearing Tribunal finds that the tone in the written correspondence was not what the Hearing Tribunal, members of the dental profession and members of the public receiving services from a health care professional would expect. As a result of the above, the Hearing Tribunal finds that the collection practices were not acceptable in the circumstance").

[128] Appeal Panel Decision ¶¶ 79-80, Appeal Record 80 ("It is clear that the Hearing Tribunal did not agree with Mr. Renouf's description of the Final Notice/Demand letter as 'professional if not polite.' In the opinion of the Appeal Panel, it was open to the Hearing Tribunal to conclude that the tone and content of the Final Notice to a patient was unprofessional and this conclusion was not unreasonable in the circumstance").

[129] Alberta Dental Association and College, Practice Management Manual at 64-65 (2003) ("Sample letter for accounts 61-90 days overdue 'Dear _____, Your account with this office is seriously overdue. We have contacted you on _____ and _____ by letter and on _____ and _____ by telephone. Each time, you agreed to pay and did not. On the advice of our attorney, we intend to turn this account over for collection unless we have payment in full by _____. Please contact my office immediately at 555-1212 to discuss this matter with our financial secretary. Regards, Dr. _____D.D.S.'") & Letter from Dr. Jinnah to patient dated April 1, 2015 ("This is your final notice concerning your past due account. Because you have not contacted Smilemakers Dental Centre to discuss options for payment or to set up a payment plan, we must take further action. A great deal of time, effort and cost In attempting to work out arrangements for payment of your account has been invested. At this time, we must, therefore, insist that payment or contact be made immediately to discuss acceptable options available to you if you are having difficulties paying off your balance. Please accept responsibility for this obligation. Smilemakers Dental Centre would prefer not to resort to a professional agency to collect what you owe, however, it is prepared to do so. I know this will damage your credit rating. Please do not force us to take extreme measures to obtain payment. ... This being your final notice, before

[90] While some patients may characterize the tone of the "Final Notice" as aggressive, one must not overlook the fact that it is designed to cause a patient-debtor to pay an outstanding account. It is, after all, a business letter – from a creditor to a debtor.

[91] One part of the "Final Notice" is questionable. Dr. Jinnah incorrectly described the additional charge as a 100% upward adjustment. The financial agreement set the upward adjustment at fifty percent. But Dr. Jinnah corrected this error in her April 22, 2015 email to her patient:[130] "Unfortunately, your account is now in arrears and we have no choice but to forward the account to a third party collection agency. As per your signed financial policy (attached). You will note the additional administration fee of 50% to be added to your balance". A mistake of this nature, although unfortunate and the product of carelessness, is not unprofessional conduct.[131]

D. The Appeal Panel Erred in Holding that the Term in the Financial Agreement Adjusting the Outstanding Balance by Fifty Percent Under Stipulated Conditions Constituted Unprofessional Conduct

[92] The appeal panel agreed with the hearing tribunal that Dr. Jinnah committed unprofessional conduct when she asked her patient to agree to a term that increased the amount outstanding by fifty percent if the patient failed to pay her bill within three months and Dr. Jinnah turned the account over to a collection agency.

[93] The appeal panel also agreed with the hearing tribunal's reasons, the key part of which follows: "Dr. Jinnah's 50% administration fee carried with it an implied threat [adversely affect a patient's credit score] that is incongruent with a dentist-patient relationship".[132]

[94] We disagree with the appeal panel on both points.

[95] Dealing with the latter conclusion first, the contested contract provision does nothing more than allow for an upward adjustment of the amount outstanding if the patient does not pay as promised and Dr. Jinnah retains a collection agency so that the collection agency's fee is passed on to the patient and not borne by Dr. Jinnah. The provision does not threaten the patient, either expressly or implicitly.

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initiating third party collection procedures please govern yourself accordingly and immediately begin steps to repay your entire outstanding balance. Please call our office immediately to resolve this matter"). Respondent's Extracts of Key Evidence 13.

[130] Respondent's Extracts of Key Evidence 16.

[131] We also note that the April 22, 2015 email strongly suggests that Dr. Jinnah had no idea a staff member had spoken with her patient on April 10 and that the patient promised to pay the outstanding account on receipt of the detailed statement of services provided.

[132] Appeal Panel Decision ¶ 110, Appeal Record 85.

[96] Second, the disputed contract term is not inconsistent with the common law.

[97] Commercial contracts often impose on a defaulting promisor the obligation to pay the legal costs the promisee incurs to enforce compliance on the part of the promisor.

[98] Here is an example of such a term in a residential mortgage:[133]

> 14. I also covenant and agree with the mortgagee that
>
> ...
>
> (e) All solicitor's ... fees and expenses ... in exercising or enforcing or attempting to enforce or in pursuance of any right, power, remedy or purpose hereunder ..., and legal costs as between solicitor and client are to be secured hereby and shall be a charge on the mortgaged premises, together with interest thereon ... and all such moneys shall be repayable to, the Mortgagee on demand ... and all such sums together with interest thereon are included in the expression 'the mortgage moneys'.

[99] We also reject as irrelevant the evidence of a chartered accountant "that he … never … [came] across a collection practice … where the account is doubled before being sent to a collection agency"[134] or the experience of the professional members of the hearing tribunal to the same effect.

[100] There is no provision in the Code of Ethics that states a dentist may adopt only "usual and customary business practices" when pursuing delinquent debtor-patients. While Article B5.1 of the Code of Ethics incorporates that language it does so in a different context. Article B5.1 focuses on dental plans with third party carriers and directs a dentist to "engage in usual and customary business practices to collect such co-payments from the patient". This is a minimum standard that a dentist who has received a payment from an insurer must meet to discharge his or her ethical

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[133] This provision was enforced in *Central Mortgage and Housing Corp. v. Conaty*, 61 D.L.R. 2d 97 (Alta. Sup. Ct. App. Div. 1967). See also id. 105 per Allen, J.A. ("I must … hold that in an action against the original mortgagor the mortgagee in this case would have been entitled to *add* to the amount secured by the mortgage, fair and reasonable legal costs incurred by him as between solicitor and client in exercising or enforcing or attempting to enforce his rights under the mortgage and in connection with collection of mortgage arrears, and it is admitted that the solicitor and client charges involved in this matter were so incurred and are fair and reasonable") (emphasis added); *Canada Deposit Ins. Corp. v. Canadian Commercial Bank*, 1989 ABCA 150, ¶ 19; 61 D.L.R. 4th 161, 170 ("Solicitor-client costs … have frequently been ordered in Alberta foreclosure actions, as a matter of course, in accordance with the contract between the parties"); *Re Griffith, Jones and Co*., 50 L.T.R. 434, 434 (C.A. 1883) ("a mortgagor must pay all the costs of the mortgagee including those payable by the latter to his solicitor") & *Credit Foncier Trust Co. v. Hornigold*, 59 A.R. 103, 106; 35 Alta. L.R. 2d 341, 345-36 (Q.B. 1984) ("Contractual provisions entitling the mortgagee to … total indemnification … have been held valid in this jurisdiction and elsewhere").

[134] Hearing Tribunal Decision, ¶ 52 & Transcript 101:11-15, Appeal Record 22 & 202. The financial agreement contained a 50% upward adjustment. This does not result in a two-fold increase of the outstanding balance.

obligations. Article B5.1 does not prohibit a dentist from adopting more aggressive collection methods.

[101] Suppose a charity operates a lemonade stand and advertises that the charge for a glass of lemonade is not less than $5. This does not prevent a consumer and donor from giving the charity $100 for a glass of lemonade. The $5 reference is a minimum charge and not a statement that the charity will refuse larger donations.

[102] The correct inquiry is whether Dr. Jinnah's stipulated-consequence-on-breach term is oppressive.[135] A stipulated-consequence-on-breach term is oppressive if it is "so manifestly grossly one-sided that its enforcement would bring the administration of justice into disrepute".[136] In making this determination an adjudicator must be mindful of the well-known fact that dentists are not in short supply, like family doctors are, and that a patient who does not like the business terms a dentist proposes can easily seek out another service provider. This is not a case of inequality of

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[135] *Elsley v. J.G. Collins Ins. Agencies Ltd*., [1978] 2 S.C.R. 916, 937 ("the power to strike down a penalty clause is a blatant interference with freedom of contract and is designed for the sole purpose of providing relief against oppression for the party having to pay the stipulated sum. It has no place where there is no oppression"). Canadian courts regularly enforce stipulated-consequence-on-breach terms that are not oppressive. E.g., *RCAP Leasing Inc. v. Martin*, 2016 ABQB 542; 62 B.L.R. 5th 336 (Master) (the Master refused to enforce an administrative fee payable on the lessee's default in an equipment lease agreement because it was unconscionable and oppressive); *City of Edmonton v. Triple Five Corp.*, 158 A.R. 293 (Q.B. 1994) (the Court enforced a term allowing the City to draw on a letter of credit because the term was not oppressive); *Prudential Ins. Co. of America v. Cedar Hills Properties Ltd.*, [1995] 3 W.W.R. 360, 369-70 (B.C.C.A. 1994) (the Court enforced a $100,000 interest-rate-standby fee in a $6.4 million commercial loan agreement because it was not oppressive); *Bankers Mortgage Corp. v. Plaza 500 Hotels Ltd.*, 2016 BCSC 722; 65 R.P.R. 5th 120, aff'd, 2017 BCCA 66 (the Court enforced a $96,000 exit fee in a loan agreement on the basis that it was not an unenforceable penalty); *Volvo Truck Finance Canada Ltd. v. Premier Pacific Holdings Inc.*, 2002 BCSC 1137; 29 B.L.R. 3d 213 (the Court enforced an interests-escalation-on-default term in a commercial contract because the promissor had not demonstrated that it was oppressive) & *Wolfe Chevrolet Oldsmobile Ltd. v. 552234 B.C. Ltd.*, 2004 BCPC 154; 49 B.L.R. 3d 247 (the Court enforced a term in a vehicle-sale agreement that obliged the purchaser to pay the vendor $5,000 if the purchaser resold the vehicle in the United States).

[136] *Capital Steel Inc. v. Chandos Construction Ltd.*, 2019 ABCA 32, ¶ 106; 438 D.L.R. 4th 195, 241, majority aff'd, 2020 SCC 25, per Wakeling, J.A. This is the test used to identify unenforceable terms in commercial contracts between entities that have sufficient resources to retain counsel. There is no inequality in bargaining power. Courts will seldom conclude that a stipulated-consequence-on-breach term in a commercial contract between parties with sufficient resources to retain counsel is oppressive. Id. at ¶ 108, 438 D.L.R. 4th at 241. "The oppression concept may be engaged more frequently in consumer contracts. A less demanding standard for oppression in consumer contracts – rental-car, parking, credit-card and utility adhesion contracts and perhaps also increasingly online contracts of adhesion, such as Facebook's 'terms of use' – may be appropriate. In these situations a dominant party provides a service or a product to a large number of consumers who are not in a position to extract any concessions from the service or product provider. If the consumer wishes to acquire the services or the product provided by the dominant party, it will be only on the terms stipulated by the dominant party". Id. at ¶ 109, 438 D.L.R. 4th at 241. It is not accurate to characterize a dentist as the dominant party in the dentist-patient relationship. There are hundreds of dentists who are potential service providers. A patient who does not like the terms one dentist proposes can seek out another service provider. It is safe to say that the oppression concept may not be engaged in cases like this as frequently as in contracts of adhesion.

bargaining power [137] that is a component of the "unconscionability" equitable doctrine incorporating the "improvident bargain" concept.[138]

[103] If a term is oppressive, a court will not enforce it. If it is not, a court will enforce it.

[104] We are satisfied that a dentist who asks a patient to agree to an oppressive provision engages in conduct that harms the integrity of the profession and is unprofessional conduct. And we are also of the view that a dentist who asks a patient to agree to a term that is not oppressive is not guilty of unprofessional conduct.

[105] The complaints director has not led any evidence[139] that supports the conclusion that the contested term in Dr. Jinnah's financial agreement is oppressive – it is "so manifestly grossly one-sided that its enforcement would bring the administration of justice into disrepute".[140] The evidence before the hearing tribunal supports the opposite conclusion. Dr. Jinnah's evidence is that collection agencies charge her a fee and that the contested provision allows her to pass this cost on to her patient.[141]

[106] This term is not "manifestly grossly one-sided".

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[137] *Uber Technologies Inc. v. Heller*, 2020 SCC 16, ¶¶ 66 & 74 per Abella & Rowe, JJ. ("An inequality of bargaining power exists when one party cannot adequately protect their interests in the contracting process. …. A bargain is improvident if it unduly advantages the stronger party or unduly disadvantages the more vulnerable").

[138] A term may be an "improvident bargain" but not be "so manifestly one-sided and grossly unfair that its enforcement would bring the administration of justice into disrepute". In other words, it is easier to establish that a term is an "improvident bargain" as opposed to "oppressive" – "so manifestly one-sided and grossly unfair that its administration would bring the administration of justice into disrepute".

[139] See *Capital Steel Inc. v. Chandos Construction Ltd.*, 2019 ABCA 32, ¶ 110; 438 D.L.R. 4th 195, 241 majority aff'd, 2020 SCC 25, per Wakeling, J.A. ("A promisor that asks to be relieved of a burden that it promised to discharge bears the legal burden of establishing the facts it relies on to support its oppression claim"); *Mortgage Makers Inc. v. McKeen*, 2009 NBCA 61, ¶ 47; 312 D.L.R. 4th 82, 104 per Robertson, J.A. ("At common law the onus is on the defendant to establish that the clause is not a genuine pre-estimate of damages") & *Robophone Facilities Ltd. v. Blank*, [1966] 3 All E.R. 128, 142 (C.A.) per Diplock, L.J. ("The onus of showing that such a stipulation is a 'penalty clause' lies on the party who is sued on it").

[140] *Capital Steel Inc. v. Chandos Construction Ltd.*, 2019 ABCA 32, ¶ 106; 438 D.L.R. 4th 195, 241, majority aff'd, 2020 SCC 25 per Wakeling, J.A.

[141] Transcript 142:27 - 143:1-3; Appeal Record 243-244. Collection agencies, most certainly, will charge customers who use their services infrequently to collect a very small sum a significant portion of any sum ultimately secured.

[107] Nor is it an improvident bargain,[142] the test applied if there is unequal bargaining power between the promisor and the promisee.[143] It does not unduly disadvantage Dr. Jinnah's patient. It does nothing more than pass on the costs a collection agency imposes on Dr. Jinnah to her debtor-patient. A debtor-patient cannot reasonably complain about being asked to pay a reasonable cost that never would have been incurred if the debtor had paid the account in a timely manner.

[108] The appeal panel's determination that Dr. Jinnah has violated the *Health Professions Act* by asking her patient to agree to the contested term must be set aside.

E. The Appeal Panel Did Not Err in Holding that Dr. Jinnah Obstructed the Complaint Process

[109] A regulated member obstructs the complaint process under the *Health Professions Act*[144] if he or she acts in a manner that would, objectively assessed,[145] cause a patient with backbone to consider withdrawing a complaint already filed or, if not filed, not proceeding with a complaint under consideration.[146]

[110] The appeal panel did get it right when it held that Dr. Jinnah's April 22, 2015 email to her patient constituted unprofessional conduct:[147]

> [T]he concern of the Hearing Tribunal regarding Dr. Jinnah threatening an action in defamation against a patient for making a complaint to the … [College] was valid. The right of patients to file a complaint against a dentist that is then investigated by the … [College] is a fundamental aspect of the role of the … [College] as part of a self-regulating profession that acts to protect the public

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[142] *Uber Technologies Inc. v. Heller*, 2020 SCC 16, ¶ 74 per Abella & Rowe, JJ. ("A bargain is improvident if it unduly advantages the stronger party or unduly disadvantages the more vulnerable").

[143] Id. ¶ 54 ("Unconscionability is an equitable doctrine that is used to set aside 'unfair agreements [that] resulted from an inequality of bargaining power'").

[144] R.S.A. 2000, c H-7.

[145] *Lane v. Registrar of the Supreme Court of New South Wales*, [1981] HCA 35, ¶ 10; 148 C.L.R. 245, 258 per Gibbs, C.J. & Mason, Murphy, Wilson & Brennan, JJ. ("An intention to interfere with the administration of justice is not necessary to constitute a contempt; the critical question is whether the act is likely to have that effect, but the intention with which the act was done is relevant and sometimes important") & *Attorney General v. Butterworth*, [1963] 1 Q.B. 696, 726 (C.A. 1962) per Donovan, L.J. ("an intention to interfere with the proper administration of justice is not an essential ingredient of the offence of contempt of court. It is enough if the action complained of is inherently likely so to interfere").

[146] *Attorney-General v. Butterworth*, [1963] 1 Q.B. 696, 719 (C.A. 1962) per Lord Denning, M.R. ("there can be no greater contempt than to intimidate a witness before he gives his evidence or to victimize him afterwards for having given it. How can we expect a witness to give his evidence freely and frankly, as he ought to do, if he is liable, as soon as the case is over, to be punished for it by those who dislike the evidence he has given?").

[147] Appeal Panel Decision ¶ 88, Appeal Record 81.

> interest. All dentists must respect this right of a patient and conduct that attempts to discourage or threaten a patient for … [filing] a complaint breaches the conduct required of [a] dentist.

[111] From our perspective, this email, read objectively, would cause a patient with backbone to consider withdrawing a complaint already filed or not filing a complaint that he or she is contemplating filing. The likelihood that a patient who is told he or she will be sued by the subject of a filed complaint or a potential complaint[148] will consider altering course is not insignificant.

[112] This is an objective test. The fact that a patient does not change or does change course after receiving a message from a dentist is not determinative. A patient who stays the course may have a backbone of steel. This does not preclude an adjudicator from holding that a challenged message is unprofessional conduct. A patient who alters course may not be strong-willed. This does not stop an adjudicator from bestowing its stamp of approval on a contested message. What is critical is the anticipated reaction of the hypothetical reasonable patient.

[113] A dentist whose conduct assessed objectively discourages a patient from making a complaint to the College or pursuing an existing complaint frustrates the effective implementation of a valuable protocol designed to enhance the quality of the interaction between dentists and consumers of dental services.

[114] Obstructing the complaint process is conduct that harms the integrity of the profession and therefore constitutes unprofessional conduct.[149] This Court concluded that the College's finding that a dentist's demands that certain members of the Alberta Society of Orthodontists withdraw their complaints against him, accompanied by threats to make professional disciplinary complaints against a large number of the Society's members, harmed the integrity of the profession was reasonable.[150]

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[148] Respondent's Extracts of Key Evidence 16 ("Any costs incurred in my retaining a lawyer in a situation where it is deemed that the accusations are false or there is any concern of defamation of character will then rest with yourself"). See *The Queen v. Kellett*, [1976] Q.B. 372, 391 (C.A. 1975) per Stephenson, L.J. ("the exercise of a legal right or the threat of exercising it does not excuse interfering with the administration of justice by deterring a witness from giving the evidence which he wishes to give before he has given it. ... In *Shaw v. Shaw*, (1862) 6 L.T. 477 the respondent to a divorce suit called on a former servant and threatened her with prosecution for perjury if she gave evidence of his cruelty to his wife. The Judge Ordinary found that the respondent went with the intention of intimidating the servant and preventing her from giving evidence ... . [E]ven if the servant's evidence had been false and the respondent had believed that she might be prosecuted for perjury after giving it, the threatening language he used would ... have been enough to convict him of the attempt").

[149] *Zuk v. Alberta Dental Ass'n and College*, 2018 ABCA 270; 426 D.L.R. 4th 496, leave to appeal ref'd, [2018] S.C.C.A. No. 439.

[150] Id. at ¶¶ 161-67; 426 D.L.R. 4th at 540-41.

[115] The primary goal of the College is to protect the public.[151] The existence of an effective complaint process is a crucial part of maintaining the integrity of the profession, and therefore protecting the public. Protecting the complaint process is an important part of the College's obligation to ensure that professional standards of conduct are complied with.

[116] Criminal law systems generally make it an offence to obstruct the truth-seeking function of adjudicators. For example, section 139(3)(a) of the Canadian *Criminal Code*[152] provides that "every one shall be deemed wilfully to attempt to obstruct, pervert or defeat the course of justice who in a judicial proceeding, existing or proposed, … dissuades or attempts to dissuade a person by threats, bribes or other corrupt means from giving evidence".

[117] Similar prohibitions exist in labor legislation to reduce the risk that employers or trade unions penalize their employees or members for invoking a legal process that is intended to protect

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[151] *Health Professions Act*, R.S.A. 2000, c. H-7, s. 3(1)(a) ("A college must carry out its activities and govern its regulated members in a manner that protects and serves the public interest"). See *Brown v. Alberta Dental Ass'n*, 2002 ABCA 24, ¶ 30; 299 A.R. 60, 69 ("The paramount objective of any professional act is the protection of the public, which is achieved through the establishment of a self-regulating profession charged with that responsibility") & *Farooq v. Alberta College of Pharmacists*, 2010 ABCA 306, ¶ 46; 499 A.R. 223, 233, leave to appeal ref'd, [2010] S.C.C.A. No. 477 ("The primary purpose of the complaints process is public protection").

[152] R.S.C. 1985, c C-46. See *The Queen v. Pare*, 2010 ONCA 563, ¶ 9; 268 O.A.C. 118, 122 per Rosenberg, J.A. ("The gist of the offence [*Criminal Code*, s. 139(3)(a)] is the use of corrupt means to influence a witness. ... [M]erely attempting by reasoned argument to have a witness tell the truth is not an offence. But attempting to persuade a witness to change their testimony, even to change the testimony to what the witness believes is the truth, is an offence where the means of persuasion is corrupt. Offering money to a complainant in a criminal case to change her testimony is a classic example of corrupt means"). See also 18 U.S.C. § 1512 (a)(2) ("Whoever uses physical force or the threat of physical force against any person, or attempts to do so, with intent to – (A) influence, delay, or prevent the testimony of any person in an official proceeding; ... (C) hinder, delay, or prevent the communication to a law enforcement officer ... information relating to the commission or possible commission of a Federal offence or a violation of conditions of probation, supervised release, parole, or release pending judicial proceedings ... shall be punished as provided in paragraph (3)"); Cal. Penal Code § 136.1 (b) ("Except as provided in subdivision (c), every person who attempts to prevent or dissuade another person who has been the victim of a crime or who is a witness to a crime from doing any of the following is guilty of a public offence and shall be punished by imprisonment in a county jail for not more than one year or in the state prison: ... (2) Causing a complaint, indictment, information, probation or parole violation to be sought and prosecuted, and assisting in the prosecution thereof"); *Criminal Justice and Public Order Act 1994*, c. 33, s. 51(1) (U.K) ("A person commits an offence if – (a) he does an act which intimidates, and is intended to intimidate, another person ("the victim"), (b) he does the act knowing or believing that the victim is assisting in the investigation of an offence or is a witness or potential witness or a juror or potential juror in proceedings for an offence, and (c) he does it intending thereby to cause the investigation or the course of justice to be obstructed, perverted or interfered with"); *Crimes Act 1900*, No. 40, s. 315A(1) (New South Wales) ("A person who threatens to do or cause, or who does or causes, any injury or detriment to any other person intending to influence any person not to bring material information about an indictable offence to the attention of a police officer or other appropriate authority is liable to imprisonment for 7 years") & *Crimes Act 1961*, No. 43, s. 117(a) (New Zealand) ("Corrupting juries and witnesses: Every one is liable to imprisonment for a term not exceeding 7 years who ... dissuades or attempts to dissuade a person, by threats, bribes, or other corrupt means, from giving evidence in any cause or matter (whether civil or criminal, and whether tried or to be tried in New Zealand or in an overseas jurisdiction").

their interests. Section 94(3)(e)(iii) of the *Canada Labour Code*[153] stipulates that "[n]o employer … shall … seek, by intimidation, threat of dismissal or any other kind of threat, by the imposition of a financial or other penalty or by any other means, … to refrain from … making an application or filing a complaint under this Part."

[118] In coming to the conclusion that Dr. Jinnah's April 22, 2015 email contained passages that amounted to unprofessional conduct, we are not asserting that Dr. Jinnah sent it to her patient knowing it was wrong to do so. There is no reason to imply this. First, no provision in the Code of Ethics or the *Health Professions Act* [154] warns dentists of the need to be careful when communicating with patients who have filed or might file a complaint. Second, we do not think that the point would be so obvious to a lay person that a reasonably well-informed dentist should have this knowledge – should know that a dentist-creditor cannot warn a patient-debtor who has filed a complaint that the dentist will sue if the patient defames him or her in the course of the complaint process. In other words, in the dental practice environment that existed before the release of the appeal panel's decision and this Court's judgment, a dentist whose knowledge bank does not contain this information is not, on this account, *per se* culpable.[155]

[119] This determination requires us to consider whether the absence of an intention to contravene the Code of Ethics or the *Health Professions Act*[156] is inconsistent with a finding that Dr. Jinnah has committed unprofessional conduct and should result in a dismissal of the charge against her[157] or whether its effect should be confined to the sanction.[158]

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[153] R.S.C. 1985, c L-2. See also *Labour Relations Code*, R.S.A. 2000, c. L-1, s. 149(1) ("No employer ... shall ... refuse to employ or to continue to employ any person or discriminate against any person in regard to employment or any term or condition of employment because the person ... (vi) has made an application or filed a complaint under this Act").

[154] R.S.A. 2000, c H-7.

[155] R. Perkins, Criminal Law and Procedure 960 (4th ed. 1972) ("nothing could be more absurd than to suggest as a common sense conclusion, based on ordinary experience, that everyone knows all of the law").

[156] R.S.A. 2000, c. H-7.

[157] *The King v. Ross*, 84 C.C.C. 107, 110 (B.C. County Ct. 1944) (the Court allowed a conviction appeal by a hunter convicted of hunting in an area closed for hunting because an unpublished ministerial closure order was enacted while the hunter was in the closed area for the purpose of hunting: "I think it hardly compatible with justice that a person may be convicted and penalized, and perhaps lose his personal liberty …, for the violation of an order of which he had no knowledge or notice at any material time"). See G. Williams, Textbook of Criminal Law 452 (2d ed. 1983) ("What is the reason for the rule [that ignorance of the law is no excuse?] … [T]he orthodox answers are two. 1. The difficulty of proving that the defendant knew the law. 2. The risk that such a defence would make it advantageous for people to refrain deliberately from acquiring knowledge of their legal duties").

[158] *The King v. Bailey*, 168 Eng. Rep. 651, 653 (Cr. Cas. Res. 1800) (the Court recommended a pardon for a sea captain convicted of an offence created by legislation while he was sailing near the African coast).

[120] The best course is to give effect to this absence of an intention to contravene the Code of Ethics or the *Health Professions Act* when considering the appropriate sanction. Use of the unprofessional conduct concept is an effective didactic device to inform dentists that they must proceed with caution when communicating with a patient about a complaint. In our opinion, a contrary finding may harm the standing of the dental and other professionals in the community. Most people believe that ignorance of the law is no excuse. Professor Glanville Williams observed roughly forty years ago that "almost the only knowledge of the law possessed by some people is that ignorance of it is no excuse".[159] Professor Keedy opined over 100 years ago that "[*i*]*gnorantia juris non excusat, ignorantia facti excusat* is a maxim familiar to layman as well as to the lawyer".[160]

[121] In doing so, we follow the lead of the criminal law. Section 19 of the *Criminal Code*[161] declares that "[i]gnorance of the law by a person who commits an offence is not an excuse for committing that offence". But this provision does not preclude a finding that an actor who does not appreciate that a course of conduct is wrong or unlawful is less blameworthy than a person who does. For example, in *The Queen v. Campbell*,[162] Judge Kerans, then a judge of the District Court of Alberta, granted an absolute discharge to an exotic dancer who was convicted of giving an immoral performance because she did so in the belief nude dancing was lawful – a superior court judge had said so[163] – and could not reasonably predict this decision would be overturned on appeal.[164] It was asking too much of the young dancer to require her to have a better grasp of the law than a superior court judge.

[122] The appeal panel's decision to impose a reprimand as opposed to any other harsher sanction is consistent with our conclusion that Dr. Jinnah did not intend to contravene the *Health Professions Act*[165] or the Code of Ethics and her failure to know that obstruction of the complaint

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[159] G. Williams, Textbook of Criminal Law 405 (1978).

[160] "Ignorance and Mistake in the Criminal Law", 22 Harv. L. Rev. 75, 76 (1908).

[161] R.S.C. 1985, c. C-46.

[162] 10 C.C.C. 2d 26, 35-36 (Alta. Dist. Ct. 1972). This problem not infrequently arose when British values conflicted with the values of those whose lands were absorbed into the British Empire and subject to British laws. E.g., *The King v. Mukasa*, 11 E.A.C.A. 114, 115 (1944) per Sir John Gray, C.J. (the Court substantially reduced the penalties imposed on herders who had killed suspected foodstuff thieves because the community considered this justifiable: "The appellants are natives of Buganda … . [P]rior to the advent of British rule the killing of persons caught stealing food crops was held by the Buganda to be justifiable homicide. … [W]hilst the severe beating … cannot be justified and cannot be allowed to go unpunished, we are of the opinion that … the sentences are excessive") & *The King v. Chima*, 10 W.A.C.A. 223 (1944) (the Court acquitted a woman who killed her twins because she believed, as did other community members, that twins were the product of the union of the mother and evil spirits).

[163] *The Queen v. Johnson (No. 1)*, 6 C.C.C. 2d 462 (Alta. Sup. Ct. Tr. Div. 1972), rev'd, 8 C.C.C. 2d 1, rev'd, [1975] 2 S.C.R. 160.

[164] *The Queen v. Johnson*, 8 C.C.C. 2d 1 (Alta. Sup. Ct. App. Div. 1972), rev'd, [1975] 2 S.C.R. 160.

[165] R.S.A. 2000, c. H-7.

process was unprofessional conduct was not, by itself, culpable. In short, Dr. Jinnah's lack of knowledge about the impropriety of her April 22, 2015 email to her patient is not culpable. As a result, the seriousness of her unprofessional conduct is at the low end of the scale.

F. The Appeal Panel's Costs Order Was Unreasonable and Must Be Set Aside

[123] Dr. Jinnah argues that the costs the appeal panel imposed – the appeal panel reduced the $50,000 costs order issued by the hearing panel to $37,500[166] and ordered Dr. Jinnah to pay costs equal to one-quarter of the appeal panel costs[167] – were excessive for a hearing involving one allegation by a single patient unrelated to patient care on the low end of the seriousness scale.[168]

[124] We agree. These sums are so large that they, in effect, become the primary sanction. Costs are not supposed to be a sanction.

[125] Costs in a professional disciplinary context are discretionary and subject to the standard of reasonableness.[169]

[126] Sections 82(1)(j) and 89(6) of the *Health Professions Act*[170] set out a nonexhaustive list of expenses that a hearing tribunal or appeal panel may order a dentist who is found to have engaged in unprofessional conduct to pay. The dentist may be ordered to pay "all or part of the expenses of, costs of and fees related to the investigation or hearing or both".[171]

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[166] Appeal Panel Decision, ¶¶ 49-51, Appeal Record 93.

[167] Id. ¶ 157, Appeal Record 94.

[168] Appellant's Factum, ¶ 109.

[169] *Alsaadi v. Alberta College of Pharmacy*, 2021 ABCA 313, ¶ 16; 463 D.L.R. 4th 335, 348 per Watson & Slatter, JJ.A. ("Sanctions in professional disciplinary matters involve mixed questions of fact and law and engage the professional judgment of the governing bodies, and they are therefore reviewed for reasonableness. ... Decisions on the costs of hearings are also reviewed for reasonableness") & *K.C. v. College of Physical Therapists of Alberta*, 1999 ABCA 253, ¶ 94; [1999] 12 W.W.R. 339, 369 ("Costs awards of disciplinary bodies are subject to judicial review on a standard of reasonableness").

[170] *Health Professions Act*, R.S.A. 2000, c. H-7, ss. 82(1)(j) & 89(6). See Part V. of this judgment for the text of the provisions.

[171] Id. s. 82(1)(j). Legislation regulating health professions in British Columbia, Saskatchewan, Manitoba, Ontario, New Brunswick, Prince Edward Island, Nova Scotia, Newfoundland, Northwest Territories and Nunavut also allows costs awards against a disciplined professional to partially indemnify the regulatory body. *Health Professions Act*, R.S.B.C. 1996, c. 183, ss. 39(4)-(8); *The Medical Profession Act, 1981*, S.S. 1980-81, c. M-10.1, ss. 45(12)(g) & 54(1)(i); *The Regulated Health Professions Act*, C.C.S.M. c. R117, ss. 104(4) & 127(1)(a); *Regulated Health Professions Act*, S.O. 1991, c. 18, ss. 53 &53.1; *New Brunswick Dental Act, 1985*, S.N.B. 1985, c. 73, s. 48(1); *Regulated Health Professions Act*, R.S.P.E.I. 1988, c. R-10.1, s. 58(2)(g); *Discipline Regulations*, N.S. Reg. 3/2002, s. 29(1)(i) under *Dental Act*, S.N.S. 1992, c. 3; *Health Professions Act*, S.N.L. 2010, c. H-1.02, ss. 42(1)(e) & 43(2)(a) & (e) & *Dental Profession Act*, R.S.N.W.T. 1988, c. 33 (Supp), s. 64(2). However, unlike Alberta's *Health Professions Act* which does not confer jurisdiction to award costs to a professional who successfully defends allegations, British

1. The Purpose of Costs in the *Health Professions Act* Is Full or Partial Indemnification of the College in Appropriate Cases

[127] Both *K.C. v. College of Physical Therapists of Alberta*[172] and the text of sections 82(1) and 89(6) of the *Health Professions Act*[173] establish that the purpose of costs is to fully or partially indemnify the College for its costs and expenses. Costs are not to be punitive in nature.[174] Fines are punitive in nature. The College may fine a member to sanction him or her for unprofessional conduct.[175]

2. A Hearing Tribunal and an Appeal Board Must Justify a Decision To Impose Costs

[128] Costs should not be awarded in every case.[176] Statutory powers must not be confused with the manner in which they are to be exercised.[177]

[129] This Court in *K.C. v. College of Physical Therapists of Alberta*[178] held that the College must consider factors "in addition to success or failure" including "the seriousness of the charges, the

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Columbia's, Ontario's and Newfoundland's legislation allows a professional to recover costs from the disciplinary body if no professional misconduct is found. See *Health Professions Act*, R.S.B.C. 1996, c. 183, ss. 39(4)-(8); *Regulated Health Professions Act*, S.O. 1991, c. 18, ss. 53 &53.1 & *Health Professions Act*, S.N.L. 2010, c. H-1.02, s. 43(2)(a). British Columbia's College goes further and, as empowered under statute, prepared a tariff under which costs can range between $200 - $400 for investigations and $9,300 - $31,350 for hearings, depending on which items are applicable. *Health Professions Act*, R.S.B.C. 1996, c. 183, s. 19(1)(v.1) & (w.1) & Bylaws of the British Columbia College of Oral Health Professionals (September 1, 2022), Schedules I & H. The Northwest Territories, Nunavut and New Brunswick also allow the regulatory body to order a complainant to pay its costs where the complaint was unwarranted or an abuse of process. The former two jurisdictions limit to $2,000 the security for costs that a complainant may be required to pay and that could later be used towards costs. *Dental Profession Act*, R.S.N.W.T. 1988, c. 33 (Supp), s. 51; *Dental Profession Regulations*, R.R.N.W.T. 1990, c. 4 (Supp), s. 12 & *New Brunswick Dental Act, 1985*, S.N.B. 1985, c. 73, s. 48(1).

[172] *K.C. v. College of Physical Therapists of Alberta*, 1999 ABCA 253, ¶ 94; [1999] 12 W.W.R. 339, 369.

[173] *Health Professions Act*, R.S.A. 2000, c. H-7, ss. 82(1)(j), 89(6). See Part V. of this judgment for the text of the provisions.

[174] *K.C. v. College of Physical Therapists of Alberta*, 1999 ABCA 253, ¶ 94; [1999] 12 W.W.R. 339, 369 ("Costs are not a penalty, and should not be awarded on that basis").

[175] *Health Professions Act*, R.S.A. 2000, c. H-7, ss. 82(1)(k) & 158. See Part V. of this judgment for the text of the provisions.

[176] *K.C. v. College of Physical Therapists of Alberta*, 1999 ABCA 253, ¶ 94; [1999] 12 W.W.R. 339, 369.

[177] *Alsaadi v. Alberta College of Pharmacy*, 2021 ABCA 313, ¶ 119; 463 D.L.R. 4th 335, 375 per Khullar, J. (concurring), citing *H.L. v. Canada*, 2005 SCC 24, ¶ 88, [2005] 1 S.C.R. 401, 431.

[178] 1999 ABCA 253, ¶ 94; [1999] 12 W.W.R. 339, 369.

conduct of the parties and the reasonableness of the amounts" when determining whether to impose costs and in what amount.

[130] In *Alsaadi v. Alberta College of Pharmacy*,[179] Justice Khullar pointed to many of the problems with a default approach to calculating costs that often imposes a very high amount on a disciplined professional.[180] Justice Khullar favored a more principled approach to calculating costs:[181]

> A more deliberate approach to calculating the expenses that will be payable is necessary. Factors such as those described in *KC* should be kept in mind. A hearing tribunal should first consider whether a costs award is warranted at all. If so, then the next step is to consider how to calculate the amount. What expenses should be included? Should it be the full or partial amount of the included expenses? Is the final amount a reasonable number? In other words, a hearing tribunal should be considering all the factors set out in *KC*, in exercising its discretion whether to award costs, and on what basis. And of course, it should provide a justification for its decision.

3. Professions Should Bear Most, if Not All Costs Associated with the Privilege and Responsibility of Self-Regulation Unless a Member Has Committed Serious Unprofessional Conduct, Is a Serial Offender, Has Failed to Cooperate with Investigators or Has Engaged in Hearing

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[179] 2021 ABCA 313; 463 D.L.R. 4th 335.

[180] Id. at ¶ 108; 463 D.L.R. 4th at 373 ("The costs situation under *HPA* is unique. It is not like civil litigation where the successful party is presumptively entitled to costs ... . It is not like criminal law where, generally speaking, no costs are awarded and the state bears the cost for the investigation and the hearing, even when the state is successful. Rather, the *HPA* creates a scheme where only the professional is liable to pay costs, only the College can recover costs, and the quantum is potentially very high"). See *Pillar Resource Services Inc. v. PrimeWest Energy Inc*., 2017 ABCA 19; 96 C.P.C. 7th 1, per Wakeling, J.A. (concurring) for an overview of costs in the civil litigation context. For example, the prospect of a costs award on a full-indemnity basis may not discourage civil litigants with a defensible legal position given the rarity of such substantial awards. Id. at ¶¶ 113-15; 96 C.P.C. 7th at 46. However, it may have a much stronger deterrent effect on investigated professionals because the costs are often more severe than the sanctions imposed on the professional. See *Alsaadi v. Alberta College of Pharmacy*, 2021 ABCA 313, ¶ 114; 463 D.L.R. 4th 335, 374 per Khullar, J. (concurring).

[181] *Alsaadi v. Alberta College of Pharmacy*, 2021 ABCA 313, ¶ 120; 463 D.L.R. 4th 335, 375-76 per Khullar, J. (concurring).

Misconduct, in Which Case, the Disciplined Member Must Assume Some of the Costs

[131] A costs problem presents a number of related questions that if posed in the correct order increase the likelihood that the most defensible answer will be produced.[182] A defensible answer is one that is principled and predictable.

[132] As Justice Khullar observed, the first question is whether a hearing tribunal or an appeal panel should make a costs order against a regulated member.

[133] A number of considerations are at play in answering this question.

[134] It is the profession as a whole, not just the disciplined member, that benefits from the privilege of self-regulation. A regulator's decision adjudging a member to have committed unprofessional conduct communicates an unequivocal message to the public that the regulator protects the public's interest. This, in turn, increases the public's belief that the utilisation of professional services will protect their health and best interests. This positive evaluation of the profession probably increases the public's utilization rate of dental services. Arguably, the professional found to have committed misconduct does not receive a benefit from this determination.

[135] Costs are an inevitable part of self-regulation:[183]

> Professions in Alberta are extended the privilege of self-regulation. With that comes the responsibility to supervise and, when necessary, discipline members. The disciplinary process must necessarily involve costs, and any self-regulating professional organization must accept those costs as an inevitable consequence of

[182] *Humphreys v. Trebilcock*, 2017 ABCA 116, ¶ 162; [2017] 7 W.W.R. 343, 394, leave to appeal ref'd, [2017] S.C.C.A. No. 228 ("the motions court failed to ask the right questions in the correct order. The failure to adopt this strategy unnecessarily increases the risk that the decision maker will overlook an important consideration and arrive at an unsound conclusion"); *Estate of Rogers v. Commissioner of Internal Revenue*, 320 U.S. 410, 413 per Frankfurter J. ("In law also the right answer usually depends on putting the right question"); *Alberta Union of Provincial Employees v. Alberta*, 2019 ABCA 411, ¶ 105; 440 D.L.R. 4th 245, 282 per Wakeling, J.A. ("The likelihood that an adjudicator will select the best solution to a legal problem increases significantly if the adjudicator poses the right questions in the correct order") & Lederman, "The Balanced Interpretation of the Federal Distribution of Legislative Powers in Canada" in The Future of Canadian Federalism 107 (P.A. Crepeau & C. MacPherson ed. 1965) ("If you can frame the right questions and put them in the right order, you are half way to the answers").

[183] *College of Physicians & Surgeons Alberta v. Ali*, 2017 ABCA 442, ¶ 110; 67 Alta L.R. 6th 16, 46, leave to appeal ref'd, [2018] S.C.C.A. No. 433 per Slatter, J.A., dissenting. See also *Tan v. Alberta Veterinary Medical Ass'n*, 2022 ABCA 221, ¶ 42 ("Professions in Alberta are extended the privilege of self-regulation. With that comes the responsibility to supervise and, when necessary, discipline members. The disciplinary process must necessarily involve costs, and any professional regulator must accept some of those costs as an inevitable consequence of self-regulation. It is acceptable for the profession to attempt to recover some of those costs from disciplined members, but some burden of the costs of regulation is unavoidable and a proper consequence of the regulator's mandate").

> self-regulation. It is acceptable for the profession to attempt to recover some of those costs back from disciplined members, but the burden of the costs of regulation are to some extent inevitable.

[136] The imposition of all or a significant percentage of the costs of self-regulation on the profession as a whole is fair because all members benefit from self-regulation. These advantages include the profession's ability to limit competition by restricting who may enter the profession and implementing other anti-competitive measures such as fee schedules and restrictions on advertising. These measures increase the income and status of the profession's members.[184]

[137] Most regulated members of a profession are likely to benefit, in some way, from the public review of the conduct of members.[185] Some dentists may not appreciate that a specific behavior is inappropriate. They may never have turned their minds to it or, if they had, failed to appreciate the problems associated with the behavior. A decision of a hearing tribunal or an appeal panel may remind a segment of the dentist population of the high standards to which dentists must adhere. It may reinforce in the minds of regulated professionals the very existence of boundaries that a member may not cross.

[138] While it is true that a member who commits unprofessional conduct displays a trait that distinguishes him or her from other members of the profession who have not committed unprofessional conduct,[186] this fact, by itself, does not convince us that it is appropriate, as a general

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[184] E.g., *Goldsmith v. National Bank of Canada*, 2015 ONSC 4581, ¶ 8 per Belobaba, J. ("the legal profession continues to enjoy protection from market forces") & *Ontario Ass'n of Architects v. Ass'n of Architectural Technologists of Ontario*, 2002 FCA 218, ¶ 69; 215 D.LR. 4th 550, 572, leave to appeal ref'd, [2002] S.C.C.A. No. 316 per Evans J.A. ("I would also agree with the Applications Judge that the fact the activities of the AATO may also benefit its members is not a fatal objection to characterizing them as benefiting the public. The mix of public and private benefit tends to be a feature of professional self-regulation, even when, as in the case of the legal profession for example, a statutory body regulates the practice of the profession and a non-statutory body acts as its advocate. Both perform functions (professional education, for example) that serve the interests of the public as citizens and clients, as well as those of members of the profession)". See Adams "Health professional regulation in historical context: Canada, the USA and the UK (19th century to present)" 18 Human Resources for Health 1, 4 (2020).

[185] See 3 Royal Commission Inquiry into Civil Rights 1183 (J. McRuer Commissioner 1968) ("There are three groups with an interest in the efficacy and fairness of disciplinary proceedings of self-governing bodies. They are: (1) The public, whose benefit and protection are the primary objectives of the whole process; (2) Members of the self-governing body, who are or may be subjected to discipline; and (3) The profession or occupation itself, which has a general interest in ensuring the maintenance of high standards of professional or occupational conduct").

[186] *Shulakewych v. Alberta Ass'n of Architects*, 1997 ABCA 157, ¶ 6; 196 A.R. 312, 314 ("We think it would be grossly unfair to leave the costs of the successful prosecution on the shoulders of the general membership of the Association"); *Hoff v. Alberta Pharmaceutical Ass'n*, 18 Alta. L.R. 3d 387, 395 (Q.B. 1994) ("As a member of the pharmacy profession the appellant enjoys many privileges. One of them is being part of a self-governing profession. Proceedings like this must be conducted by the respondent association as being part of its public mandate to assure to the public competent and ethical pharmacists. Its costs in so doing may properly be borne by the member whose conduct is at issue and has been found wanting. Appellant's request for cancellation or reduction [of costs likely to be in excess of $27,000] is accordingly refused") & *Chuang v. Royal College of Dental Surgeons of Ontario*, 211 O.A.C.

principle, to impose a significant portion of the costs of an investigation into and hearing of a complaint on a disciplined dentist unless a compelling reason to do so exists.[187]

[139] When does a compelling reason exist?

[140] A compelling reason exists in four different scenarios.[188] While we refer to dentists in this discussion, our observations apply to all professionals[189] regulated by the *Health Professions Act*.[190]

[141] First, a dentist who engages in serious unprofessional conduct[191] – for example, a sexual assault on a patient,[192] a fraud perpetrated on an insurer,[193] the performance of a dental procedure while suspended or the performance of a dental procedure in a manner that is a marked departure

281, 284 (Div. Ct. 2006), leave to appeal refused, 2006 CarswellOnt 8677 (C.A.), leave to appeal refused, [2006] S.C.C.A. No. 482 ("The members of the Royal College of Dental Surgeons should not be liable for the costs of guilty members").

[187] In our experience, regulators do not impose costs or a significant costs award on a regulated member unless there is a compelling reason to do so. This may be attributable to the fact that the objectives of the regulation process are to edify the member, to vindicate professional boundaries and to reengage the member with the profession's standards. The practical realities may be different for each regulated profession. See *Vavilov v. Canada*, 2019 SCC 69, ¶90 ("The approach to reasonableness review that we articulate in these reasons accounts for the diversity of administrative decision making by recognizing that what is reasonable in a given situation will always depend on the constraints imposed by the legal and factual context of the particular decision under review. These contextual constraints dictate the limits and contours of the space in which the decision maker may act and the types of solutions it may adopt").

[188] See *Essa v. Ass'n of Professional Engineers and Geoscientists of Alberta*, 2021 ABCA 116, ¶ 22; 22 Alta. L.R. 7th 239, 245 ("A costs award requires consideration of many factors, including the outcome of the hearing, the reasons the complaint arose, the financial burden on the regulator and the professional, and the way the defence was conducted").

[189] See *Vavilov v. Canada*, 2019 SCC 65, ¶ 90 ("The approach to reasonableness review that we articulate in these reasons accounts for the diversity of administrative decision making by recognizing that what is reasonable in a given situation will always depend on the constraints imposed by the legal and factual context of the particular decision under review. These contextual constraints dictate the limits and contours of the space in which the decision maker may act and the types of solutions it may adopt").

[190] R.S.A. 2000, c. H-7, Part 10.

[191] *Alsaadi v. Alberta College of Pharmacy*, 2021 ABCA 313, ¶ 64; 463 D.L.R. 4th 335, 362 per Watson & Slatter, JJ.A. ("The sanctity of private healthcare information is obviously an important consideration. Healthcare professionals who have access to that information have a duty not to misuse it or access it unless medically necessary. However, the appellant's conduct did not involve any risk of harm to any patient, did not demonstrate any lack of pharmaceutical skill, did not involve sexual misconduct or fraud, and did not involve any misuse of drugs. The appellant did not profit or gain from his conduct").

[192] *Clokie v. Royal College of Dental Surgeons of Ontario*, 2017 ONSC 2773, ¶ 3 (Div. Ct.) (the Court upheld the College's decision to revoke the license of a dentist who had sexual intercourse with a patient).

[193] *Piros v. Newfoundland Dental Board*, 363 A.P.R. 73, 79-91 (Nfld. Sup. Ct. Tr. Div. 1993) (the Dental Board imposed a three-month suspension and other conditions on a dentist who defrauded the insurer by billing for services never performed).

from the ordinary standard of care[194] – can justifiably be ordered to indemnify the College for a substantial portion or all of its expenses in prosecuting a complaint. A dentist guilty of breaches of this magnitude *must have known* that such behavior is completely unacceptable and constitutes unprofessional conduct. It is not unfair or unprincipled to require a dentist who knowingly commits serious unprofessional conduct to pay a substantial portion or all the costs the regulator incurs in prosecuting a complaint.

[142] Second, a dentist who is a serial offender engages in unprofessional conduct on two or more occasions may be ordered to pay some costs. If a dentist is guilty of two acts of unprofessional conduct and both of the findings of unprofessional conduct were serious breaches, a costs order indemnifying the College for a substantial portion or all of its expenses would be appropriate.[195] If both breaches were not serious, a small amount of costs – something less than twenty-five percent – could be justified. If only the first breach was serious and the dentist had already been ordered in a previous proceeding to pay a substantial costs order on account of the serious offence, a small costs order for the second breach may be appropriate. If only the second breach was serious, a costs order indemnifying the College for a substantial portion or all of its costs would be appropriate. There is a big difference between a dentist who has been sanctioned once and a dentist who has been sanctioned two or more times. A dentist who has been sanctioned once should be extra vigilant in how he or she practices dentistry. It seems to us, based on our review of the College's 2019, 2020 and 2021 annual reports[196] and the decisions finding

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[194] *Tan v. Alberta Veterinary Ass'n*, 2022 ABCA 221 (a veterinarian performed an unnecessary operation on a dog – he had not conducted the necessary presurgical tests).

[195] See *Chuang v. Royal College of Dental Surgeons*, 211 O.A.C. 281 (Div. Ct. 2006) & 216 O.A.C. 207, 208 (Div. Ct. 2006) (the College's Discipline Committee revoked Dr. Chuang's license after finding him guilty of fifteen acts of professional misconduct that the Divisional Court described as "outrageous" and ordered him to pay $250,000 of the $400,000 in costs incurred to investigate and hear the charges; the Court reduced the costs award to $200,000 on the ground that the $250,000 costs order was "unduly high").

[196] Our review of the College's 2019, 2020 and 2021 annual reports demonstrates that in this period the number of new complaints as a ratio of the number of regulated dentists is less than five percent. Alberta Dental Association and College, Annual Report 2019, at 12 & 18 (2020), Alberta Dental Association and College, Annual Report 2020, at 13 & 22 (2021) & Alberta Dental Association and College, Annual Report 2021, at 17 & 22 (2022). For example, in 2020 there were 2,930 regulated dentists and 119 new complaints filed. The ratio of complaints to regulated dentists is four percent. Out of the 281 complaints before the college that year – of which 162 carried over from previous years – ten complaints and dentists were referred to a hearing, and 141 complaints were closed. This suggests that a large proportion of complaints are resolved without any finding that the dentist has committed unprofessional conduct.

unprofessional conduct published[197] on the College's website,[198] that only a very small percentage of dentists engaged in active practice have ever been sanctioned. And of this group, we strongly suspect that an even smaller fraction are repeat offenders.[199] It is not unfair to place on the shoulders of this small group of dentists a disproportionate share of the costs of implementing the discipline process.

[143] Third, a dentist who fails to cooperate with College investigators and forces the College to expend more resources than is necessary to ascertain the facts related to a complaint cannot, with justification, object when ordered to pay costs set at an amount roughly equal to the unnecessary expenditures attributable to his or her intransigence.

[144] Fourth, a dentist who engages in hearing misconduct – behavior that unnecessarily prolongs the hearing or otherwise results in increased costs of prosecution that are not justifiable[200] – should expect to pay costs that completely or largely indemnify the College for its unnecessary hearing expenditures.

[145] It follows that the profession as a whole should bear the costs in most cases of unprofessional conduct.

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[197] Alberta Dental Association and College Bylaws, s. 19.7 (January 1, 2022) ("In the event that an investigated member is found by a Hearing Tribunal to have engaged in unprofessional conduct, then a summary of the Hearing Tribunal's decision shall be published in the newsletter of the Alberta Dental Association and College and on the Alberta Dental Association and College's websites. The summary shall include the name of the investigated member").

[198] There are thirty-three penalty decisions finding unprofessional conduct available on the webpage between 2017 and 2022. Of these, we count eight decisions issued in 2020 and eleven in 2021. https://www.cdsab.ca/patients-general-public-protection/solving-a-concern/hearing-tribunal-decision-summaries/.

[199] Of the 35 dentists with respect to whom the College published unprofessional conduct decisions between 2017 and 2022, we count only two that were the subject of more than one such determination in separate decisions – Dr. Jinnah and another dentist.

[200] See *Al-Ghamdi v. College of Physicians and Surgeons of Alberta*, 2020 ABCA 71, ¶ 47;6 Alta. L.R. 7th 42, 59, leave to appeal ref'd, [2020] S.C.C.A. No. 272 ("The appellant was largely responsible for the complexity of the proceedings. The appellant commenced 14 pre-hearing applications for various kinds of relief. The 47 days of hearing generated 10,039 pages of transcript. Counsel for the College estimates that 10 days would have been required to put in its case, but that the proceedings were lengthened by excessive, repetitive and irrelevant cross-examination by the appellant. The appellant called 50 witnesses, and attempted to call even more. Many of the witnesses he called had nothing of substance to add to the record, and did not assist his case. Ordering the appellant to pay costs proportionate to the number of particulars that were proven was likely generous to the appellant") & *Law Society of Ontario v. Khan*, 2021 ONLSTA 7, ¶ 12 ("The Lawyer's conduct of the appeal and numerous motions brought all of which were without merit, unnecessarily complicated the appeal").

[146] This presumption has merit and makes good sense.

[147] First, it will force the College to carefully evaluate the investigative and prosecutorial options that it has in a given case and select the course that makes the most sense, keeping in mind that the members as a whole will often ultimately bear the costs incurred. The College will probably have little or no appetite for expenditures that it must absorb itself unless they provide a significant benefit to the overall administration of the discipline process.[201] Some forms of unprofessional conduct may be adequately dealt with by an informal reminder of what is expected of a dentist[202] and a recommendation that a dentist apologize to a patient for what may be nothing more than a misunderstanding.

[148] Second, it will improve the position of a dentist charged with an act that is not serious unprofessional conduct. A dentist will know in advance what the costs consequences of an unsuccessful defence are very likely to be. He or she will not be pressured unduly to plead guilty to avoid the prospect of a burdensome costs order.[203] A prospective costs sanction should not be the primary reason why a dentist decides to plead guilty to a charge of unprofessional conduct. A dentist's right to provide a full answer and defence[204] should not be undermined by a potential large costs order. "The disciplinary system should not include a cost regime that precludes professionals raising a legitimate defence".[205]

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[201] Most people tend to be better stewards of their own money than that of others. See *Tan v. Alberta Veterinary Medical Ass'n*, 2022 ABCA 221, ¶ 43 ("Leaving some of the burden of the costs of disciplinary proceedings on the professional regulator helps to ensure that discipline proceedings are commenced, investigated, and conducted in a proportional … [manner], with due regard to the expenses being incurred") & A. Roberts, George III The Life and Reign of Britain's Most Misunderstood Monarch 179 (2021) ("[Lord] North had been a Lord of the Treasury from 1759 to1765, and was considered to be a good financier (except with regard to his own money, his management of which was a disaster)").

[202] Id. ¶ 44 ("the regulator must always ascertain whether perceived shortcomings in the profession are serious enough to justify the expense of disciplinary proceedings").

[203] 2 J. Casey, The Regulation of Professions in Canada 14-18 (looseleaf release no. 2021-4 June 2021) ("An award of costs can have a devastating impact on an individual with the financial hardship arising from the award of costs often being greater than the imposition of the discipline").

[204] *Alsaadi v. Alberta College of Pharmacy*, 2021 ABCA 313, ¶ 29; 463 D.L.R. 4th 335, 352 per Watson & Slatter, JJ.A. ("A member charged with professional misconduct is entitled to a fair opportunity to make full answer and defence to the charges").

[205] *Tan v. Alberta Veterinary Medical Ass'n*, 2022 ABCA 221, ¶ 45. See also *Alsaadi v. Alberta College of Pharmacy*, 2021 ABCA 313, ¶ 115; 463 D.L.R. 4th 335, 375 per Khullar, J.A. ("A reasonable opportunity to defend oneself can become hollow if the spectre of paying exorbitant costs creates a disincentive to do so").

[149] Third, the presumption will mean that most dentists found guilty of unprofessional conduct will not be subject to a costs order.[206] This, in effect, levels the playing field. The governing legislation does not allow either the hearing tribunal or the appeal panel to order the College to pay costs to a dentist who successfully defends a complaint.[207] This one-sided norm is of questionable merit.[208]

[150] Fourth, professional bodies' discipline proceedings share with regulatory prosecutions the practical factor that "selective enforcement"[209] is at play. Whether or not a particular professional body has a zero-tolerance policy for any type of misconduct, the fact remains that only some cases will be subject to discipline proceedings. The situation is akin to the reality that only a small portion of traffic violations come to the attention of traffic law enforcement officers and that not all of these will be prosecuted. With this in mind, it is important to ask whether the imposition of the burden of the costs of enforcement on specific offenders who happen to be prosecuted is fair.

[151] Fifth, the protocol will have marginal, if any impact, on dentists' membership fees.[210] The College's financial statements for the years ending December 31, 2020 and December 31, 2021

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[206] Most complaints are about the care the patient received. In 2019 roughly 94% of the 139 new complaints, in 2020 roughly 99% of the 119 new complaints, and in 2021 roughly 94% of the new complaints, this was the case. In this three-year period only 11 complaints alleged sexual misconduct. Alberta Dental Association and College, Annual Report 2019, at 18 (2020), Alberta Dental Association and College, Annual Report 2020, at 19 (2021) & Alberta Dental Association and College, Annual Report 2021, at 22 (2022).

[207] *Alsaadi v. Alberta College of Pharmacy*, 2021 ABCA 313, ¶ 103; 463 D.L.R. 4th 335, 372 per Khullar, J.A. ("costs can only be awarded one way – against a professional who has been found guilty of unprofessional conduct. There is no jurisdiction for a hearing tribunal to award costs *to* a professional who successfully defends allegations") (emphasis in original).

[208] Id. at ¶ 108; 463 D.L.R. 4th at 373 ("The costs situation under ... [the *Health Professions Act*] is unique. It is not like civil litigation where the successful party is presumptively entitled to costs, whoever that is. It is not like criminal law where, generally speaking, no costs are awarded and the state bears the cost for the investigation and the hearing, even when the state is successful. Rather, the ... [*Health Professions Act*] creates a scheme where only the professional is liable to pay costs, only the College can recover costs, and the quantum is potentially very high").

[209] *The Queen v. Beaudry*, 2007 SCC 5, ¶ 37; [2007] 1 S.C.R. 190, 208 per Charron, J. ("Applying the letter of the law to the practical, real-life situations faced by police officers in performing their everyday duties requires that certain adjustments be made. Although these adjustments may sometimes appear to deviate from the letter of the law, they are crucial and are part of the very essence of the proper administration of the criminal justice system … . The ability – indeed the duty – to use one's judgment to adapt the process of law enforcement to individual circumstances and to the real-life demands of justice is in fact the basis of police discretion").

[210] The College's 2022 fee structure obliged a member to pay a practice permit fee of either $5,050 or $5,550 depending on when the payment was made. Alberta Dental Assoc. and College 2022 Fee Structure available at https://www.cdsab.ca/becoming-a-dentist/. See also *Alsaadi v. Alberta College of Pharmacy*, 2021 ABCA 313, ¶ 115; 463 D.L.R. 4th 335, 375 per Khullar, J.A. ("A reasonable opportunity to defend oneself can become hollow if the spectre of paying exorbitant costs creates a disincentive to do so").

indicate that revenues exceeded expenditures by $2,353,867 in 2020 and $1,921,226 in 2021.[211] The College's 2021 complaints statistics report that there were only seventeen hearings conducted in 2021, and 105 complaints were closed.[212] While we do not know when the corresponding hearings took place, in 2021 the College's Hearing Tribunal released eleven decisions finding unprofessional conduct[213] and ordered the disciplined dentist to pay costs in all of them – between half and all the costs of the investigation and hearing in ten and a specified sum in the remaining one.[214] The College spent $1,314,000 for "Professional Conduct" that year.[215]

[152] And the propositions we have formulated are relatively easy to follow. A norm that simplifies and clarifies is usually beneficial in any regulated process.[216] It substantially increases the likelihood that parties affected by it can accurately predict the adjudicator's ultimate response. This relieves the parties of the need to contest the issues before the adjudicator. Time and money are saved.

[153] We encourage the College's complaints director to continue to take an active role in resolving complaints as soon as they reach the College.[217] The low number of hearings compared to the high number of resolved complaints suggests that this already happens to an extent. Resolution of complaints at the earliest opportunity is in the interest of patients, dentists, the College, and the public. Not only does timely resolution minimize the College's costs and resources, but it leads to more satisfactory outcomes and minimizes the psychological burden on patients and dentists. This is also in the public interest.

[154] In cases where the College decides to impose costs, exercising its discretion in accordance with the principles set out in this judgment, the College must provide clear and transparent

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[211] Alberta Dental Association and College, Annual Report 2020, at 31 (2020) & Alberta Dental Association and College, Annual Report 2021, at 35 (2021).

[212] Alberta Dental Association and College, Annual Report 2021, at 22 (2021).

[213] https://cdsab.ca/patients-general-public-protection/solving-a-concern/hearing-tribunal-decision-summaries.

[214] The tribunal ordered the dentist to pay 50% of the costs in four decisions, 75% in four decisions, 80% in one decision, all of the costs in one decision, and $20,000 towards costs in the remaining decision. Id.

[215] Alberta Dental Association and College, Annual Report 2021, at 35 (2021).

[216] *Alberta Teachers' Ass'n v. Buffalo Trail Public Schools Regional Division No. 28*, 2022 ABCA 13, ¶ 36 per Wakeling, J.A. ("Judges should strive to simplify the law whenever possible and not, without good reason, complicate it").

[217] *Health Professions Act*, R.S.A 2000, c. H-7, ss. 55(a.)-(b). See also Alberta Dental Association and College, Annual Report 2021, at 21 (2021) ("Where formal complaints are made to the ADA&C, dentists and complainants are encouraged by the Complaints Director, or with the assistance of the Complaints Director, to work together to resolve the complaint").

justification for a costs order against a disciplined dentist[218] – not, as seems to be the case in the published penalty decisions – costs are imposed on the dentist in every single instance of unprofessional conduct.[219]

4. The Appeal Panel Imposed Unreasonable Costs on Dr. Jinnah

[155] The appeal panel found reasonable the hearing tribunal's costs order[220], apart from reducing it because the evidence of one of the witnesses in relation to the interest rate was "unnecessary and irrelevant" and "extended the length and the cost of the hearing", on the basis that the Complaints Director proved the unprofessional conduct.[221] And in imposing costs for the appeal the appeal panel only appeared to consider Dr. Jinnah's success on each of her grounds of appeal.[222] Not surprisingly, it considered none of the features of the principles we have fashioned.[223] This led to an order of excessive costs in light of the nature of the charges and the conduct of the College and Dr. Jinnah.

[156] Based on the record before us, there is nothing in the circumstances of this case that justifies departing from the presumption that no costs be awarded against Dr. Jinnah. She did not engage in serious unprofessional conduct. Nor did she refuse to cooperate with investigators or engage in hearing misconduct.[224] While our research discloses that Dr. Jinnah has been subject to other findings of unprofessional conduct, we are not in a position to assess the significance of this and the impact it should have on the costs issue given the limited information available in the public

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[218] *Wright v. College and Ass'n of Registered Nurses of Alberta*, 2012 ABCA 267, ¶ 75; 355 D.L.R. 4th 197, 235, leave to appeal ref'd, [2012] S.C.C.A. No. 486 per Slatter, J.A. (a costs decision under the *Heath Professions Act* must be "justifiable, transparent and intelligible").

[219] Of the 33 published decisions finding unprofessional conduct, the hearing tribunal ordered costs in all of them, ranging from 50 to 100% of investigation and hearing costs (with 72% on average) and from $5,000 to $671,359.21 (with $74,479 on average). This does not include appeal costs.

[220] The hearing tribunal imposed a $50,000 costs order because Dr. Jinnah refused to admit any of the alleged conduct. Hearing costs were in excess of $70,000. Hearing Tribunal Decision, ¶¶ 65-67, Appeal Record 58-59. We note, however, that the tribunal has ordered costs even when the dentist admitted the charges. See, for example, Dr. Bleau (admitted guilt, ordered to pay $20,000), Dr. Buyn (admitted the charges but contested sanction, ordered to pay all of the costs), Dr. Cao (admitted charges, ordered to pay 75% of costs being $24,896.93), Dr. Chaaban (admitted charges, ordered to pay 50% of costs being $12,500). The appeal panel reduced the hearing costs award by 25% on the basis that the evidence of one of the witnesses in relation to the interest rate was "unnecessary and irrelevant" and "extended the length and the cost of the hearing".

[221] Appeal Panel Decision, ¶¶ 149-151, Appeal Record 93.

[222] Appeal Panel Decision, ¶¶ 152-157, Appeal Record 93-94.

[223] *K.C. v. College of Physical Therapists of Alberta*, 1999 ABCA 253, ¶ 94; [1999] 12 W.W.R. 339, 369.

[224] The fact that her attempt at resolution was unsuccessful and was viewed as an escalation is not an indication that she intended to be uncooperative. See Hearing Tribunal Decision, ¶ 75, Appeal Record 27.

notices.[225] For this reason, we exercise our authority under section 92(c) of the *Health Professions Act*[226] and refer back to the appeal panel the costs matter for determination in accordance with the principles set out in this judgment.

G. We Encourage the College To Take Steps To Prevent Future Similar Cases

[157] This judgment provides the direction Dr. Jinnah and other health care providers subject to the *Health Professions Act* need to avoid stepping on a mine in the minefield created when a health care professional communicates with a complainant.

[158] The regulator can also learn from this case.

[159] The College has an obligation under section 3(1)(b) of the *Health Professions Act*[227] *t*o "provide direction to … its regulated members."

[160] Dentists must understand that the complaints process is a critical component of the self-regulation of dentistry and that members must act responsibly when communicating with patients about complaints. It is certainly unprofessional conduct to threaten patients who have filed a complaint. Our review of the College's Code of Ethics did not reveal that it addressed this topic. The College could expand on the information that it provides in its guide to its members about complaints processing[228] to make this important point. Some reasonably well-informed dentists may not appreciate the importance of an effective complaints process and the harm that may occur if a dentist acts in a manner that may cause a patient with backbone to avoid using it.

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[225] The College's website lists three decisions involving Dr. Jinnah: the matter before this court – the decision "in the matter of M.S" in which the hearing tribunal found unprofessional conduct on November 10, 2020; the decision "in the matter of C.D." in which the hearing tribunal found unprofessional conduct on December 17, 2021, where Dr. Jinnah admitted that she did to ensure "information regarding fees, interest and billing is provided to patients in a clear and transparent manner"); and one "in the matter of M.K." for which a decision is pending following an appeal to the council, for which no file is linked or date provided.

[226] R.S.A. 2000, c. H-7.

[227] Id.

[228] See, for example, Alberta Dental Association and College, Guide for Members about Complaints Processing 5 ("In an investigation, the dentist's response will be forwarded to the complainant who will be provided an opportunity to respond to the letter of response. ... In any response letter it is important to consider the tone of the letter and the avoidance of threatening to sue or personally attacking the complainant. The tone in the response letter can have a significant impression on the patient and their future responses in an investigation. As a regulated professional, your professional obligations include responding to a complaint"). https://www.cdsab.ca/patients-general-public-protection/solving-a-concern/hearing-tribunal-decision-summaries/understanding-the-complaints-process/.

[161] We agree with the hearing tribunal that the College should provide more direction on how to collect unpaid accounts.[229]

[162] To date, the College has given limited guidance to the profession on standards of conduct for collection of outstanding accounts and how to respond properly to complaints.[230] Providing guidance to the profession on these questions, such as through amending the Code of Ethics or Practice Manual, adopting standards of practice and providing up-to-date sample letters that it considers acceptable in content and tone – going further than the "general background information" the College currently sets out in the Practice Management Manual that includes such letters[231] – and providing more specific guidance in its Patient Communication Guide[232] would likely go a long way to prevent similar cases from occurring in the future. The College should amend its Code of Ethics to expressly record best practices that will allow a dentist to interact with a complainant or potential complainant without making the situation worse.

[163] The College estimates that seventy percent of the complaints it receives "could have been resolved through better communication between dentist and patient".[233] Developing the tools and skills necessary for dentists to become adept at avoiding unprofessional conduct that stems from failures of communication and resolving patient concerns at an early stage is valuable for dentists, the College, and the public. The need for investigations and hearings arising from routine issues that can be resolved by better communication would decrease, leading to reduced costs for regulating the profession. And the public would benefit from helpful, professional and attentive responses to questions they might have in relation to their dental care.

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[229] Hearing Tribunal Decision, ¶ 132, Appeal Record 40.

[230] Appeal Panel Decision, ¶ 126 ("The Appeal Panel agrees with Mr. Renouf that ... the ADA&C has not provided explicit rules regarding many aspects of billing practices"), Appeal Record 88. Alberta Dental Association and College, Code of Ethics (October 2007).

[231] Alberta Dental Association and College, Practice Management Manual 1 (2003) ("This publication of the Alberta Dental Association and College is intended to provide general background information on practice management issues and financial arrangements in a dental practice. It does not constitute policy or recommendations of the Alberta Dental Association and College"). See also Chapters 7 (Communicating Financial Policies to Patients) and 8 (Collecting Patient Revenues), including sample letters and a stepped process to collect overdue accounts.

[232] Alberta Dental Association and College, Patient Communication Guide 7 ("While there are a multitude of patient needs – six basic needs stand out: ... 6 Information The patient wants to know about fees and services but in a pertinent and time-sensitive manner").

[233] Alberta Dental Association and College, Patient Communication Guide 5 ("Open dialogue with patients results in better patient retention and a reduction in complaints. It is estimated that 70% of the complaints received at the ADA&C could have been resolved through better communication between dentist and patient and never evolved into written complaints").

VII. Conclusion

[164] The appeal is allowed in part.

[165] We uphold the appeal panel's finding on the merits that the part of Dr. Jinnah's April 22, 2015 email to her patient obstructed the complaint process under the *Health Professions Act*[234] and constituted unprofessional conduct. We set aside the other misconduct determinations. The reprimand must be corrected to reflect these determinations.[235] The order that Dr. Jinnah complete a philosophy course and pay the costs of the investigation, hearing, and appeal is also set aside. We send back to the appeal panel the matter of costs before the hearing tribunal and appeal panel for determination in accordance with the principles set out in this judgment.[236]

[166] Exercising our authority under section 92(d) of the *Health Professions Act*,[237] we order the College to repay Dr. Jinnah half of the amount she paid for preparation of the record.

Appeal heard on January 5, 2022

Memorandum filed at Edmonton, Alberta
this 13th day of October, 2022

Watson J.A.

Wakeling J.A.

Feehan J.A.

[234] R.S.A. 2000, c. H-7.

[235] Revised Notice of Hearing, ¶ 1, Appeal Record 7. Hearing Tribunal Decision, ¶ 133, Appeal Record 40. Appeal Panel Decision, ¶ 164(a), Appeal Record 95.

[236] *Health Professions Act*, R.S.A. 2000, c. H-7, s. 92(c) ("The Court of Appeal on hearing an appeal may ... refer the matter back to the council for further consideration in accordance with any direction of the Court").

[237] Id. s. 92(d) ("The Court of Appeal on hearing an appeal may ... where the appellant is the investigated person, if the appeal is wholly or partly successful, direct that all or part of the cost of preparation of the record referred to in section 91 be repaid by the college to the appellant or be applied to reduce the amount of penalties or costs otherwise payable to the college by the appellant").

Appearances:

S.M. Renouf, K.C./L. Anaka
for the Appellant

J.C. Gagnon/E. Banfield
for the Respondent, Alberta Dental Association and College

D.N. Jardine
for the Respondent, Appeal Panel of Council of the Alberta Dental Association and College

Corrigendum of the Memorandum of Judgment

Page 55, counsel's name "L. Anaka" has been added.

TAB 13

DATE: 1998112
DOCKET: C28208

COURT OF APPEAL FOR ONTARIO

MOLDAVER and GOUDGE JJ.A. and FERRIER J. *ad hoc*

B E T W E E N :	)	
	)	**Dennis R. O'Connor, Q.C.**
KENTUCKY FRIED CHICKEN CANADA,	)	**David Stockwood, Q.C.**
a Division of PEPSI-COLA CANADA LTD.	)	**Nancy J. Spies and**
	)	**Timothy H. Mitchell,**
Plaintiff	)	**for the appellants**
(Respondent)	)	
	)	
and	)	**David R. Byers**
	)	**Katherine L. Kay and**
SCOTT'S FOOD SERVICES INC. and	)	**Christopher J. Cosgriffe,**
SCOTT'S HOSPITALITY INC.	)	**for the respondent**
	)	
Defendants	)	
(Appellants)	)	**Heard: May 4 and 5, 1998**
	)	

GOUDGE J.A.:

[1] This appeal was heard on May 4 and 5, 1998. This court's reasons for judgment were ready for release on July 9, 1998 when the parties contacted the court to request that this not be done. On the basis of the reasons given by the parties for this request, the court agreed to refrain from releasing its judgment until November 1, 1998 but made clear that the judgment would then be released unless prior to October 31, 1998 both parties notified the court in writing that the matter had been fully and finally settled and that the appellant wished to withdraw the appeal. This has not happened and these reasons are therefore being released.

[2] The appellant Scott's Food is the largest Kentucky Fried Chicken ("KFC") franchisee in the world. Its franchise agreement (the "license agreement") with the respondent covers some four hundred outlets, approximately half of all KFC outlets in Canada.

[3] Up until 1996, Scott's Food was owned by the appellant Scott's Hospitality whose other major business was a school bus operation. At that point, as part of a transaction with Laidlaw Inc. ("Laidlaw") in which Laidlaw acquired the school bus business, the shareholders of Scott's Hospitality replaced it as the sole shareholder of the franchisee with a new company, Scott's Restaurants. As a result, these shareholders then owned Scott's Restaurants which in turn owned Scott's Food. This change was made without the respondent's consent.

[4] There were two main issues at trial. The second, which the parties call the enhancement issue, was whether, apart altogether from the corporate changes entailed by the Laidlaw transaction, Scott's Food had upgraded its outlets as required by its contract. At trial, Steele J. found that it had not. I will come in due course to the limited appeal taken from the judgment below on this issue.

[5] The first and indeed the fundamental issue at trial, called the transfer issue, was whether the license agreement required the appellants (to whom I will refer jointly as "Scott's") to obtain the respondent's consent to the change in ownership of the franchisee failing which the respondent could terminate the agreement. Steele J. interpreted the contract as requiring consent, thereby giving the respondent the right to terminate since no consent was obtained. For the reasons that follow, I have come to the opposite conclusion and I would therefore allow the appeal on the transfer issue.

THE TRANSFER ISSUE

The Relevant Facts

[6] The license agreement that is the subject of this litigation was signed on June 9, 1989, effective January 1, 1989. The respondent was the franchisor and the appellant Scott's Food the franchisee. The latter was a wholly-owned subsidiary of Scott's Hospitality which was not a party to the agreement.

[7] At the time the license agreement was made, Scott's operated about one-half of all the KFC outlets in Canada and more than ten times as many as the next largest franchisee in the country. Unlike most franchisees, Scott's had very significant bargaining power in the negotiations which led up to the agreement.

[8] For the purposes of the transfer issue, the critical paragraphs of the license agreement are the following:

16. *Transfer*

16.1 The grant of the License hereunder is personal to Licensee. The grant of the License hereunder is based upon full disclosure in writing by the Licensee to KFC, and approval by KFC, of all directors and holders of majority control of the voting shares of Licensee and of any corporation or corporations which directly or indirectly (whether by means of any intermediate corporations or otherwise) own or control or have an interest in the shares of the Licensee. Licensee acknowledges that the restrictions provided in this Paragraph 16 are reasonable and necessary to protect the KFC System and the KFC Marks and are for the benefit and protection of all KFC licensees as well as KFC.

16.2 Licensee agrees that it shall not sell, transfer, assign, encumber, sub-license or otherwise deal with this Agreement or its rights or interest hereunder (hereinafter referred to as "transfer"), without KFC's prior written consent and Licensee's compliance in all respects with the terms and conditions of this Paragraph 16. Any transfer or any attempt to do so, contrary to Paragraph 16 shall be a breach of this Agreement and shall be void but shall give KFC the right of termination as provided in Paragraph 17.2(d).

[9] Paragraph 17.2(d) reads as follows:

17.2 KFC may, without prejudice to any other rights or remedies contained in this Agreement or at law or in equity, terminate the License upon immediate notice (or in the event advance notice is required by law, upon the giving of such notice) in the event that:

. . .

(d) Licensee makes or permits a transfer contrary to the provision of Paragraph 16;

[10] The history of Scott's as a KFC franchisee predates the license agreement by twenty years. It goes back to 1969 when Scott's Hospitality entered into an agreement to become a franchisee operating KFC outlets in Canada. The franchisor then was Col. Sanders Kentucky Fried Chicken Limited ("Colonel Sanders"), the owner of the KFC trademarks in Canada. This agreement was to run until January 1, 1994. It is noteworthy that it contained no clause like the current paragraph 16.1. It did not specify that the rights of Scott's Hospitality were personal to it, nor were there any provisions restricting the transfer of its shares. There was, however, a provision restricting the transfer of the license without the prior written consent of the franchisor.

[11] By 1985, the franchisor had developed a standard franchise agreement ("the 1985 Agreement") containing certain restrictions on the transfer of shares in the franchisee which, at that point, were standard in all KFC franchise agreements in Canada except that with Scott's Hospitality.

[12] While paragraph 16.1 of the 1985 Agreement reads identically to paragraph 16.1 in the license agreement, paragraph 16.2 of the 1985 Agreement when coupled with paragraph 16.4 contains significant differences. These two paragraphs are reproduced below, highlighting the words that do not appear in the license agreement:

> 16.2 The Franchisee agrees that it shall not sell, transfer, assign, encumber, sub-license or otherwise deal with this Agreement or its rights or interest hereunder (hereinafter referred to as "transfer"), **and shall not suffer or permit any deemed sale, transfer or assignment of this Agreement or its rights or interest hereunder (hereinafter referred to as "deemed transfer" and more particularly defined in paragraph 16.4)**, without KFC's prior written consent and **Franchisee's** compliance in all respects with the terms and conditions of this Paragraph 16. Any transfer **or deemed transfer**, or any attempt to do so, contrary to this Paragraph 16 shall be a breach of this Agreement and shall be void but shall give KFC the right of termination as provided in paragraph 17.2(d).
>
> **16.4 For the purposes of this Paragraph 16, a deemed transfer of this Agreement or the rights and interest hereunder shall include:**

(a) . . .

(b) in the event that Franchisee is a corporation, any change (including but without limitation any issuance, sale, assignment, transfer, redemption or cancellation of, or conversion of any securities into, voting shares of the corporate Franchisee or any other corporation referred to in paragraph 16.1, or any amalgamation, merger or other reorganization of the corporate Franchisee or any such other corporation) in any of the holdings of voting shares referred to in paragraph 16.1; provided that, in the case of any such corporation the voting shares of which are listed and publicly traded on a stock exchange, no such change in any of the holdings of its voting shares shall constitute a deemed transfer unless, in the sole opinion of KFC, direct or indirect control of the corporate Franchisee would thereby be changed.

[13] In 1987, Col. Sanders sold its entire interest in the KFC trademarks in Canada to Kentucky Fried Chicken's corporation ("KFC Corp." or "KFC") which held those rights for the rest of the world.

[14] Just prior to this sale, by letter agreement dated July 16, 1987, KFC Corp. agreed that when the sale from Col. Sanders was concluded, it would grant Scott's Hospitality a ten-year renewal of the 1969 agreement. This letter agreement suggested no constraint on the transfer of shares of the franchisee.

[15] Pursuant to the 1987 letter agreement, negotiations ensued between KFC and Scott's Hospitality. In these negotiations, Scott's Hospitality refused to agree to terms in the language of the 1985 agreement, just as it had previously refused to do with Col. Sanders. The Scott's representative made clear to KFC that Scott's would not agree to any restrictions on changes of ownership in the licensee.

[16] The relative bargaining power of Scott's and KFC in these negotiations was the subject of some considerable attention at trial. The chief KFC negotiator testified that Scott's was at least the equal of KFC in bargaining power. The leading expert for KFC testified that it was unusual for a franchisee to be in such a position.

[17] Because of these unique circumstances, the trial judge concluded that the evidence of the experts as to the usual practice in the franchising industry must be applied with caution. Ultimately, he found that Scott's had sufficient bargaining power to negotiate a contract in which there would be no restriction on the transferability of shares. The question he had to decide was whether the resulting license agreement contained such a restriction.

[18] The first of the two Laidlaw transactions, which triggered the need to answer this question, began in January 1996 with an unsolicited offer from Laidlaw to purchase all of the shares of Scott's Hospitality. Laidlaw's intention was that following a successful takeover, it would sell off Scott's Food and retain the school bus business operated by Scott's Hospitality. Laidlaw's offer contained a condition that it be satisfied that there was no impediment to its disposing of the shares of Scott's Food to a third party without affecting the franchisee's rights under the license agreement. KFC was not prepared to give its consent to this transaction and indeed commenced this litigation in response. As a result, this Laidlaw proposal could not be completed within its time frame and hence it did not proceed.

[19] Rather, a second Laidlaw transaction was structured in which Scott's Restaurants was incorporated as a subsidiary of Scott's Hospitality. Scott's Hospitality then transferred its shares in Scott's Food to Scott's Restaurants in exchange for shares of Scott's Restaurants which were dividended out to the shareholders of Scott's Hospitality. The shareholders of Scott's Hospitality thereby became the owners of Scott's Restaurants which, in turn, became the owner of the franchisee, Scott's Food. Laidlaw then purchased the shares of Scott's Hospitality thereby acquiring the school bus business.

[20] KFC was kept fully informed of this transaction but continuously opposed it. Indeed, its consent was never expressly sought. The simple question at trial was whether that consent was required.

The Judgment Below

[21] The trial judge found that while Scott's Food as franchisee was bound by the license agreement, Scott's Hospitality was not bound by its terms. He concluded that Scott's Food was neither the alter ego nor the agent of Scott's Hospitality. The respondent does not contest this conclusion.

[22] He then went on to his core finding on the transfer issue, namely, the construction of paragraph 16.1 of the license agreement. He construed that paragraph to contain a continuing obligation on the part of the franchisee to obtain approval of KFC to any transfer of the shares of either Scott's Food or its controlling shareholder. He put his findings in these terms:

> In my opinion the disclosure and approval of the directors and holders of majority control would be meaningless unless it was a continuing obligation and not merely at the time of execution. Based on good business sense section 16.1 must be construed as being a continuing obligation.
>
> . . .
>
> In my opinion there is nothing in section 16 that prohibits or gives the right of approval to KFC of trading of shares of Scott's Food or Hospitality provided that there is no issue of a change of control.
>
> There are no clearly expressed words requiring the approval of KFC to any transfer of the shares of Scott's Food or its controlling shareholders. However section 16.1 referring to the grant being personal and the reference to the directors and holders of majority control of the shares of Scott's Food and the broad reference to any other corporations with control make it clear that any transfer of the controlling shares of Scott's Food or Hospitality are subject thereto. To interpret the section otherwise would defeat the personal aspect and not make good business sense and would be contrary to the generally accepted practice in the franchise industry.

[23] He then moved directly and without elaboration to a finding that paragraph 16.2 prohibits a transfer or an attempted transfer of the license agreement without consent and since the first Laidlaw proposal was an attempted transfer and the second was an actual transfer, each breached paragraph 16.2 and gave KFC the right to terminate the license agreement pursuant to paragraph 17.2(d).

Analysis

[24] The question to be determined on the transfer issue is one of contractual interpretation: properly construed, does either paragraph 16.1 or paragraph 16.2 of the license agreement require KFC's consent to either Laidlaw transaction? The trial judge determined that this was not a case of ambiguity and on this basis, he declined to consider evidence of the subjective intentions of the parties which were not communicated to each other. Equally he excluded the various draft documents leading up to the license agreement. He did, however, consider the relationship between the parties and the custom of the industry, including the license agreements between the respondent and other franchisees in Canada, as part of the factual matrix that must be looked at in interpreting the agreement.

[25] I agree with this approach. While the task of interpretation must begin with the words of the document and their ordinary meaning, the general context that gave birth to the document or its "factual matrix" will also provide the court with useful assistance. In the famous passage in *Reardon Smith Line Ltd. v. Yngvar Hansen-Tangen*, [1976] 1 W.L.R. 989 at 995-96 (H.L.) Lord Wilberforce said this:

> No contracts are made in a vacuum: there is always a setting in which they have to be placed. The nature of what is legitimate to have regard to is usually described as "the surrounding circumstances" but this phrase is imprecise: it can be illustrated but hardly defined. In a commercial contract it is certainly right that the court should know the commercial purpose of the contract and this in turn presupposes knowledge of the genesis of the transaction, the background, the context, the market in which the parties are operating.

[26] The scope of the surrounding circumstances to be considered will vary from case to case but generally will encompass those factors which assist the court "... to search for an interpretation which, from the whole of the contract, would appear to promote or advance the true intent of the parties at the time of entry into the contract.": *Consolidated Bathurst Export Ltd. v. Mutual Boiler and Machinery Insurance Co.*, [1980] 1 S.C.R. 888 at 901.

[27] Where, as here, the document to be construed is a negotiated commercial document, the court should avoid an interpretation that would result in a commercial absurdity[1]. Rather, the document should be construed in accordance with sound commercial principles and good business sense[2]. Care must be taken, however, to do this objectively rather than from the perspective of one contracting party or the other, since what might make good business sense to one party would not necessarily do so for the other.

[28] With these broad principles of interpretation in mind, I turn first to the construction to be given to paragraph 16.1 of the license agreement. Properly construed, does it give KFC the right to approve a change in the controlling shareholder of the franchisee? It is the second Laidlaw transaction that requires this question to be answered. Given that the first Laidlaw transaction was not proceeded with, KFC did not argue at trial or on appeal that it breached paragraph 16.1.

[29] It is helpful at this point to set out the provision again:

> 16.1 The grant of the License hereunder is personal to Licensee. The grant of the License hereunder is based upon full disclosure in writing by the Licensee to KFC, and approval by KFC, of all directors and holders of majority control of the voting shares of Licensee and of any corporation or corporations which directly or indirectly (whether by means of any intermediate corporations or otherwise) own or control or have an interest in the shares of the Licensee. Licensee acknowledges that the restrictions provided in this Paragraph 16 are reasonable and necessary to protect the KFC System and the KFC Marks and are for the benefit and protection of all KFC licensees as well as KFC.

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1 *City of Toronto v. W.H. Hotel Ltd.* (1966), 56 D.L.R. (2d) 539 at 548 (S.C.C.).

2 *Scanlon v. Castlepoint Development Corporation et al.* (1992), 11 O.R. (3d) 744 at 770 (Ont. C.A.).

[30] I have concluded that this clause does not give KFC a right to approve a change in the controlling shareholder of its franchisee Scott's Food. In other words, paragraph 16.1 does not extend to the second Laidlaw transaction. I say this for a number of reasons.

[31] First, the license agreement was signed in 1989. The Laidlaw transactions occurred in 1996. The ordinary meaning of the language used in paragraph 16.1 suggests that the franchisor KFC had the right on entering the contract to know and approve the shareholders of the franchisee. There is nothing to suggest a right to approve a change in those shareholders some seven years later.

[32] Second, such a right would mean a significant change from the agreement which had governed this franchise relationship since 1969 which clearly contained no such right. Moreover, Scott's had refused to enter into an agreement like the 1985 standard franchise agreement which did provide the franchisor with this right. The trial judge found that prior to executing the license agreement, KFC knew this and had been told that Scott's would not agree to any restriction on changes of ownership in the franchisee.

[33] Third, the language of the 1985 standard franchise agreement is revealing. In 1989, when the license agreement was concluded, every other KFC franchise agreement in Canada expressly provided for the franchisor's right to approve a change in the shareholders of the franchisee. This was done not by means of paragraph 16.1 but rather through the "deemed transfer" language of paragraphs 16.2 and 16.4. Paragraph 16.1 in the license agreement ought not to be construed to provide the franchisor with this right where the identical language in the 1985 standard franchise agreement was clearly not intended to have that effect. The corollary to this is that the deemed transfer language which does provide this right to the franchisor in the 1985 standard franchise agreement is conspicuously absent from the license agreement.

[34] Fourth, paragraph 16.1 extends the right of approval to the holders of majority control of the franchisee and any corporation which has an interest in the shares of the franchisee. If this language is read to give KFC a right to approve any subsequent change in the majority shareholder of the franchisee, it must also give KFC the right to approve a subsequent change in shareholder control of any corporation which owns any interest in the franchisee, even if it is only a single share. In argument, the respondent conceded that this would be a commercial absurdity. To find, as the trial judge did, that the franchisor's right of approval is limited to a change of control in the franchisee is, in my opinion, to read out of paragraph 16.1 the phrase "have an interest in". By contrast, to extend this right of approval to the majority shareholder and also to shareholders who have an

interest in the shares of the franchisee does not create a commercial absurdity if that right applies simply at the point of entering the license agreement.

[35] Fifth, paragraph 16.4 provides support for this interpretation. It requires the franchisee to seek KFC's consent to a transfer to a third party of the franchisee's interest under the license agreement. To allow an informed consent, this paragraph expressly obliges the franchisee to give KFC the same information about the shareholders of the third party that paragraph 16.1 provided concerning the franchisee. However, if paragraph 16.1 contained an ongoing right of KFC to be informed of and approve the shareholders of the party holding the franchise, paragraph 16.4 would be superfluous.

[36] Finally, and with respect, it is my view that the three reasons offered by the trial judge for the opposite interpretation of paragraph 16.1 do not withstand scrutiny.

[37] The first reason given by the trial judge was that the meaning I would accord to paragraph 16.1 would defeat the personal aspect of the license agreement. That paragraph certainly makes clear that the grant of the license is personal to the licensee. However, that licensee is clearly and expressly Scott's Food, not its controlling shareholder. A change in the latter leaves the licensee unchanged. Following the second Laidlaw transaction, the license is still granted personally to Scott's Food.

[38] The second reason was that it would not make good business sense to read paragraph 16.1 so that it did not extend to a change in the shareholders of the franchisee. While this might not make good business sense from the perspective of the franchisor, it might well make good business sense for the franchisee. In my view, neither of these is helpful in the required task of contractual interpretation. Rather, in applying objectively the interpretive principle of what accords with sound commercial principles and good business sense, the key fact is that for twenty years, from 1969 to 1989, this franchise relationship operated with apparent viability without the right of approval contended for by the respondent. In light of this history, it cannot be concluded that the meaning I give to paragraph 16.1 would not make good business sense.

[39] Finally, it was said that reading paragraph 16.1 as I do would be contrary to the generally accepted practice in the franchise industry. The fallacy in this reasoning is that, as the trial judge recognized, this was a very unusual franchising relationship. This franchisee appeared to have bargaining power at least equal to that of KFC and certainly sufficient power to achieve a contract with no restriction on the transferability of shares. By contrast, the trial judge found the industry standard to be that the franchisor has

control over the franchisee. In these circumstances, the generally accepted industry practice is of little use in interpreting this particular license agreement.

[40] Hence, I conclude that paragraph 16.1 of the license agreement cannot be construed to give KFC the right to approve a change in the shareholders of Scott's Food. This paragraph, therefore, was not breached when Scott's did not obtain KFC's approval of the second Laidlaw transaction.

[41] It is next necessary to consider the proper interpretation to be given to paragraph 16.2 of the license agreement. It is helpful to reproduce this provision a second time:

> 16.2 Licensee agrees that it shall not sell, transfer, assign, encumber, sub-license or otherwise deal with this Agreement or its rights or interest hereunder (hereinafter referred to as "transfer"), without KFC's prior written consent and Licensee's compliance in all respects with the terms and conditions of this Paragraph 16. Any transfer or any attempt to do so, contrary to Paragraph 16 shall be a breach of this Agreement and shall be void but shall give KFC the right of termination as provided in Paragraph 17.2(d).

[42] The respondent's primary argument was that the second Laidlaw transaction engaged the last sentence of this paragraph. It was said to be a transfer contrary to paragraph 16.1 which, because of paragraph 16.2, triggered the right of termination in paragraph 17.2(d). Given the conclusion I have reached concerning paragraph 16.1, this argument must fail.

[43] Apart altogether from paragraph 16.1, however, the respondent also argues that for the purposes of paragraph 16.2, the first Laidlaw transaction was an attempted transfer and the second was an actual transfer and that KFC's prior written consent was therefore required.

[44] In my view, this argument also must fail. On the ordinary meaning of the words used in paragraph 16.2, it is the licensee Scott's Food that is constrained from dealing with its interest under the license agreement. Once the alter ego argument is dismissed, this paragraph simply cannot reach Scott's Hospitality, the shareholder of the franchisee. Nor does it reach the shareholders of Scott's Hospitality. Neither an attempted change nor

an actual change in the shareholders of the franchisee constitutes the franchisee dealing with its interest under the license agreement.

[45] This conclusion is assisted by examining the language of the counterpart paragraph 16.2 in the 1985 standard franchise agreement. The two Laidlaw transactions would be encompassed by that provision only because of the inclusion of the "deemed transfer" concept. As I have said, this concept is conspicuously absent from paragraph 16.2 of this license agreement.

[46] The respondent argues that its proposed reading of paragraph 16.2 is consistent with good business sense and industry practice. However, as I have indicated in connection with the argument on paragraph 16.1, in the circumstances of this case, neither of these aids to interpretation requires that paragraph 16.2 be read to give KFC the right to consent to a change in the shareholders of its franchisee.

[47] Finally, the respondent relies on *GATX v. Hawker-Siddely Canada Inc.* (1996), 27 B.L.R. (2d) 251 (Ont. Gen. Div.) to assert a broad meaning for the phrase "or otherwise deal with" as found in paragraph 16.2. That case is different from this one in that, there, the contracting party was clearly dealing indirectly with its interest under the agreement. Here, neither Laidlaw transaction involved the franchisee dealing in any way with its interest under the license agreement.

[48] I therefore find that, properly construed, paragraph 16.2 does not give KFC the right to prior written consent to either Laidlaw transaction.

[49] Given my conclusions about paragraphs 16.1 and 16.2 of the license agreement, it is unnecessary to deal with the appellant's alternative arguments: that paragraph 16.1 is limited to a change in ultimate control of the franchisee; that KFC could not have reasonably refused its approval of the second Laidlaw transaction; that a breach of paragraph 16.1 entitles KFC to terminate only if it was a fundamental breach of the license agreement; but in any event, for KFC to terminate would be a breach of its good faith duty under the license agreement; and finally, that the appellants are entitled to relief from forfeiture. Nor is it necessary to deal with the respondent's alternative argument that a breach of paragraph 16.1 allows it to terminate through direct resort to paragraph 17.3 of the license agreement.

[50] Before leaving the transfer issue, the remaining matter required to be dealt with arises from the finding below that pursuant to paragraph 16.3 of the license agreement,

KFC had a right of first refusal in the circumstances of both Laidlaw transactions. That paragraph reads in part as follows:

> 16.3 In the event that **Licensee receives** a bona fide offer, which **licensee is willing to accept**, from a third party to purchase or otherwise acquire any of the Licensee's rights and interest in this Agreement, ..., Licensee shall first offer to sell the same to KFC at the same price and on the same terms and conditions as in the third party's offer ... In the event that KFC so accepts such offer to sell, a binding agreement of purchase and sale shall thereby be constituted between Licensee and KFC at the said price and upon the said terms and conditions.... [Emphasis added.]

[51] The reasons below reveal no analysis of the language in this paragraph by the trial judge in reaching his conclusion.

[52] In my opinion, the ordinary meaning of the words used in the paragraph dictates the opposite conclusion -- that neither Laidlaw transaction triggered a right of first refusal. Neither an offer to purchase the shares of Scott's Hospitality nor an offer to change the controlling shareholder of Scott's Food is an offer which the franchisee receives or one which the franchisee can accept. The licensee cannot receive a takeover bid for the licensee's parent or for the licensee itself.

[53] In summary, therefore, the appellant did not breach either paragraph 16.1 or paragraph 16.2 of the license agreement because of the Laidlaw transactions and KFC does not have the right to terminate the license agreement as a result. Nor did either Laidlaw transaction give KFC a right of first refusal.

[54] I would accordingly allow the appeal on the transfer issue and set aside the declarations in paras. 1, 2, 3 and 4 of the judgment below. Instead, an order will go dismissing the claims for these declarations. Finally, I would set aside para. 13 of the judgment below and would grant the declaration sought therein.

THE ENHANCEMENT ISSUE

[55] The other major issue at trial was whether Scott's Food had failed to meet its obligations to enhance its KFC outlets. These obligations are contained in the license agreement and the addendum to it, the Master Development Agreement, signed at the same time. The trial judge's two principal findings on this issue were that Scott's Food had failed to enhance its outlets as required by paragraph 7.2 of the Master Development Agreement and, secondly, because more than five to ten per cent of the outlets had not been enhanced as required, the failure was material and substantive, thereby entitling KFC to terminate the license agreement pursuant to paragraph 17.2(e) unless Scott's Food corrects the failure within three months. The appellants appeal neither of these findings. Indeed, they raise only two grounds of appeal in connection with the enhancement issue.

[56] Firstly, they appeal the declaration that KFC is also entitled to terminate the license agreement pursuant to paragraphs 17.2(e) and 17.3 because Scott's Food's enhancement failures were breaches of paragraphs 3.2, 5 and 6 of the license agreement. While the judgment contains this declaration, the reasons for judgment do not reveal the basis upon which the declaration was made.

[57] Second, they appeal the finding that to avoid KFC's right to terminate under paragraph 17.2(e), Scott's Food must, within three months, enhance all of its outlets, not just a sufficient number that the failure becomes less than material and substantive.

[58] Turning to the first of these two grounds of appeal, it is helpful to set out paragraphs 17.2(e) and 17.3 of the license agreement:

> 17.2 KFC may, without prejudice to any other rights or remedies contained in this Agreement or at law or in equity, terminate the License upon immediate notice (or in the event advance notice is required by law, upon the giving of such notice) in the event that:
>
> . . .
>
> (e) Licensee fails to satisfy, in a material and substantive manner, the requirements for enhancement and development contained in Articles 3.3, 3.4, 7.2 and 7.3 of the Addendum, provided that notice of any such failure is delivered to

> Licensee and Licensee shall not have corrected such failure within (3) months from the delivery of such notice.
>
> 17.3 The License will terminate on the termination date specified in any notice by KFC to Licensee (without any further notice of termination unless required by law), provided that (a) the notice is hand delivered or mailed at least thirty (30) days (or such longer period as may be required by law) in advance of the termination date, (b) the notice reasonably identifies one or more breaches or defaults in Licensee's obligations or performance hereunder, (c) the notice specifies the manner in which the breach(es) or default(s) are not fully remedied before, and as of, the termination date.

[59] In my view, paragraph 17.2(e) deals explicitly and exhaustively with the enhancement obligations on the franchisee that, if not met, give KFC the right to terminate the license agreement. None of paragraphs 3.2, 5 or 6 of the license agreement is included in that list.

[60] Moreover, as indicated by the trial judge, paragraph 17.3 merely sets out the procedure of formal notice. It does not accord to KFC a substantive right to terminate for any failure by Scott's Food to discharge its enhancement obligations. To so interpret paragraph 17.3 would fly in the face of paragraph 17.2 where the parties have carefully selected the enhancement obligations that, if breached, justify termination. Hence I would reverse the declaration that because the franchisee's enhancement failures breached paragraphs 3.2, 5 and 6 of the license agreement, KFC is entitled to terminate pursuant to paragraphs 17.2(e) and 17.3.

[61] As to the second ground of appeal on the enhancement issue, paragraph 17.2(e) of the license agreement provides that failure <u>in a material and substantive manner</u> (my emphasis) to meet the franchisee's enhancement obligations as specified therein gives KFC the right to terminate if the failure is not corrected within three months. As I have said, the trial judge found that where more than five to ten per cent of the outlets fall below this required standard, Scott's Food was in substantial breach for the purposes of this paragraph. He went on to say this:

> ... KFC must give three months' notice from the date of this judgment to Scott's to allow it to remedy the default found in this decision on the enhancement issue. In other words, Scott's must be given three months in which to upgrade all of its remaining outlets to certification standards. If it chooses not to do so, it may close those stores under other termination procedures.

[62] There is nothing in the actual judgment appealed from that requires the franchisee to enhance or close all of its remaining outlets to avoid termination. Hence, I propose to make no order on this ground of appeal.

[63] However, in my opinion, if failure in a material and substantive manner to meet the enhancement requirements occurs when five to ten per cent of the outlets are below standard, correcting that failure means enhancing at least enough outlets so that there is no possibility of this line being crossed. This means that to correct that failure within three months, Scott's Food must ensure that no more than five per cent of its outlets are substandard. I would therefore not think it necessary that to correct the failure, the franchisee must sufficiently upgrade all its remaining outlets. To do so would make the correction incongruent with the failure contrary to what I think is meant by the final phrase of paragraph 17.2(e).

[64] The view I have expressed is also consistent with paragraph 6.3 of the Master Development Agreement. It contemplates that the franchisee could operate outlets for a limited period of time even if they had not been enhanced to the required standard. This paragraph is inconsistent with a correction requirement that would compel the franchisee to properly enhance all of its remaining outlets.

[65] In summary, I would allow the appeal on the enhancement issue. I would set aside the declaration in para. 9 of the judgment below and order that the claim for this declaration be dismissed.

COSTS

[66] The trial judge ordered that there be no costs of the trial on the basis of paragraph 18.3 of the license agreement which required this result unless one party prevailed entirely, something that did not occur at this trial.

[67] Before us, neither party sought to disturb this order and I do not do so. Both parties submitted that costs of the appeal should follow the result. I can see no reason why this should not happen.

[68] In conclusion, I would allow the appeals with costs on the transfer issue and the enhancement issue in accordance with these reasons. The trial judgment is otherwise undisturbed.

RELEASED:

TAB 14

Court of Queen's Bench of Alberta

Citation: Mimi's Parlour Ltd v 1816112 Alberta Ltd, 2021 ABQB 254

Date: 20210401
Docket: 2003 21089
Registry: Edmonton

Between:

Mimi's Parlour Ltd

Applicant/Cross-Respondent

- and -

1816112 Alberta Ltd

Respondent/Cross-Applicant

Reasons for Judgment
of the
Honourable Mr. Justice M. J. Lema

A. Introduction

[1] A restaurant tenant seeks an interlocutory injunction or relief from forfeiture against its landlord. Injunction-wise, and on "serious issue to be tried", the tenant argues that it did not default on rent and, in fact, is in a surplus position. Accordingly, rent-default termination of the lease was unwarranted. If the lease was validly terminated, forfeiture relief should be granted, largely on the basis of significant leasehold improvements made by it.

[2] The landlord points to ongoing and increasing rental defaults as justifying termination and the equities overall as precluding forfeiture relief.

[3] I find that the lease was validly terminated, with injunctive relief inapplicable, but grant relief from forfeiture, as explained below.

B. Lease termination

Rental Arrears

[4] The restaurant says that the landlord owes it $300,000 for the latter's share of leasehold improvements (constituting a credit against which rental arrears can be deducted), that in any case the restaurant overpaid rent for a number of months in 2020, that the landlord inexplicably failed to sign up for a rent-relief program offered by the federal government, and that the landlord's rent accounting is inaccurate, the net result of which is that the restaurant is either in a surplus or a square position on rent.

[5] The landlord says that its share of the leasehold improvements was addressed by reduced rental payments over the life of the lease, that the tenant actually underpaid rent for the months in question, that its decision not to participate in the rent-relief program was justified and, in any case, does not justify less-than-required lease payments, and that its accounting is accurate.

[6] I find that:

- the restaurant produced no material evidence of a side (or other) agreement on the $300,000. In any case, Article 9 of the lease ("Entire Agreement") confirms that the lease, which makes no reference to any such indebtedness, "shall supersede and take the place of any and all previous agreements and representations of any kind, written or verbal, heretofore, made by anyone in reference to the demised premises or in any way affecting the building or equipment of which the same forms a part …". In any case, the restaurant acknowledges, at para 3 of its application brief and para 10 of its witness's February 25, 2021 affidavit, that "[the $300,000] was to be repaid to the [landlord] by way of a rent reduction program through to September 14, 2025";

- while the restaurant asserts a "150 per cent overpayment" of rent for certain periods, it produced no evidence of such payments. The restaurant refers to its "payment plan", which the landlord never signed on to, as the benchmark for calculating overpayments. In a nutshell, that plan called for payments on a reduced scale (25 per cent of per-lease payments) i.e. as if the landlord had participated in the noted (*Canada Emergency Commercial Rent Assistance*) rent-relief program. With no actual participation by the landlord, reduced payments were not warranted, meaning no overpayments – instead, underpayments – were made. The possible impact of the program is a red herring on the termination aspect;

- the restaurant did not show that the landlord's accounting (reflected in the rental ledger attached as exhibit C to its witness's affidavit) was off-target in any way. The landlord's demand letters and associated accounting for this period are crystal-clear in outlining the rental and other (operating cost and common-area) amounts owing. The landlord first referred to **apparent credits of approximately**

$19,000, but half of that amount was applied as pre-paid rent (for July through October, 2018), and the other half continues to be held by the landlord as a security deposit, per s. 3.12(b) of the lease, against the restaurant's entire lease obligations. The restaurant then emphasized that, at various points, it had reduced accrued rental arrears to zero. However, the last fully-paid-up point was April 9, 2020. After that, rent and associated charges (up to December 1, 2020) tallied to $21,247.14, compared to total payments of $4,713.67 i.e. approximately 22 per cent of the per-lease payments, leaving a shortfall of $15,590.50. The restaurant did not produce any evidence undercutting or shaking the landlord's calculations in any way; and

- finally, I note that, via its counsel's November 4, 2020 letter and pursuant to the *Commercial Tenancies Protection Act*, the landlord proposed a payment plan for clearance of the rental arrears attributable to the pandemic "emergency period" (May 17, 2020 through August 31, 2020), folding in as well certain September and "common area management" costs. It proposed that those combined arrears (approximately $11,000) be paid at the rate of approximately $900 per month i.e. a pay-out period of approximately one year. However, the restaurant did not respond to that proposal or make one of its own by the appointed deadline (November 16, 2020).

[7] Accordingly, I find that the restaurant had in fact defaulted as reflected in the landlord's demand letters and that it was entitled, given those defaults, to terminate the lease, per s. 8.03(1) of the lease.

Impact of provincial Covid-19 legislation re commercial tenancies

[8] The restaurant also argued that, through the combined effect of the ***Commercial Tenancies Protection Act*** and the same-named regulation, the landlord is barred from terminating or otherwise enforcing the lease for any rent defaults.

[9] However, that Act's core protection existed only from March 17, 2020 to August 31, 2020. The latter date comes from the Act's definition of "emergency end date", as meaning "August 31, 2020 or such alternative date as may be prescribed by the regulations."

[10] The regulation in question -- ***Commercial Tenancies Protection Regulation*** (AR 138/2020) – does not provide for or address in any way an alternative end date.

[11] Accordingly, the ***CTPA***'s embargo on enforcement expired at the end of August 2020.

[12] As for the restaurant's reference to para 6(2)(a) ***CTPA*** (recognition of payment plans possibly extending beyond August 31, 2020), with no evidence of any plan entered into at all, the provision does not assist.

[13] The landlord proposed a plan, to which the tenant did not counter-propose or respond at all. Its proposal was sparked by s. 6 ***CTPA***, which states:

> (1) If a tenant is unable to meet the tenant's rent obligations under a tenancy agreement and this is caused by the Covid-19 pandemic, the **landlord and tenant shall enter into a payment plan for the payment of rent**.
>
> (2) A payment plan
>
> (a) may extend beyond the emergency end date [i.e. August 31, 2020], and
>
> (b) must account for any payment of fees, penalties or rent by a tenant that the landlord was prohibited by section 4 or 5 from charging and that has not been refunded to the tenant.
>
> (3) A payment plan has the **effect of amending the tenancy agreement to the extent necessary to give effect to the payment plan**, and **in the event of a failure by the tenant to adhere to a payment plan after the emergency end date, a landlord shall have all remedies available to the landlord under the tenancy agreement as modified by the payment plan**. [emphasis added]

[14] Subsection 10(1) ***CTPA*** (regulation-making power) refers to regulations "respecting payment plans (paragraph (d)), but the Regulation makes no reference to payment plans.

[15] I note that, per ss 28(2) of the ***Interpretation Act***, "shall" is to be construed as imperative i.e. per ss 6(1) ***CTPA***, the landlord and tenant **must** enter into a payment plan.

[16] But what if they fail to do so?

[17] Not only is there no evidence of the landlord and tenant actually making a payment plan, the restaurant's own description of the "plan" it perceived confirms that one was not made:

> [The restaurant's witness] testified that there was a plan in place to pay, and in fact [it] did pay 25% and the remaining 75% was to be paid through the Federal Commercial Relief Program.

[18] However, per s. 2 ("Application of the Act"), the ***Regulation*** confirms that:

> The [***CTPA***] does not apply to commercial premises if the landlord and tenant have, at any time, participated in the Canada Emergency Commercial Rent Assistance program with respect to the commercial premises.

[19] In other words, if the federal program had applied (and it did not), the ***CTPA*** would not have applied to these parties. Accordingly, the **"plan" asserted by the restaurant could not have existed.**

[20] The ***CTPA*** does not expressly address the circumstance of a failure to make a s. 6 plan, for instance, by providing a default formula for a payment plan, a mechanism (e.g. court application or arbitration) for setting a plan failing agreement, a provision deeming acceptance of the latest offer or counter-offer after a defined period, or otherwise.

[21] I find it is implicit that, where one party (here, the landlord) proposes a plan and the other (here, the restaurant) does not accept the plan, make a counter-proposal or respond at all

(even to request more time to consider a proposed plan) within a reasonable time, the proposing party is permitted to pursue enforcement (here, terminate the lease for non-payment of rent).

[22] In the circumstances here, with the **increasing arrears** ($12,762.77 as of October 13, 2020), and with the landlord's obvious **heightened interest**, as of late October (when it retained counsel), **in enforcing the lease according to its terms**, and with the restaurant being **put on notice** then that the landlord would **pursue all available rights and remedies if further rent defaults continued**, and with the landlord expressly referring in its November 4, 2020 letter to the ***CTPA* requirement to make a payment plan and proposing a plan** (and an at-first-glance reasonable one, spreading out the approximately $11,000 arrears over the following twelve months), and providing almost two weeks for a response, and with a **second request on November 19th for a counter-proposal or any response at all**, and with **no acceptance of the landlord's plan, no counter-proposal and no response at all by December 7th** (i.e. over one month from the initial plan proposal), which I find was a **reasonable waiting period**, the landlord was entitled to treat the restaurant as **unwilling to make any plan** and, as a consequence, to **enforce the lease according to its terms**.

[23] In other words, I find that where (as here) a tenant effectively shuts its ears to a landlord's payment proposal, the tenant loses whatever shelter a s. 6 payment plan would have provided, leaving the landlord free to terminate the lease for payment breaches as if s. 6 had not been enacted.

Impact of the Canada Emergency Commercial Rent Assistance Program

[24] The restaurant also did not show that this voluntary program somehow applied without the landlord's cooperation or assistance.

[25] In ***HAS Novelties Limited v 1508269 Ontario Limited***, 2021 ONSC 642, Steele J.'s program description reflects its voluntary nature:

> … in April 2020, the federal government introduced a program called Canada Emergency Commercial Rent Assistance ("CECRA"). CECRA was a **voluntary program under which eligible landlords and tenants could enter into agreements whereby tenants would pay 25% of their rent, the government would pay 50% of the rent to the landlord, and the remaining 25% of the rent would be absorbed or forgiven by the landlord**. The program was available from April through September 2020, and was retroactive, provided the application was made within the applicable time period. [para 10] [emphasis added]

[26] In that case, the landlord and tenant did not make such an agreement, but the tenant argued that the landlord had signaled that it would participate and could not disavow that intention. Steele J. found otherwise:

> I am satisfied that **despite the Landlord's apparent undertaking to submit the CERCA application, he was not obliged to proceed with the application**. He had the right to refuse to apply for CECRA, not based on his own failure to inspect the corporate books and records, but because he would have the most to lose (i.e., 25% of the rent) by

> submitting the application. **It was a voluntary program and the Landlord elected not to participate**. [para 21]
>
> … I find that **although the Landlord may have given the impression that he would apply for CECRA, there was no promise or assurance made by his conduct which was intended to affect their legal relationship. It is clear that the Landlord was considering the CECRA program and was leveraging this on the noise complaint issue. However, based on the record before me, the Landlord did not by his words or conduct promise that the application for CECRA would be made. This was a voluntary program. The Landlord was certainly looking at it and considering it but did not proceed.**
>
> Accordingly, having found that **there was no promise or assurance made by the Landlord regarding CECRA that was intended to affect the legal relationship between the Landlord and the Tenant, I find that the Landlord was not obliged to submit the CECRA application**. [paras 53 and 55] [emphasis added]

[27] In ***2487261 Ont Corporation v 2612123 Ont Inc***, 2021 ONSC 336 (Lemon J.), the parties acknowledged (para 13) that that program "was optional for landlords."

Conclusion on lease termination

[28] For these reasons, I confirm that the landlord was entitled to, and did, terminate the lease for the cited payment failures, with no restriction under either the provincial or federal commercial-tenancy-assistance programs.

[29] Accordingly, there is no basis for injunctive relief. Here I invoke Morgan J.'s decision in ***Jungle Lion Management Inc v London Life Ins Co***, 2020 ONSC 165:

> … these introductory facts signal that there are **no grounds for the injunction** sought in the first instance by the Plaintiff. Under art. 14.2 of the Lease, the Landlord was **entitled to terminate the tenancy for non-payment of rent** as soon as the rent went unpaid on the first of each month. In fact, that article provides that the Landlord can terminate without notice in the event of non-payment of rent, although the Landlord did as a courtesy provide the Plaintiff with notice of termination.
>
> In any case, the Plaintiff delivered its rent cheque to the Landlord on November 11, 2019 and the cheque was returned by the bank. There is **no *prima facie* case or issue to be tried with respect to the termination of the tenancy under the Lease.** The Plaintiff concedes that at the time of termination it was in default of rent. **The Landlord had the right to terminate, and there are no grounds on which to enjoin it from doing so**: *RJR-Macdonald Inc. v Canada (Attorney General)*, 1994 CanLII 117 (SCC), [1994] 1 SCR 311. [paras 5 and 6 of ***Jungle Lion***]

[30] Same here: the tenant does not have even a *prima facie* case against the lease having terminated, in the face of its clear rent-payment failures, the lease's default terms, the expiry of more than seven days after the late November payment demand (among others), and the non-application of the provincial and federal programs.

[31] The focus then shifts to the tenant's back-up argument i.e. relief from forfeiture.

C. Relief from forfeiture

Core principles

[32] The core principles governing this relief were reviewed in ***Ontario (Attorney General) v. 8477 Darlington Crescent***, 2011 ONCA 363:

> **… Courts of equity have always had the power to relieve against the forfeiture of property consequent upon a breach of contract:** see *McBride v. Comfort Living Housing Co-Op* (1992), … 7 O.R. (3d) 394 at 402 (C.A.). **That power is now expressed in various statutes dealing with specific kinds of contracts (*e.g.* contracts of insurance, leases) and has been given more general expression in s. 98 of the *Courts of Justice Act* …:**
>
> > **A court may grant relief against penalties and forfeitures, on such terms as to compensation or otherwise as are considered just. [**Alberta equivalent is s. 10 of the *Judicature Act***: Subject to appeal as in other cases, the Court has the power to relieve against all penalties and forfeitures and, in granting relief, to impose any terms as to costs, expenses, damages, compensation and all other matters that the Court sees fit.]**
>
> The power to relieve from forfeiture is **discretionary and fact-specific**: *Saskatchewan River Bungalows Ltd. v. Maritime Life Assurance Co.*, … [1994] 2 S.C.R. 490 at p. 504. The power is predicated on the existence of **circumstances in which enforcing a contractual right of forfeiture, although consistent with the terms of the contract, visits an inequitable consequence on the party that breached the contract**. Relief from forfeiture is **particularly appropriate where the interests of the party seeking enforcement by forfeiture can be fully vindicated without resort to forfeiture**. Relief from forfeiture is **granted sparingly** and the **party seeking that relief bears the onus** of making the case for it: *1497777 Ontario Inc. v. Leon's Furniture Ltd.* (2003), … 67 O.R. (3d) 206 at paras. 67-69, 92 (C.A.).
>
> In *Saskatchewan River Bungalows*, at p. 504, Major J. identified the factors relevant to the exercise of the power to grant relief against forfeiture:
>
> > ... The factors to be considered by the court in the exercise of its discretion are the **conduct of the applicant**, the **gravity of the breaches**, and the **disparity between the value of the property forfeited and the damage caused by the breach.**
>
> The first factor, the conduct of the breaching party, requires an **examination of the reasonableness of the breaching party's conduct as it relates to all facets of the contractual relationship, including the breach in issue and the aftermath of the breach**. Osborne J.A. explained the nature of this inquiry in *Williams Estate v. Paul Revere Life Insurance Co.* (1997), 1997 CanLII 1418 (ON CA), 34 O.R. (3d) 161 at p. 175 (C.A.):
>
> > The reasonableness test requires consideration of the **nature of the breach, what caused it and what, if anything, the insured attempted to do about it**. All of the circumstances, including those that go to explain the act or omission that caused the lapse (forfeiture) of the policy, should be taken into account. It is only

> by considering the relevant background that the reasonableness of the insured's conduct can be realistically considered. [Emphasis added.]

The examination of the reasonableness of the breaching party's conduct lies at the heart of the relief from forfeiture analysis. **A party whose conduct is not seen as reasonable cannot hope to obtain relief from forfeiture**: see *Paul Revere* at p. 175; *Saskatchewan River Bungalows* at pp. 504-05.

The second factor identified in *Saskatchewan River Bungalows*, the gravity of the breach, looks both at the **nature of the breach itself and the impact of that breach on the contractual rights of the other party**: see *Leon's Furniture* at paras. 75-78. If, for example, the **forfeiture provision operated as a means of securing payment of the rent required under a lease, the fact that the breaching party had paid all amounts owing could obviate the need to resort to forfeiture and support a claim for relief from forfeiture.**

The third factor identified in *Saskatchewan River Bungalows* engages a kind of **proportionality analysis. If there is a large difference between the value of the property to be forfeited and the amount owing as a result of the breach, equity will favour relief from forfeiture**. For example, in *Liscumb v. Provenzano* (1985), 1985 CanLII 2051 (ON SC), 51 O.R. (2d) 129 (H.C.), aff'd (1986), 1986 CanLII 2595 (ON CA), 55 O.R. (2d) 404 (C.A.), the trial judge, in granting relief from forfeiture, observed that the property to be forfeited was worth between three and four times the amount owing on the debt giving rise to the breach. The trial judge relied on this disproportionality between the debt owing and the consequences of the forfeiture as one factor in favour of granting relief from forfeiture. [paras 86-92] [emphasis added]

Application of the principles (case-law examples)

[33] In ***Alwell Mechanical Ltd v Royal Bank of Canada***, 1985 ABCA 193, the Court of Appeal granted forfeiture relief (by allowing an appeal), emphasizing the **proportionality factor**:

> During the course of the lease the appellant **has put more than $400,000.00 in improvements into the property.** Indeed, it is evident that some money which should have been paid in rent and for the other charges stipulated by the lease has been channeled into improvements. The arrears as at the date of this hearing amount to some $90,000.00 even after giving effect to the terms of an order made in this court staying the order below. Under the terms of the stay order $11,000.00 a month has been paid to cover current rent of $4,000.00 and to reduce the arrears.
>
> We are all of the view **that if the termination of the lease is permitted to stand, the apparent windfall to the respondent is so out of proportion to the amount of arrears that a court of equity ought to intervene subject to terms which make the respondent whole for the moneys wrongfully withheld**. Consequently, we allow the appeal and substitute for the order made an order relieving against the forfeiture of the lease. This order will be subject to the following terms:
>
> 1. That the appellant will by December 31st, 1985 **pay all arrears including interest in the amounts provided by the lease**, so that as at that date the lease payments will be completely current. During the period until

December 31st a minimum of $15,000.00 will be paid on the first day of each month with the balance due by December 31st.

2. The appellant will by December 31st, 1985 pay to the respondent **solicitor and client costs of the application** in the court below and of this appeal.

If the appellant fails to abide by the terms stipulated the respondent will be entitled to an order declaring the lease terminated and to a writ of possession effective immediately thereafter. [paras 1-3] [emphasis added]

[34] The proportionality factor was also noted in ***Canpar Holdings Ltd v Petrobank Energy and Resources Ltd***, 2011 ABCA 62:

> Relief from forfeiture should be granted when forfeiture would result in a **lessor receiving an amount out of proportion to the arrears**: see ***Chroniaris Enterprises Ltd. v. MKRS Pub Inc.***, 2008 ABCA 172, 432 A.R. 286; ***Alwell Mechanical Ltd. v. Royal Bank*** (1985), 1985 ABCA 193 (CanLII), 41 Alta. L.R. (2d) 8 (Alta. C.A.). Disproportion was found to exist in the latter case, where the value of the loss was just under 4.5 times the value of the lessee's improvements into the property. [para 47]

[35] In ***1198816 Alberta Ltd v Bourbon Lounge Inc***, 2008 ABQB 600, S. Martin J. (as she then was) elaborated on the **"tenant's conduct" factor**:

> A court does not favour forfeiture and the **burden of proof is on the tenant, as applicant, to establish why forfeiture would be unfair**. In *Armenian Community Centre v. Morland Marketing Inc.*, [1995] O.J. No. 3730 (Ont. Ct. Just (Gen. Div.)) (QL), Justice Cumming outlined when such a burden has not been met at para. 76:
>
> > A court will decline to exercise its equitable discretion in favour of an applicant: the applicant has failed to attempt diligently to comply with the terms of the lease; the **applicant has failed to come to court with clean hands**; the applicant has engaged in improper conduct; or the applicant has in any way attempted to mislead the court: *Kochhar v. Ruffage Food (*1992) 23 R.P.R. (2d) 200 (Ont. Gen. Div.); *Dominelli Service Stations Ltd. v. Petro-Canada Inc.*, [1992] O.J. No. 1158 (Ont. Gen. Div.); rev'd [1992] O.J. No. 1823 (C.A.).
>
> The **conduct of the tenant is a relevant consideration in determining whether relief from forfeiture will be granted and is of fundamental importance. If conduct is reprehensible, substantial and persistent, no relief from forfeiture can be granted. Failure to remedy one's breaches bars relief from forfeiture**: *931576 Ontario Inc.; King Street West Ltd. v. 418 Wellington Parking Ltd.* (1994), 40 R.P.R. (2d) 220, (Ont. Ct. Just. (Gen. Div.)). [paras 228-229] [emphasis added]

[36] After reviewing the **tenant's conduct and the other forfeiture factors**, S. Martin J. denied forfeiture relief:

> The Respondent has failed to establish why relief against forfeiture should be granted. The **conduct surrounding the Lease Amending Agreement [described at paras 242-254], and to a much lesser extent not disclosing an existing Written Lease in attempts to seek better rents, operate to undermine any equities the Respondent**

could invoke. In my view, the tenant has not established the first threshold of coming to court with clean hands.

In turning to the other factors in relation to forfeiture while I am not persuaded there are other breaches in relation to the parkade, the use of the premises as a bar or the interaction with the fire marshal, there has been a history of tension and distrust between the parties, even if they have tried to remain business like. **There are many issues on which they differ, and even though main issue is the proper amount of the rent, it cannot be said that money is all that is at issue**.

There was **not much evidence on the relative value of the property forfeited and the damage which may be caused. However, forfeiture would work hardship for the [tenant]. Likely the business would be lost and he was entrusted with monies from his family. A Court is reluctant to grant forfeiture but the facts in the case at bar support that remedy.**

Nor has there been a waiver of forfeiture. This is not the case where a landlord has simply accepted rent with the full knowledge of the tenant's breach of covenant as in *Delilha's Restaurants Ltd. v. 8-788 Holding's Ltd.* (1994), 1994 CanLII 3170 (BC CA), 92 B.C.L.R. (2d) 342 (C.A.)and *Fitkid (York) Inc. v. 1277633 Ontario Ltd.*, [2002] O.T.C. 749 (Ont. S.C.J.).The courts will look at the **conduct of the landlord to determine if there has been an election not to terminate the lease in the circumstances after the right of forfeiture arises**. No such forfeiture arises on the facts in the case at bar. [paras 255-258] [emphasis added]

[37] In ***Bank of Montreal v Phoenix Rotary Equipment Ltd***, 2007 ABQB 86, Bielby J. (as she then was) explained the proper approach to proportionality (**rejecting a landlord's focus on lost higher-rent opportunities**):

… York [the landlord] argues that the disparity between the value of the property forfeited and the damage caused by the breach should resound in its favour, pointing out that it will **lose $2 million in additional rental and the increase in market value of the building** should the Option be exercised by Reliance, losses which it says make the $460,000 recovery which the creditors will lose if the assignment of the Lease to Reliance is inoperable pale by comparison. This argument rather brazenly confuses the test. It is **not the loss of a windfall to a landlord which a Court should strive to avoid in considering relief from forfeiture but rather the loss of rent and other benefits to the landlord under the original lease.** That loss in this case is nil, given that the Receiver/Trustee has committed to payment of all rental arrears owing under the Lease forthwith upon this decision being rendered.

Ample case authority supports the proposition that **loss of a windfall is no reason to deny relief from forfeiture.** In ***S.M.L. Industries Ltd. v. Highlander Cleaners Ltd.*** 1987 CanLII 3455 (AB QB), [1987] 78 A.R. 110 a receiver was granted relief from forfeiture of a 30 year lease which the landlord purported to terminate simply because a receiver had been appointed, under lease terms similar to the ones in question here. **One of the factors considered in granting relief was that the forfeiture would have resulted in a substantial windfall to the landlord because it would result in significant realty improvements vesting in it 20 years earlier than what had been provided for in the**

> **lease;** see also ***Gentra Canada Investments Inc. v. 724270 Ontario Ltd.*** 1994 CarswellOnt 3852, aff'd 1995 CarswellOnt 3912. [paras 43-44] [emphasis added]

[38] In ***Rahawanji v. Gwendolyn Shop*** (1973) Ltd., 2011 ONCA 771, the ONCA upheld a denial of forfeiture relief, emphasizing a **non-timely application by the tenant, many months of overdue rent, and no evidence of "demise risk" to the tenant's business**:

> The appellants seek to set aside the order of Murray J. dismissing their application for relief from forfeiture in relation to their tenancies of two commercial leases in a small shopping plaza in downtown Oakville. Ms. Lev-Farrell **argues strongly on their behalf that the application judge erred in failing to take into account that relief from forfeiture is generally granted where all that is involved is the question of monetary arrears and in failing to address him mind to whether the default could be cured on terms in order to avoid the loss of their businesses.**
>
> **We do not agree.** Relief from forfeiture is a discretionary remedy and is not granted as a matter of course. As Doherty J.A. noted in *Ontario (Attorney General) v. 8477 Darlington Crescent*, 2011 ONCA 363, at para. 93, both in civil and criminal cases:
>
> > Relief from forfeiture is very much the exception and will be granted only where the party seeking that remedy clearly makes the case that forfeiture would be an inequitable and unjust order in all the circumstances.
>
> This is particularly so with respect to a commercial lease. Here, we are satisfied that the application judge considered the relevant circumstances and he was particularly entitled to take into account the fact that the appellants had **not proceeded to the hearing of the application in a timely fashion and that they had not paid any rent in the meantime in spite of the landlord's offer to accept payment on a without prejudice basis. There were arrears of seven month's rent at the time of the hearing. In addition, there is no evidence of any real prejudice to the appellants if relief from forfeiture is not granted in the sense that that, in itself, would result in the demise of their businesses**.
>
> Accordingly, we see no error in the exercise of the application judge's discretion and the appeal is dismissed. [emphasis added] [paras 1-4]

[39] In ***Ontario International College Inc v Consumers Road Investments Inc***, 2020 ONSC 6772, Schabas J. declined relief from forfeiture, finding **tenant shortcomings on all three key factors**:

> The **conduct of OIC has been unreasonable. It has missed payments or made payments that came back "NSF" throughout the tenancy. Understandings to make payment have been reached several times and then been breached by OIC**. This conduct pre-dates the COVID-19 pandemic and the tightening of currency controls by China, the latter of which is a business risk to be borne by the applicants. Promises have been repeatedly made and broken, including non-compliance with court orders since the commencement of the application.
>
> The gravity of the breaches is significant. The **amount not paid is substantial**. The **length of time these breaches have been continuing is also a consideration** in assessing the gravity of the breach. Furthermore, OIC has **failed to provide financial**

> **information, leading to the inference that it is not able to pay the amounts outstanding**. This is despite assertions made by Jiang in July that business prospects were expected to improve and that funds would be available to make payments of $300,000.00 and $150,799.77 in August.
>
> The respondent, on the other hand, has been patient and provided OIC, and OIT, many opportunities to bring rent payments into good standing, including during this litigation. It has taken steps to mitigate its losses by entering into a lease with another entity for a portion of the premises, but has been prevented from complying with that lease due to this application. This supports the conclusion that the **right of re-entry and forfeiture is not being exercised to secure the payment of money**; indeed, the respondent has provided OIC with access to the premises and the ability to remove its possessions and equipment.
>
> As to the **disparity, or proportionality, factor, while OIC claims it has invested approximately $1 million in improvements, it has failed to prove expenses of more than $200,000.00, and much of that is for equipment or other items that the respondent expects will be removed. On the other hand, as of August 1, 2020, OIC owed $450,779.77, an amount that has increased considerably since then. And the related company, OIT, which has abandoned its claim for relief, was in arrears in the amount of $517,695.86 as of August 1, 2020**.
>
> Accordingly, this is **not a case** like *Jungle Lion* where the **termination of the tenancy will have a disproportionate impact on the tenant such that the equities favour relief from forfeiture**. Unlike *Jungle Lion*, in this case the **tenant may not lose its entire investment in the property, court orders have already been issued and not been complied with, and the amount of the loss to the tenant is considerably smaller than the amount of rent outstanding**.
>
> In my view, therefore, the test for relief from forfeiture has not been met by OIC. [paras 39-44]

[40] In ***Jungle Lion*** (cited above), Morgan J. highlighted various tenant shortcomings (NSF rent cheque, failure to provide monthly sales reports, apparently causing a flood of the rental premises, and using fire-hazard heaters) but **nonetheless granted relief from forfeiture (on strict conditions), emphasizing the proportionality (otherwise-lost investment in leasehold improvements) factor**:

> In my view, the Plaintiff has done little to foster confidence in the Landlord or to prompt a court to invoke an equitable remedy on its behalf. That said, **if Justice Brown was correct that the Plaintiff stands to lose a $300,000 investment in the Premises, a termination of the tenancy will certainly have a disproportionate impact on it. It will effectively lose its entire investment in the Premises**. [para 21]

Covid-19 pandemic as a factor

[41] In ***2487261 Ont Corporation v 2612123 Ont Inc*** (cited above), Lemon J. restated the relief-from-forfeiture principles and granted relief, emphasizing (among other factors) **landlord-created-uncertainty over whether it was planning to seek relief under a government rental-assistance program**:

The parties agree that the necessary principles for me to apply with respect to granting such relief are set out in *Jungle Lion Management Inc. v. London Life Insurance Company,* 2019 ONSC 780 and *Michele's Italian Ristorante Inc. v. 1272259 Ontario Ltd.*, 2016 ONSC 4888. That is to say that I should consider:

1. The conduct of the applicant and gravity of the breaches;
2. Whether the object of the right of forfeiture in the lease was essentially to secure the payment of money;
3. The disparity or disproportion between the value of the property forfeited and the damage caused by the breach;
4. Whether the tenant comes to court with clean hands;
5. Whether there has been an outright refusal to pay rent;
6. Whether the rent has been in arrears for a short or long time; and
7. Whether the landlord has suffered a serious loss by reason of the moving party's delay in paying rent.

Given those factors and the circumstances in total, I find that Symphony is entitled to relief from forfeiture. I find that forfeiture would be an excessive remedy. I take into consideration the following factors.

Symphony [tenant] was reasonable in assuming that 261 was not expecting full payment of rent and was making application pursuant to the outstanding process. 261 was unreasonable in lulling Symphony into thinking that the rent was in abeyance or reduced.

While 261 was within its rights to not apply for the program, it was unreasonable to lull Symphony into thinking otherwise. Those circumstances were compounded by the inconsistent notices in early October. While I have no evidence of whether 261 was eligible for the program, in hindsight, it might have been well to do so. Even if I am wrong with respect to my finding above, if 261 did not agree, it showed bad faith in not making its intentions clear. In any event, Symphony showed good faith in making the payments it did in a time of pandemic. [paras 50-53] [emphasis added]

[42] In ***Hunt's Transport Limited v. Eagle Street Industrial GP Inc***., 2020 ONSC 5768 (Broad J. rejected a generalized invocation of the pandemic in a bid for forfeiture relief:

… the Tenant submits that the court **should take into consideration the Coronavirus pandemic currently impacting businesses across the world. It says that businesses which are ineligible for government assistance "should receive relief in the form of equitable solutions granted by the courts**." It relies upon the recent case of *The Second Cup v. 2410077 Ontario Ltd.*, 2020 ONSC 3684 at para. 58 in support of this submission.

I **do not accept the Tenant's submission that the effect of the COVID-19 pandemic is a relevant consideration in the circumstances of this case**. As indicated above, it advances the policy argument in its Factum that businesses such as it which do not qualify for rental reduction through government programs should receive equitable relief from the courts.

> In *The Second Cup* [cited below], Kimmel J. at para. 58 referred to the following circumstance as one of four which favoured the exercise of the court's equitable jurisdiction and discretion to grant relief from forfeiture to the tenant:
>
> In the midst of an unprecedented pandemic that shut down most of Second Cup's operations and the country's economy and had its senior management scrambling to negotiate with multiple landlords and franchisees over a short period of time, the landlord terminated the Lease for failure to pay 25.5% of one month's rent, totalling $4,527.55 in April 2020 and on the first business day after the May 2020 rent was due.
>
> This passage does **not support the broad policy proposition advanced by the Tenant in its Factum. It is simply an example of the court considering the relevant circumstances in applying the three factors from *Saskatchewan River Bungalows* and, in particular, the third factor which calls for a weighing of the impact of forfeiture on the tenant against the effect of the tenant's breach on the Landlord.**
>
> At paras. 86 to 91 of her Affidavit filed in support of the Application, Darlene Hilliard addressed the impact of the COVID-19 pandemic, deposing that "Hunt's has not been spared [from the economic downturn due to the pandemic] and we are facing significant issues and uncertainty." She offers **no particulars of the specific impact of the pandemic on the Tenant's business. It is evident that, as a commercial trucking/logistics company, it was not required to cease operations at any time since the onset of the pandemic.** [decision: temporary relief from forfeiture to give tenant a chance to clear arrears, with interest, within 20 days] [paras 68, 76-78, and 80] [emphasis added]

[43] In ***The Second Cup Ltd v 2410077 Ontario Ltd***, 2020 ONSC 3684, Kimmel J. granted relief from forfeiture, emphasizing these factors (including the pandemic's impact):

> The circumstances **favouring the exercise of the court's equitable jurisdiction and discretion to grant relief from forfeiture** to Second Cup include many of the circumstances described in paragraph 98 of Second Cup's factum and address all of these three criteria, namely that:
>
> (a) **In the midst of an unprecedented pandemic that shut down most of Second Cup's operations and the country's economy** and had its senior management scrambling to negotiate with multiple landlords and franchisees over a short period of time, **the landlord terminated the Lease for failure to pay 25.5% of one month's rent, totalling $4,527.55 in April 2020 and on the first business day after the May 2020 rent was due**.
>
> (b) Second Cup **had been a tenant at the premises for 10 years** and had recently signed an extension for an additional 10 to 20 years and made payments to the landlord in excess of $50,000.00 in addition to paying rent for the month of March 2020.
>
> (c) The **demands of the landlord preceding its re-possession of the premises and termination of the Lease had been focussed on the payment of past and future rent**.

(d) The plaintiffs' uncontested evidence is that the RSA application and the planned cannabis shop at the premises are of the utmost importance to them and the **termination of the Lease could jeopardize not only the licence for the premises but the licences for their other proposed locations as well, which they value at well in excess of the rent arrears at issue**.

The landlord defendants argue that when a party seeks to be relieved from forfeiture based on a non-payment of rent the court should consider criteria from *Michele's Italian Ristorante Inc. v. 1272259 Ontario Ltd.*, 2016 ONSC 4888, at paras. 35-36. In that decision, the court set out criteria for relief from forfeiture generally at para. 35, and separate, more specific criteria at para. 36, **where the alleged default is based upon the non-payment of rent:**

(a) the tenant comes to court with clean hands;

(b) whether there is an outright refusal to pay rent;

(c) the extent of the rental arrears; and

(d) whether the landlord has suffered serious loss due to the delay in paying rent.

See also: *2324702 Ontario Inc. v. 1305 Dundas*, 2019 ONSC 1885, aff'd 2020 ONCA 353.

I have considered these additional factors, and they all favour the plaintiffs.

(a) The fact that there was **one prior dispute in 2015 about the payment of rent that led to an amendment to the Lease does not suggest a pattern of default or lack of clean hands. The rental arrears were not significant as of the beginning of May, especially when considered in light of what was happening in the world as a result of the COVID-19 pandemic**.

(b) **Nor was the March 25 letter from Second Cup indicating that it and its franchisees would not be able to pay April rent on the first of the month an outright refusal to pay rent** as the landlord defendants suggest. It was a reasonable and transparent communication to landlords by a responsible corporate tenant of numerous premises across the country.

(c) Further, the **landlord defendants claim that they have significant mortgage carrying costs but have not put in any evidence about actual prejudice that they have suffered as a result of not having been paid the balance of April's rent and May's rent under the Lease**. [paras 58-60] [emphasis added]

Key factors here

[44] Applying the guidance of the above cases, these are the key factors here:

- **reasonableness of the tenant's actions:**

- the tenant was admittedly **haphazard in paying its rent** from summer 2018 through until April 2020, as reflected in the landlord's rent ledger. However, at various points, it **squared up its arrears**, bringing its rental account current in October 2018, January 2019, November 2019, December 2019, January 2020, February 2020, March 2020, and April 2020, aside from making other rental payments along the way. While the landlord frequently had to demand rent payments via letter, it was **not required to commence legal proceedings or otherwise step up enforcement, until the fall of 2020**. As far as I can tell, the **landlord effectively acquiesced to the tenant's haphazard payments** and, in any case, was made whole as late as April 2020;
- from that point, **rental arrears began accumulating again**, up to approximately $15,000 by early September. But the larger context is important here, in understanding how and why those initial arrears came about. In early May 2020, the tenant emailed the landlord's agent requesting (in part):

  > Please review the attached **Government announcement in relation to [presumably Covid-19-related] rent subsidies**. [A tenant contact] indicated that she made full payment for April rent. With that payment we are **satisfying our portion for May and June's rent**. Please note that July's rent will be discounted by 25% due to overpayment. …

- in other words, proceeding on assumptions that the landlord had decided, or would decide, to participate in a government rent-subsidy program and that the tenant's rent would effectively be reduced to one-quarter of standard rent, **the tenant decided to treat its April rent payment as satisfaction of its (perceived) 25 per cent rent obligation for April, May, June and July**. As it turned out, with the program in question being voluntary and requiring (at minimum) landlord participation, the tenant's "only one-quarter payment" proposal was **premature**. But the point here is that the tenant was proceeding on **an apparently good-faith basis (and the landlord did not shake that appearance on cross-examination of the tenant's representative) that a government rent-subsidy program was applying or would apply** i.e. these spring and summer 2020 rent payments were **not arbitrarily or randomly reduced**;
- interestingly, the landlord's only apparent response (or non-response) was a May 20, 2020 letter demanding payment of $1,885.36 (rent and related amounts due May 1, 2020). However, the letter made **no reference to the tenant's May 6 email asking the landlord to review the government rent-subsidy announcement**. And the landlord's next demand letter was not sent until on or around July 13 (demanding May, June and July 2020 rent payments totalling approximately $5,500). It too **did not make any reference to the tenant's "please review rent subsidy program" request**. In other words, with its May letter, the landlord left the **reasonable impression that it had not yet received, or at least**

processed, the tenant's request that it consider the rent-subsidy program. And the lack of any communication at all from the landlord for the rest of May, for June, and the first half of July 2020 did nothing to dispel that impression i.e. that the tenant's "please review program" request was **alive or at least had not been rejected**;

- this is reflected in the tenant's July 26, 2020 email to another of the landlord's agents, stating (in part): "I am forwarding my May 6, 2020 email … which is self-explanatory. I will also forward you additional Government press released for July rent on a separate email for you tomorrow." At that stage, and despite the landlord's May 6 and July 13 letters (again, making no mention of the rent-subsidy program), the **tenant still reasonably, or perhaps naively, understood that the landlord was participating, or would participate, in the program**;
- it was not until August 7, 2020 that the landlord's agent advised (in part): "The Landlord will not be applying for the CERCA program. The option to open for take-out and pick-up services was available for restaurants early on in this Covid pandemic." In other words, for the first time, the landlord addressed the tenant's request to examine the rent-subsidy program and advised it was not participating. The point here is not that the landlord was obliged to participate in that program (it was not); it is that **the landlord allowed the tenant to believe or at least hope that the landlord was participating, or would participate, for the months of May, June, July and August 2020**;
- the tenant's representative gave evidence on cross-examination that, even after receiving that notice, he was still not sure that the landlord was not participating. His explanation was that he was not sure that the landlord's agent actually spoke for the landlord. I find his **explanation somewhat puzzling** and do not place any weight on it. As I see it, by mid-August, the tenant knew, or should reasonably, have known, that the landlord was not participating in the program. This is borne out in his August 16th and 28th messages effectively acknowledging the landlord's decision;
- per the landlord's rental ledger, the rental tab was approximately $5,700 by the end of July 2020, against which the tenant had paid $1,885 (i.e. the "allocated against four months" payment in early April) i.e. the **tenant had paid approximately one-third of what it assumed was owing (i.e. if the rent-subsidy program applied) i.e. more than its perceived "25 per cent" share**;
- then **August and September rents came due, plus a common-property-area charge of approximately $5,000**. At the end of August, the tenant sent another email to the landlord's other agent, stating (in part):

> Responding to your recent [August 19, 2020 email confirming the landlord was not participating in the rent-subsidy program], please note that the rent for April, May, June and July are covered 75% by Government and 25% by tenant (according to the government

> initiative and rule). As you notice, under this rule, the Landlord gets 100% rent. [Actually, the program called for landlords to bear 25% of the weight i.e. forego that percentage of the rent.] Attached I am sending you a copy of our mailed cheque. This cheque covers the **rent for the months of August and September**. Our solicitor will be handling the rent for the above-noted months [i.e. May-July] accordingly.

- the rent ledger indeed reflects **receipt of a $3,770.70 cheque** in early September, which represents the August and September 2020 rental payments;
- however, even with that payment, the combined effect of the underpaid May-August rents, plus the common-property-area payment was **arrears of approximately $11,000 as of early September, which grew, with October, November and December 2020 rents, to approximately $15,500 by the time of termination**. (The tenant made one other payment ($942.97) that fall, on November 2, 2020);
- as for the **reasons for the latter defaults**, the tenant's representative gave evidence (December 15, 2020 affidavit, para 6) that:

> During the COVID-19 pandemic in 2020, and having its greatest economic effect beginning in April 2020, the [tenant] suffered a decrease in revenues and even with the reduction in revenue the [tenant] kept all staff employed and the [tenant's] proprietors paid the shortfalls personally to keep the business alive;

- on cross-examination, that witness was simply asked (on this subject):

  [QUESTION] Okay. And you've indicated that Mimi's revenues went down following the COVID pandemic. Does Mimi's keep track of its monthly revenues?

  [ANSWER] Absolutely.

  [QUESTION] Okay. So, you could determine on a month-by-month basis for each month since you've been open what your revenues are?

  [ANSWER] Correct.

  [QUESTION] Okay. And you could determine that after, I guess, March of [2020] when the pandemic sort of started, the first shutdown and the subsequent shutdowns, you could show me exactly what the dollar amount was in each month and the difference between the year previous.

  [ANSWER] Absolutely.

- the landlord did not actually ask for the revenue figures, presumably satisfied that, on the injunction aspect, the tenant had conceded its losses could be quantified. The key here is that the landlord did **not challenge the tenant's evidence that its revenues deteriorated throughout, and because of, the pandemic**;

- in the end, the landlord's "terminating lease" letter (December 7, 2020) outlined total accumulated arrears of $15,590.50. On December 10, 2020, the tenant **delivered a cheque for that amount to the landlord** "which brings the lease into good standing", which the landlord refused to accept on that (lease-in-good-standing) condition and which it has still yet to cash;
- **conclusion on reasonableness of the tenant's actions**: the tenant's actions were not perfect by any stretch, but in all the circumstances, they were reasonable or were at least not so unreasonable as to weigh heavily against the tenant here. Fundamentally, this dispute is about **unpaid rentals i.e. not other lease breaches**. Some of the arrears accrued during a period when the **tenant plausibly understood that a rent-subsidy program was operating or would operate**. Even in that period, the tenant paid its **perceived appropriate rent**. After the tenant learned that the landlord was not participating, it paid its **full August and September 2020 rent**, albeit not the common-property-area charge, and it defaulted on October, November, and December rent. But this was in the **depths of the pandemic, when it is common knowledge that restaurants were almost universally hard hit by decreased patronage and decreased service capacity**, which the tenant's evidence confirmed. And, admittedly post-termination, the tenant **tendered the full amount of the rental arrears** (albeit on the condition that the lease would be reinstated). In all these circumstances, I cannot conclude that the tenant's actions were fundamentally unreasonable;

- **gravity of the tenant's breaches**: this somewhat overlaps with the "reasonableness" review. The tenant allowed rental arrears to accrue up to approximately $15,500, representing approximately five months rent, plus common-property-area costs. But, as noted, the tenant tendered the full amount of the arrears i.e. the landlord would be whole if it cashed the December 10th cheque.

  The landlord **did not point to other adverse consequences or other (non-rent) lease breaches** or at least **did not detail them**. (The landlord gave evidence (January 6, 2021 affidavit, para 4) that "Mimi's failure to pay its obligations caused difficulties for [the landlord] to pay its obligations", but it provided no details of those difficulties.)

  The landlord acknowledged that the rental amount charged to the tenant was "significantly below typical market rates", in light of "certain [leasehold] improvements" made by the tenant (discussed further below). Presumably, the landlord could rent the premises to another tenant at a significantly higher rate; but (per the analysis of Bielby J. (as she then was) in ***BMO v Phoenix Rotary*** (cited above)), that is not a consideration in the forfeiture analysis.

  I conclude that, while the rental arrears accumulated to a material amount, the **tendering of the full arrears, within three days of termination (and**

admittedly coming too late to prevent termination) effectively counters the gravity of the rent-payment breaches.

- **proportionality factor**: here the tenant stressed its **investment of approximately $950,000 to rehabilitate what the landlord admitted was a "dilapidated" and "in disrepair" vacant building**, making it suitable for a restaurant. The landlord's witness stated she had "no idea" how much the tenant had actually invested to rehabilitate the building and outfit it for its restaurant. She said "I have never seen his invoices. It could be $9,000. It could be $900,000. I have not seen a single thing."

  As I understand it, it was a **sore point** between the landlord and the **tenant that the latter did not provide sufficient or timely (or both) documentation of its construction costs to the landlord to allow it to access certain municipal grants** for building-façade improvements. That is one reason why the landlord alleges uncertainty over the tenant's actual costs.

  The tenant's witness gave this evidence (December 15, 2020 affidavit, para 5):

  > The [tenant] built the restaurant, including the building, on the Commercial Space, and the **approximate cost to the [tenant] to complete the construction was $950,000** CAD, which was paid by the [tenant]. As such, the [tenant] has invested a significant sum in the improvement of the Commercial Space. Furthermore, **$300,000 of the aforementioned amount has been spent on behalf of the [landlord], by the [tenant], whereby the [landlord] agreed to repay this amount through a rent reduction program** by September 14, 2025 as outlined as a rent reduction at the top of page 6 of the Lease Agreement.

  Here is the cross-examination on that evidence:

  QUESTION: I understand you have indicated … that Mimi's completed construction of the restaurant prior to opening and that the cost of that was in the range of $950,000 ….

  ANSWER: Correct.

  QUESTION: Could you provide invoices in relation to the amount spent by Mimi's improving … the restaurant?

  ANSWER: That would be no problem.

  As far as I can tell, that dialogue did not **crystallize into a formal undertaking** or at least one recorded as such in the cross-examination transcript. I do not know whether the landlord followed up on its request.

  However, during his submissions at the application, the landlord's counsel commented, as part of his submissions on irreparable harm (injunction issue):

  > What my friend's brief has said, as well as mine, is that a party's **monetary loss or significant expenditure will usually not amount to irreparable harm**. In this case, the evidence that we have comes from Mr. Rahmani [tenant's witness] and it is one paragraph in his affidavit,

> paragraph 21, and what he said is the irreparable harm here is money that was spent on construction. So, he has actually defined it in a number of different places [including para 5 of his affidavit, as reproduced above], and **my friend has argued "it is $950,000." We did not see any receipts or anything, but, you know, it is a defined dollar amount**. By its nature, this is expressly quantified – "We know down to the dollar, this is how much money I am losing here". So, this is clearly not irreparable.

In light of the landlord's approach here (effectively taking the tenant's construction-costs evidence at **face value**), and (as I recall) having heard **no complaints from the landlord at the application about non-production of construction receipts**, and noting a landlord acknowledgment, during questioning, that the construction of Mimi's Restaurant was "a **major undertaking**" and again the above-noted acknowledgments that the building was **previously dilapidated and in disrepair**, and also noting landlord evidence that "We have provided [the tenant] **very, very cheap rent in return for him going to get the [municipal] grant, in return for his investment in the building**", I am prepared to accept the tenant's evidence of $950,000 in construction costs.

If those factors are insufficient to anchor that finding, I also cite this lease description of required improvements to the rented premises (Schedule C, including "Lessee's Work) (in part):

> The Lessee accepts the premises "as is" and shall be responsible for **all construction (including structural and roofing elements required), improvements and renovation costs in order to complete the demised premises as a neighbourhood pub.** …
>
> The Lessee shall be responsible for the ceiling make-up unit for the demised premises. Lessee will have the **sprinkler systems re-routed, electrical, heating / ventilation, and plumbing installed** to accommodate the appropriate building code in common and staff areas. …
>
> The Lessee shall be responsible for **interior demolition of the space removing all interior demising walls**, drywall (including ceiling) and floor coverings, **replacing overhead garage doors and all other panel glass/plexiglass with new panel glass** … and concrete backfilling/levelling of the floor drain area ….
>
> The Lessee shall be responsible for the installation of **new rooftop mechanical HVAC units and make-up air unit** as required ….
>
> The Lessee shall have a **new roof installed and complete necessary structural work to the roof rafters and sheeting system** …. [emphasis added]

I take **judicial notice** that work on this scale obviously required the investment of **hundreds of thousands of dollars**.

The tenant's witness referred to a lease for 28 years (from 2017). But the lease is actually for 144 months i.e. 12 years i.e. until 2029, with an option for a further ten years.

The lease began in late February 2017 i.e. has been running for **just over four years**, with a **further eight years to run** (and possibly longer, if restored and if the tenant meets its ongoing obligations and the preconditions for renewal).

I conclude, on **proportionality**, that forfeiture of the lease at this point would **cost the tenant its very substantial investment in building rehabilitation and leasehold improvements and deprive it of its negotiated-for opportunity to recoup that investment over the lifespan of the lease**, including through the acknowledged-by-the-landlord less-than-market-value rent. Such forfeiture would be **completely out of proportion to the consequences, to the landlord, of the above-described rent-payment breaches.**

- **other "relief from forfeiture" factors:**
    - the tenant did not delay unduly here, tendering the rental arrears within three days of the termination and, when that did not move the landlord to reinstate the lease, applying for, and obtaining, an interim injunction to get the tenant back into the premises eight days after that (on December 18, 2020);
    - while it is not crystal-clear from the cross-examination of the tenant's witness, it appears that the tenant has paid the required rent and associated payments since regaining occupancy of the restaurant on an interim basis, pursuant to the interim injunction granted by Friesen J. on December 18, 2020 and continued by me at the March 19, 2021 application until (at minimum) release of this decision; and
    - I saw no evidence that the landlord has taken any steps, even tentative, to lease the premises to another tenant.

D. Conclusion

[45] For all these reasons, I confirm that the landlord validly terminated the lease and that injunctive relief is not available to reverse that termination; however, I find that the tenant is entitled to relief from forfeiture, on the following terms:

- payment of the arrears through to December 10, 2020 ($15,590.50), which the tenant has already tendered (as noted), via the landlord cashing the cheque it has been holding;
- if any rent arrears have accrued since that date, clearance of those arrears in full by no later than April 9, 2021; and
- payment of any April 2021 rent payment(s) due April 1st by the end of today.

[46] If the parties require clarification of these terms, I invite them to contact me via my assistant.

[47] If the parties are unable to agree on costs, their respective submissions (three-page maximum) are due by April 30, 2021.

[48] I thank the parties for their helpful briefs and oral submissions.

Heard via WEBEX on the 19th day of March, 2021.
Dated at the City of Edmonton, Alberta this 1st day of April, 2021.

M. J. Lema
J.C.Q.B.A.

Appearances:

Robert W. Hladun, Q.C.
Hladun & Company
Barrister's and Solicitors
for the Applicant/Cross-Respondent

Raymond Bastedo
DLA Piper (Canada) LLP
Barristers and Solicitors
for the Respondent/Cross-Applicant

TAB 15

IN THE SUPREME COURT OF BRITISH COLUMBIA

Citation: ***MTK Auto West Ltd. v. Allen,***
2003 BCSC 1613

Date: 20031023
Docket: S80205
Registry: New Westminster

Between:

MTK Auto West Ltd. doing business as MINI Richmond

Plaintiff

And

Cheryl Allen

Defendant

Before: The Honourable Madam Justice Kirkpatrick

(In Chambers)

Reasons for Judgment

Counsel for the plaintiff:	J.L. Randall
Counsel for the defendant:	J.S. Mackoff
Date and Place of Hearing:	October 1, 2003 New Westminster, B.C.

[1] The defendant, Cheryl Allen, applies under Rule 18A for a declaration that the plaintiff, MTK Auto West Ltd. ("MTK"), suffered no loss for which the plaintiff is lawfully entitled to compensation. Alternatively, the defendant seeks a declaration that the clause under which the plaintiff seeks damages is unenforceable as a penalty.

[2] The facts are not in serious dispute.

[3] In January 2002, MTK entered into a distributor's agreement with BMW Canada. Under that agreement, MTK agreed that it would not sell vehicles to a purchaser if it knew or ought to have known that the "direct or indirect purchaser resides outside Canada or intends to export the vehicle from Canada." In the event of a breach of that term of the distributor's agreement, MTK was liable to pay MINI Canada (a division of BMW Canada) the difference between the retail price of the vehicle and the effective wholesale value of the vehicle, including any taxes.

[4] The defendant was sometimes employed to drive vehicles bought in Canada to the United States for resale. On February 6, 2002, Ms. Allen ordered a vehicle from MTK and paid a $1,000 deposit. As part of the transaction, she signed a standard form "MINI Non-Export Agreement", the terms of which provided, in part, as follows:

> IN CONSIDERATION of the intended sale of the vehicle to the Customer and other good and valuable consideration, the sufficiency of which is hereby acknowledge, the Customer agrees and acknowledges that:
>
> 1. This Agreement forms an integral part of the agreement of purchase and sale of the Vehicle between the Retailer and the Customer;
>
> 2. The Vehicle is not purchased by the Customer for export purposes;
>
> 3. The Customer will not, within twelve (12) months of delivery, either directly or indirectly, export the Vehicle, or permit the Vehicle to be exported, from Canada without the express written consent of MINI Canada;
>
> 4. The Customer will not, within twelve (12) months of delivery, either directly or indirectly, enter into or acquiesce in any agreement whereby the Vehicle is leased or sold for use outside of Canada;
>
> 5. The Customer will indemnify and save the Retailer harmless of and from any loss arising out of, under or pursuant to any breach of the obligations set forth in this Agreement; and
>
> 6. In lieu of this indemnity set forth in Section 5 above, the Retailer may claim, in its sole discretion, liquidated damages from the Customer in the amount of Ten Thousand Dollars ($10,000.00) for any breach of this Agreement and the Customer agrees to pay this amount. The liquidated damages are not a penalty and represent a genuine estimate of damages that the Retailer would suffer in the event of the export of the Vehicle.

[5] As a condition of the sale, BMW Canada required that the purchaser sign the MINI Non-Export Agreement.

[6] On April 24, 2002, MTK sold and delivered a vehicle to Ms. Allen for $28,295. A third party provided all of the purchase price funds to Ms. Allen. MTK's profit on the transaction was $2,850. Ms. Allen knew that the vehicle was going to be exported to the United States at the time she picked up the vehicle from MTK on April 24, 2002. However, MTK did not know, nor is there any evidence that it should have known, that Ms. Allen, or those who financed the purchase, intended to export the vehicle.

[7] The parties agree that the vehicle found its way to a purchaser in the United States.

[8] BMW Canada, in the exercise of its purported right under the distributorship agreement, placed a charge back on MTK for its $2,850 profit on the sale to Ms. Allen.

[9] The defendant argues that BMW Canada unlawfully extracted a charge back to which it was not entitled and consequently MTK has not suffered any loss at law for which MTK is entitled to compensation.

[10] I note first that BMW Canada is not joined in this action and was not represented, or indeed given notice of the defendant's motion. Counsel for Ms. Allen was candid in advising the court that Ms. Allen had considered joining

BMW Canada to the action but, for reasons not elaborated upon, she had not done so.

[11] On that ground alone, I would not grant the first declaration sought by the defendant.

[12] Furthermore, the evidence establishes that, rightly or wrongly, BMW Canada levied a $2,850 charge back on MTK and MTK is out-of-pocket that amount. The evidence also discloses that the president and director of MTK, Joachim Neumann, protested the charge back, but was advised by BMW Canada that it had grounds for the charge back and was, in Mr. Neumann's words, "standing behind the wording of the dealer agreement". Mr. Neumann testified that he ultimately acceded to the charge back because he was concerned about BMW Canada cancelling his franchise.

[13] Absent evidence and argument from BMW Canada with respect to whether or not the charge back to MTK is lawful, I will not declare that MTK has suffered no loss to BMW Canada for which MTK is lawfully entitled to compensation.

[14] There remains to be considered the alternative question, namely whether the clause under which MTK seeks damages is unenforceable. MTK seeks judgment against Ms. Allen for $10,000 in liquidated damages. The statement of defence

alleges, among other things that are specifically excluded from the Rule 18A summary trial, that the claim for liquidated damages is in fact a penalty.

[15] The law in this area is well-settled. Lord Dunedin, in ***Dunlop Pneumatic Tyre Co. Ltd. v. New Garage and Motor Co. Ltd.***, [1915] A.C. 79 (H.L.), which was accepted in Canada in ***H.F. Clarke Ltd. v. Thermidaire Corp. Ltd.***, [1976] 1 S.C.R. 319, states at p. 86-88:

> In view of that fact, and of the number of authorities available, I do not think it advisable to attempt any detailed review of the various cases, but I shall content myself with stating succinctly the various propositions which I think are deducible from the decisions which rank as authoritative:-
>
> 1. Though the parties to a contract who use the words "penalty" or "liquidated damages" may prima facie be supposed to mean what they say, yet the expression used is not conclusive. The Court must find out whether the payment stipulated is in truth a penalty or liquidated damages. This doctrine may be said to be found passim in nearly every case.
>
> 2. The essence of a penalty is a payment of money stipulated as in terrorem of the offending party; the essence of liquidated damages is a genuine covenanted pre-estimate of damage (*Clydebank Engineering and Shipbuilding Co. v. Don Jose Ramos Yzquierdo y Castaneda*, [1905] A.C. 6).
>
> 3. The question whether a sum stipulated is penalty or liquidated damages is a question of construction to be decided upon the terms and inherent circumstances of each particular contract, judged of as at the time of the making of the contract, not as at the time of the breach (*Public*

Works Commissioner v. Hills, [1906] A.C. 368, and *Webster v. Bosanquet*, [1912] A.C. 394).

4. To assist this task of construction various tests have been suggested, which if applicable to the case under consideration may prove helpful, or even conclusive. Such are:

(a) It will be held to be penalty if the sum stipulated for is extravagant and unconscionable in amount in comparison with the greatest loss that could conceivably be proved to have followed from the breach. (Illustration given by Lord Halsbury in *Clydebank Case*, [1905] A.C. 6).

(b) It will be held to be a penalty if the breach consists only in not paying a sum of money, and the sum stipulated is a sum greater than the sum which ought to have been paid (*Kemble v. Farren* 6 Bing. 141). This though one of the most ancient instances is truly a corollary to the last test. Whether it had its historical origin in the doctrine of the common law that when A. promised to pay B. a sum of money on a certain day and did not do so, B. could only recover the sum with, in certain cases, interest, but could never recover further damages for non-timeous payment, or whether it was a survival of the time when equity reformed unconscionable bargains merely because they were unconscionable, - a subject which much exercised Jessel M.R. in *Wallis v. Smith*, 21 Ch. D. 243 – is probably more interesting than material.

(c) There is a presumption (but no more) that it is penalty when "a single lump sum is made payable by way of compensation, on the occurrence of one or more or all of several events, some of which may occasion serious and others but trifling damage" (Lord Watson in *Lord Elphinstone v. Monkland Iron and Coal Co.*, 11 App. Cas. 332).

On the other hand:

(d) It is no obstacle to the sum stipulated being a genuine pre-estimate of damage, that the consequences of the breach are such as to make precise pre-estimation almost an impossibility. On

> the contrary, that is just the situation when it is probable that pre-estimated damage was the true bargain between the parties (*Clydebank Case*, Lord Halsbury, [1905] A.C. at p. 11; *Webster v. Bosanquet*, Lord Mersey, [1912] A.C. at p. 398).

[16] In ***Thermidaire***, *supra*, Laskin C.J.C. stated the court's finding on the point at p. 338:

> I regard the exaction of gross trading profits as a penalty in this case because it is, in my opinion, a grossly excessive and punitive response to the problem to which it was addressed; and the fact that the appellant subscribed to it, and may have been foolish to do so, does not mean that it should be left to rue its unwisdom. *Snell's Principles of Equity* (27th ed. 1973), at p. 535 states the applicable doctrine as follows:
>
> > The sum will be held to be a penalty if it is extravagant and unconscionable in amount in comparison with the greatest loss that could conceivably be proved to have followed from the breach.

[17] Having regard to the principles stated above, it is obvious that the sum claimed by MTK is a penalty. First, MTK gave no consideration to any potential loss at the time it made the contract with Ms. Allen. The MINI Non-Export Agreement formed part of the transaction only because BMW Canada would not process the sale without it in place. Second, under the terms of its distributor's agreement with BMW Canada, the most MTK would be obliged to pay was the difference between the retail and effective wholesale price of

the vehicle. In this instance that sum was $2,850. MTK now claims more than three times the amount of the greatest loss that could have been contemplated at the time it entered the contract. Although MTK acceded to the payment of the charge back to preserve the franchise, it is not a plausible inference that potential loss of the franchise was a consideration in stipulating the liquidated damages amount in the MINI Non-Export Agreement.

[18] MTK argued that, even if the sum claimed is found to be a penalty, the court must go on to consider whether the penalty is oppressive, relying on the decision in ***Volvo Truck Finance Canada Ltd. v. Premier Pacific Holdings Inc.***, [2002] B.C.J. No. 1768 (S.C.) (QL).

[19] There is higher authority for the proposition put forward by MTK. In ***Elsley v. J.G. Collins Ins. Agencies Ltd.***, [1978] 2 S.C.R. 916, the Supreme Court of Canada held at p. 937:

> It is now evident that the power to strike down a penalty clause is a blatant interference with freedom of contract and is designed for the sole purpose of providing relief against oppression for the party having to pay the stipulated sum. It has no place where there is no oppression.

[20] Where a party seeks relief from a penalty, the factors to be considered by the court include the conduct of the applicant, the gravity of the breach, and the disparity

between the value of the property forfeited and the damage caused by the breach: ***Shiloh Spinners Ltd. v. Harding***, [1973] A.C. 69 (H.L.).

[21] The assessment of oppression was addressed in ***Dimensional Investments Ltd. v. Canada***, [1968] S.C.R. 93, which sets out a broad framework in determining whether a penalty clause is or is not oppressive, or as Ritchie J. asks, whether it would be unconscionable for the party who claims the penalty amount to retain the money. Ritchie J. states at p. 101 that "the question of unconscionability must depend upon the circumstances of each case at the time when the clause is invoked" rather than on the agreement itself, which is the difference between the characterization of the clause as being a penalty in the first place versus its being oppressive.

[22] A court should not strike down a penalty clause as being unconscionable lightly because it is a significant intrusion on freedom of contract. There must be clear evidence of oppression for the court to intrude (see ***32262 B.C. Ltd. v. See-Rite Optical Ltd.***, [1998] A.J. No. 312 at ¶ 13 (C.A.) (QL)).

[23] The factors that are relevant to the assessment of oppression in the case at bar include:

(a) Both parties are sophisticated clients (see ***Edmonton (City) v. Triple Five Corp.*** (1994), 158 A.R. 293 at ¶ 74 (Q.B.)).

(b) MTK was not genuinely concerned with whether or not the vehicles it sold were to be exported; rather this was a concern of BMW Canada (see ***Edmonton (City)***, *supra*, at ¶ 74).

(c) $10,000 is over three times more than MTK's greatest loss - $2,850 (see ***Ashland Scurlock Permian Canada Ltd. v. NESI Energy Marketing Canada Ltd.*** (1998), 226 A.R. 242 at ¶ 11 (Q.B.)).

(d) Ms. Allen knowingly breached the contract and in fact intended to do so before signing the contract (see ***Vohra Enterprises Ltd. v. Creative Industrial Corp.*** (1988), 23 B.C.L.R. (2d) 394 at ¶ 11-12 (S.C.)).

[24] The last factor is the most problematic because granting relief from the application of a penalty clause or from forfeiture is an exercise of the court's equitable jurisdiction and equity makes much of "clean hands". However, the maxims of equity are "not to be taken as positive laws of equity which will be applied literally and relentlessly in

their full width but rather as trends or principles" (see John McGhee, ed., *Snells's Equity*, 13th ed. (London: Sweet & Maxwell, 2000) at ¶ 3-01). With respect to the clean hands principle specifically:

> what bars the claim is not a general depravity but one which has an 'immediate and necessary relation to the equity sued for,' and is not balanced by any mitigating factors. [at ¶ 3-15]

Ms. Allen's "depravity" is related to the clause from which she seeks relief.

[25] ***Vohra***, *supra*, referred to ***Pam-Cor Investments Ltd. v. Friends and Neighbours Family Restaurant Ltd.*** (1987), 12 B.C.L.R. (2d) 387 (C.A.), where the court refused to grant relief from forfeiture of a lease because the claimant had deliberately breached the lease agreement. The lease stated that the claimant was to operate a restaurant on the premises under a particular name but could not use the space for any other purpose and the claimant operated a restaurant under a different name. The ***Pam-Cor*** case was referred to in ***5000 Kingsway Ltd. v. F & A Enterprises Ltd.*** (1994), 36 R.P.R. (2d) 140 (B.C.S.C.), as well, where the claimant wanted relief from forfeiture of a lease where it had not paid rent for several months. Hogarth J. distinguished ***Pam-Cor*** on the basis that in ***Pam-Cor*** the breaches were non-financial and the lessor

suffered serious prejudice. In this case, MTK has not suffered serious prejudice but the breaches are non-financial and premeditated.

[26] I have already concluded that the amount of the penalty is too remote from the actual or contemplated damage that MTK could have suffered. The fact that MTK knew or was capable of calculating its potential loss brings the penalty within the ambit of what is oppressive or unconscionable, even though there is force to MTK's argument that Ms. Allen knew the financial consequences of breaching the MINI Non-Export Agreement and the court should not interfere with that bargain. To enforce the clause would permit MTK to recover a bonus of $7,150 more than the $2,850 it was potentially liable to pay BMW Canada. Furthermore, MTK had no interest in preventing the export of vehicles, other than to avoid the charge back from BMW Canada. The only entity apparently concerned with export was BMW Canada, which is not a party to the MINI Non-Export Agreement or this action. Thus, any damages which flowed from the export of the vehicle (apart from the $2,850) was damage to BMW Canada, not to MTK.

[27] I want to make clear that I am in no way condoning or excusing Ms. Allen's behaviour in refusing to uphold the penalty clause. Her deliberate and calculated breach of the

MINI Non-Export Agreement deserves censure. However, there is authority stating that the fact that a party does not have clean hands does not remove the court's discretion to grant equitable relief (see ***Asfordby Storage and Haulage Ltd. v. Bauer***, [1989] O.J. No. 2614 (H.C.)). Having regard to all the relevant factors, this is an appropriate case to exercise my discretion.

[28] I therefore conclude that, although parties to a contract ought generally to be held to their bargains, to enforce the penalty clause at bar would, in all the circumstances, be unconscionable.

[29] However, notwithstanding my conclusion that the liquidated damages clause is an unenforceable penalty, there is sufficient evidence to make a damage award in favour of MTK. Section 24 of the ***Law and Equity Act***, R.S.B.C. 1996, c. 253 states that:

> The court may relieve against all penalties and forfeitures, and in granting the relief may impose any terms as to costs, expenses, damages, compensations and all other matters that the court thinks fit.

Therefore, the court may relieve a party from compliance with a penalty clause on the condition that she pay another proven sum of damages (see ***Elsley***, *supra* at 937). This option is

only open to the court when it substitutes an amount that is lower than the penalty amount, as in the case at bar. The evidence establishes that MTK is out-of-pocket $2,850 as a result of Ms. Allen's breach and MTK should be compensated by Ms. Allen in that amount.

"P.A. Kirkpatrick, J."
The Honourable Madam Justice P.A. Kirkpatrick

TAB 16

Date: 20100628
Docket: CI 08-01-57939
(Winnipeg Centre)
Indexed as: Pioneer Hi-Bred International, Inc.
v. Richardson International Limited
Cited as: 2010 MBQB 161

COURT OF QUEEN'S BENCH OF MANITOBA

BETWEEN:	)	**APPEARANCES:**
	)	
PIONEER HI-BRED INTERNATIONAL, INC. and PIONEER HI-BRED LIMITED,	)	Michael D. Manson, Karen F. MacDonald and Michael G. Finlayson
Plaintiffs/Defendants by Counterclaim,	)	for the Plaintiffs/Defendants by Counterclaim
	)	
- and -	)	
	)	E.W. Olson, Q.C. and Sarantos Mattheos
RICHARDSON INTERNATIONAL LIMITED (formerly JAMES RICHARDSON INTERNATIONAL LIMITED), and RICHARDSON PIONEER LIMITED (formerly PIONEER GRAIN COMPANY, LIMITED),	)	for the Defendants/Plaintiffs by Counterclaim
	)	
Defendants/Plaintiffs by Counterclaim.	)	Judgment delivered: June 28, 2010

JOYAL, A.C.J.Q.B.

INTRODUCTION

[1] This is a motion for summary judgment brought by the defendants/plaintiffs by counterclaim, RICHARDSON INTERNATIONAL LIMITED (formerly JAMES RICHARDSON INTERNATIONAL LIMITED) and RICHARDSON

PIONEER LIMITED (formerly PIONEER GRAIN COMPANY, LIMITED), hereinafter collectively referred to on this motion as "PGCL". The responding parties on this motion are the plaintiffs/defendants by counterclaim, PIONEER HI-BRED INTERNATIONAL, INC. and its wholly owned subsidiary PIONEER HI-BRED LIMITED, hereinafter collectively referred to on this motion as "PHI".

[2] This motion arises out of a dispute between the two companies in connection with the termination by PHI of the 1996 cross-license agreement which regulated the use of the trademark "PIONEER".

The Main Action

[3] The main action commenced on August 28, 2008 when PHI filed in this court, a statement of claim alleging breach of contract. PHI has launched a parallel action in the Federal Court of Canada against PGCL alleging trademark infringement, passing off and deprivation of goodwill in respect of PHI's PIONEER trademark.

[4] PHI's initial breach of contract claim arises from its termination of the 1996 agreement. That termination occurred by way of PHI's invocation of that agreement's termination clause (paragraph 12(1)(c)). PHI has, since that time, re-amended its statement of claim such so as to now include the additional claim of fundamental breach.

[5] As part of its claim in the main action, PHI is seeking declarations regarding what it alleges are PGCL's breaches of the 1974 and 1996 agreements and PHI's ownership of the PIONEER trademark and trade name. PHI also seeks

in its main action, an injunction restraining PGCL from directly making use of the trademark or trade name PIONEER in association with agricultural seed products. It also seeks damages or an accounting of profits caused by the breach of the 1974 and 1996 agreements.

[6] For its part, PGCL denies that they have breached the 1974 agreement (as amended by the 1996 agreement) or the 1996 agreement (as alleged or at all). Accordingly, PGCL seeks in its counterclaim a declaration stipulating that it has not breached the above agreements and that those agreements are valid and in force. As part of that declaration, amongst other things, PGCL seeks a pronouncement that it is entitled to use, advertise and display the word or words PIONEER, PIONEER GRAIN, THE PIONEER or RICHARDSON PIONEER or any other words which include the word PIONEER as or in a trademark, corporate name or trade name in the relevant area in association with the wares and services as defined in the 1996 agreement. PGCL specifies that the wares and services are not restricted to wares or services produced, supplied or offered by PHI, but it does acknowledge, that any license respecting the word PIONEER is subject to each of the conditions set out in the 1996 agreement.

THE PRESENT MOTION FOR SUMMARY JUDGMENT

[7] On this motion for summary judgment, PGCL seeks an order that:

1. dismisses PHI's claim;
2. grants PGCL's declarations stipulating that:
    (a) there was no breach of the 1974 and 1996 agreements;

(b) the 1974 agreement (as amended by the 1996 agreement) and the 1996 agreement are valid and in force; and

(c) that pursuant to the 1996 agreement:

(i) PIONEER GRAIN is entitled to continue with the license granted under the 1996 agreement;

(ii) the license grant is not restricted to wares or services produced, supplied or offered by PHI;

(iii) such license is subject to each of the conditions set out in the 1996 agreement; and

(iv) solicitor and client costs.

[8] PGCL's motion for summary judgment focuses on what it says was PHI's invalid termination of the 1996 agreement. Specifically, PGCL takes aim first, at PHI's use of the termination clause (paragraph 12(1)(c) of the 1996 agreement) and second, the absence of proof to support a claim for fundamental breach.

[9] PGCL seeks summary judgment based upon its contention that it has proven *prima facie* that PHI was not entitled to terminate the 1996 agreement pursuant to paragraph 12(1)(c) of the agreement due to the fact that many of the alleged breaches to the agreement were not breaches. PGCL also asserts that there was no or inadequate notice respecting both the so-called breaches and termination. Finally, if and where proper notice was given and could be discerned, PGCL contends that any identifiable breaches were cured within 30 days of notification of any such breaches. PGCL goes further and argues that

the required and responding evidence of PHI has failed to demonstrate that there is a genuine issue for trial as to whether PHI was entitled to terminate the 1996 agreement pursuant to paragraph 12(1)(c) of that agreement.

[10] PGCL also argues that PHI is unable to put forward a genuine issue for trial with respect to its claim of fundamental breach. In that regard, PGCL submits that based on the evidence adduced in this motion, even if individual breaches can be found, such breaches are very few in number when considered in the context of the 12-year period in question. Moreover, any such breaches were not serious and were not perceived by PHI to be serious. PGCL also contends that there was no damage or potential damage to PHI or its trademark as a result of any breaches committed by PGCL. In short, PGCL argues that it has proven on a *prima facie* basis that PHI was not entitled to terminate the 1996 agreement based on a fundamental breach and that when this court takes a "good hard look" at the totality of the evidence, PHI has again, not put forward a genuine issue for trial.

ISSUES

[11] Given the nature of this motion and the positions of the parties, the issues on this motion reduce to the following:

1. Is there a genuine issue for trial with respect to whether PHI was entitled to terminate the 1996 agreement pursuant to paragraph 12(1)(c) of that agreement?

2. Is there a genuine issue for trial with respect to whether PHI was entitled to terminate the 1996 agreement on the basis of fundamental breach?

BACKGROUND

[12] PHI and their predecessors have carried on business in Canada since at least, 1948, and since that time have been involved in the sale and distribution of agricultural seeds to farmers in association with the trademark PIONEER (the "PIONEER trademark"), as well as the tradename PIONEER (the "PIONEER trade name"). PHI Canada is the licensee of PHI and the distributor in Canada of agricultural seed bearing the PIONEER trademark and trade name.

[13] As with any company possessing a trademark and trade name, PHI maintains quality control standards for all seeds and related services offered in Canada in association with the PIONEER trademark and trade name. It has at significant cost advertised, offered for sale and sold seed in association with the PIONEER trademark and trade name throughout Canada since at least 1948. The PIONEER trademark and trade name, are and have been, continuously used by PHI and PHI Canada in Canada in association with their seeds and have never been abandoned.

[14] The substantial sale of its seed products in Canada and the significant amount of money spent on advertising in Canada and throughout the world, has, according to PHI, led to the establishment of its well-known reputation and goodwill in the PIONEER trademark and trade name for such seeds in Canada.

The goodwill associated with the PIONEER trademark and trade name is of substantial value to PHI and PHI Canada and of fundamental importance to their overall business in Canada.

[15] PGCL, the predecessor of the defendant, RICHARDSON PIONEER LIMITED, was incorporated under the laws of Manitoba on July 18, 1913 and, since that time, has carried on business as a grain merchant and has operated grain elevators in western Canada in association with the trademarks and trade names “PIONEER GRAIN”, “PIONEER” and “THE PIONEER”.

[16] Since its inception, PGCL has been providing “grain merchant services” to its customers including grain handling (i.e. buying and selling grain) and crop planning and management assistance services (such as providing advice to customers regarding planting decisions, crop inputs and market trends). Since at least the 1930’s, PGCL has been making “local sales” out of the PIONEER grain elevators in western Canada. This involved grain that was sold back to farmers and the local community which was used primarily either for planting purposes (i.e. agricultural seed) or for feed. Since that time, PGCL has sold agricultural seeds produced by various third party suppliers.

[17] A number of registered trademarks are owned by the parties for the word “PIONEER”, including the two registered trademarks summarized below:

PGCL

...	**REGISTRATION NUMBER**:
...	TMA203786

...
FILED: 1972-05-19
REGISTERED: 1974-12-13

REGISTRANT:
PIONEER GRAIN COMPANY, LIMITED,
...

WARES:
(1) Herbicides.
(2) Field sprayers or application of herbicides.
(3) Livestock feed supplements.
(4) Chemical fertilizers.
(5) Baling twine.

SERVICES:
(1) The services of grain merchants including receiving and paying for farmers' grain; cleaning, storing and shipping it; and the operation of grain elevators.
(2) Transportation and shipping of grain, ore and other bulk commodities by water.

CLAIMS:
Used in CANADA since at least as early as 1951 on wares (1), (2).
Used in CANADA since at least as early as September 1970 on wares (3).
Used in CANADA since at least as early as December 1970 on wares (4).
Used in CANADA since at least as early as July 1971 on wares (5).
Used in CANADA since at least as early as 1913 on services (1).
Declaration of Use filed October 28, 1985 on services (2).

...

PHI

... **REGISTRATION NUMBER**:
... TMA179893

...
FILED: 1969-06-05
REGISTERED: 1971-12-03

REGISTRANT:
PIONEER HI-BRED LIMITED,
...

> **WARES**:
> (1) Agricultural seeds, grains and legumes.
> (2) Animal semen and live animals and animals for breeding.
> (3) Agricultural seed inoculants and agricultural seed inoculants sold as a component of agricultural seeds; chemical composition which causes seed inoculants to cling to seeds.
>
> **CLAIMS**:
> Used in CANADA since 1948 on wares (1).
> Declaration of Use filed November 18, 1971 on wares (2).
> Declaration of Use filed April 06, 1984 on wares (3).
> ...

[18] In the early 1970's, PHI became concerned with the proposed use by PGCL of the trademark PIONEER for livestock feed supplements, based on PHI's prior rights to the PIONEER trademark and trade name for agricultural seeds, grains, legumes, animal semen and live animals and animals for breeding. It had been PHI's understanding that until that time, PGCL's use of the trade name PIONEER GRAIN and trademark PIONEER had been limited to providing grain merchant services. In an attempt to settle the parties' dispute concerning use of the trademark and trade name PIONEER, predecessors of PGCL entered into a written co-existence agreement (the 1974 agreement) with PHI Canada.

The 1974 Agreement

[19] Paragraph 2 of the 1974 agreement reads as follows:

> 2. The Parties of the First Part, jointly and severally, undertake, covenant, promise and agree on behalf of themselves, their successors, licensees and assigns not to register or use the trade mark PIONEER or any trade mark embracing such word, in Canada, in association with agricultural seeds, grains, legumes, animal semen and live animals and animals for breeding, nor to challenge the use or any registration of the trade mark PIONEER, in Canada, for agricultural seeds, grains, legumes, animal semen and live animals and animals for breeding by or in the name of PIONEER HI-BRED, its successors and assigns;
> [Emphasis added.]

Pursuant to paragraph 2 of the 1974 agreement (also set out at para. 117 of this judgment), the predecessors of PGCL undertook and agreed not to register or use the trademark PIONEER or any trademark embracing such a word, in Canada, in association with agricultural seeds, grains, legumes, animal semen and live animals and animals for breeding. Pursuant to paragraph 2, PGCL also undertook to not challenge the use and registration of the PIONEER trademark in Canada for such products acquired in the name of PHI Canada, its successors and assigns.

[20] By virtue of the 1974 agreement, the predecessors of PGCL therefore also waived any right to challenge the validity and use of the PIONEER trademark of PHI as used in Canada in association with agricultural seeds, grains, legumes, animal semen and live animals and animals for breeding.

[21] Pursuant to paragraph 5 of the 1974 agreement, PHI Canada agreed not to challenge use of the trade name of PIONEER GRAIN, in Canada, in association with the services of grain merchants including receiving and paying for farmers' grain; cleaning, storing and shipping it; and the operation of grain elevators and in association with herbicides, field sprayers for application of herbicides, paint, livestock feed supplements, chemical fertilizers and bailing twine. Nowhere in the 1974 agreement did PHI consent to any use or registration of any trademarks or trade names incorporating PIONEER in association with the importation, advertisement, offer for sale and/or distribution of seeds, grains or legumes.

The 1996 Agreement

[22] Subsequent to the 1974 agreement, disputes arose between the parties arising from the use by PGCL's predecessors, PIONEER GRAIN and JAMES RICHARDSON INTERNATIONAL LIMITED (JRI), of the PIONEER trademark and trade name in connection with marketing, distributing and selling seed products, and particularly canola seed. As a result of extensive negotiations between the parties between 1993 and 1996, they entered into cross-license agreements, including a Trademark License Agreement dated February 13, 1996 from PHI to PIONEER GRAIN (the 1996 agreement).

[23] The 1996 agreement permitted PIONEER GRAIN, under a non-exclusive license, to use PIONEER in western Canada in association with agricultural seed products and in association with the offer for sale, sale, consultation, distribution and delivery of agricultural seed. Any such usage would need to be in compliance with the terms of the 1996 agreement.

[24] The 1996 agreement contains the following relevant provisions:

> RECITALS
>
> ...
>
> 5. LICENSEE [PGCL] represents that it carries on business under its corporate name, and under the trade-marks and trade-names PIONEER GRAIN, PIONEER, The PIONEER and others which include the word "Pioneer" in Western Canada (the Provinces of Manitoba, Saskatchewan, Alberta and British Columbia and the Territories West of the longitudinal line defining the Manitoba-Ontario Border are hereinafter the "Territory") in association with the wares and services listed in Schedule B.
>
> ...

7. LICENSEE has, in the course of its business as described in the preceding paragraph, sold, out of its grain elevators and/or associated buildings, agricultural seeds, grains and legumes (in this Agreement, the term “agricultural seeds, grains and legumes” is intended to mean seeds, grains and legumes sold for the purposes of planting as agricultural crops, and not the derivative crop used for processing or consumption). LICENSEE represents that it has carried on such activities since at least as early as 1939.

...

9. The parties acknowledge that they each have the right to render support services ancillary to their basic services comprising, in the case of PHI and PHL, the distribution of agricultural seed, and in the case of PG, the services of grain merchants, such support services including agricultural crop planning and management assistance services and agronomy services.

...

NOW, THEREFORE, ...

1. Subject to the other provisions of this Agreement, PHI grants to LICENSEE a royalty-free, non-exclusive license to use, advertise and display the word PIONEER in the Territory as or in a trade-mark, corporate name or trade-name in association with agricultural seeds, grains and legumes; agricultural seed inoculants and agricultural seed inoculants sold as a component of agricultural seeds, chemical composition which causes seed inoculants to cling to seeds (the “Wares”) and in association with the offer for sale, sale, consultation, distribution and delivery of agricultural seed (the “Services”), provided that the Wares sold or distributed by LICENSEE conform to the standards defined in paragraph 5 of this Agreement, provided that any such use of the word PIONEER by LICENSEE does not depreciate the goodwill attaching to PHI’s trade-mark and trade-name PIONEER, and provided that nothing in this Agreement confers on LICENSEE any right to use the word PIONEER as or in a trade-mark, trade-name or corporate name on any Wares exported by LICENSEE from Canada or shipped and/or sold outside the Territory, and provided further that nothing this paragraph grants to LICENSEE any right of sub-license.

2. Whenever LICENSEE uses, advertises or displays the word PIONEER on printed promotional and advertising materials, or portions thereof, primarily directed to the Wares or Services, pursuant to the license granted under paragraph 1, LICENSEE shall clearly identify such use, advertisement or display as being licensed, and shall identify PHI as the owner of the right to use the word PIONEER in association with the Wares and/or the Services in accordance with the following wording:

> "PIONEER, in association with the sale and distribution of seed, is a trade-mark of Pioneer Hi-Bred International, Inc., used under license by Pioneer Grain Company Limited",

or such other form of notice as may be greed by the parties. PHI and PHL acknowledge that advertisements of the type identified as attached Schedule C are not primarily directed to the Wares or Services and do not give rise to any notice requirement pursuant to this paragraph. LICENSEE shall post a conspicuous notice containing the wording set out above in each of its grain elevators or other facilities in which Wares is sold, and on each contract primarily directed to the sale of seed.

...

8. Any advertising, promotional or informative materials distributed or displayed by or for LICENSEE, or authorized by LICENSEE, in relation to the offer for sale, sale, consultation, and/or delivery of Wares, that include the word PIONEER as or in a trade-mark or trade-name, shall conform to applicable laws relating to such advertising materials, and shall not mislead or deceive the public regarding the origin of the advertised products.

9. PHI, PHL, RICHARDSON and LICENSEE acknowledge the full force and effect of the 1974 Agreement which, subject to this Agreement, continues in force between the parties, but recognize that the parties may construe its rights and obligations differently.

10. To the extent that the LICENSEE and RICHARDSON may have acquired any right, title in or to the trade-mark and trade-name PIONEER (whether alone or in combination with other words) for use in association with Wares, or with the Services of the offer for sale, sale, consultation, distribution and/or delivery of agricultural seed to farmers, and notwithstanding any terms and conditions of the 1974 Agreement interpreted as prohibiting such acquisition and use, LICENSEE and RICHARDSON assign and quit claim any right, title or interest in or to such trade-mark and trade-name to PHI.

...

12. (1) The license conferred by this Agreement may, at the option of PHI or LICENSEE, be terminated in the event of the occurrence of any one or more of the following:

> ...
>
> (c) breach of this Agreement by the other party, provided that PHI shall give the other party written notice of any such

> apprehended breach, and the other party shall have thirty (30) days after receipt of such notice in which to remedy such breach;
>
> ...
>
> (2) The termination of this Agreement shall not terminate the parties' mutual obligations under paragraphs 3(1), 4, 7, 9, 10, 11, 13, 14, 15, 16 and 17 of this Agreement or under the 1974 Agreement.
>
> 13. If any instance of actual confusion among farmers, end users, or any other party, as to the mistaken belief that LICENSEE and PHI are in fact the same company or related or affiliated companies, the parties agree to promptly take those steps necessary to avoid such confusion from reoccurrence including, but not limited to, LICENSEE using and/or displaying a disclaimer of any formal or corporate affiliation or relationship with PHI.
>
> ...

Interpreting the 1996 Agreement

[25] All of the parties agree on the appropriate principles that guide contractual interpretation. A contract should be construed as a whole, with all words in the contract given meaning, if possible, and the absence of words being given consideration. The goal is to determine the objective intent of the parties at the time of execution. See ***Bell Mobility Inc. v. MTS Allstream Inc.***, 2009 MBCA 28, 236 Man.R. (2d) 167 (C.A.), at paras. 17 and 42.

[26] In ***Moore Realty Inc. v. Manitoba Motor League***, 2003 MBCA 71, 173 Man.R. (2d) 300, at paras. 11 and 12, the Court of Appeal provides a concise summary of the law as follows:

> [11] The cardinal principle of contract interpretation is that the court "should give effect to the intentions of parties as expressed in their written document." See **Manulife Bank of Canada v. Conlin**, [1996] 3 S.C.R. 415 ... at para. 79. If the contract is clear and unambiguous, the contract itself should be all that is required to determine the parties' intentions. That is, it will not be necessary to consider extrinsic evidence to assist in interpreting the contract. In **Eli Lilly & Co. et al. v.**

> **Novopharm Ltd. et al.,** [1998] 2 S.C.R. 129 ... Iacobucci, J. wrote (at para. 55):
>
> > "Indeed, it is unnecessary to consider any extrinsic evidence at all when the document is clear and unambiguous on its face."
>
> And later (at para. 57):
>
> > "[I]t cannot properly be said, in my view, that the supply agreement contains any ambiguity that cannot be resolved by reference to its text. No further interpretative aids are necessary."
>
> [12] There are three other well-known principles of contract interpretation that should not be overlooked when considering the text of a contract:
>
> 1) all the words in the contract are to be given meaning, if possible (**National Trust Co. v. Mead**, [1990] 2 S.C.R. 410) ...;
>
> 2) the contract should be construed as a whole (**Scanlon v. Castlepoint Development Corp. et al.** (1992), ... 11 O.R. (3d) 744 (C.A.), leave to appeal refused, [1993] 2 S.C.R. x; ...); and
>
> 3) the absence of words may be considered (**Controls & Equipment Ltd. v. Ramco Contractors Ltd. et al.** (1999), 209 N.B.R. (2d) 1; ... (C.A.)).

[27] In his oral submissions, counsel for PGCL acknowledged that the relevant terms of the 1996 agreement are properly and fairly interpreted as explained at paragraphs 15 to 26 of PHI's written argument on this motion.

[28] Furthermore, both PGCL and PHI agreed as to the surrounding circumstances leading up to the 1996 agreement, although both parties also accepted that there was no ambiguity in the agreement such so as to require the introduction or use of extrinsic evidence in discerning the meaning and purpose of that agreement. For the purposes of setting out the above-mentioned common ground respecting the meaning of the 1996 agreement, I reproduce

below, those paragraphs (15-26) from PHI's motions brief, which, as mentioned, were endorsed by PGCL in its oral submission:

> 15. The 1996 Agreement permitted Pioneer Grain, under a non-exclusive license, to use PIONEER in Western Canada in association with agricultural seed products and in association with the offer for sale, sale, consultation, distribution and delivery of agricultural seed, *as long as such usage was in compliance with the terms of the 1996 Agreement*.
>
> ...
>
> 16. At the time of the negotiations for the 1996 Agreement, Pioneer Grain was concurrently making arrangements to sell seed products originating from PHI Canada through United Grain Growers ("UGG"), and a fundamental purpose of the 1996 Agreement was to allow such sales to occur through Pioneer Grain, without causing confusion or depreciating the value of goodwill in the PIONEER Trade-mark and Trade Name. The cross-licenses entered into between the parties confirmed the delineation between the parties' businesses, and ensured that their respective trade-mark rights would be protected. Another core purpose of the 1996 Agreement and the corresponding cross-license was to exchange mutual assignments of trade-mark rights. The primary benefit that the Plaintiffs were to derive from the 1996 Agreement was that the goodwill and distinctiveness of the PIONEER Trade-mark and Trade Name would be protected and maintained. That was the essence of and commercial purpose for the 1996 Agreement.
>
> ...
>
> 17. Pursuant to paragraph 1 of the 1996 Agreement, PHI granted Pioneer Grain a non-exclusive license (the "License") to use, advertise and display the word PIONEER in Western Canada, as or in a trade-mark, corporate name or trade name in association with agricultural seeds, grains and legumes; agricultural seed inoculants and agricultural seed inoculants sold as a component of agricultural seeds; chemical composition which causes seed inoculants to cling to seeds (the "Wares"), and in association with the offer for sale, sale, consultation, distribution and delivery of agricultural seed (the "Services"), subject to certain terms and conditions.
>
> ...
>
> 18. The License granted by paragraph 1 has several conditions, prefaced by the words "[s]ubject to" and "provided that". The Defendants have admitted that the License included conditions.
>
> ...

19. For example, it was a condition to the License that it is granted to Pioneer Grain only "provided that any such use of the word PIONEER by [Pioneer Grain] *does not depreciate the goodwill attaching to PHI's trade-mark and trade name PIONEER* [emphasis added]". Pioneer Grain was also required to comply with standards provided for under paragraph 5 of the 1996 Agreement.
...

20. Further, paragraph 2 of the 1996 Agreement requires that wherever Pioneer Grain uses, advertises or displays the word PIONEER on printed promotional and advertising materials, or portions thereof, primarily directed to the Wares or Services, pursuant to the License, "[Pioneer Grain] shall *clearly* identify such use, advertisement or display as being licensed, and shall identify PHI as the owner of the right to use the word PIONEER in association with the Wares and/or the Services [emphasis added]" in accordance with the following wording:

> "PIONEER" in association with the sale and distribution of seed, is a trade-mark of Pioneer Hi-Bred International, Inc., used under license by Pioneer Grain Company Limited".

Paragraph 2 also requires Pioneer Grain to "post a *conspicuous* notice containing the wording set out above in *each* of its grain elevators or other facilities in which Wares [are] sold, and on *each* contract primarily directed to the sale of seed [emphasis added]".
...

21. Paragraph 8 of the 1996 Agreement requires that "[a]ny advertising, promotional or informative materials distributed or displayed by or for [Pioneer Grain], or authorized by [Pioneer Grain], in relation to the offer for sale, sale, consultation and/or delivery of Wares, that include the word PIONEER as or in trade-mark or trade name ... *shall not mislead or deceive the public regarding the origin of the advertised products* [emphasis added]".
...

22. Paragraph 10 of the 1996 Agreement contains an assignment and quit claim from Pioneer Grain and JRI to PHI of any right, title and interest in or to the trade-mark and trade name PIONEER (whether alone or in combination with other words) that Pioneer Grain or Richardson may have acquired for use in association with Wares, or with the Services of the offer for sale, sale, consultation, distribution and/or delivery of agricultural seed to

> farmers. In paragraph 7, Pioneer Grain also agreed that all use of the word PIONEER by Pioneer Grain pursuant to the License has the legal effect of use by PHI and inures to the benefit of PHI. Accordingly, under these terms of the 1996 Agreement, Pioneer Grain and JRI have confirmed that, as between the parties, PHI is the owner of all trade-marks and trade names incorporating PIONEER, in association with the Wares and Services, both as of the date of the 1996 Agreement and through any subsequent use by Pioneer Grain under the License.
> ...
>
> 23. Paragraph 12(1)(c) of the 1996 Agreement allows for PHI to terminate the License upon breach by Pioneer Grain or Richardson, provided that PHI shall give Pioneer Grain/Richardson written notice of any such apprehended breach, and the other party shall have thirty (30) days after receipt of such notice in which to remedy such breach.
> ...
>
> 24. Paragraph 12(2) of the 1996 Agreement provides that specific paragraphs of the 1996 Agreement survive termination of the License, including the assignment and quit claim of paragraph 10. However, the License granted in paragraph 1 does not survive termination of the License.
> ...
>
> 25. Paragraph 16 of the 1996 Agreement provides that no failure or delay by PHI in giving notice or in exercising the rights or remedies available to it by reason of any default on the part of Pioneer Grain shall constitute or be deemed to or construed to be a waiver of such default or any subsequent default, whether of the same or similar nature. Paragraph 16 also confirms that the exercise by PHI of any right or remedy provided in the 1996 Agreement does not prevent PHI from exercising any other right or remedy, either concurrently or separately.
> ...
>
> 26. Further, the 1974 Agreement was confirmed to be in full force and effect by virtue of paragraph 9 of the 1996 Agreement.
> ...

[29] PHI argues that during the period from the commencement of the 1996 agreement until termination, the activities of PGCL included activities which constitute what they characterize as “numerous” and continuous breaches of

both the 1974 and 1996 agreements as they relate to PGCL's use of trademarks incorporating the name PIONEER.

[30] PGCL disagrees and responds by asserting that the evidence on this motion suggests that during the relevant period of time, the activities of PGCL were not such that they gave rise to the sort of complaints by PHI that would have been expected; complaints consistent with and suggestive of the kind of frequency and seriousness of breaches now asserted by PHI. Based on the sworn affidavit of Mr. Jean-Marc A. Ruest, Vice-President, Corporate Affairs and General Counsel of RICHARDSON INTERNATIONAL LIMITED and Secretary of RICHARDSON PIONEER LIMITED, PGCL's position is set out clearly at paragraph 19 of their brief:

> 19. By all appearances, the parties peacefully co-existed in the marketplace over the course of the next ten years. PGCL continued to sell agricultural seeds produced by various suppliers, including varieties produced by PHI. Any issues which developed during this period of time were dealt with practically and on an amicable basis.

Interaction Between the Parties from 1996 - 2008

[31] It would appear there is no evidence on this motion which suggests that there are any potential breaches of the 1996 agreement by PGCL between early 1996 and early 1999. This was in fact acknowledged by Mr. Bruce A. Hall, Assistant Secretary of PHI, during his cross-examination of March 11, 2010.

[32] Third party investigators were, however, hired by PHI's counsel in 1999 for the purposes of conducting covert investigations of several of PGCL's facilities. The fact of these investigations and the involvement of third party

investigators were not known to PGCL until PHI provided their answers to undertakings in 2009.

[33] On August 17, 1999 (following the 1996 investigations), Mr. Hall sent a letter to Mr. David Fraser (General Counsel to RICHARDSON), wherein he stated it had come to PHI's attention that a number of PGCL's distribution centres did not display the notice required by paragraph 2 of the 1996 agreement. Mr. Hall also noted that various bags used by PGCL containing sample seed did not carry this wording, nor did some invoices or pick-up slips for seed. At the conclusion of the letter, Mr. Hall asked Mr. Fraser to "kindly remind" each distribution centre that the notice should be conspicuously displayed to review all printed materials to be sure that any seed-related ads, brochures and business forms carried this wording as well.

[34] A response to the August 17, 1999 letter came from Ms. Sandra Swystun, Corporate Counsel for RICHARDSON, in a letter to Mr. Hall on September 23, 1999. In that letter, Ms. Swystun stated the following, at p. 1:

> As requested, we are reminding our managers to post the disclaimer notice on our grain elevators and other facilities for the sale of seed. We have a form of pre-printed laminated notice designed for this purpose (photocopy attached). In addition, we are reviewing printed materials and advertisements to ensure that they carry the disclaimer in cases where they are directed primarily to the sale and distribution of seed.
>
> With respect to bags of sample seed, we are not clear as to which practices you are referring to. PGC uses bags of sample grain, not seed, to send samples of producers' grain from our grain elevators to our quality assurance department, independent testing laboratories and regulatory authorities (e.g. Canadian Grain Commission) for determination or confirmation of the grade or other qualities of such grain, and/or to end-users such as flour mills and food processors for

> testing of the suitability of such grain. PGC does not bag seed for sale, distribution or delivery.
>
> Finally, with respect to invoices and pick-up slips. PGC uses the same standard form of those documents for all crop inputs, including seed, and is permitted under the Licensing Agreements to use such form even if a transaction relates to the sale of seed only.

[35] There appears to have been no direct response by Mr. Hall to the facts set out in Ms. Swystun's letter regarding PGCL's use of seed bags, nor did he respond to the position put forward by Ms. Swystun respecting PGCL's ability to use PGCL's standard form invoices and pick-up slips for the sale of agricultural seeds. Instead, on September 27, 1999 Mr. Hall sent a letter to Ms. Swystun which letter stated:

> Your fax dated September 23, 1999 was received. I wish to thank you for your review of the licensing agreement and reminders to your grain elevators and other facilities regarding the disclaimer notice.
>
> As you realize, it is important as a trademark owner to make sure our marks are being used correctly.
>
> I appreciate your help.

[36] Between 1999 and 2001, except for what PGCL has described as an "inadvertent error" (the details of which are set out in the following two paragraphs), I accept PGCL's assertion that there would appear to be no evidence before the court which suggests that there were any obvious or potential breaches of the 1996 agreement by PGCL (i.e. between the investigations conducted by PHI in 1999 and the investigations conducted by PHI in 2001).

[37] On April 30, 2001, three of PGCL's locations placed a joint advertisement for seed in the *Southeast Agripost* (a small local newspaper). In accordance with the 1996 agreement, the proofs submitted by PGCL to the printer included the notice set out in paragraph 2 of the 1996 agreement. It would seem that during the typesetting process, the printer omitted the notice and the advertisement appeared in the newspaper without the notice. The managing editor of the newspaper acknowledged responsibility for the omission and agreed to run a correction notice and reprint the advertisement with a notice in the next issue of the newspaper. It was Mr. W.D. (Bill) Mooney, Vice-President, Organizational Development, of JRI, who reported the inadvertent error to PHI in a letter dated May 10, 2001. At the conclusion of the letter, Mr. Mooney stated:

> We trust that the actions taken to remedy this situation are satisfactory to PHI. As indicated in our last letter to you, we have taken steps to ensure compliance with the licensing agreements and continue to be vigilant in that regard. ...

[38] It was Mr. Hall, on May 24, 2001, who then sent a letter to Mr. Mooney wherein he stated:

> Thank you for your letter of May 10, 2001, regarding the inadvertent omission of the disclaimer in an ad placed by Pioneer Grain Company, Limited in **The Southeast AgriPost**. We feel the matter has been remedied quite satisfactorily and very much appreciate your contacting us.

[39] In 2001, PHI's counsel had once again retained third party investigators to conduct covert investigations of several of PGCL's facilities. Again, PGCL was not aware that these investigations had been conducted and did not become aware until PHI provided their answers to undertakings in 2009. Following the 2001

investigations, PHI did not express any concerns to PGCL or communicate any potential breaches of the 1996 agreement to PGCL.

[40] Respecting the period between 2001 and September 18, 2006, there would appear to be little if any evidence adduced on this motion which would suggest any communication by PHI to PGCL respecting the issues in this litigation. Mr. Hall himself acknowledged this fact during his cross-examination on March 11, 2010. It would seem that Mr. Hall's letter dated August 17, 1999 represents the only time PHI raised an issue or complaint under the 1996 agreement during the period February 1996 to September 18, 2006 (the date of the letter about field signs referred to immediately below). Again, this was acknowledged by Mr. Hall during his cross-examination on March 11, 2010.

[41] In a letter dated September 18, 2006, Mr. Hall sent a letter to Mr. Peter Entz, Manager, Seek Products & Agronomy for RICHARDSON, which attached a photograph of a "PIONEER" field sign alongside a DeKalb field sign in a field of soya beans. In that letter, Mr. Hall stated:

> We are concerned that your Pioneer sign appearing along side the DeKalb field sign wrongly imparts the message that the resulting crop is either grown from our company's seed and/or a collaborative seed product from us and DeKalb.

[42] At the conclusion of the letter, Mr. Hall added:

> I appreciate your attention to this and seeing if there is a way to more clearly identify Pioneer Grain. It would help to avoid any more confusion in an already confused marketplace.

[43] A responding letter was sent on September 21, 2006 by Mr. Entz of RICHARDSON. The letter was sent to Mr. Hall in which Mr. Entz apologizes for

the use of "PIONEER" field signs in the identified manner. Mr. Entz also stated that instructions had been sent to field staff not to place "PIONEER" field signs in conjunction with seed products in any field and to remove any field signs from fields in which PIONEER and its seed product were being promoted. Mr. Hall did not respond to Mr. Entz's September 21, 2006 letter.

[44] During the next several months, the issue of field signs was discussed internally by various representatives of PGCL and RICHARDSON, including Mr. Ruest. PGCL ultimately decided that field signs would only be used if accompanied by the notice set out in paragraph 2 of the 1996 agreement. To that end, new signs were ordered with the notice printed directly on the signs. PGCL also ordered stickers with the requisite language on the notice they were to use on signs in inventory from the previous year.

[45] On October 26, 2007, PHI's counsel sent a letter to PGCL which complained about three issues - including PGCL's use of field signs. During the next number of months, the parties exchanged numerous letters which addressed several issues. Those letters would have included letters dated May 16, 2008 and July 22, 2008.

[46] On August 28, 2008, Mr. Hall sent a letter to the President of PGCL (the "termination letter") which stated that the 1996 agreement had been previously terminated by PHI pursuant to letters dated October 26, 2007, May 16, 2008 and July 22, 2008 (these letters are collectively referred to as "the three letters"). Mr. Hall's letter of August 28, 2008 suggested that the three letters "gave formal

notice that JRI and Pioneer Grain used PHI's PIONEER trade-mark and trade name in association with agricultural seed products improperly and in an unauthorized manner and failed to cure or cease such use." The termination date specified in the August 28, 2008 termination letter was said to be one of November 26, 2007, 30 days after either May 16, 2008 or July 22, 2008. The termination letter of August 28, 2008 did not outline the specific breaches that PGCL allegedly failed to cure. Neither had PHI in its previous letters notified PGCL of its position that the 1996 agreement had been terminated.

[47] As earlier indicated, as part of its main action filed in this court in August 2008, PHI specifically alleges that PGCL has breached paragraph 2 of the 1974 agreement along with paragraphs 1, 2, 8 and 9 of the 1996 agreement. PHI argues that they were accordingly entitled to terminate (as described in para. 46 above) the license in accordance with paragraph 12(1)(c).

[48] On the basis of a comparatively newer argument raised much later (in its re-re-amended statement of claim dated February 25, 2010), PHI also argues PGCL's repudiation of the 1996 agreement as constituted by the identified "ongoing" breaches which PHI says amounted individually and/or cumulatively to a fundamental breach of the 1996 agreement.

[49] PGCL's earlier-described motion for summary judgment was brought December 16, 2009, although not heard until April 13 and 14, 2010 (over a two-day period). The voluminous supporting material filed by both parties need not be formally enumerated. It will suffice to note that in addition to the many

affidavits filed, cross-examinations took place respecting the affidavits of Mr. Hall (of PHI) and Mr. Ruest (of PGCL).

THE TEST FOR SUMMARY JUDGMENT

[50] The test on a motion for summary judgment is whether there is a genuine issue for trial. Court of Queen's Bench Rule 20.03(1) states:

> **Where no genuine issue**
>
> 20.03(1) Where the court is satisfied that there is no genuine issue for trial with respect to a claim or defence, the court shall grant summary judgment accordingly.

[51] In a motion for summary judgment, there are different burdens and shifting onuses attaching to either a moving or a responding party. The jurisprudence has used various language to describe in what circumstances a party can and cannot succeed on a motion for summary judgment. In ***Homestead Properties (Canada) Ltd. v. Robert***, 2007 MBCA 61, 214 Man.R. (2d) 148 (C.A.), Freedman J.A. described the test for summary judgment in the following manner, at paras. 14 to 17:

> **14** The test for summary judgment is well established, and no further detailed explanation is needed. The test is to the same effect regardless of whether the moving party is the plaintiff or the defendant. When the defendant moves, as here, he must prove, on a *prima facie* basis, that the plaintiff's action must fail. If he meets that burden, then the plaintiff has the burden to establish that there is a genuine issue for determination. He must show that his claim is "one with a real chance of success" (see *Hercules Managements Ltd. v. Ernst & Young*, [1997] 2 S.C.R. 165 at para. 15; see also *Manitoba Hydro Electric v. Inglis (John) Co. et al.* (1999), 142 Man.R. (2d) 1 (C.A.)). If he fails to do so, summary judgment dismissing the claim will follow.
>
> **15** When a plaintiff moves, he must prove, on a *prima facie* basis, that his action will succeed. If he meets that burden, then the defendant has the burden to establish that there is a genuine issue for

> determination. If he fails to do so, summary judgment granting the claim will follow. As was made clear in *Blanco et al. v. Canada Trust Co. et al.*, 2003 MBCA 64, 173 Man.R. (2d) 247 at para. 62, regardless of who is the moving party, the analysis is a two-step process.
>
> **16** These principles are based on Rule 20 of the Court of Queen's Bench Rules. That rule has been discussed and analyzed in numerous cases including *Podkriznik v. Schwede* (1990), 64 Man.R. (2d) 199 (C.A.), *Fidkalo v. Levin* (1992), 76 Man.R. (2d) 267 (C.A.), *Somers Estate v. Maxwell* (1995), 107 Man.R. (2d) 220 (C.A.), *Kleysen et al. v. Canada (Attorney General) et al.*, 2001 MBQB 205, 159 Man.R. (2d) 17, and *Blanco*.
>
> **17** Whether the test is cast in terms of "the action fails in law" (*Somers*, at para. 10), or that the defendant must show "the absence of a valid claim in law" (*Somers*, at para. 11), or that "the action must fail in law" (*Somers*, at para. 16), or "that at a trial it will succeed" (*Blanco*, at para. 28), or some other like phrase, the expressions amount to the same thing. The moving party must show that, *prima facie*, on the facts the responding party's case must fail. If he does, then the second step of the analysis commences, and the responding party has the burden of showing that there is a genuine issue for trial.
>
> [Emphasis added.]

[52] In ***Klassen (Next Friend of) v. Morden Hospital District, No. 21*** (1992), 80 Man.R. (2d) 195 (Q.B.), Monnin J. (as he then was) cited with approval ***Pizza Pizza Ltd. v. Gillespie*** (1990), 75 O.R. (2d) 225 (Gen. Div.), at p. 238:

> Rule 20 contemplates a radically new attitude to motions for judgment; the objective is to screen out claims that in the opinion of the court, based on evidence furnished as directed by the rule, ought not to proceed to trial because they cannot survive the “good hard look”.
>
> ...
>
> It is not sufficient for the responding party to say that more and better evidence will (or may) be available at trial. The occasion is now. The respondent must set out specific facts and coherent evidence organized to show that there is a genuine issue for trial.

See also ***Towers Ltd. v. Quinton's Cleaners Ltd.***, 2009 MBQB 34, 237 Man.R. (2d) 100 (Q.B.), at para. 79.

[53] In taking a "good hard look" at the merits of an action, the court is making an accompanying determination as to whether there is, in the case of a responding party, a position or a defence that has "a real chance of success". (***Towers Ltd. v. Quinton's Cleaners Ltd.***, *supra*, para. 80, citing ***Fidkalo v. Levin*** (1992), 76 Man.R. (2d) 267 (C.A.).)

[54] In assessing for and determining what constitutes "a real chance of success", MacInnes J. (as he then was) provided the following nuance in ***Manitoba (Hydro Electric Board) v. John Inglis Co.***, 2000 MBQB 218, 101 A.C.W.S. (3d) 1103 (Man. Q.B.), at para. 20:

> **20** I take from the authorities that on a summary judgment motion I am to review all of the evidence before me. That includes considering credibility, where possible, not for the purpose of weighing the evidence to determine whether the plaintiff will or will not succeed in its litigation, that is, whether its case passes muster on a balance of probabilities, but rather to determine whether the case has a realistic chance of success. And, in this context, "real" is not intended to establish a level of probability. Rather, it is to denote a realistic rather than theoretical prospect of success; in other words, the plaintiff's case, when held up to scrutiny in light of all of the evidence available for consideration on the motion, must have an air of reality to it and not be merely the product of wishful, fanciful or imaginative thinking on the part of the plaintiff.

See ***Towers Ltd. v. Quinton's Cleaners Ltd.***, at para. 81.

[55] I wish to underscore that I have addressed the issues on this motion for summary judgment mindful of the now well-established proposition that any summary disposition of an action or part of an action ought not to occur where there are credibility issues and factual conflicts in the evidence. Having said

that, the possibility of ending an action by summary disposition ought not to immobilize a presiding judge from acting on the evidentiary record, where the so-called credibility issues and factual conflicts are not real. Such misplaced caution could lead to an unjustified timidity where the consequent failure of the judge to take a "good hard look" would risk compromising the purpose of the rule that specifically permits disposing of actions that ought not to continue. In ***Bellboy Corp. v. 3763383 Manitoba Ltd.***, 2002 MBQB 69, 164 Man.R. (2d) 17 (Q.B.), Hamilton J. (as she then was) observed the following at para. 9:

> **[9]** I add to this summary the principle that real issues of credibility creating real conflicts in the evidence require determination at a trial based upon *viva voce* evidence and assessments of credibility by the trial judge. Having said that, a defendant cannot simply argue that there are matters of credibility and leave it at that. The defendant "... must set out specific facts and coherent evidence organized to show that there is a genuine issue for trial. Apparent factual conflict in the evidence does not end the inquiry. The court may, on a common sense basis, draw inferences and may look at the overall credibility of the plaintiff's action" (as per Henry, J., in **Pizza Pizza Ltd. v. Gillespie et al.** (1990), 75 O.R. (2d) 225 (Gen. Div.)).

[56] Further to the above, I repeat my earlier comments as stated in ***Towers Ltd. v. Quinton's Cleaners Ltd.*** at para. 83:

> **[83]** In its application of the governing test on a motion for summary judgment, the court must exercise a restraint that recognizes the well established limits respecting the making of findings of fact where the contested evidence more appropriately requires a trial of an issue. The relevant jurisprudence in that regard is comprehensively reviewed in **Danylchuk et al. v. Wolinsky et al.** (2007), 225 Man. R. (2d) 2; 419 W.A.C. 2; 2007 MBCA 132, at paras. 28-39. It is well to remember however, Monnin J.A.'s comments:
>
> > "[35] It is not simply because a party, as the appellants do in this case, disputes every material fact that a judge is precluded from considering the matter on the basis of affidavit evidence. The judge can review those facts and come to a conclusion that

> the facts are really not in dispute or that the disputed aspect of those facts are not relevant or material to the question to be decided."
>
> [Emphasis added.]

ANALYSIS

1. Is there a genuine issue for trial with respect to whether PHI was entitled to terminate the 1996 agreement pursuant to paragraph 12(1)(c) of that agreement?

[57] PHI purports to have terminated the 1996 agreement pursuant to paragraph 12(1)(c) of that agreement. For the sake of convenience, I set out again paragraph 12(1)(c) of the 1996 agreement:

> 12. (1) The license conferred by this Agreement may, at the option of PHI or LICENSEE, be terminated in the event of the occurrence of any one or more of the following:
>
> ...
>
> (c) breach of this Agreement by the other party, provided that PHI shall give the other party written notice of any such apprehended breach, and the other party shall have thirty (30) days after receipt of such notice in which to remedy such breach;
>
> ...

[58] It would seem clear that the purpose of the above type of notice provision is to give the party in breach an opportunity to remedy its breach. For such a remedy to be forthcoming, specifics of the particular breach complained of must be given in sufficient detail so as to enable the party to understand the behaviour being impugned by the other party. Notice need be clear and concise as its time period for termination has started as of a given letter. Such clarity should leave no doubt in the mind of the other party of the possible and expected consequences of non-compliance. See ***Heep v. Thimsen***, [1941] 1

D.L.R. 424 (B.C.C.A.), at para. 6.; and ***M.L. Baxter Equipment Ltd. v. Geac Canada Ltd.*** (1982), 36 O.R. (2d) 150 (Ont. H.C.J.), at paras. 16 and 17.

[59] On August 28, 2008, Assistant Secretary for PIONEER HI-BRED INTERNATIONAL, INC., Mr. Hall, sent the following letter to PGCL:

> August 28, 2008
>
> ORIGINAL SENT BY
> OVERNIGHT COURIER
>
> Pioneer Grain Company Limited
> 2500 1 Lombard Place
> Winnipeg, MB H3B 0X8
>
> Attention: President
>
> Dear Sir:
>
> RE: Formal Confirmation of Termination of the February 13, 1996 Trade-mark License Agreement between Pioneer Hi-Bred International, Inc. ("PHI") and Pioneer Hi-Bred Ltd.; and Pioneer Grain Company Ltd. ("Pioneer Grain"), James Richardson & Sons Ltd. ("JRI").
>
> Pursuant to a October 26, 2007 letter from plaintiffs' Canadian trade-mark counsel and further May 16, 2008 and July 22, 2008 letters from PHI to JRI and Pioneer Grain, PHI gave formal notice that JRI and Pioneer Grain used PHI's PIONEER trade-mark and trade-name in association with agricultural seed products improperly and in an unauthorized manner and failed to cure or cease such use.
>
> Pursuant to paragraphs 10 and 12 of the February 13, 1996 Trade-mark License Agreement between the parties, the 1996 Agreement was terminated, at least as early as November 26, 2007 and/or thirty days following each of the above referenced May 16 and July 22, 2008 letters.
>
> This letter confirms that termination.
>
> Yours very truly,
>
> "Signed"
>
> Bruce A. Hall
> Assistant Secretary
> Pioneer Hi-Bred International, Inc.
>
> BAH:sue

[60] In the present case, this termination letter (of August 28, 2008) asserts that PHI gave notice of certain breaches to PGCL in previous letters dated October 26, 2007, May 16, 2008 and July 22, 2008 (the three letters) and that those breaches were not cured. The termination letter goes on to state that in the circumstances, the 1996 agreement was terminated within 30 days of one or more of those letters.

[61] I endorse and adopt the analytical framework suggested by PGCL for the purposes of determining whether PHI was entitled to terminate the 1996 agreement using paragraph 12(1)(c). Accordingly, I will be examining each of the three letters mentioned in the August 28, 2008 termination letter with reference to some or all of the following salient questions:

1. What if any apprehended breaches were clearly identified in the letters?
2. If any apprehended breaches were clearly identified, did any of those apprehended breaches constitute a breach of the 1996 agreement?
3. Did PGCL remedy all actual breaches of the 1996 agreement within 30 days?
4. If not, was clear notice given to PGCL that the 1996 agreement would or could be terminated if it failed to remedy any such breaches?

The letter from PHI dated October 26, 2007

[62] PHI's legal counsel, Mr. Mark Evans, sent a letter dated October 26, 2007 to Mr. Ruest of PGCL. That letter is reproduced below:

Our Ref: 90927-310

VIA FACSIMILE NO. 204 943 2574
VIA E-MAIL Jean-MarcRuest@jri.ca

October 26, 2007

Jean-Marc Ruest
Vice-President, Corporate Affairs
and General Counsel
James Richardson International
2800 One Lombard Place
Winnipeg, Manitoba
Canada R3B 0X9

Dear Mr. Ruest:

Re: Pioneer Field Signs

We represent Pioneer Hi-Bred International, Inc. ("Pioneer Hi-Bred") in Canadian intellectual property matters.

Our client has recently learned that field signs bearing the trade-mark/trade-name PIONEER are being used by your company. Photographs of representative signs are attached.

As you are aware from previous correspondence from our client, Pioneer Hi-Bred is very concerned about the usage of these signs. The signs display the trade-mark/trade-name PIONEER used in association with the trade-marks DeKalb and InVigor, for identification of seed crops in the fields. These signs thereby falsely suggest that the resulting crop is either grown from our client's seed, and/or a collaborative seed product from Pioneer Hi-Bred and DeKalb or InVigor.

Furthermore, while these signs appear to bear an almost illegible notice that PIONEER, in association with seeds, is a trade-mark of our client and under licence, the text is so small that it fails to reasonably provide notice to the public, or indeed, effective notice at all.

Understandably, our client considers this to be [an] extremely serious and important matter.

It is particularly troublesome that this issue also arose last year, as noted by the enclosed correspondence.

Your company has expressly apologized for the use of such signs, recognized that the use of these signs "goes against the spirit of our trade-mark agreement", and indicated that all such signs had been removed.

Given your failure to comply with the terms of the 1996 cross-licences between the parties, and continued misuse of our client's trade-mark and trade-name in association with seeds, our client requires your written undertaking, within **ten (10) days** of this letter, that all such field signs have been removed. Furthermore, in the circumstances, Pioneer Hi-Bred requires an executed affidavit confirming that all such signs have been removed and destroyed, and will not be used again in the future.

Additionally, we have been provided with a copy of your August 28, 2007 letter to our client, in relation to use of the trade-name "Richardson Pioneer" or "Pioneer" *per se*. We also request that you confirm that you will not be conducting business, outside Canada, under any trade-name or trade-mark using "Pioneer", given that your letter failed to address this point.

Finally, with respect to the proposed use of "Richardson Pioneer" or "Pioneer" *per se*, we remind you that paragraph 5 of the February 14, 1996 cross-licence specifically provides that such use is not to depreciate the goodwill attaching to our client's trade-mark and trade-name PIONEER. Consequently, the use by your company of either "Richardson Pioneer" or "Pioneer", *per se*, would breach both the spirit and terms of the April 22, 1974 agreement and the February 13, 1996 cross-licences.

Should your company fail to comply with its obligations and the terms of these agreements, you will appreciate that our client will be compelled to take necessary action. However, in order to determine whether any such action may be avoided, our client is prepared to meet with you in order to discuss and try to reconcile these important issues further.

We look forward to hearing from you as soon as possible.

Yours very truly,

SMART & BIGGAR

"Signed"

Mark K. Evans

MKE/sl
Encls.

[63] This October 26, 2007 letter (the "first letter") raised three apprehended breaches of the 1996 agreement. They related:

1. to field signs,
2. the use of PIONEER trademark outside of Canada, and
3. the use of "RICHARDSON PIONEER" or "PIONEER" by PGCL.

Field Signs

[64] Respecting field signs, this first letter stated that PHI had recently learned "PIONEER" field signs were being used by PGCL in association with the trademarks DeKalb and InVigor. Photographs of representative signs were attached to the letter. Mr. Evans stated those signs falsely suggested that the resulting crop was either grown from PHI's seed and/or a collaborative seed product from PHI and DeKalb or InVigor. The letter made the following demand with respect to those signs:

> Given your failure to comply with the terms of the 1996 cross-licences between the parties, and continued misuse of our client's trade-mark and trade-name in association with seeds, our client requires your written undertaking, within **ten (10) days** of this letter, that all such field signs have been removed. Furthermore, in the circumstances, Pioneer Hi-Bred requires an executed affidavit confirming that all such signs have been removed and destroyed, and will not be used again in the future.

[65] Having received the above first letter, Mr. Ruest directed Tom Hamilton, Assistant Vice-President of PGCL, to instruct all area business managers and location managers to stop using all field signs and to remove those in use. Mr. Hamilton provided those instructions to all PGCL business managers. Those instructions were in turn communicated down the chain of command to PGLC's

75 location managers. By November 27, 2007, Mr. Hamilton had received confirmation from all area business managers that all "PIONEER" field signs had been removed.

[66] Pursuant to the confirmation received, on November 27, 2007, PGCL's counsel at the time sent a letter to Mr. Evans responding to the issues set out in the first letter. Counsel, Mr. Stéphane Caron, stated the following:

> Our client confirms that steps have been taken to remove the field signs in issue. To the best of our client's knowledge, all such composite field signs have now been removed. This is being done in the spirit of cooperation with your client and without prejudice. Further, while it appears that this issue has arisen once before in 2006, the matter was dealt with promptly at the time and the signs were immediately removed. In the same spirit of cooperation, our client is also taking steps to address the matter going forward. Our client has noted your concerns with respect to the sufficiency of the notice of licence. In the circumstances, we do not see the need for an affidavit to be executed. Such measure appears inconsistent with the longstanding relationship between our clients. [Emphasis added.]

[67] PHI's counsel, Mr. Evans, sent a letter in response to Mr. Caron dated January 23, 2008. The letter states, at p. 1:

> We acknowledge receipt of your representation and undertaking that your client has removed the PIONEER field signs in issue, and that your client "is also taking steps to address the matter going forward". While we are hopeful that this activity will not be repeated, we must stress that any future breaches will not be tolerated in any manner, and will force our client to consider terminating the licence agreements. [Emphasis added.]

[68] As indicated in his affidavit sworn December 11, 2009 at page 19, paragraph 38, it was Mr. Ruest's understanding that the above underlined wording indicated PHI's acceptance that the steps had been taken by PGCL to rectify this issue. Such an understanding on the part of Mr. Ruest, in my view, was not unreasonable. I note that PGCL has adduced evidence that it (PGCL)

had never used field signs subsequent to November 27, 2007 (the date of Mr. Caron's letter). Mr. Hall of PHI has in fact conceded that PHI had no evidence of PGCL using any field signs subsequent to November 27, 2007.

[69] I agree with PGCL that the 1996 agreement is clear. When provided with notice of an apprehended breach, PGCL is required to rectify the breach in 30 days (and not 10 days as per the demands set out in the first letter). The 1996 agreement does not state that the rectification must be supported by an undertaking or an affidavit or that the rectification must be to the satisfaction or approval of PHI. Based on my review on the entirety of the evidence, there appears to be no evidence which would demonstrate that the issue of the field signs was not remedied within 30 days.

[70] Accordingly, PGCL's use of "PIONEER" field signs was, in fact, a breach of the 1996 agreement. However, on the evidence before me, I find and have concluded that that breach was rectified in 30 days in accordance with paragraph 12(1)(c) of the 1996 agreement.

Use of PIONEER Trademark Outside Canada

[71] The second apprehended breach set out in the first letter concerns any use by PGCL of the trademark or trade name PIONEER outside Canada. Mr. Evans requested of PGCL in the first letter, to confirm that it would not be conducting business outside Canada under any trademark or trade name using PIONEER.

[72] The license in the 1996 agreement would seem to be directed to the use of the trademark in a defined territory (in Canada). Activities outside of the territory are neither licensed nor prohibited by the 1996 agreement. As a result, PGCL is right to argue that the second apprehended breach raised by Mr. Evans in the first letter is not relevant in this litigation. This was acknowledged by Mr. Hall during his examination for discovery. PHI is not relying on this issue in this litigation.

Use of "RICHARDSON PIONEER" or "PIONEER" by PGCL

[73] The final apprehended breach referred to in the first letter concerns PGCL's intended use of the trademark RICHARDSON PIONEER and its ongoing use of the trademark PIONEER.

[74] The subject of the RICHARDSON PIONEER trademark was first discussed by the parties in a telephone conversation between Mr. Kevin Jacobson of RICHARDSON and Mr. Hall in early June 2007. In that conversation, Mr. Jacobson advised Mr. Hall that RICHARDSON and PGCL were considering a rebranding initiative whereby PGCL would use in the future, the trademark and trade name RICHARDSON PIONEER (rather than PIONEER). Mr. Jacobson asked Mr. Hall whether PHI had any concerns with the rebranding initiative. Mr. Hall said that he would review the request with a few people within the PHI organization and then respond to Mr. Jacobson. In an e-mail dated June 19, 2007, Mr. Hall communicated to Mr. Jacobson that he had concerns about the rebranding initiative. In that e-mail, Mr. Hall stated as follows:

> To the extent JRI is only considering the name change in Canada, then, as explained, we are willing to work with you to find a solution for your grain elevator services. However, you may not use "Pioneer" (in any context) as a name or mark for seeds and inputs other than as set forth in our existing agreement. As advised, we believe your use of the "Richardson Pioneer" name or mark for the distribution of seed products will cause confusion in the marketplace. The "Grain" portion of the "Pioneer Grain" name helped differentiate our companies' separate identities. Its removal undermines the delicate balance reached from carefully crafted agreements and significantly raises the prospects of marketplace confusion. As such, without a concrete timing proposal for phasing out the "Pioneer" name with the "Richardson" name, we cannot provide our "OK" to your use of the "Richardson Pioneer" name.

[75] In a letter dated August 7, 2007, Mr. Daniel Jacobi of PHI sent a letter to Mr. Ruest wherein he advised that PHI would not consent to the rebranding initiative because the trademark RICHARDSON PIONEER would create a heightened opportunity for confusion among the trade as to a possible relationship between PGCL and PHI. Mr. Jacobi went on to state:

> We have learned that JRI is now referring to Pioneer Grain simply as "Pioneer" (without the word "Grain"). Further still, we understand that JRI has notified at least one Canadian seed company that it can now access "global markets through Pioneer." A copy of a mailing you sent to the trade is attached for your reference.
>
> This issue needs to be promptly resolved, as the "Pioneer Grain" trade name may not be shortened to simply "Pioneer" in Canada. While it is not completely clear from the text of the attached letter, we want to reiterate that you may not conduct business outside Canada under any name or mark using "Pioneer." Failing our ability to promptly address these concerns, we will take all further action to ensure "Pioneer" (on its own, as opposed to "Pioneer Grain") is not used to refer to your company in Canada, and that any use of "Pioneer" (in any manner) is not used outside of Canada. [Emphasis added.]

[76] It is clear that Mr. Ruest did not accept Mr. Jacobi's interpretation of the 1996 agreement. On August 28, 2007, Mr. Ruest sent Mr. Jacobi a letter which sets out PGCL's differing position. In the letter, Mr. Ruest notes:

> Neither the agreement nor the licenses require Pioneer Grain Company, Limited to refer to itself as "Pioneer Grain" and not "Pioneer". In fact the license issued in favour of Pioneer Grain Company, Limited specifically recognizes that Pioneer Grain Company, Limited carries on business under its corporate name, and under the trade-marks and trade-names PIONEER GRAIN, PIONEER, THE PIONEER and others which include the word "Pioneer". The license agreement further provides Pioneer Grain Company, Limited with a license to use and display the word "Pioneer" in a trade-mark, corporate name or trade-name subject to certain terms and conditions.
>
> Accordingly, the corporate use of "Pioneer" either alone or in combinations such as "Pioneer Grain" or "Richardson Pioneer" does not contravene the terms of the aforementioned agreements. We are also aware of the restrictions imposed by the license on our use of the word "Pioneer" as a trade-mark, corporate name or trade name and are satisfied that we are in full compliance with our obligations.

[77] In contrast to Mr. Ruest's interpretation of the 1996 agreement as expressed above, it is interesting to note the different interpretation put forth by PHI as it was set out in the first letter, at p. 2:

> Finally, with respect to the proposed use of "Richardson Pioneer" or "Pioneer" *per se*, we remind you that paragraph 5 of the February 14, 1996 cross-licence specifically provides that such use is not to depreciate the goodwill attaching to our client's trade-mark and trade-name PIONEER. Consequently, the use by your company of either "Richardson Pioneer" or "Pioneer", *per se*, would breach both the spirit and terms of the April 22, 1974 agreement and the February 13, 1996 cross-licences. [Emphasis added.]

[78] Again, based on his understanding which in my view, was not unreasonable, Mr. Ruest believed that the position of PHI in the above letter was that PGCL was never allowed to use the trademark RICHARDSON PIONEER or PIONEER under the 1996 agreement. As set out in Mr. Ruest's letter dated August 28, 2007, paragraph 5 of the Recitals on the 1996 agreement states that PGCL "carries on business under its corporate name, and under the trade-marks and trade-names PIONEER GRAIN, PIONEER, The PIONEER and others which

include the word 'Pioneer' in Western Canada ...". For its part, paragraph 1 of the grant provides PGCL with a license to "use, advertise and display the word PIONEER in the Territory as or in a trade-mark, corporate name or trade name in association with agricultural seeds, grains and legumes; ...". When these two paragraphs are taken together, it seems clear that Mr. Evans' interpretation of the 1996 agreement could lead to an absurdity. I agree with PGCL's argument that, properly understood, the 1996 agreement permits PGCL to use the word "PIONEER" provided that PGCL uses the trademark in a manner that complies with the balance of the terms set out in that agreement. Indeed, during his examination for discovery, Mr. Hall acknowledged that that interpretation of the 1996 agreement is correct.

[79] Respecting then the first letter, Mr. Evans was not taking issue with the manner in which the trademarks were being used. Rather, he seems to be questioning whether they could be used at all. On my reading of the 1996 agreement, such a stark preemption seems inconsistent with both the spirit and terms of the agreement. For that reason, Mr. Ruest believed (and did so reasonably) that the demand made by Mr. Evans in that regard was unjustified and that PGCL was within its rights to ignore it.

[80] Accordingly, I have come to the conclusion that the alleged second apprehended breach set out in the first letter (that the use by PGCL of the trademarks "RICHARDSON PIONEER" or "PIONEER" would, in and of itself, breach the spirit and terms of the 1996 agreement) was not in fact an actual

breach of the 1996 agreement. There was thus no obligation on the part of PGCL to follow the demand made by Mr. Evans.

The Second Letter of May 16, 2008 and The Third Letter of July 22, 2008

[81] The termination letter sent by Mr. Hall on August 28, 2008, also made reference to PHI's letter dated May 16, 2008 (the "second letter") and PHI's letter dated July 22, 2008 (the "third letter"). While those second and third letters raised many of the issues set out in the first letter, there was also raised in the termination letter, what could be considered the following new issues:

1. an allegation by PHI that PGCL had expanded its involvement in the seed business;
2. an allegation that PGCL had increased its use of the PIONEER trademark; and
3. an allegation that some use of the trademark PIONEER in PGCL's advertising and marketing of third party seed products was confusing.

[82] In the second letter sent by PHI's Canada Business Director and President, Ian Grant, the following is noted, at pp. 1, 2:

> ... Our people have also seen an increase in stand-alone use of PIONEER in your marketing materials and website, as well as some use of PIONEER in your advertising and marketing of third party seed products, which we think is confusing.
>
> These activities greatly concern us because they depreciate and hurt the goodwill of our PIONEER name for our seed business in Canada. A[s] such, we need you to stop such use.

[83] On July 22, 2008, in the third letter, Mr. Jacobi of PHI writes as follows, at pp. 1, 2:

> As you know, it is PHI's position that we have always owned the exclusive rights to the PIONEER brand in association with any seed business in Canada. While JRI may have sold small amounts of secondary farm seeds at your grain elevators some time prior to 1996, the only reason we licensed JRI that year was because JRI began selling PHI's canola seed then, and the parties wished to avoid any confusion as to the source of that canola seed given that Pioneer Grain was selling such seed.
>
> As you know, under the 1996 cross licenses, JRI and Pioneer Grain assigned all right, title, and interest in and to the PIONEER brand name that you may have acquired in association with agricultural seed products prior to 1996. Accordingly, any rights you may have owned were acquired by PHI. Since that date, any use by you in Canada has been under license and is deemed use by PHI, not JRI or Pioneer Grain. To the extent any use was unlicensed, such use would constitute an infringement of PHI's exclusive rights to the PIONEER trade-mark and trade name as used with any seed business.
>
> Since that license, and in particular more recently, JRI appears to have expanded its involvement in the seed business through an affiliation originally with United Grain Growers and now with the DeKalb, In[V]igor and Nexera brands, to market and sell third party seed products in association with the PIONEER GRAIN trade name and PIONEER brand alone. This expanded activity is unacceptable to PHI. The only means to avoid confusion and depreciation of PHI's goodwill and reputation in its PIONEER brand is for JRI to cease all use of PIONEER GRAIN or PIONEER in association with the marketing, distribution, and sale of any seed products, including third party seed products. Unless you are prepared to take steps to do so, no amicable resolution of this matter will occur.

[84] I agree with PGCL that PHI's position (as set out in its second and third letters) that there is a limit with respect to how often "PIONEER" can be used as a stand-alone trademark (or that there is a cap on the amount of third party seed that can be sold by PGCL) is erroneous.

[85] Again on my reading of the entirety of the 1996 agreement, there appear to be no such limits set out. Further, it would appear that the trademark PIONEER can be used by PGCL to sell third party seed provided that PGCL uses

the trademark in a manner that complies with the balance of the terms of the 1996 agreement. This was acknowledged by Mr. Hall of PHI in his examination for discovery.

[86] The other issue raised by PHI in the second letter arises where Mr. Grant writes "Our people have also seen … some use of PIONEER in your advertising and marketing of third party seed products, which we think is confusing". In making that comment, I note that no details or examples were provided respecting the advertisements or marketing materials that PHI alleges were confusing. PGCL is right to pose the following questions:

- How was PGCL supposed to know what the precise issue was?
- How was it supposed to correct any such issue?

[87] As earlier noted in ***Heep v. Thimsen***, *supra*, and ***M.L. Baxter Equipment Ltd. v. Geac Canada Ltd.***, *supra*, for notice to be effective, specifics of the particular breach complained of must be given in sufficient detail so as to enable the party to understand the purported complaint.

[88] Having read Mr. Grant's comments in the second letter respecting the confusing advertisements and marketing materials, I have determined that those comments are far too general so as to constitute effective notice under the 1996 agreement. Insofar as PHI may have clarified its position with respect to the precise nature of PHI's complaints in the three letters (see Mr. Hall's transcript from his examination for discovery attached as Exhibit W to Mr. Ruest's affidavit sworn December 11, 2009), that precision seems to relate to PGCL's use of the

PIONEER trademark in advertisements without including the notice provision set out in paragraph 2 of the 1996 agreement (or, alternatively, that the notice included in the advertisements was too small or otherwise insufficient). Again, even with such subsequent clarification, no mention was made in the three letters with respect to the notice provisions in paragraph 2 of the 1996 agreement nor were examples provided. Put simply, PGCL was entitled to receive clear details of the breach complained of so that it would have full opportunity to correct the breach. No such information was provided.

Was Notice of Termination Given or Required in any of "The Third Letters"?

[89] Separate and apart from what PGCL has properly argued was PHI's inadequate compliance with paragraph 12(1)(c)'s notice requirements (respecting any alleged breaches), PGCL also raises the issue concerning the absence of clear notice regarding termination of the agreement.

[90] Respecting the manner in which a notice of default must be given, the court in ***M.L. Baxter Equipment Ltd. v. Geac Canada Ltd.***, noted the following at pp. 156, 157:

> The purpose of the 90-day period, as I have said, is to allow the defendant to remedy his breach. If he can do so, then according to the terms of the 1976 Agreement, the plaintiff has no cause to complain. It follows, therefore, that the notice which commences this time period must be very clear and precise in order that the defendant realize its import. The defendant must be made aware that the period has begun to run. The letter of April 13th is lacking in many respects. The plaintiff does not say in the letter that the defendant is in breach or in default of its obligation. Nowhere in the letter is reference made to the termination clause nor is any statement made that after 90 days of default Baxter intended to terminate the contract. Taken in the perspective of the relationship between these parties, it is quite easy to see that the

> defendant may not have construed the letter as having the same import which the plaintiff now relies on it for. The parties had numerous communications regarding completion dates for the project, all of which passed with little comment. Now for the plaintiff to rely on this relatively mild letter as notice in respect of the termination of the contract is a distinctly different attitude.
>
> The termination of an agreement is a very serious matter. It is the cessation of a legal relationship between two parties which most often leads to costly legal actions, such as this one, in order to settle the differences between them. A notice, therefore, which is the commencement of the termination procedure must be one which brings home to the party to be charged the purpose thereof so that it may be said that there was no doubt that the defendant realized the serious consequences of his inaction. The letter of April 13th is not such a notice. No proper notice having been given to the defendant, it follows that the 90-day period never began to run and, therefore, the plaintiff's termination was a wrongful one.
>
> [Emphasis added.]

[91] I note that in none of the three letters in question, was reference made to the termination clause, nor was there any statement that after 30 days in default, PHI intended to terminate the 1996 agreement. Even if PGCL did not and does not now acknowledge or concede that all of the demands made in the letters were justified, it is nonetheless reasonable to ask how, notwithstanding PHI's various demands for compliance, was PGCL to know that termination was even contemplated as a possibility, let alone one which might be imminent?

[92] Respecting PHI's termination of the 1996 agreement pursuant to paragraph 12(1)(c), I have determined that if any breaches were clearly identified in the three letters and if any of those alleged breaches did in fact constitute actual breaches, such breaches were remedied by PGCL within 30 days.

[93] I have also concluded that if and when any alleged breaches were not remedied by PGCL, I have determined that sufficiently clear notice of such breaches (and the intention to terminate) was not provided to PGCL.

[94] In the result, I have concluded that PGCL has established on a *prima facie* basis that insofar as part of PHI's action rests on its termination of the 1996 agreement based on its invocation of paragraph 12(1)(c) of that agreement, that part of PHI's action must fail. I have further concluded that in its responding proof (and on the basis of the totality of the evidence) PHI has failed to establish that there is, respecting its termination pursuant to paragraph 12(1)(c), a genuine issue for trial with "a real chance of success".

2. Is there a genuine issue for trial with respect to whether PHI was entitled to terminate the 1996 agreement on the basis of fundamental breach?

[95] PGCL argues that when the evidence on this motion respecting all of the so-called breaches (individually and collectively) is examined, it should be apparent that PGCL committed only a very small number of breaches over a 12-year period. Moreover, PGCL maintains that those breaches were not for the most part (as reflected in PHI's responses or non-responses) perceived by PHI to be serious.

[96] PGCL also emphasizes that to the extent any breaches might have occurred (and only a small number are conceded), there was no actual or potential harm to PHI as a result of any such breaches. In that regard, PGCL vigorously argues that the evidence on this motion is inadequate to support PHI's

position that “serious” breaches over an extended period of time have had the cumulative effect of deceiving or confusing customers or potential customers and/or depreciating the distinctiveness and goodwill attaching to PHI’s trademark and trade name PIONEER.

[97] In addition to minimizing the number, frequency and seriousness of any such alleged breaches and any alleged corresponding effect on the depreciation of the distinctiveness of the trademark and trade name, PGCL specifically impugns the evidence or the absence of evidence respecting “confusion”. In that connection, PGCL points to Mr. Hall’s examination for discovery in June 2009 where he acknowledged that he was not aware of any instances of actual confusion subsequent to the parties’ entering into the 1996 agreement. PGCL also impugns the reply affidavits of PHI wherein they attempt to adduce evidence (respecting confusion) through what PGCL describes as “double and triple hearsay statements” originating from individuals who have apparently refused to swear affidavits in this proceeding.

[98] In short, it is PGCL’s position that when the court takes a “good hard look” at the totality of the evidence, the court ought to conclude that there was no actual or potential harm to the distinctiveness attaching to PHI’s trademark and trade name PIONEER. According to PGCL, the relevant evidence to be considered on this motion should encompass the number of and responses by sales representatives that PHI had in the community, sales representatives who were aware of PGCL’s activities and who, presumably, would have been vigilant

about and sensitive to the issues of confusion and potential confusion. PGCL also suggests that the relevant evidence to be examined would include the manner in which Mr. Hall himself responded (or did not respond) to any ongoing issues and/or any of the relatively small number of minor breaches that PGCL concedes might have occurred over a 12-year period.

[99] It is on the basis of the above that PGCL suggests it has proven, *prima facie*, that PHI was not entitled to terminate the 1996 agreement for fundamental breach. Further, PGCL submits that, for its part, PHI has not presented evidence that identifies a genuine issue for trial.

[100] PHI responds by insisting the evidence demonstrates that PGCL has committed numerous breaches of the 1996 agreement, starting in 1999 and continuing to the present day.

[101] PHI reminds the court that the very purpose and intent of the parties entering into the 1996 agreement was to confirm and ensure the integrity and distinctiveness of the PIONEER trademark and trade name. In connection with how that intended protection and benefit to PHI has been compromised, it is alleged by PHI (as set out in its motions brief, at pp. 53, 54) that the following represents instances of breaches of the 1974 and 1996 agreements:

> (a) The Defendants' use of trade-marks incorporating PIONEER without any notice of the License and PHI's ownership of the PIONEER Trade-mark in association with the sale of seed on:
>
> (i) grain elevators/distribution centers, from 1999 to as late as December 2009; ...

(ii) plastic bags containing seed samples, from 1999 to as late as May 2001; ...

(iii) invoices for the sale of seed only, from 1999 to as late as March 2010; ...

(iv) marketing materials, from 1999 to as late as 2007; ...

(v) field signs from at least 2001 to as late as April 2007; and

...

(vi) on the Defendants' website from at least February to September 2008. ...

(b) The Defendants' use of trade-mark incorporating PIONEER with notice, but where such notice was not adequate to clearly or conspicuously put consumers on notice of the License and PHI's ownership of the PIONEER Trade-mark in association with the sale of seed, on

(i) field signs, from April 2007 to as late as November 2007; and ...

(ii) marketing materials, in at least 2001; and ...

(iii) assuming that the Defendants' affiants are believed, on the Defendants' website from at least February to September 2009. ...

(c) The Defendants' increased use of PIONEER (on a stand alone basis), PIONEER GRAIN and PIONEER RICHARDSON in association with the distribution and sale of seed products, including

(i) increased sale and distribution of third party competitor seed products, some of lower quality [than] the Plaintiffs' seed; and ...

(ii) stand alone use of PIONEER on field signs and marketing materials, including the Defendants' website. ...

(d) The Defendants' filing of three trade-mark applications for RICHARDSON PIONEER, and associated design trade-marks, in association with the sale of seed.

[102] By doing the above, PHI accuses PGCL of affecting the core value and goodwill (and therefore the distinctiveness) of PHI PIONEER's trademark and

trade name. PHI argues that the impugned activities of PGCL are likely to mislead or deceive the public of the origin of seed product coming from PGCL and the worrying result is the consequent depreciation in the value of the goodwill attaching to that trademark and trade name.

[103] Based on the evidence adduced on this motion and the nature of the issues at play in this action, PHI argues that it is not possible for PGCL to contend that it has proved *prima facie*, that PHI's action as to fundamental breach must fail. Neither can it be convincingly argued, says PHI, that it has failed to demonstrate a genuine issue for trial.

[104] Given the nature of the evidence on this motion and what I find was the apparent "give and take" and ongoing dialogue that existed between the parties (during the period from 1996 to 2008) in what was clearly a delicate *modus vivendi* (based upon the 1996 agreement), PHI's actions or inactions (see paras. 31-44, *supra*) at the time of many of the alleged pre-2008 breaches, seem somewhat inconsistent with its current allegation of fundamental breach. Although I acknowledge the existence of paragraph 16 of the 1996 agreement (stipulating that no failure or delay by PHI in giving notice or in exercising the rights or remedies available to it constitutes a waiver of such rights and remedies), the timing in this action of PHI's somewhat belated claim of "fundamental" breach, in light of its own previous inaction, seems both incongruous and as PGCL suggests, suspect. In that regard, I note that PHI did not raise the issue of fundamental breach or repudiation until after PHI was

served with PGCL's pre-trial brief, wherein PGCL's analysis compellingly identified the weaknesses in PHI's termination of the agreement on the basis of paragraph 12(1)(c). My acknowledged suspicion in that regard, while not determinative, has relevance to the credibility of PHI's use of the adjective "fundamental" when describing the gravity of the alleged individual and cumulative breaches. In that regard, I note that in ***1193430 Ontario Inc. v. Boa-Franc (1983) Ltée.*** (2005), 260 D.L.R. (4th) 659, the Ontario Court of Appeal placed weight on the conduct of the plaintiff. At para. 56 the court observed the following:

> **56** Although the trial judge was clearly very concerned about this behaviour on the part of M. Thabet, she concluded that it did not change the fact that Boa-Franc was entitled to terminate the contract because of Salem's breach of its obligation of good faith. It may be true that the innocent party's conduct will not change the effect of an ordinary breach on which one could sue for damages. But where the innocent party seeks to terminate its obligations under the contract for fundamental breach, relying in part on the effect of the breach, the innocent party's own conduct under the agreement becomes an important barometer of the true significance of the same breach by the offending party. Where M. Thabet was prepared to conceal critical information from Salem that he was considering taking over the distribution of the product himself, and where he was prepared to lie to Salem in order to collect his accounts receivable during the currency of their arrangement, it can hardly be said that he valued good faith and good communications as critical features of their business arrangement. [Emphasis added.]

[105] Not only is there on the totality of the evidence a general absence of a commensurate reaction and response by PHI and its agents (to the impugned PGCL's activities they knew about at the time), I find to the contrary that the available evidence suggests that Mr. Ruest's earlier mentioned characterization (as set out at paragraph 19 of PGCL's brief) more or less accurately describes the state of the *modus ivendi:*

> 19. By all appearances, the parties peacefully co-existed in the marketplace over the course of the next ten years. PGCL continued to sell agricultural seeds produced by various suppliers, including varieties produced by PHI. Any issues that developed during this period of time were dealt with practically and on an amicable basis.

[106] To the extent required to decide the first issue on this motion (respecting the validity of PHI's termination of the 1996 agreement pursuant to paragraph 12(1)(c)), I have already made certain determinations respecting some of what PHI says were pre-2008 breaches. Respecting any and all other pre-2008 breaches as identified by PHI, I am not persuaded that those now identified other alleged pre-2008 breaches (if and where they exist) - either individually or with their so-called cumulative force - constitute either in seriousness or frequency, the sort of violation or violations that would represent the suggested fundamental breach that would justify PHI's assertion that PGCL repudiated the 1996 agreement. In so commenting, however, I wish to emphasize my stipulated reference to alleged pre-2008 breaches. Such chronological precision is relevant because, as will become apparent from these reasons, for the purposes of disposing of this part of PGCL's summary judgment motion (respecting PHI's claim of fundamental breach), "the genuine issue for trial" that does more specifically and obviously manifest, is an alleged breach that occurs as late as July 2008.

[107] I have determined that based on the evidence on this motion, the following does indeed constitute the one and only genuine issue for trial:

> *Did PGCL commit a fundamental breach amounting to repudiation when it filed in July 2008, three trademark applications (for RICHARDSON*

> *PIONEER and associated design trademarks) in association with the sale of seed?*

[108] The remainder of this judgment will set out my analysis and reasons for having found the one genuine issue that I identified above.

The Governing Law Respecting Fundamental Breach

[109] The leading case in respect of the doctrine of fundamental breach had been the Supreme Court of Canada judgment of ***Hunter Engineering Co. v. Syncrude Canada Ltd.***, [1989] 1 S.C.R. 426. In that case, the court suggested that whether a breach was "fundamental" was a question of contract construction. In that regard, Wilson J., at page 499, quoting Lord Diplock in ***Photo Production Ltd. v. Securicore Transport Ltd.***, [1980] A.C. 827 (H.L.), at p. 849, noted that a fundamental breach occurs:

> ... "Where the event resulting from the failure by one party to perform a primary obligation has the effect of depriving the other party of substantially the whole benefit which it was the intention of the parties that he should obtain from the contract" (emphasis added).

and at page 500:

> ... It seems to me that this exceptional remedy should be available only in circumstances where the foundation of the contract has been undermined, where the very thing bargained for has not been provided.

[110] In its more recent decision in ***Tercon Contractors Ltd. v. British Columbia (Transportation and Highways)***, 2010 SCC 4, 315 D.L.R. (4th) 385, the Supreme Court of Canada "laid to rest" the concept of fundamental breach in respect of exclusion clauses. While not doing away with the doctrine of fundamental breach altogether, the court did express its view that some of the phraseology or jargon associated with fundamental breach is not always of

assistance and that in the end, the main issue for determining the gravity of the breach or breaches remains the proper interpretation of the entire contract in light of its purposes and commercial context.

[111] Although decided prior to the Supreme Court of Canada judgment in ***Tercon***, *supra*, the Manitoba Court of Appeal in ***Selkirk Petroleum Products Ltd. v. Husky Oil Ltd.***, 2008 MBCA 87, 231 Man.R. (2d) 1 (C.A.), reviewed and set out the still relevant and underlying principles of fundamental breach of contract. In my view, those principles continue to be reconcilable and consistent with ***Tercon***. In that regard the following should be noted:

1. a fundamental breach can be described as one that has "frustrated the commercial purpose of the entire venture";
2. the question of a fundamental breach must be reviewed contextually depending on the particular contract in question;
3. in determining the issue of fundamental breach, the court needs to consider the terms of the contract, the intended benefit to the innocent party, the purpose of the contract, and the extent to which the loss incurred by the innocent party can be remedied adequately by an order of damages; and
4. the concept of fundamental breach seems to transcend the normal issues of contractual interpretation insofar as it involves investigating the underlying nature and purpose of the contract into

> which the parties have entered and the respective benefits designed to be maintained or ensured by agreement.

[112] Where there is a breach of an agreement by a party in a manner that is fundamental, it is said that the breaching party repudiates (refuses to perform) the agreement. The other party who continues to have obligations to perform is then entitled to accept the repudiation and treat the agreement as at an end, thereby releasing both parties from further performance. However, the breaching party remains liable to perform obligations incurred at the time of election by the innocent party and also to pay damages. The contract is not rescinded, but the parties are discharged from future obligations. At the same time, any rights and obligations that have already matured are not extinguished. See ***Doman Forest Products Ltd. v. GMAC Commercial Credit Corp. - Canada***, 2007 BCCA 88, 65 B.C.L.R. (4th) 1, at para. 88, ***Selkirk Petroleum Products Ltd. v. Husky Oil Ltd.***, *supra*, at para. 38; and ***Guarantee Co. of North America v. Gordon Capital Corp.***, [1999] 3 S.C.R. 423, at paras. 41 and 48.

[113] A fundamental breach may be found in the cumulative effect of numerous breaches, even where each breach individually would perhaps not be fundamental. See ***Kussmann v. AT & T Capital Canada, Inc.***, 2002 BCCA 281, 100 B.C.L.R. (3d) 278 (C.A.), at para. 16.

[114] Whether a party knew of a fundamental breach at the time of termination, or whether a party may have terminated the contract for different reasons, is not

determinative with respect to a claim for fundamental breach. The important question is whether the allegedly aggrieved party has a right to terminate under the general law (as opposed to a right specifically conferred by contract), and, if the aggrieved party has such a right, it is immaterial that the aggrieved party chose to exercise a contractual right to terminate. See ***Carr v. Fama Holdings Ltd.*** (1989), 40 B.C.L.R. (2d) 125 (C.A.) and ***Celgar Limited v. Star Bulk Shipping Company***, [1979] 4 W.W.R. 248 (B.C.C.A.).

[115] I note as argued by PHI, that a contract can be terminated for fundamental breach despite the existence of termination provisions in the agreement, including termination through notice provisions. In that regard, PHI reminds the court that paragraph 16 of the 1996 agreement confirms this principle, namely, that the exercise by PHI of any right or remedy provided by the 1996 agreement does not prevent PHI from exercising any other right or remedy, either concurrently or separately. See also ***Norwood Construction Ltd. v. Post 83 Co-operative Housing Association*** (1988), 30 C.L.R. 231 (B.C.C.A.); ***Cheater (B.J.) Enterprises Ltd. v. Minox Equities Ltd.*** (1992), 79 Man.R. (2d) 167 (Q.B.).

The 1974 and 1996 Agreements and PGCL's July 2008 Trademark Applications

[116] The 1974 and 1996 agreements contain provisions which in my view, have obvious relevance as to PGCL's trademark applications and PHI's connected claim for fundamental breach.

[117] Paragraph 2 of the 1974 agreement reads as follows:

> 2. The Parties of the First Part, jointly and severally, undertake, covenant, promise and agree on behalf of themselves, their successors, licensees and assigns not to register or use the trade mark PIONEER or any trade mark embracing such word, in Canada, in association with agricultural seeds, grains, legumes, animal semen and live animals and animals for breeding, nor to challenge the use or any registration of the trade mark PIONEER, in Canada, for agricultural seeds, grains, legumes, animal semen and live animals and animals for breeding by or in the name of PIONEER HI-BRED, its successors and assigns;
> [Emphasis added.]

[118] Paragraphs 9 and 10 of the 1996 agreement read as follows:

> 9. PHI, PHL, RICHARDSON and LICENSEE acknowledge the full force and effect of the 1974 Agreement which, subject to this Agreement, continues in force between the parties, but recognize that the parties may construe its rights and obligations differently.
>
> 10. To the extent that LICENSEE and RICHARDSON may have acquired any right, title in or to the trade-mark and trade-name PIONEER (whether alone or in combination with other words) for use in association with Wares, or with the Services of the offer for sale, sale, consultation, distribution and/or delivery of agricultural seed to farmers, and notwithstanding any terms and conditions of the 1974 Agreement interpreted as prohibiting such acquisition and use, LICENSEE and RICHARDSON assign and quit claim any right, title or interest in or to such trade-mark and trade-name to PHI.

[119] On July 25, 2008 and July 28, 2008, PGCL filed the following Canadian trademark applications:

- Serial number 1404840 - RICHARDSON PIONEER
- Serial number 1405127 - RICHARDSON PIONEER & Design; and
- Serial number 1405128 - RICHARDSON PIONEER & Design.

[120] Each of the above applications included a claim of proposed use of the trademarks in Canada in association with, *inter alia*, the sale of seeds and legumes and the sale of oil seeds. In addition to representing what they say is a fundamental breach of the 1974 and 1996 agreements, PHI argues that the

above trademark applications represent more generally, a culmination in the attempted expansion of PGCL's activities in the seed business and the use of the PIONEER trademark since entering into the 1996 agreement (at which time PGCL was primarily selling UGG seed sourced from PHI). PHI contends that the trademark applications and the expanded activities of PGCL generally, increase the likelihood of confusion in the marketplace as it related to the PIONEER trademark. Avoiding such confusion and the dilution of distinctiveness is a basic and fundamental purpose of any trademark. The same purpose can be ascribed to the relevant provisions of the 1974 and 1996 agreements.

[121] Although I will in no way predict the trial judge's ultimate determination, I am of the view that as it relates to PHI's fundamental breach claim, PHI's specific arguments concerning the issue of PGCL's July 2008 trademark applications represent the basis of an issue with "a real chance of success".

[122] It is obvious that in the present case, when addressing issues connected to such phrases as the likelihood of "confusion in the marketplace", this court risks entering the realm of trademark law. Although I recognize that PHI's action in this court is "in contract" and is not intended to adjudicate an alleged trademark infringement *per se*, given the nature and purpose of the 1974 and 1996 agreements - and the intended benefit for PHI - the consideration on this motion of trademark concepts and principles is both necessary and unavoidable in order to explain why there is indeed a genuine issue as to whether PGCL's July

2008 trademark applications represent a potential breach "frustrating the commercial purpose of the entire venture". See ***Selkirk Petroleum Products***.

Basic Trademark Principles and Concepts

[123] The fundamental purpose of trademarks is to distinguish wares or services manufactured, sold, leased, hired or performed by the trademark owner from the wares and services of others. See ***Mattel, Inc. v. 3894207 Canada Inc.***, 2006 SCC 22, [2006] 1 S.C.R. 772, at para. 2.

[124] In addition to that purpose, trademarks serve at least two important functions. First, trademarks protect the interests of trademark owners from unfair competition. Second, trademarks protect consumers from deception due to confusing use of trademarks. This is done in part by assuring consumers that they are buying from a single source, and receiving the character and quality of wares or services that they associate with that particular trademark. See ***Ciba-Geigy Canada Ltd. v. Apotex Inc.***, [1992] 3 S.C.R. 120, at pp. 134-141; ***Mattel, Inc. v. 3894207 Canada Inc.***, *supra*, at paras. 2 and 21.

[125] The foundation for trademark rights is the concept of "distinctiveness". "Distinctiveness" requires that the trademark actually distinguish the wares or services of one owner from the wares or services of others. "Distinctiveness" is at the very root and is the fundamental requirement of a trademark. Only a distinctive mark will allow the consumer to identify the source of wares or services. See ***Mattel, Inc. v. 3894207 Canada Inc.***, at para. 75; and ***Kirkbi AG v. Ritvik Holdings Inc.***, 2005 SCC 65, [2005] 3 S.C.R. 302, at para. 39.

[126] Confusing or unauthorized use of a party's trademark by others, can result in a lack of distinctiveness in that trademark. Such confusing use or unauthorized use thereby neutralizes the rudimentary purpose of such a trademark. That in turn negates the value of the trademark. See ***Unitel Communications Inc. v. Bell Canada*** (1995), 61 C.P.R. (3d) 12 (F.C.T.D.), at paras. 69 and 70; and ***Windmere Corp. v. Charlescraft Corp. Ltd.*** (1988), 23 C.P.R. (3d) 60 (F.C.T.D.), at paras. 68 and 69.

[127] The importance and prevention of confusing trademark usage has long been recognized at common law in the tort of passing off. That tort involves three elements:

1. the existence of goodwill;
2. the deception of the public due to a misrepresentation; and
3. actual or potential damage to the plaintiff.

See ***Ciba-Geigy Canada Ltd. v. Apotex Inc.***, *supra*, at p. 297.

[128] In a passing-off action, it is not necessary to show any intent by the defendant to deceive or misrepresent, nor it is necessary to show actual confusion, or actual damage to the plaintiff; the probability of confusion and of damages sufficient. The question is whether an ordinary person, presented in a commercial background with a presentation of a product or a business, having at best a general recollection of the product or business of the plaintiff, would, on first impression, be left in a state of confusion as to whether the product or business of the defendant is that of the plaintiff. See ***Eastern Star***

Enterprises Ltd. v. Baci's Pasta Fresca Ltd. (1992), 44 C.P.R. (3d) 199 (B.C.S.C.), at para. 202; and ***Walt Disney Productions v. Triple Five Corp.*** (1994), 53 C.P.R. (3d) 129 (Alta. C.A.), at paras. 141, 142, 144 and 152.

[129] In considering whether there is a likelihood of confusion, a court will look to such factors as the inherent distinctiveness of the trademarks and the extent to which they have become known, the length of time the trademarks have been in use, the nature of the wares, services and business and nature of the trade. A court will also examine the degree of resemblance between the trademarks. See the ***Trade-marks Act***, R.S.C. 1985, c. T-13, s. 6(5). Where there is at least some evidence of actual confusion, such evidence would be adequate to support an inference of the likelihood of confusion, whatever the evidence is on the other side. See ***Asbjorn Horgard A/S v. Gibbs/Nortac Industries Ltd.*** (1987), 14 C.P.R. (3d) 314 (F.C.A.), at para. 331; and ***Coca-Cola Co. of Canada Ltd. v. Bernard Beverages Ltd.*** (1948), 9 C.P.R. 121 (Ex. Ct.), at para. 135.

[130] I have concluded that in filing the trademark applications they did, PGCL may very well be in breach of paragraph 2 of the 1974 agreement, a paragraph whereby PGCL had agreed not to register any trademark embracing the word PIONEER in Canada in association with agricultural seeds, grains and legumes. Paragraph 2 seems clearly designed to protect against confusion and ensure the ongoing distinctiveness of the PIONEER trademark belonging to PHI. PHI's genuine issue and related arguments become no less compelling when one examines paragraph 2 of the 1974 agreement in conjunction with paragraph 10

of the 1996 agreement. In pointing to paragraph 10, PHI reasonably asserts that PGCL gave up any claim that it may have had in and to the trademark and trade name PIONEER in association with the wares and services of the offer for sale, consultation, distribution and/or delivery of agricultural seed to farmers.

[131] On my reading of the 1996 agreement, I agree with PHI that that agreement in no way modified the 1974 agreement prohibiting the registration of any trademark incorporating or using the word PIONEER, in association with agricultural seeds, grains or legumes. In fact, the 1996 agreement, in paragraph 9, confirms the terms of the 1974 agreement and confirms that its terms continue in full force and effect between the parties.

[132] Although PGCL argues that its applications cover services and not wares, and therefore do not constitute a breach of paragraph 2 of the 1974 agreement, I am of the view the jurisprudence in Canada has established that where there exists a relationship between one party's wares and another party's services (in terms of there being overlap in their respective trades), there may well be a likelihood of confusion. Given the longstanding use by PHI of the PIONEER trademark and trade name in Canada in association with seed products, any related services such as sale or distribution of seed could lead to a likelihood of confusion. See ***T. Eaton Co. Ltd. v. Horne & Pitfield Foods Ltd.*** (1976), 32 C.P.R. (2d) 273 (T.M.O.B.), at paras. 282 and 283; and ***Canadian Olympic Association v. Molson Co. Ltd.*** (1978), 47 C.P.R. (2d) 263 (T.M.O.B.), at paras. 272 and 273.

[133] Given the existence of paragraph 2 of the 1974 agreement and what can reasonably be argued is the likelihood of confusion were the trademarks to be granted, I am persuaded that by seeking to register trademarks embracing the PIONEER trademark and trade name in association with seed-related services, PGCL gave rise to the genuine issue as to whether it, PGCL, may be in breach of both the 1974 agreement and as well, paragraph 9 of the 1996 agreement (which affirms the terms of the 1974 agreement).

[134] If a breach is found to have occurred to paragraph 2 of the 1974 agreement, that breach, in my view, could be of a nature so fundamental, that it could have the effect of undermining the foundation of the 1974 and 1996 agreements. A substantial part of that foundation for PHI would have been the intended benefit of protecting the distinctiveness of the PIONEER trademark. Insofar as it can genuinely be argued that there is a likelihood of confusion in the event of the granting of new trademarks which have been applied for, it is reasonable to suggest that PGCL's trademark applications will have had the effect of depriving PHI of "substantially the whole benefit" which it intended to obtain from the 1974 and 1996 agreements. In such circumstances, a claim of fundamental breach has "a real chance of success".

[135] As I indicated to counsel for PGCL during oral submissions, it is difficult to envision how, if the July 2008 trademark applications are in fact granted, the existence of those new trademarks could be reconciled with the overall purpose and the relevant terms and conditions set out in the 1996 agreement.

[136] In the result, I have concluded that there is a genuine issue for trial with respect to whether PHI was entitled to terminate the 1996 agreement on the basis of fundamental breach.

CONCLUSION

[137] PGCL has established on a *prima facie* basis that insofar as part of PHI's action rests on its termination of the 1996 agreement based on its invocation of paragraph 12(1)(c) of that agreement, that part of PHI's action must fail. For its part, in its responding proof (and on the totality of the evidence), PHI has failed to establish that there is, respecting its termination pursuant to paragraph 12(1)(c), a genuine issue for trial with "a real chance of success".

[138] Respecting PHI's claim for fundamental breach, PGCL has established *prima facie* (without convincing responding proof from PHI) that none of the alleged pre-2008 breaches (if and when they exist) - either individually or with their so-called cumulative force - constitute either in seriousness or frequency, the sort of breach or breaches that would represent the suggested fundamental breach that would justify PHI's assertion that PGCL repudiated the 1996 agreement. Although that determination significantly narrows the breadth and scope of that part of PHI's claim for fundamental breach which has "a real chance of success", I have, at the same time, also concluded that the following question does constitute the one and only genuine issue for trial:

> *Did PGCL commit a fundamental breach amounting to repudiation when it filed in July 2008, three trademark applications (for RICHARDSON*

PIONEER and associated design trademarks) in association with the sale of seed?

[139] Given the genuine issue that remains, I cannot at this time, grant the order requested by PGCL (with all the conclusive relief contemplated therein) as such order is described in para. 7 of this judgment.

[140] As success on this motion has been somewhat divided, I will exercise my discretion to not award costs.

_____

A.C.J.Q.B.

TAB 17

CA018339
Vancouver Registry

Court of Appeal for British Columbia

BETWEEN:

THE PRUDENTIAL INSURANCE COMPANY OF AMERICA

PLAINTIFFS
(APPELLANTS)

AND:

CEDAR HILLS PROPERTIES LTD. and STEVEN P. LEE
and HAMPTON DEVELOPMENT GROUP LTD.

DEFENDANTS
(RESPONDENTS)

Before: The Honourable Mr. Justice Legg
The Honourable Mr. Justice Goldie
The Honourable Madam Justice Rowles

Margaret C. Hollis — Counsel for the Appellants

No one appearing for the Respondents

Place and Date of Hearing: Vancouver, British Columbia
December 9, 1994

Place and Date of Judgment: Vancouver, British Columbia
December 23, 1994

Written Reasons by:
The Honourable Mr. Justice Goldie

Concurred in by:
The Honourable Mr. Justice Legg
The Honourable Madam Justice Rowles

Court of Appeal for British Columbia

The Prudential Insurance Company of America

v.

Cedar Hills Properties Ltd. and Steven P. Lee and Hampton Development Group Ltd.

Reasons for Judgment of Mr. Justice Goldie:

1 The question raised in this appeal is whether the borrower under a commercial loan agreement is required to pay an interest rate standby fee (the "standby fee") to the lender. The borrower failed to provide the required security for the loan and no monies were disbursed to it.

2 In a judgment of the Supreme Court of British Columbia pronounced January 11, 1994 the claim of the plaintiff Prudential Insurance Company of America (the "lender") to a standby fee in the amount of $100,000 was dismissed on the ground the fee was an unenforceable penalty.

3 The lender is the appellant in this Court. No factum has been filed on behalf of the respondents. As a matter of courtesy, counsel for the respondents appeared solely to inform us he has been unable to obtain instructions since filing a notice of cross-appeal on February 6, 1994, and accordingly that he was compelled to withdraw.

4 The lender, an insurance company, is a commercial lender of funds in a large way. The respondent, Cedar Hills Properties Ltd., wished to refinance a shopping centre it owned and applied to the lender for a loan of $6,400,000 to be secured by a first mortgage. The loan application of October 8, 1992 (the "loan application") runs to some 20 pages. The closing, at which the lender's initial disbursement was to take place and interest was to commence accruing, was to be on or before December 15, 1992. Section 9(b) of the loan application provided:

> 9. Loan Fees
> (a) ...
> (b) Interest Rate Standby Fee
> Prudential hereby acknowledges receipt of an interest rate standby fee in the amount of $100,000.00, in the form of an irrevocable and unconditional Letter of Credit. Applicant acknowledges that the interest rate standby fee represents consideration for Prudential's reservation of funds and fixing the Mortgage Loan interest rate at the time of Prudential's receipt of this Application. Upon the Closing of the Loan, Prudential shall return the interest rate standby fee, without interest, to Applicant. However, in the event that Applicant (i) withdraws this Application before Prudential issues a Loan Commitment, or (ii) fails to accept Prudential's Loan Commitment, if issued, or (iii) fails to close the Loan in accordance with Prudential's Loan Commitment for any reason (other the Prudential's breach of the terms of the Loan Commitment), Prudential shall have the right to collect the amount stated in the Letter of Credit and to retain the interest rate standby fee. In no event shall Prudential's receipt of the interest rate standby fee be in derogation of Applicant's obligation to pay legal and survey costs and costs of any other reports required herein.

What arose is covered by clause (iii).

5 The lender accepted an uncertified cheque drawn by the respondent Hampton Development Group Ltd. in lieu of a letter of credit. The cheque was held pending the approval of the loan application and the closing.

6 The lender approved the loan October 21, 1992, upon which the loan application became a commercial loan agreement binding on both parties.

7 The mortgage was drawn in accordance with the terms stipulated in the loan agreement, including interest at the rate of 8.75%. The respondent Stephen Lee executed the mortgage as an officer of the borrower and in his personal capacity as a principal debtor and covenantor.

8 On November 30 the lender put the borrower's solicitor in funds on terms. It became evident by December 4 the borrower could not clear title and the funds were returned to the lender's solicitors on that date.

9 On December 15, 1992 the lender sought to certify the cheque it held to pay the standby fee. The drawer's bank refused as sufficient funds were not available.

10 The lender claimed the borrower owed it legal fees for the preparation of the mortgage documents, accrued interest and the standby fee. Its writ was issued February 4, 1993. The two relevant defenses raised by the respondents were

(a) the amounts claimed constituted interest at a criminal rate; and

(b) the standby fee was a penalty.

11 The first was rejected by the trial judge. It was the subject matter of the counterclaim and of the cross-appeal in this Court. The second was accepted at trial and is the issue on the appeal.

DISCUSSION

12 The trial judge commenced his consideration of the contention that the standby fee was a penalty by referring to ***Dunlop Pneumatic Tyre Company Limited v. New Garage and Motor Company Limited***, [1915] A.C. 79 (H.L.).

13 In that case a manufacturer who generally sold at wholesale required the buyer to agree to some five conditions, two of which were: not to sell to a retailer at less than list prices and not to sell to any person to whom the manufacturer had suspended selling. The terms were intended to secure retail price maintenance. The profit of the wholesaler and the retailer lay in discounts from list prices, presumably reflecting the volume of

sales. For each item of manufacture sold in breach of the terms or any one of them the wholesaler or retailer was bound to pay the manufacturer £5 - a sum described as liquidated damages and not as a penalty. The breach of contract on the part of the defendant in selling an item at less than list price having been proven a master assessed damages at £250 on the basis the £5 sum stipulated being liquidated damages.

14 The majority of the Court of Appeal reversed the trial judge's adoption of the master's award on the ground the provision was a penalty. The manufacturer's appeal to the House of Lords succeeded. The evidence demonstrated that if wholesalers and retailers could undercut the list price with impunity, it was likely others would abandon their contractual relationship with the manufacturer and purchase the goods in question from other manufacturers who made no like stipulation.

15 The law lords were all agreed that in these circumstances it would be impossible to forecast the damage from the sale of one item in breach of the price maintenance provision but the potential for the larger damage was certain.

16 The trial judge referred, correctly if I may say so, to propositions stated by Lord Dunedin in his speech at p. 86-88 of the report:

1. Though the parties to a contract who use the words "penalty" or "liquidated damages" may prima facie be supposed to mean what they say, yet the expression used is not conclusive. The Court must find out whether the payment stipulated is in truth a penalty or liquidated damages. This doctrine may be said to be found passim in nearly every case.

2. The essence of a penalty is a payment of money stipulated as in terrorem of the offending party; the essence of liquidated damages is a genuine covenanted pre-estimate of damage . . . .

3. The question whether a sum stipulated is penalty or liquidated damages is a question of construction to be decided upon the terms and inherent circumstances of each particular contract, judged of as at the time of the making of the contract, not as at the time of the breach . . . .

4. To assist this task of construction various tests have been suggested, which if applicable to the case under consideration may prove helpful, or even conclusive. Such are:

(a) It will be held to be a penalty if the sum stipulated for is extravagant and unconscionable in amount in comparison with the greatest loss that could conceivably be proved to have followed from the breach. ...

(b) It will be held to be a penalty if the breach consists only in not paying a sum of money, and the sum stipulated is a sum greater than the sum which ought to have been paid. ...

(c) There is a presumption (but no more) that it is a penalty when "a single lump sum is made payable by way of compensation, on the occurrence of one or more or all of several events, some of which may occasion serious and others but trifling damage". ...

On the other hand:

(d) It is no obstacle to the sum stipulated being a genuine pre-estimate of damage, that the consequences of the breach are such as to make precise pre-estimation almost an impossibility. On the contrary, that is just the situation when it is probable that pre-estimated damage was the true bargain between the parties. ...

(the emphasis is that of the trial judge)

17 He concluded the standby fee was "... to bind the defendants to the loan agreement by creating a penalty for breach of the conditions for making the loan". This conclusion would meet the description of a penalty set out in para. 2 in the above quotation.

18 The trial judge further found the sum stipulated in the case at bar was "extravagant and unconscionable" - a finding which dictates setting aside a penalty. This appears to rest on his conclusion there could be no loss "... due to fixing the interest rate on this transaction if the loan is never made" and the following:

> The plaintiff has not satisfied the Court that the amount stipulated was not extravagant and not unconscionable. No firm evidence was presented with respect to other transactions lost or lack of availability with respect to lending funds during the period the funds were blocked.
>
> The Standby Fee does not represent a reasonable loss to the plaintiff.

19 It will be seen the foregoing reflects the emphasis the trial judge placed on para. 4(a) of Lord Dunedin's propositions.

20 I have concluded the trial judge erred in the construction he placed on the "terms and inherent circumstances of each particular contract, judged of as at the time of the making of the contract,..." to repeat the words of Lord Dunedin's proposition 3

as well as in the burden of proof he apparently placed on the lender.

21 I turn then to the question of construction.

22 I will refer first to s-s. 9(b) itself, then with its meaning in relation to the loan application as a whole and finally in the context of the "inherent circumstances" of the loan application.

23 The first matter of construction to note is that the provision in question is not expressed in terms of liquidated damages payable on a breach. The fee is payable on the application for a loan but is not earned unless one or more of three events occur. These are not easily described as breaches of a concluded contract. They more conveniently fall into the category of a pre-contractual sequence where a serious intention to enter into a contract has become manifest. The reference to a loan commitment reflects implicity or explicitly a representation by the lender of the availability of funds; the securing of the payment of the standby fee by a letter of credit implicitly or explicitly reflects a representation by the borrower that it is in earnest.

24 From an examination of the loan application itself it is clear the parties were much further advanced towards an agreement that might be inferred from s-s. 9(b) standing alone. From s. 2 of the

loan application it appears an understanding had been reached on the basic terms of the loan: the amount; the term; the amortization period; the interest rate; repayment terms; prepayment privilege (none in the case at bar) and the closing date. Section 3 describes the security and a draft mortgage of considerable length is appended. It is unnecessary to go through it. Five further items in this section describe the security collateral to the first mortgage. These and other provisions make it apparent the mortgaged premises consisted of a shopping centre housing tenants occupying leased space. Before the closing the prospective borrower was to provide, amongst other things, assurances of compliance with zoning bylaws and environmental regulations evidence of satisfactory hazardous waste disposition and copies of the leases producing a stipulated annual rental income.

25 The borrower's prospective obligations in making the loan application are expressed in s. 8(a) in these words:

> Applicant understands and agrees that this Application constitutes an offer to borrow, and if Prudential accepts this offer in the method provided below, Applicant covenants and agrees to comply fully and in a timely manner with all of the provisions of this Application and to borrow the full amount of the Loan in accordance with the terms and conditions hereof.

26 The lender's obligation when it issues its loan commitment is to make the loan in accordance with agreed terms and conditions.

27 The terms were sufficiently settled by the time the loan application was filed that Prudential's loan commitment was expressed in a one page letter. When the borrower signed the loan application the terms applicable to its circumstances had been thoroughly sifted and understood.

28 Further confirmation of this is found in s-s. 9(a) which records the lender's receipt of a fee of $8,000 paid in consideration "... of the substantial services Prudential shall render or fees or expenses which it shall incur in connection with the evaluation, preparation and processing of this Application". The prospective borrower acknowledges in this sub-section this fee will be earned if the lender commits on terms substantially similar to those contained in the loan application or if the borrower withdraws prior to the lender's committing to the loan.

29 No objection has been made to this fee. It must be taken the standby fee in s-s. 9(b) refers to other considerations and circumstances than those recited in s-s. 9(a).

30 I turn to the larger context within the ambit of Lord Dunedin's phrase "inherent circumstances of each particular contract". The evidence of Mr. Bosley, the lender's general manager of mortgage investments in Canada, established two components of the standby fee as recited in s-s. 9(b): one, the

reservation of funds, and two, the fixing of the interest rate as of the date of application. He said in his evidence in chief:

> Q I'd like you to read back to page 16 of tab 1. Look at 9(b) on that page. In the first few lines, sixth line down, is the phrase "reservation of funds." What does that mean?
>
> A Well, we make a commitment to fund a loan, to make a mortgage loan, we have to -- Prudential is obviously committing to fund in this case I believe it was $6.4 million. We every day are looking at new investments and we have to make our selection about which investments we're going to select. Prudential has, as all commercial lenders have these days, limited funds available for commercial loans. Reservation of funds here requires us to liquify some of our other investments so that we have this monies available for the date of disbursement.
>
> Q And the next phrase there on the same line "fixing the mortgage loan interest rate at the time of Prudential's receipt of this application." How much -- in your experience, over the period of, say, six weeks, how much can interest rates vary?
>
> A A lot. Interest rates can and do vary quite a bit day-to-day. For example, they -- interests rates moved one percent, a full percent yesterday.
>
> THE COURT: Down, I take it?
>
> A That's correct. They often go up one percent. It's not always down. Rates go up as well as down. Prudential operates slightly differently than some other life companies. Some companies act the same as we do. We fix the interest rate at the date of application which is quite a bit different than some of my competitors who commit to fund a loan but the interest rate isn't set until the -- very close to the day of funding of the loan itself. The borrower, in that case, has knowledge, of course, that he has a loan but he doesn't know what the interest rate is. We require the interest rate standby fee to be paid at the time of application because we are committing to a fixed rate now and in this case approximately two months from the date of commitment. We think that is a very valuable commodity to certain borrowers, not all borrowers, but some borrowers find that that's something that they want.

31 This, however briefly, evidences the existence and effect of market forces at work in the field of commercial lending. The final determination of, amongst other things, the amount of the loan; the term; the interest rate; the amortization period, if not coincidental with the term, together with other variables more specific to the circumstances of the parties is the product of negotiation in which market forces are at work. The lender seeks a trouble-free investment. The terms he offers reflects his appraisal of the risk and the availability of investment opportunities. The borrower seeks terms which reflect his appraisal of the security he can offer and his need. The balance of bargaining power does not always rest with the lender.

32 The lender is not the only lender. The prospective borrower is not the only borrower. There are lenders who do not fix the interest rate. The borrower has a choice and the lender's terms must reflect the competitive forces inherent in choice.

33 One factor was elicited in Mr. Bosley's cross-examination which was persuasive with the trial judge:

> Q Well, either it has to do with the use of the money, you're charging this $100,000 fee for the use of the money?
> A No. We're not charging him a fee for the use of money. We're charging him a fee for a commitment to fund the loan in the future.
> Q Would you agree with me it's a stick to make sure that the debtor in good faith proceeds with the loan?
> A It's partially for that, that's correct.

> Q Okay. Something to ensure enforcement?
> THE COURT: To ensure he won't back out, presumably, after you've gone through all the trouble of processing the --
> A Partially, yeah, that's correct. I mean, if interest rates, you know, go the wrong way here, at least we -- he has a commitment to fund this loan at this rate.

34 Let us assume the term was to ensure enforcement. That was the purpose of the clause in the ***Dunlop Tyre*** case. The term in question here does not thereby become unconscionable or oppressive.

35 If a borrower believes interest rates are declining he will go to those of the lender's competitors who do not include in their standby fee an interest fixing component. If a borrower believes interest rates are rising it will seek out what this lender offers. For some, the standby fee will be of little interest as they will have taken other steps to protect themselves against interest rate fluctuations.

36 The short point is this: a provision that has the effect of discouraging shopping after the lender has committed, which as Mr. Bosley pointed out, usually means realizing on present investments to fund the proposed loan, is as much a matter of contract as the rate of interest or the term of the loan. In this sense, the prospective borrower is in a less constrained position than the

buyer in the ***Dunlop Tyre*** case. There, if the buyer wanted Dunlop products he could do so only on Dunlop's terms. Competitive products were available but not those bearing the Dunlop label. In the case at bar, the lender's dollar is no different than a dollar from a competitor.

37 Subsection 9(b) reflects part of a bargain. To single out this provision in the absence of any circumstances suggesting oppression or overreaching is, in my view, an unwarranted interference with freedom of contract. Even a stated penalty clause will not be struck down unless oppression is demonstrated. See: ***Elsley v. J.F. Collins Insurance Agencies Ltd.***, [1978] 2 S.C.R. 916, (1978), 83 D.L.R. (3d) 1 (S.C.C.) at p. 15. There was no allegation of oppression.

38 The trial judge faulted the lender for failing to prove actual loss. In doing so he appears to have overlooked an important part of Lord Dunedin's third proposition and rejected evidence relevant to proposition 4(a), namely, evidence of the greatest loss that could conceivably be proved to have followed from the breach.

39 Mr. Bosley said an estimate of actual loss would be impossible. This is manifestly so if it is accepted that it is impossible to foretell interest rates three months in the future. In response to questions from the trial judge, he said he

calculated after the event a present value of the lender's loss over the three year term of the loan in the following manner:

> Q How did you arrive at that figure?
> A I took the three-year bond at that day with the assumption that now that we're not getting a mortgage at eight and a half or eight and -- whatever the interest rate is on this deal. The only thing we can do then instantly to replace this loan was to go out and buy a Government of Canada bond which at the time was yielding --
> Q I thought you told us earlier that you have these problems with committing funds. In other words, one of your principal problems once you make a commitment for a loan you're losing other business presumably or you're -- once the money's committed you're losing; right?
> A Correct.
> Q And you calculated your losses on the basis of what you could have earned on that money elsewhere? Is that what you're saying?
> A No. What I've calculated it on is a substitute investment as of the day that I discovered that we weren't going to end up with a mortgage.
> Q What period of time did you calculate the loss over?
> A The same term as this loan was contemplated.
> Q You've calculated your total loss on the loan?
> A Present value of the difference of the two rates for three years.

40 If one borrower could escape payment of the standby fee when interest rates declined the provision would lose its meaning and the lender would be forced to accept a term it thought undesirable in its business. Mr. Bosley's calculation was some evidence that actual loss could come within the range of $100,000. He further testified with respect to the amount of the standby fee as follows:

> A Over years of -- you know, Prudential has been lending in Canada since, I think, 1919, and we've tended to use a figure that's somewhere between, in this case, about one and a half to two and a half

> percent is the kind of money that we like to have put up.

41 The fee in question here is approximately 1.56% of the principal sum advanced. This standby fee is a term of all the lender's commercial loans. This is some evidence of the reasonableness, if not the utility, of the standby fee.

42 In my view, there is no basis in the evidence before us that the standby fee is extravagant or unconscionable.

43 In short, I can find nothing in the record of this case which persuades me that a court of law ought, upon equitable principles, to interfere with freedom of contract. I am strengthened in this conclusion by the judgment of the Alberta Court of Appeal in ***B.L.T. Holdings Ltd. v. Excelsior Life Insurance Co.***, [1986] 6 W.W.R. 534.

44 In my view the appellant is entitled to succeed on the appeal. I would vary the judgment below by adding to the damages of $5,285.84 awarded the plaintiff the sum of $100,000.

45 I would dismiss the cross-appeal as abandoned.

46 Ms. Hollis raised with us but did not press the question of whether costs were recoverable in the terms provided in the

mortgage, namely, solicitor and own client costs. Section 18.2 of the *Law and Equity Act* provides a discretion in the application of such terms in foreclosure proceedings. In the absence of submissions representing a mortgagor's interest on the point and as I am not convinced the term in question has application to the circumstances of this appeal I would not make such an order.

47 The appellant is entitled to its costs here on the basis of the amount involved exceeding $100,000 and in the court below on scale 3. I would not award costs in respect of the cross-appeal.

"The Honourable Mr. Justice Goldie"

I AGREE: "The Honourable Mr. Justice Legg"

I AGREE: "The Honourable Madam Justice Rowles"

TAB 18

Resolute FP Canada Inc. *Appellant*

v.

Her Majesty The Queen as represented by the Ministry of the Attorney General and Weyerhaeuser Company Limited *Respondents*

- and -

Her Majesty The Queen as represented by the Ministry of the Attorney General *Appellant*

v.

Weyerhaeuser Company Limited and Resolute FP Canada Inc. *Respondents*

- and -

Weyerhaeuser Company Limited *Appellant*

v.

Her Majesty The Queen as represented by the Ministry of the Attorney General *Respondent*

and

Attorney General of British Columbia *Intervener*

Produits forestiers Résolu *Appelante*

c.

Sa Majesté la Reine représentée par le ministère du procureur général et Compagnie Weyerhaeuser Limitée *Intimées*

- et -

Sa Majesté la Reine représentée par le ministère du procureur général *Appelante*

c.

Compagnie Weyerhaeuser Limitée et Produits forestiers Résolu *Intimées*

- et -

Compagnie Weyerhaeuser Limitée *Appelante*

c.

Sa Majesté la Reine représentée par le ministère du procureur général *Intimée*

et

Procureur général de la Colombie-Britannique *Intervenant*

Indexed as: Resolute FP Canada Inc. *v.* Ontario (Attorney General)

2019 SCC 60

File No.: 37985.

2019: March 28; 2019: December 6.

Present: Abella, Moldaver, Karakatsanis, Côté, Brown, Rowe and Martin JJ.

ON APPEAL FROM THE COURT OF APPEAL FOR ONTARIO

Répertorié : Produits forestiers Résolu *c.* Ontario (Procureur général)

2019 CSC 60

N° du greffe : 37985.

2019 : 28 mars; 2019 : 6 décembre.

Présents : Les juges Abella, Moldaver, Karakatsanis, Côté, Brown, Rowe et Martin.

EN APPEL DE LA COUR D'APPEL DE L'ONTARIO

Contracts — Interpretation — Indemnity — River system contaminated by mercury waste discharged by operation of pulp and paper mill — Action for damages commenced against mill owners in relation to contamination — Province granting indemnity in context of settlement of action to current and former mill owners in relation to environmental damage caused by mercury discharge — Remediation order later issued by provincial environment regulator in relation to waste disposal site on mill property — Whether indemnity applies to cover costs of complying with remediation order.

In 1985, Ontario granted an indemnity (the "Indemnity") to Reed Ltd. and Great Lakes Forest Products Limited, both former owners of a pulp and paper mill located in Dryden, Ontario, as well as to their successors and assigns, "from and against any obligation, liability, damage, loss, costs or expenses incurred by any of them" after the date of the Indemnity, "as a result of any claim, action or proceeding, whether statutory or otherwise", because of "any damage, loss, event or circumstances, caused or alleged to be caused by or with respect to, either in whole or in part, the discharge or escape or presence of any pollutant by Reed or its predecessors, including mercury or any other substance, from or in the plant or plants or lands or premises", as set out in para. 1 of the Indemnity. The Indemnity was agreed to by the parties pursuant to the settlement of litigation brought by two First Nations in relation to the mercury waste contamination of two rivers caused by the operation of the Dryden mill.

Twenty-six years later, the Ministry of the Environment and Climate Change issued a remediation order in relation to monitoring and maintaining a mercury waste disposal site at the Dryden mill. In the intervening period, ownership of the mill had changed hands in several transactions. The Director's order was issued to both Resolute, Great Lakes' corporate successor, and Weyerhaeuser, who also owned the Dryden property for a time. Weyerhaeuser commenced an action in Superior Court, seeking a declaration that the terms of the Indemnity required Ontario to compensate it for the cost of complying with the Director's order. Resolute sought leave to intervene in order to claim the same protection. Weyerhaeuser, Resolute and Ontario each moved for summary judgment.

Contrats — Interprétation — Indemnité — Réseau hydrographique contaminé par des déchets mercuriels rejetés par l'exploitation d'une usine de pâtes et papiers — Action en dommages-intérêts intentée contre les propriétaires de l'usine pour la contamination — Indemnité accordée par la province dans le cadre du règlement de l'action aux propriétaires actuels et aux anciens propriétaires de l'usine pour le dommage environnemental causé par le rejet de mercure — Arrêté de remédiation pris plus tard par une autorité provinciale de l'environnement en ce qui concerne le lieu d'élimination des déchets situé sur la propriété de l'usine — L'indemnité s'applique-t-elle aux frais engagés pour se conformer à l'arrêté de remédiation?

En 1985, l'Ontario a accordé une indemnité (l'« Indemnité ») à Reed Ltd. et à Great Lakes Forest Products Limited, toutes deux anciennement propriétaires d'une usine de pâtes et papiers située à Dryden, en Ontario, ainsi qu'à leurs successeurs et ayants droit, à l'égard de « l'ensemble des obligations, responsabilités, dommages, pertes, frais ou dépenses qu'est susceptible d'entraîner pour l'une ou l'autre d'entre elles », après la date de l'Indemnité, « toute réclamation, action ou procédure, qu'elle soit prévue par la loi ou autrement », du fait de « dommages, pertes, événements ou circonstances dus ou présumés dus ou en ce qui a trait, en tout ou en partie, au rejet ou à la fuite de polluants, notamment le mercure ou toute autre substance, par Reed ou ses prédécesseurs, à partir des usines, des terrains ou des lieux [. . .], ou encore à la présence de tels polluants dans ces usines, terrains ou lieux », tel qu'énoncé au par. 1 de l'Indemnité. L'Indemnité a été convenue entre les parties dans le cadre du règlement de la poursuite intentée par deux Premières Nations pour la contamination de deux rivières par des déchets mercuriels, contamination causée par l'exploitation de l'usine de Dryden.

Vingt-six ans plus tard, un arrêté de remédiation a été pris par le ministère de l'Environnement et de l'Action en matière de changement climatique en ce qui concerne la surveillance et l'entretien d'un lieu d'élimination de déchets mercuriels à l'usine de Dryden. Dans l'intervalle, l'usine avait changé de propriétaires à la suite de plusieurs opérations. L'arrêté du directeur a été adressé à Résolu, société ayant succédé à Great Lakes, et à Weyerhaeuser, à qui avait également déjà appartenu la propriété de Dryden pendant une certaine période. Weyerhaeuser a intenté une action devant la Cour supérieure et sollicité un jugement déclaratoire portant que, selon les modalités de l'Indemnité, l'Ontario était tenu de l'indemniser pour les frais engagés pour se conformer à l'arrêté du directeur. Résolu a demandé l'autorisation d'intervenir pour réclamer la même protection. Weyerhaeuser, Résolu et l'Ontario ont chacun présenté une motion en jugement sommaire.

The motion judge held that the Indemnity applied to a statutory claim brought by an agent of the Province and that both Resolute and Weyerhaeuser were entitled to indemnification for their costs of complying with the Director's order. He therefore granted summary judgment in their favour. Ontario appealed. The majority at the Court of Appeal agreed with the motion judge's finding that the Indemnity applied to the Director's order, but held that Resolute was not entitled to indemnification and remitted Weyerhaeuser's entitlement to indemnification to the Superior Court. The dissenting judge would have allowed Ontario's appeal. In his view, the motion judge made reversible errors in his interpretation of the Indemnity; properly construed, the Indemnity was intended to cover only pollution claims brought by third parties, not first party regulatory claims such as the Director's order. Ontario, Weyerhaeuser and Resolute appeal to the Court.

Held (Côté, Brown and Rowe JJ. dissenting in part): Ontario's appeal should be allowed and summary judgment granted in its favour. Resolute and Weyerhaeuser's appeals should be dismissed.

Per Abella, Moldaver, Karakatsanis and Martin JJ.: The Indemnity does not cover the Director's order. As the dissenting judge in the Court of Appeal concluded, the motion judge made palpable and overriding errors of fact and failed to give sufficient regard to the factual matrix when interpreting the scope of the Indemnity, justifying appellate intervention.

The motion judge erred when he found that the waste disposal site continues to discharge mercury into the environment. His mistaken finding that discharges of mercury from the waste disposal site were an ongoing source of serious environmental liability undoubtedly drove his conclusion that these discharges could give rise to pollution claims, and that unless the Indemnity covered first party claims, Resolute and Weyerhaeuser would be exposed to significant liability. The motion judge misconstrued the purpose and effect of the waste disposal site — this site was not a source of ongoing mercury contamination or environmental liability, and therefore its creation would not give rise to a pollution claim. Rather, the waste disposal site was created and used as a solution to the mercury pollution problem, effectively as a burial site for mercury-contaminated waste. There was no evidence of mercury-contaminated waste being discharged from the waste disposal site. This erroneous factual finding was key

Le juge des motions a conclu que l'Indemnité s'appliquait aux réclamations prévues par la loi présentées par un agent de la province, et que Résolu et Weyerhaeuser avaient toutes deux droit à une indemnisation pour les frais engagés pour se conformer à l'arrêté du directeur. Il a donc rendu un jugement sommaire en leur faveur. L'Ontario a interjeté appel. Les juges majoritaires de la Cour d'appel ont souscrit à la conclusion du juge des motions selon laquelle l'Indemnité visait l'arrêté du directeur, mais ont conclu que Résolu n'avait pas droit à une indemnisation et ont renvoyé à la Cour supérieure la question du droit de Weyerhaeuser à une indemnité. Le juge dissident aurait fait droit à l'appel interjeté par l'Ontario. À son avis, le juge des motions a commis des erreurs justifiant infirmation dans son interprétation de l'Indemnité; interprétée comme il se doit, celle-ci devait s'appliquer seulement aux réclamations pour pollution présentées par des tiers, et non aux réclamations réglementaires de première partie, tel l'arrêté du directeur. L'Ontario, Weyerhaeuser et Résolu interjettent appel devant la Cour.

Arrêt (les juges Côté, Brown et Rowe sont dissidents en partie) : Le pourvoi de l'Ontario est accueilli et un jugement sommaire est rendu en sa faveur. Les pourvois de Résolu et de Weyerhaeuser sont rejetés.

Les juges Abella, Moldaver, Karakatsanis et Martin : L'Indemnité ne s'applique pas à l'arrêté du directeur. Comme l'a conclu le juge dissident de la Cour d'appel, le juge des motions a commis des erreurs de fait manifestes et déterminantes et n'a pas tenu suffisamment compte du fondement factuel dans son interprétation du champ d'application de l'Indemnité, ce qui justifie une intervention en appel.

Le juge des motions s'est trompé en concluant que le lieu d'élimination des déchets continuait de rejeter du mercure dans l'environnement. Sa conclusion erronée suivant laquelle les rejets de mercure depuis le lieu d'élimination des déchets constituaient une source constante de lourde responsabilité environnementale l'a sans nul doute amené à conclure que les rejets en question pourraient donner lieu à des réclamations pour pollution, et qu'à moins que l'Indemnité ne s'applique aux réclamations de première partie, Résolu et Weyerhaeuser seraient exposées à une responsabilité considérable. Le juge des motions a mal interprété l'objet et l'effet du lieu d'élimination des déchets — ce site n'était pas une source constante de contamination par le mercure ou de responsabilité environnementale, et sa création n'était donc pas susceptible de donner lieu à une réclamation pour pollution. Le lieu d'élimination des déchets a plutôt été créé et utilisé en tant que solution au problème de pollution au mercure, c'est-à-dire,

to his conclusion that the Director's order was a pollution claim within the meaning of the Indemnity.

Furthermore, the Indemnity was a schedule to a broader settlement agreement, so its scope was limited to the issues defined in that agreement, namely the discharge by Reed and its predecessors of mercury and any other pollutants into the river systems, and the continued presence of any such pollutants discharged by Reed and its predecessors in the related ecosystems. The motion judge failed to consider this context when interpreting the scope of the Indemnity. Properly interpreted, the Indemnity was intended to cover only proceedings arising from the discharge or continued presence of mercury in the related ecosystems, not those related to the mere presence of mercury contained in the waste disposal site.

The Indemnity must be read in the context of two prior indemnities given by Ontario in 1979 and 1982 in the context of the litigation brought by the First Nations. The Indemnity was given in partial consideration for Great Lakes and Reed releasing Ontario from its obligations under those prior indemnities. It is clear that the 1979 and 1982 indemnities were in response to the ongoing litigation, which involved claims brought by third parties, not by Ontario directly. There is no language in those indemnities that would imply Ontario intended to provide protection against the costs of regulatory compliance.

The motion judge's view of the importance of the phrase "statutory or otherwise" in the Indemnity and of why the parties entered into the Indemnity was materially affected by a palpable and overriding factual error. The motion judge found that the Indemnity was provided in consideration for commitments from Great Lakes to make significant financial investments in the Dryden plant. Given what he found to be the rationale for entering into the Indemnity, the motion judge concluded that it would be commercially absurd if Ontario could still impose remediation costs. However, Great Lakes' financial commitments were actually provided as part of the prior 1979 indemnity. Later, Great Lakes gave no new commitments to modernize in consideration for the Indemnity. The motion judge thus premised his interpretation of the Indemnity on an incorrect

dans les faits, en tant que site d'enfouissement pour les déchets contaminés par le mercure. Rien ne prouvait que des déchets contaminés par le mercure étaient rejetés du lieu d'élimination des déchets. Cette conclusion de fait erronée a joué un rôle déterminant dans la conclusion du juge selon laquelle l'arrêté du directeur constituait une réclamation pour pollution au sens de l'Indemnité.

De plus, l'Indemnité constituait une annexe à une convention de règlement plus large, de sorte que son champ d'application se limitait aux points en litige définis dans cette convention, à savoir le rejet par Reed et ses prédécesseurs de mercure et de tout autre polluant dans le réseau hydrographique, ainsi que la présence continue de ces polluants dans les écosystèmes connexes. Le juge des motions n'a pas tenu compte de ce contexte lorsqu'il a interprété le champ d'application de l'Indemnité. Interprétée comme il se doit, l'Indemnité était censée s'appliquer seulement aux procédures découlant du rejet ou de la présence continue de mercure dans les écosystèmes connexes, et non à celles liées à la simple présence de mercure dans le lieu d'élimination des déchets.

L'Indemnité doit être interprétée à la lumière de deux indemnités accordées précédemment par l'Ontario en 1979 et en 1982 dans le cadre de la poursuite intentée par les Premières Nations. L'Indemnité a été accordée en contrepartie partielle du fait que Great Lakes et Reed avaient déchargé l'Ontario de ses obligations en vertu de ces précédentes indemnités. Il est clair que les indemnités de 1979 et de 1982 ont été consenties en réponse au litige qui était en instance, et qui concernait des réclamations présentées par des tiers, et non par l'Ontario directement. Rien dans le libellé de ces indemnités ne tend à indiquer que l'Ontario avait l'intention d'offrir une protection à l'égard des frais engagés pour se conformer à la réglementation.

L'opinion que s'est formée le juge des motions sur l'importance des mots « prévue par la loi ou autrement » dans l'Indemnité ainsi que sur les raisons pour lesquelles les parties ont conclu l'Indemnité a été entachée de manière importante par une erreur de fait manifeste et déterminante. Le juge des motions a estimé que l'Indemnité avait été accordée en contrepartie des engagements pris par Great Lakes de procéder à des investissements financiers considérables dans l'usine de Dryden. Étant donné ce qui, à son avis, constituait la raison d'être de l'Indemnité, il a conclu qu'il serait absurde sur le plan commercial que l'Ontario puisse toujours imposer des frais de remédiation. Cependant, les engagements financiers de Great Lakes étaient en réalité prévus dans la précédente indemnité de 1979. Par la suite, Great Lakes n'a pris aucun nouvel

factual basis — one that led him to place too much emphasis on a change in language and misconstrue the bargain actually struck in the Indemnity.

The motion judge also erred by failing to consider the Indemnity as a whole when determining whether or not the Director's order fell within its scope. Paragraphs 2 and 3 of the Indemnity are critical to its interpretation. Paragraph 2 provides that in any pollution claim, Ontario has the right to elect to take carriage of the defence or to participate in the defence and/or settlement of the claim and any proceeding relating thereto as it deems appropriate. Paragraph 3 requires the parties to cooperate with Ontario in the defence of a claim. These clauses would be utterly meaningless for first party claims. Their inclusion is completely inconsistent with the notion that para. 1 of the Indemnity contemplates first party claims. Nothing in the Indemnity suggests that pollution claims included both first and third party claims, but that the requirements of paras. 2 and 3 would apply only to the subset of pollution claims brought by third parties. To the contrary, para. 2 applies in "any Pollution Claim". The fact that the requirements of paras. 2 and 3 would be utterly meaningless in first party claims implies that pollution claims encompass only those brought by third parties. Properly interpreted, the Indemnity only applies to third party claims, and therefore does not cover the Director's order.

Per Côté, Brown and Rowe JJ. (dissenting in part): The appeals brought by Ontario and Weyerhaeuser should be dismissed and the appeal brought by Resolute should be allowed. The Indemnity enures to the benefit of the successors and assigns of the Province, Reed and Great Lakes. Resolute is entitled to rely on the Indemnity to cover past and future costs incurred in complying with the Director's order as a corporate successor of Great Lakes, but Weyerhaeuser is neither an assignee of the benefit of the Indemnity nor a corporate successor of either Great Lakes or Reed, and it has no entitlement to benefit under the Indemnity.

The Indemnity is a contract which must be interpreted with a view to ascertaining the objective intentions and reasonable expectations of the contracting parties with respect to the meaning of the contractual provision. The

engagement de modernisation en contrepartie de l'Indemnité. Le juge des motions a donc fait reposer son interprétation de l'Indemnité sur un fondement factuel erroné, lequel l'a amené à accorder trop d'importance à la modification au libellé et à mal interpréter la transaction réellement intervenue dans l'Indemnité.

Le juge des motions a également eu tort de ne pas considérer l'Indemnité globalement au moment de déterminer si l'arrêté du directeur entrait ou non dans son champ d'application. Les paragraphes 2 et 3 de l'Indemnité revêtent une importance cruciale pour son interprétation. Le paragraphe 2 dispose que, dans toute réclamation pour pollution, l'Ontario a le droit de choisir d'assumer la défense ou de participer à la défense et/ou au règlement de la réclamation et de toute procédure y afférente, selon ce qu'il estime approprié. Le paragraphe 3 exige des parties qu'elles collaborent avec l'Ontario à la défense d'une réclamation. Ces clauses seraient dénuées de tout sens en ce qui a trait aux réclamations de première partie. Leur inclusion est tout à fait incompatible avec l'idée selon laquelle le par. 1 de l'Indemnité vise les réclamations de première partie. Rien dans l'Indemnité ne tend à indiquer que les réclamations pour pollution comprenaient aussi bien les réclamations de première partie que celles de tiers, mais que les exigences des par. 2 et 3 s'appliqueraient seulement au sous-ensemble des réclamations pour pollution présentées par des tiers. Au contraire, le par. 2 s'applique à « toute réclamation pour pollution ». Le fait que les exigences des par. 2 et 3 soient dénuées de tout sens en ce qui a trait aux réclamations de première partie signifie que les réclamations pour pollution englobent seulement celles présentées par des tiers. Interprétée comme il se doit, l'Indemnité s'applique seulement aux réclamations de tiers et ne vise donc pas l'arrêté du directeur.

Les juges Côté, Brown et Rowe (dissidents en partie) : Les pourvois interjetés par l'Ontario et Weyerhaeuser devraient être rejetés et le pourvoi de Résolu devrait être accueilli. L'Indemnité bénéficie aux successeurs et ayants droit de la province, de Reed et de Great Lakes. Résolu a le droit de bénéficier de l'Indemnité pour couvrir les frais passés et futurs engagés pour se conformer à l'arrêté du directeur à titre de successeur corporatif de Great Lakes, mais Weyerhaeuser n'est ni cessionnaire du bénéfice de l'Indemnité ni un successeur corporatif de Great Lakes ou de Reed, et elle n'a donc pas droit au bénéfice de l'Indemnité.

L'Indemnité est un contrat qui doit être interprété dans le but de déterminer les intentions objectives et les attentes raisonnables des parties contractantes en ce qui concerne la signification des dispositions contractuelles. L'approche

approach is rooted in practicalities and common sense. It considers the language that the parties employed to express their agreement, objective evidence of the background facts that was or reasonably ought to have been within the knowledge of both parties at or before the date of contracting, and the principle of commercial reasonableness and efficacy. The factual matrix cannot overwhelm the words of the contract and cannot change the words of the contract in a manner that would modify the rights and obligations that the parties assumed.

The Indemnity covers the costs of complying with the Director's order. The motion judge did not make any of the four errors alleged by the Province in interpreting the Indemnity.

First, he did not err in failing to consider the text of the Indemnity with reference to the factual matrix, including the two earlier indemnities, the asset purchase agreement in which Reed sold the entire property to Great Lakes, the settlement agreement to which the Indemnity was a schedule, and certain provisions added to the *Environmental Protection Act* in 1985. Like the Indemnity, the two earlier indemnities addressed the mercury contamination, but they represent distinct agreements given for distinct purposes in distinct sets of negotiations. The Indemnity captures a broad scope relative to the other indemnities. In addition, the earlier indemnities were replaced by the Indemnity, which suggests that the parties themselves did not view those earlier indemnities as being co-extensive in scope with the Indemnity. The Indemnity is a separate agreement and must be interpreted by considering the words the parties used in it, not a previous agreement. The asset purchase agreement is of substantially the same scope as the Indemnity, but it exempted the costs of complying with an earlier regulatory order. The Province was aware of its terms, and nothing prevented the parties to the Indemnity from expressly providing that such orders would not fall within the scope of the Indemnity, as the parties to the asset purchase agreement had done. As to the settlement agreement, the issues which that agreement was intended to address included government actions taken in consequence of the mercury contamination. Further, the Indemnity expressly applies in respect of the presence of mercury in the affected lands, and the settlement agreement cannot overwhelm the text in the Indemnity. As for the statutory amendments, even accepting that they are objective and admissible evidence of what the parties had or ought to have had in contemplation when entering into the Indemnity, it is a far leap to the conclusion that they would have understood the reference to statutory claims in the Indemnity to refer solely to claims brought under the amendments or other third party statutory claims which

se fonde sur des considérations pratiques et sur le bon sens. Elle prend en compte les termes employés par les parties pour exprimer leur accord, la preuve objective des renseignements qui appartenaient ou auraient raisonnablement dû appartenir aux connaissances des deux parties à la date de signature ou avant celle-ci, et le principe de la raisonnabilité et de l'efficacité commerciales. Le fondement factuel ne peut pas supplanter les termes du contrat et ne peut changer ceux-ci de manière à modifier les droits et les obligations des parties.

L'Indemnité couvre les frais engagés pour se conformer à l'arrêté du directeur. Le juge des requêtes n'a commis aucune des quatre erreurs invoquées par la province en interprétant l'Indemnité.

Premièrement, il n'a pas commis d'erreur en n'examinant pas le libellé de l'Indemnité à la lumière du fondement factuel, y compris les deux indemnités précédentes, la convention d'achat d'actifs dans laquelle Reed a vendu l'ensemble de la propriété à Great Lakes, la convention de règlement dont l'Indemnité était une annexe et certaines dispositions incorporées dans la *Loi sur la protection de l'environnement* en 1985. Tout comme l'Indemnité, les deux indemnités antérieures visaient à corriger la contamination par le mercure, mais il s'agit d'ententes distinctes conclues à des fins distinctes dans le cadre de négociations distinctes. L'Indemnité a un large champ d'application par rapport à celui des autres indemnités. De plus, les indemnités antérieures ont été remplacées par l'Indemnité, ce qui tend à indiquer que les parties elles-mêmes ne considéraient pas qu'elles avaient le même champ d'application que l'Indemnité. Cette dernière est une entente distincte que l'on doit interpréter en tenant compte des mots employés par les parties à celle-ci et non d'une entente intervenue antérieurement. La convention d'achat d'actifs a essentiellement le même champ d'application que celui de l'Indemnité, mais elle soustrayait les frais engagés pour se conformer à une ordonnance réglementaire antérieure. La province en connaissait les modalités et rien n'empêchait les parties à l'Indemnité de prévoir expressément que de telles ordonnances ne seraient pas visées par l'Indemnité, comme les parties à la convention d'achat d'actifs l'avaient fait. En ce qui concerne la convention de règlement, les points en litige que cette convention visait à régler incluaient les mesures gouvernementales prises à l'égard de la contamination par le mercure. De plus, l'Indemnité s'applique expressément à la présence de mercure dans les terrains touchés et la convention de règlement ne saurait supplanter le texte de l'Indemnité. Pour ce qui est des modifications législatives, même en acceptant qu'elles constituent une preuve objective et admissible de ce que les parties avaient envisagé ou auraient dû envisager au moment de conclure l'Indemnité,

could have been brought at that time. Moreover, reading the Indemnity as excluding first party claims cannot be reconciled with the amendments' creation of a right of action for the Province, or the Indemnity's references to "any province" and statutory actors.

Second, the motion judge did not err in failing to interpret the indemnification clause in para. 1 of the Indemnity in light of the agreement as a whole. His reading of that clause was consistent with the notice/control and cooperation provisions at paras. 2 and 3 of the Indemnity, which are typical of third party indemnities and are meaningful only for third party claims against the indemnified parties.

Third, the motion judge did not make any palpable and overriding errors in characterizing the reason Great Lakes expended certain money or in concluding that the waste disposal site was the source of the mercury contamination. To the extent that these were errors, they could not possibly have had an overriding effect on the conclusion reached by the motion judge. Such minor and collateral factual findings could not determine the outcome of the case, particularly where the motion judge's ultimate conclusion on the scope of the Indemnity rested on different factual and contextual considerations.

Fourth, the motion judge did not err in interpreting the Indemnity so as to impermissibly fetter the legislature's law-making powers, thereby rendering the Indemnity unenforceable. As a matter of constitutional law, the executive of the Canadian state cannot bind or restrict the legislature's sovereign law-making power, whether by contract or otherwise. It follows that a contract entered into by the executive that purports to require that a certain law be enacted, amended or repealed cannot be enforced by way of injunction or specific performance. However, there is an important difference between a contract that impermissibly fetters the legislature's power to enact, amend and repeal legislation, and a contract whose breach by the Crown exposes it to liability. Where the legislature exercises its law-making power in a manner inconsistent with the terms of a contract, the Crown may still face consequences in the form of liability in damages. While the possibility of such liability may deter the legislature

il est difficile de conclure que les parties comprenaient que la mention de réclamations prévues par la loi dans l'Indemnité renvoyait seulement aux réclamations présentées en vertu des modifications ou aux autres réclamations statutaires qui auraient pu être présentées par des tiers à ce moment-là. De plus, une interprétation de l'Indemnité selon laquelle celle-ci exclut les réclamations de première partie n'est pas conciliable avec le fait que les modifications créent un droit d'action en faveur de la province, ou que l'Indemnité renvoie à « toute province » et à tout acteur statutaire.

Deuxièmement, le juge des requêtes n'a pas commis l'erreur de ne pas avoir interprété la clause d'indemnisation figurant au par. 1 de l'Indemnité à la lumière de l'entente dans son ensemble. Sa lecture de cette clause était compatible avec les dispositions d'avis/contrôle et de collaboration aux par. 2 et 3 de l'Indemnité, qui sont typiques des indemnités de tiers et n'ont de sens qu'à l'égard des réclamations de tiers présentées à l'encontre des parties indemnisées.

Troisièmement, le juge des requêtes n'a pas commis d'erreurs manifestes et déterminantes en décrivant les raisons qui ont poussé Great Lakes à faire certaines dépenses ou en concluant que le lieu d'élimination des déchets était la source de la contamination par le mercure. Dans la mesure où il s'agissait d'erreurs, celles-ci ne sauraient avoir eu d'effet déterminant sur la conclusion du juge des requêtes. Pareilles conclusions de fait mineures et accessoires ne pouvaient déterminer l'issue de l'affaire, en particulier lorsque la conclusion finale du juge des requêtes sur le champ d'application de l'Indemnité reposait sur des considérations factuelles et contextuelles différentes.

Quatrièmement, le juge des requêtes n'a pas commis l'erreur d'avoir interprété l'Indemnité de manière à entraver de manière inacceptable les pouvoirs de légiférer de la législature, de sorte que l'Indemnité est devenue non exécutoire. Sur le plan constitutionnel canadien, le pouvoir exécutif ne peut lier l'exercice souverain du pouvoir législatif ni restreindre celui-ci, que ce soit par contrat ou autrement. Il s'ensuit qu'un contrat conclu par le pouvoir exécutif qui vise à obliger à ce qu'une certaine loi soit adoptée, modifiée ou abrogée ne peut faire l'objet d'une exécution par injonction ou en nature. Toutefois, il y a une différence importante entre un contrat qui entrave de façon inacceptable le pouvoir de la législature d'adopter, de modifier et d'abroger une loi, et un contrat dont une violation par la Couronne expose celle-ci à une responsabilité. Si la législature exerce son pouvoir de légiférer d'une manière incompatible avec les modalités d'un contrat, la Couronne peut quand même être exposée à des conséquences prenant

from acting in a manner that runs contrary to the Crown's contractual promises — sometimes referred to as an "indirect fetter" — the legislature is not thereby truly fettered.

In this case, the enactment of new statutory claims might expose the Province to greater liability under the Indemnity, but the Indemnity in no way prevents the legislature from exercising its sovereign authority to make or unmake any law whatever, and deterring or otherwise discouraging the legislature from exercising its law-making power in a certain way would not render it unenforceable at law. The legislature's freedom of action is not impacted.

As to whether Resolute and Weyerhaeuser could benefit from the Indemnity as successors and assigns of Great Lakes, the motion judge made no error in interpreting the Indemnity as covering the costs imposed on the successors and assigns of Great Lakes by the Director's order. Although his analysis on this point was rooted primarily in the wording of the Indemnity, he also considered its meaning in light of the agreement as a whole and the circumstances surrounding its formation in 1985. However, he found that neither supported an interpretation of the Indemnity that would exclude coverage for first party claims.

However, the motion judge did err in principle in holding that a predecessor of Resolute had assigned the benefit of the Indemnity to Weyerhaeuser. He failed to read the impugned contractual term in light of the factual matrix and in a commercially sensible way, focussing his analysis solely on the text of the relevant provisions of the asset purchase agreement between the predecessor and Weyerhaeuser. Although an indemnified party cannot continue to enjoy the benefit of the Indemnity after it assigns its rights thereunder to a third party, the parties structured the agreement in a way that imposed all risk in relation to environmental liabilities on the predecessor while the predecessor relinquished its own protection. This risk-allocation structure makes commercial sense only if the predecessor's interests remained protected by the Indemnity.

The motion judge also committed a palpable and overriding error when he concluded that the Indemnity's enurement clause extended the benefit of the Indemnity

la forme d'une responsabilité pour dommages. Bien que l'éventualité d'une telle responsabilité puisse dissuader la législature d'agir d'une manière qui va à l'encontre des promesses contractuelles de la Couronne, ce qu'on appelle parfois une « entrave indirecte », la législature n'est pas de ce fait véritablement entravée.

En l'espèce, l'édiction de mesures permettant de nouvelles réclamations statutaires pourrait exposer la province à une plus grande responsabilité en vertu de l'Indemnité, mais l'Indemnité n'empêche nullement la législature d'exercer son droit souverain de faire ou d'abroger quelque loi que ce soit, et dissuader ou autrement décourager la législature d'exercer son pouvoir de légiférer d'une certaine façon ne rendrait pas cette indemnité non exécutoire en droit. La liberté d'action de la législature n'est pas touchée.

En ce qui concerne la question de savoir si Résolu et Weyerhaeuser pouvaient bénéficier de l'Indemnité à titre de successeurs et ayants droit de Great Lakes, le juge des requêtes n'a commis aucune erreur en interprétant l'Indemnité comme couvrant les frais que l'arrêté du directeur a imposés aux successeurs et ayants droit de Great Lakes. Bien que son analyse sur ce point ait reposé principalement sur le libellé de l'Indemnité, le juge s'est aussi penché sur sa signification à la lumière de l'entente dans son ensemble et des circonstances ayant entouré sa conclusion en 1985. Cependant, il est arrivé à la conclusion que ni l'une ni l'autre de ces considérations n'étayait une interprétation de l'Indemnité qui exclurait les réclamations de première partie.

Le juge des requêtes a toutefois commis une erreur de principe en concluant qu'un prédécesseur de Résolu avait cédé le bénéfice de l'Indemnité à Weyerhaeuser. Il n'a pas lu la clause contractuelle contestée à la lumière du fondement factuel et d'une manière qui a du sens sur le plan commercial, et a centré son analyse exclusivement sur le libellé des dispositions pertinentes de la convention d'achat d'actifs entre le prédécesseur et Weyerhaeuser. Bien qu'une partie indemnisée ne puisse continuer à jouir du bénéfice de l'Indemnité après avoir consenti à un tiers une cession des droits qu'elle lui confère, les parties ont structuré la convention de façon à ce que le prédécesseur assume tous les risques en matière de responsabilités environnementales tout en renonçant à sa propre protection. Cette structure de répartition du risque n'a de sens sur le plan commercial que si l'Indemnité continuait à protéger les intérêts du prédécesseur.

Le juge des requêtes a également commis une erreur manifeste et déterminante en concluant que la clause d'extension des bénéfices de l'Indemnité étendait le bénéfice

to successors-in-title of the Dryden property. The Indemnity's enurement clause is a standard contractual term and certainty in commercial transactions is best protected where courts give effect to the common understanding and inclusion of such terms in contracts, absent any indication that the parties intended them to have a different effect. When used in relation to corporations, a "successor" generally denotes another corporation which, through some type of legal succession, assumes the burdens and becomes vested with the rights of the first corporation. Nothing in the language of the Indemnity or in the circumstances surrounding the formation of the contract suggests that "successor" in the Indemnity should extend to both corporate successors of Great Lakes and successors-in-title to the Dryden property. However, it may be possible, in other circumstances, for the term "successors" to refer to a successor-in-title.

Cases Cited

By Côté and Brown JJ. (dissenting in part)

Sattva Capital Corp. v. Creston Moly Corp., 2014 SCC 53, [2014] 2 S.C.R. 633; *Ledcor Construction Ltd. v. Northbridge Indemnity Insurance Co.*, 2016 SCC 37, [2016] 2 S.C.R. 23; *Mandamin v. Reed Ltd.*, No. 14716/77, June 26, 1986; *Royal Devon and Exeter NHS Foundation Trust v. ATOS IT Services UK Ltd.*, [2017] EWCA Civ 2196, [2018] 2 All E.R. (Comm.) 535; *Scanlon v. Castlepoint Development Corp.* (1992), 11 O.R. (3d) 744; *Antaios Compania Naviera S.A. v. Salen Rederierna A.B.*, [1985] 1 A.C. 191; *Interprovincial Co-operatives Ltd. v. The Queen*, [1976] 1 S.C.R. 477; *Benhaim v. St-Germain*, 2016 SCC 48, [2016] 2 S.C.R. 352; *South Yukon Forest Corp. v. R.*, 2012 FCA 165, 4 B.L.R. (5th) 31; *Reference re Canada Assistance Plan (B.C.)*, [1991] 2 S.C.R. 525; *West Lakes Ltd. v. South Australia* (1980), 25 S.A.S.R. 389; *Reference re Pan-Canadian Securities Regulation*, 2018 SCC 48, [2018] 3 S.C.R. 189; *Wells v. Newfoundland*, [1999] 3 S.C.R. 199; *Pacific National Investments Ltd. v. Victoria (City)*, 2000 SCC 64, [2000] 2 S.C.R. 919; *Andrews v. Canada (Attorney General)*, 2014 NLCA 32, 354 Nfld. & P.E.I.R. 42; *Rio Algom Ltd. v. Canada (Attorney General)*, 2012 ONSC 550; *Ontario First Nations (2008) Limited Partnership v. Ontario (Minister of Aboriginal Affairs)*, 2013 ONSC 7141, 118 O.R. (3d) 356; *Pacific National Investments Ltd. v. Victoria (City)*, 2004 SCC 75, [2004] 3 S.C.R. 575; *King v. Operating Engineers Training Institute of Manitoba Inc.*, 2011 MBCA 80, 341 D.L.R. (4th) 520; *Nickel Developments Ltd. v. Canada Safeway Ltd.*, 2001 MBCA 79, 156 Man. R. (2d) 170; *Humphries v. Lufkin Industries Canada Ltd.*, 2011 ABCA

de celle-ci aux successeurs en titre quant à la propriété de Dryden. La clause d'extension des bénéfices de l'Indemnité est une clause contractuelle type et la certitude en matière d'opérations commerciales est mieux protégée lorsque les tribunaux donnent effet au sens courant et à l'inclusion de telles clauses figurant dans les contrats, en l'absence d'indication que les parties ont voulu que celles-ci aient un effet différent. Employé à l'égard de sociétés, le terme « successeur » désigne généralement une autre société qui, par une forme de succession juridique, assume les obligations et acquiert les droits de la première société. Rien dans le libellé de l'Indemnité ou dans les circonstances entourant la conclusion du contrat ne suggère que le terme « successeurs » dans l'Indemnité devrait s'étendre aux successeurs corporatifs de Great Lakes et aux successeurs en titre quant à la propriété de Dryden. Cependant, il se peut que dans d'autres circonstances, le terme « successeurs » renvoie aux successeurs en titre.

Jurisprudence

Citée par les juges Côté et Brown (dissidents en partie)

Sattva Capital Corp. c. Creston Moly Corp., 2014 CSC 53, [2014] 2 R.C.S. 633; *Ledcor Construction Ltd. c. Société d'assurance d'indemnisation Northbridge*, 2016 CSC 37, [2016] 2 R.C.S. 23; *Mandamin c. Reed Ltd.*, nº 14716/77, 26 juin 1986; *Royal Devon and Exeter NHS Foundation Trust c. ATOS IT Services UK Ltd.*, [2017] EWCA Civ 2196, [2018] 2 All E.R. (Comm.) 535; *Scanlon c. Castlepoint Development Corp.* (1992), 11 O.R. (3d) 744; *Antaios Compania Naviera S.A. c. Salen Rederierna A.B.*, [1985] 1 A.C. 191; *Interprovincial Co-operatives Ltd. c. La Reine*, [1976] 1 R.C.S. 477; *Benhaim c. St-Germain*, 2016 CSC 48, [2016] 2 R.C.S. 352; *South Yukon Forest Corp. c. R.*, 2012 CAF 165, 4 B.L.R. (5th) 31; *Renvoi relatif au Régime d'assistance publique du Canada (C.-B.)*, [1991] 2 R.C.S. 525; *West Lakes Ltd. c. South Australia* (1980), 25 S.A.S.R. 389; *Renvoi relatif à la réglementation pancanadienne des valeurs mobilières*, 2018 CSC 48, [2018] 3 R.C.S. 189; *Wells c. Terre-Neuve*, [1999] 3 R.C.S. 199; *Pacific National Investments Ltd. c. Victoria (Ville)*, 2000 CSC 64, [2000] 2 R.C.S. 919; *Andrews c. Canada (Attorney General)*, 2014 NLCA 32, 354 Nfld. & P.E.I.R. 42; *Rio Algom Ltd. c. Canada (Attorney General)*, 2012 ONSC 550; *Ontario First Nations (2008) Limited Partnership c. Ontario (Minister of Aboriginal Affairs)*, 2013 ONSC 7141, 118 O.R. (3d) 356; *Pacific National Investments Ltd. c. Victoria (Ville)*, 2004 CSC 75, [2004] 3 R.C.S. 575; *King c. Operating Engineers Training Institute of Manitoba Inc.*, 2011 MBCA 80, 341 D.L.R. (4th) 520; *Nickel Developments Ltd. c. Canada Safeway Ltd.*, 2001 MBCA 79, 156 Man. R. (2d) 170;

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APPEALS from a judgment of the Ontario Court of Appeal (Laskin, Lauwers and Brown JJ.A.), 2017 ONCA 1007, 13 C.E.L.R. (4th) 28, 77 B.L.R. (5th) 175, [2017] O.J. No. 6654 (QL), 2017 CarswellOnt 20156 (WL Can.), reversing a decision of Hainey J., 2016 ONSC 4652, 3 C.E.L.R. (4th) 278, 60 B.L.R. (5th) 237, [2016] O.J. No. 3900 (QL), 2016 CarswellOnt 11807 (WL Can.). Appeal of Resolute FP Canada Inc. dismissed, Côté, Brown and Rowe JJ. dissenting. Appeal of Her Majesty The Queen as represented by the Ministry of the Attorney General allowed, Côté, Brown and Rowe JJ. dissenting. Appeal of Weyerhaeuser Company Limited dismissed.

Andrew Bernstein, *Jeremy Opolsky* and *Jonathan Silver*, for the appellant/respondent Resolute FP Canada Inc.

Leonard F. Marsello, *Tamara D. Barclay* and *Nansy Ghobrial*, for the appellant/respondent Her Majesty The Queen as represented by the Ministry of the Attorney General.

Christopher D. Bredt and *Markus Kremer*, for the appellant/respondent Weyerhaeuser Company Limited.

Elizabeth J. Rowbotham, for the intervener the Attorney General of British Columbia.

The following is the judgment delivered by

[1] Abella, Moldaver, Karakatsanis and Martin JJ. — In 1985, the Province of Ontario granted an indemnity (the "1985 Indemnity") to Reed Ltd. and Great Lakes Forest Products Limited, both former owners of a pulp and paper mill located in Dryden, Ontario, as well as their successors and assigns, for "any damage, loss, event or circumstances, caused or alleged to be caused by or with respect to, either in whole or in part, the discharge or escape or presence of any pollutant by Reed or its predecessors, including mercury or any other substance, from or in the plant or plants or lands or

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POURVOIS contre un arrêt de la Cour d'appel de l'Ontario (les juges Laskin, Lauwers et Brown), 2017 ONCA 1007, 13 C.E.L.R. (4th) 28, 77 B.L.R. (5th) 175, [2017] O.J. No. 6654 (QL), 2017 CarswellOnt 20156 (WL Can.), qui a infirmé une décision du juge Hainey, 2016 ONSC 4652, 3 C.E.L.R. (4th) 278, 60 B.L.R. (5th) 237, [2016] O.J. No. 3900 (QL), 2016 CarswellOnt 11807 (WL Can.). Pourvoi de Produits forestiers Résolu rejeté, les juges Côté, Brown et Rowe sont dissidents. Pourvoi de Sa Majesté la Reine représentée par le ministère du procureur général accueilli, les juges Côté, Brown et Rowe sont dissidents. Pourvoi de Compagnie Weyerhaeuser Limitée rejeté.

Andrew Bernstein, *Jeremy Opolsky* et *Jonathan Silver*, pour l'appelante/intimée Produits forestiers Résolu.

Leonard F. Marsello, *Tamara D. Barclay* et *Nansy Ghobrial*, pour l'appelante/intimée Sa Majesté la Reine représentée par le ministère du procureur général.

Christopher D. Bredt et *Markus Kremer*, pour l'appelante/intimée Compagnie Weyerhaeuser Limitée.

Elizabeth J. Rowbotham, pour l'intervenant le procureur général de la Colombie-Britannique.

Version française du jugement rendu par

[1] Les juges Abella, Moldaver, Karakatsanis et Martin — En 1985, la province d'Ontario a accordé une indemnité (l'« Indemnité de 1985 ») à Reed Ltd. et à Great Lakes Forest Products Limited, toutes deux anciennement propriétaires d'une usine de pâtes et papiers située à Dryden, en Ontario, ainsi qu'à leurs successeurs et ayants droit, pour les [traduction] « dommages, pertes, événements ou circonstances dus ou présumés dus ou en ce qui a trait, en tout ou en partie, au rejet ou à la fuite de polluants, notamment le mercure ou toute autre substance, par Reed ou ses prédécesseurs, à partir des usines, des

premises". The 1985 Indemnity was agreed to by the parties in the context of the settlement of litigation brought by two First Nations in relation to mercury pollution caused by the operation of the Dryden mill.

[2] Twenty-six years later, the Director of the Ministry of the Environment and Climate Change issued a remediation order in relation to monitoring and maintaining a mercury disposal site at the Dryden mill. In the intervening period, ownership of the mill had changed hands in several transactions. The Director's Order was issued to both Resolute, Great Lakes' corporate successor, and Weyerhaeuser, which also owned the Dryden property for a time. Both Resolute and Weyerhaeuser sought indemnification from Ontario for the costs of complying with the Director's Order.

[3] Although the parties in these appeals raise a number of issues relating to Resolute and Weyerhaeuser's claims for indemnification, the threshold question is whether the 1985 Indemnity covers the Director's Order. In our view, and for the dissenting reasons of Laskin J.A. (2017 ONCA 1007, 77 B.L.R. (5th) 175), it does not. We would, therefore, allow Ontario's appeal, and grant Ontario's motion for summary judgment.

[4] In the 1960s, the Dryden Paper Company Limited owned and operated a pulp and paper mill in Dryden. As part of the operation of the paper mill, Dryden Paper — through a related company, Dryden Chemicals Limited — operated a mercury cathode chlor-alkali plant on property near the mill. The chlor-alkali plant released untreated mercury waste into the English and Wabigoon rivers, which resulted in harm to the health of some local residents, the closure of a commercial fishery and damage to the region's tourism industry. Many of the affected people were members of the Grassy Narrows and

terrains ou des lieux [. . .], ou encore à la présence de tels polluants dans ces usines, terrains ou lieux ». L'Indemnité de 1985 a été convenue entre les parties dans le cadre du règlement de la poursuite intentée par deux Premières Nations relativement à la pollution par le mercure causée par l'exploitation de l'usine de Dryden.

[2] Vingt-six ans plus tard, un arrêté de remédiation a été pris par le directeur du ministère de l'Environnement et de l'Action en matière de changement climatique en ce qui concerne la surveillance et l'entretien d'un lieu d'élimination du mercure à l'usine de Dryden. Dans l'intervalle, l'usine avait changé de propriétaires à la suite de plusieurs opérations. L'arrêté du directeur a été adressé à Résolu, société ayant succédé à Great Lakes, et à Weyerhaeuser, à qui avait également déjà appartenu la propriété de Dryden pendant une certaine période. Tant Résolu que Weyerhaeuser ont réclamé une indemnité à l'Ontario pour les frais engagés pour se conformer à l'arrêté du directeur.

[3] Bien que les parties aux présents pourvois aient soulevé un certain nombre de questions liées aux demandes d'indemnisation de Résolu et de Weyerhaeuser, la question préliminaire qui se pose est celle de savoir si l'Indemnité de 1985 s'applique à l'arrêté du directeur. À notre avis, et pour les motifs dissidents exprimés par le juge Laskin de la Cour d'appel (2017 ONCA 1007, 77 B.L.R. (5th) 175), elle ne s'y applique pas. En conséquence, nous sommes d'avis d'accueillir le pourvoi de l'Ontario ainsi que la motion en jugement sommaire de l'Ontario.

[4] Dans les années 1960, la société Dryden Paper Company Limited possédait et exploitait une usine de pâtes et papiers à Dryden. Dans le cadre de l'exploitation de l'usine, Dryden Paper, par l'intermédiaire d'une société affiliée, Dryden Chemicals Limited, exploitait une usine de chlore et de soude caustique utilisant le procédé à cathode de mercure sur une propriété située près de l'usine. Cette usine de chlore et de soude caustique a rejeté des déchets mercuriels non traités dans les rivières English et Wabigoon, ce qui a eu un effet préjudiciable sur la santé de certains résidents locaux, en plus d'avoir

Islington First Nations who lived on reserves downstream.

[5] In 1971, Dryden Paper constructed a waste disposal site on its lands to serve as a burial site for mercury-contaminated waste from the chlor-alkali plant. Six monitoring wells were installed when the waste disposal site was created, with three additional wells installed in 2002, and one in 2010. These monitoring wells were sampled and analyzed twice per year. Since 1977, the waste disposal site has been the subject of various certificates under the *Environmental Protection Act*, R.S.O. 1990, c. E.19. The initial Provisional Certificate of Approval required the monitoring of groundwater and surface water by the owner of the waste disposal site. In 2011, the site was thought to have 35 years remaining in its "contaminating lifespan".

[6] In 1976, Dryden Paper and Dryden Chemicals amalgamated to form Reed.

[7] In June 1977, the two First Nations bands sued Reed, Dryden Paper and Dryden Chemicals for damages in relation to the mercury waste contamination of the rivers (the "Grassy Narrows Litigation").

[8] In 1978, the Ministry of the Environment issued two further Provisional Certificates of Approval that required Reed to maintain the water monitoring program at the waste disposal site.

[9] By 1979, Reed wanted to sell its Dryden properties. Its prospective purchaser, Great Lakes, expressed reluctance to complete the sale because of the Grassy Narrows Litigation. Concerned that the local economy would suffer if the pulp and paper mill closed, Ontario intervened. It agreed to limit the combined liability of Great Lakes and Reed for any environmental damages caused by Reed prior

entraîné la fin de la pêche commerciale et causé du tort à l'industrie touristique de la région. Bon nombre des personnes touchées étaient des membres des Premières Nations de Grassy Narrows et d'Islington qui vivaient dans des réserves situées en aval.

[5] En 1971, Dryden Paper a construit sur ses terres un lieu d'élimination des déchets devant servir de site d'enfouissement des déchets contaminés par le mercure qui provenaient de l'usine de chlore et de soude caustique. Six puits de surveillance ont été installés lors de la création du lieu d'élimination des déchets, auxquels se sont ajoutés trois puits supplémentaires en 2002, puis un autre en 2010. Ces puits de surveillance faisaient l'objet d'un échantillonnage et d'une analyse deux fois par année. Depuis 1977, le lieu d'élimination des déchets a été visé par plusieurs certificats sous le régime de la *Loi sur la protection de l'environnement*, L.R.O. 1990, c. E.19. Selon le certificat d'autorisation provisoire initial, le propriétaire du lieu d'élimination était tenu d'assurer la surveillance des eaux souterraines et des eaux de surface. En 2011, on estimait qu'il restait 35 années à la « durée de vie de la charge contaminante » du site.

[6] En 1976, Dryden Paper et Dryden Chemicals ont fusionné pour former la société Reed.

[7] En juin 1977, les deux Premières Nations ont intenté une poursuite en dommages-intérêts contre Reed, Dryden Paper et Dryden Chemicals pour la contamination des rivières par les déchets mercuriels (le « litige de Grassy Narrows »).

[8] En 1978, le ministère de l'Environnement a délivré deux autres certificats d'autorisation provisoires selon lesquels Reed était tenue de maintenir le programme de surveillance des eaux au lieu d'élimination des déchets.

[9] En 1979, Reed a voulu vendre ses propriétés de Dryden. L'acheteuse potentielle, Great Lakes, s'est montrée réticente à finaliser la vente en raison du litige de Grassy Narrows. Craignant que l'économie locale ne souffre de la fermeture de l'usine de pâtes et papiers, l'Ontario est intervenu et a accepté de limiter à 15 millions de dollars la responsabilité combinée de Great Lakes et de Reed pour les dommages

to Great Lakes' purchase of the Dryden operation to $15 million. Great Lakes and Reed agreed to share the financial consequences of the Grassy Narrows Litigation up to that limit. Great Lakes also agreed to spend approximately $200 million on the expansion and modernization of the Dryden facilities in consideration for the indemnity granted by Ontario (the "1979 Indemnity").

[10] On December 4, 1979, the Ministry of the Environment issued another Provisional Certificate of Approval. It required Reed to register the certificate against title to the waste disposal site. That same month, the sale of the Dryden properties to Great Lakes closed in accordance with the terms set out in a Memorandum of Agreement dated December 7, 1979.

[11] In January 1980, the Ministry issued another Provisional Certificate of Approval requiring Great Lakes to maintain the groundwater monitoring and testing program at the waste disposal site.

[12] Contemporaneously, the Governments of Ontario and Canada engaged in mediation with the Islington and Grassy Narrows First Nations to address the harms caused by mercury discharge. These discussions involved the Grassy Narrows Litigation. Great Lakes, meanwhile, was reluctant to contribute to any settlement of the litigation unless it obtained a release from liability. On January 28, 1982, the then Provincial Secretary for Resources Development wrote to Great Lakes, indicating that Ontario was "prepared to indemnify Great Lakes Forest Products Limited against any claims related to mercury pollution" (the "1982 Indemnity" (A.R., vol. III, at p. 176)). The 1982 Indemnity stated that Ontario would indemnify Great Lakes for any damages awarded by a court or any settlement above $15 million. Any mercury pollution-related actions were to be brought to the attention of Ontario, which would then become involved in the litigation.

environnementaux causés par Reed avant l'achat par Great Lakes de l'exploitation de Dryden. Great Lakes et Reed ont convenu de partager les conséquences financières du litige de Grassy Narrows jusqu'à concurrence de ce montant. Great Lakes a également accepté de consacrer environ 200 millions de dollars à l'agrandissement et à la modernisation des installations de Dryden en contrepartie de l'indemnité accordée par l'Ontario (l'« Indemnité de 1979 »).

[10] Le 4 décembre 1979, le ministère de l'Environnement a délivré un autre certificat d'autorisation provisoire selon lequel Reed était tenue d'enregistrer le certificat sur le titre de propriété du lieu d'élimination des déchets. Le même mois, la vente des propriétés de Dryden à Great Lakes a été conclue conformément aux modalités énoncées dans un protocole d'entente daté du 7 décembre 1979.

[11] En janvier 1980, le Ministère a délivré un autre certificat d'autorisation provisoire, cette fois pour exiger de Great Lakes qu'elle maintienne le programme de surveillance et d'analyse des eaux souterraines au lieu d'élimination des déchets.

[12] À la même époque, les gouvernements de l'Ontario et du Canada ont pris part à un processus de médiation avec les Premières Nations d'Islington et de Grassy Narrows visant à réparer les préjudices causés par le rejet de mercure. Les discussions ont porté sur le litige de Grassy Narrows. Pendant cette période, Great Lakes était réticente à participer à tout règlement du litige, à moins d'avoir obtenu une décharge de responsabilité. Le 28 janvier 1982, le secrétaire provincial du Développement des ressources de l'époque a écrit à Great Lakes pour lui faire savoir que l'Ontario était [TRADUCTION] « prêt à indemniser Great Lakes Forest Products Limited pour toute réclamation relative à la pollution au mercure » (« Indemnité de 1982 » (d.a., vol. III, p. 176)). L'Indemnité de 1982 précisait que l'Ontario indemniserait Great Lakes pour toute somme accordée à titre de dommages-intérêts par un tribunal ou pour tout règlement s'élevant à plus de 15 millions de dollars. Toute procédure associée à la pollution au mercure devait être portée à l'attention de l'Ontario, qui prendrait alors part au litige.

[13] In late 1985, the Grassy Narrows Litigation settled. The terms of the settlement were set out in a Memorandum of Agreement dated November 22, 1985, entered into by Canada, Ontario, the Islington and Grassy Narrows First Nations, Reed and Great Lakes. The issues, as defined in the Memorandum of Agreement, pertained to "[t]he discharge by Reed and its predecessors of mercury and any other pollutants into the English and Wabigoon and related river systems, and the continu[ed] presence of any such pollutants discharged by Reed and its predecessors . . . in the related ecosystems". Significantly for the purposes of the present appeals, para. 2.4 of the Memorandum of Agreement stipulated that Ontario would indemnify Great Lakes and Reed with respect to the issues, and Great Lakes and Reed would provide Ontario releases in respect of the 1979 and 1982 Indemnities.

[14] The indemnification required by para. 2.4 of the Memorandum of Agreement is contained in a schedule to the settlement agreement entitled the "Ontario Indemnity" (referred to herein as the "1985 Indemnity") which was signed by Ontario, Great Lakes, Reed and Reed International. These appeals involve the interpretation of the 1985 Indemnity, and particularly para. 1, which reads:

1. Ontario hereby covenants and agrees to indemnify Great Lakes, Reed, International and any company which was at the Closing Date a subsidiary or affiliate company (whether directly or indirectly) of International, harmless from and against any obligation, liability, damage, loss, costs or expenses incurred by any of them after the date hereof as a result of any claim, action or proceeding, whether statutory or otherwise, existing at December 17, 1979 or which may arise or be asserted thereafter (including those arising or asserted after the date of this agreement), whether by individuals, firms, companies, governments (including the Federal Government of Canada and any province or municipality thereof or any agency, body or authority created by statutory or other authority) or any group or groups of the foregoing, because of or relating to any damage, loss, event or circumstances, caused or alleged to be caused by or with respect to, either in whole or in part, the discharge or escape or presence of any pollutant by Reed or its predecessors, including mercury or any other substance, from or in the plant or plants or lands or premises forming part of the Dryden assets sold by Reed Ltd. to Great Lakes

[13] Le litige de Grassy Narrows a été réglé à la fin de 1985. Les modalités du règlement ont été énoncées dans un protocole d'entente daté du 22 novembre 1985 conclu entre le Canada, l'Ontario, les Premières Nations d'Islington et de Grassy Narrows, Reed et Great Lakes. Les points en litige, tels qu'ils ont été définis dans le protocole d'entente, portaient sur [TRADUCTION] « [l]e rejet par Reed et ses prédécesseurs de mercure et de tout autre polluant dans le réseau hydrographique English-Wabigoon, ainsi que la présence continue de ces polluants [. . .] dans les écosystèmes connexes ». Fait important pour les besoins des présents pourvois, le par. 2.4 du protocole d'entente précisait que l'Ontario indemniserait Great Lakes et Reed relativement aux points en litige, et que Great Lakes et Reed déchargeraient l'Ontario de ses obligations en vertu des Indemnités de 1979 et de 1982.

[14] L'indemnisation requise aux termes du par. 2.4 du protocole d'entente est énoncée dans une annexe à la convention de règlement, intitulée [TRADUCTION] « Indemnité de l'Ontario » (ici appelée « Indemnité de 1985 ») et qui a été signée par l'Ontario, Great Lakes, Reed et Reed International. Les pourvois en l'espèce portent sur l'interprétation de l'Indemnité de 1985, et en particulier son par. 1, ainsi rédigé :

[TRADUCTION] 1. L'Ontario s'engage et consent à tenir Great Lakes, Reed, International et toute société qui, à la date de clôture, était (directement ou indirectement) une filiale ou une société affiliée d'International, à couvert de l'ensemble des obligations, responsabilités, dommages, pertes, frais ou dépenses qu'est susceptible d'entraîner pour l'une ou l'autre d'entre elles, après la date des présentes, toute réclamation, action ou procédure, qu'elle soit prévue par la loi ou autrement, qui existait au 17 décembre 1979 ou qui était susceptible de prendre naissance ou d'être présentée par la suite (y compris celles ayant pris naissance ou ayant été présentées après la date des présentes), par des particuliers, des firmes, des sociétés, des gouvernements (y compris le gouvernement fédéral du Canada et toute province ou municipalité du Canada, ou tout organisme ou autorité créé en vertu d'un pouvoir légal ou d'un autre pouvoir) ou un ou plusieurs groupes de ceux-ci, du fait ou à l'égard des dommages, pertes, événements ou circonstances dus ou présumés dus ou en ce qui a trait, en tout ou en partie, au rejet ou à la fuite de polluants, notamment le mercure ou toute autre

under the Dryden Agreement (hereinafter referred to as "Pollution Claims"). It is hereby expressly acknowledged and agreed that in respect of Ontario's covenant and agreement hereunder to indemnify Great Lakes that the term "Pollution Claims" shall include any obligation, liability, damage, loss, costs or expenses incurred by Great Lakes as a result of any claim, action or proceeding resulting from or in connection with the indemnity agreement of even date herewith made between Great Lakes, Reed and International. [A.R., vol. IV, at pp. 189-90]

substance, par Reed ou ses prédécesseurs, à partir des usines, des terrains ou des lieux faisant partie des actifs de Dryden que Reed Ltd. a vendus à Great Lakes en vertu de la convention de Dryden, ou encore à la présence de tels polluants dans ces usines, terrains ou lieux (ci-après appelées les « réclamations pour pollution »). Il est expressément reconnu et convenu par les présentes qu'en ce qui concerne l'engagement et le consentement de l'Ontario à indemniser Great Lakes, l'expression « réclamations pour pollution » comprend l'ensemble des obligations, responsabilités, dommages, pertes, frais ou dépenses qu'est susceptible d'entraîner pour Great Lakes toute réclamation, action ou procédure qui découle de l'entente d'indemnisation conclue à la même date que les présentes entre Great Lakes, Reed et International, ou qui y est liée. [d.a., vol. IV, p. 189-190]

[15] Paragraph 2 of the 1985 Indemnity requires Great Lakes or Reed to give Ontario prompt notice of any Pollution Claim as defined in para. 1, at which point Ontario could take carriage of or participate in the litigation. Great Lakes and Reed must cooperate with Ontario in relation to the investigation of any Pollution Claims (para. 3). The 1985 Indemnity is "valid without limitation as to time" (para. 4). An enurement clause contained in para. 6 provided that "[t]he indemnity shall be binding upon and enure to the benefit of the respective successors and assigns of Ontario, Reed, International and Great Lakes, provided however that Ontario shall not be entitled to assign this indemnity without the prior written consent of the other parties hereto" (A.R., vol. IV, at pp. 191-92).

[15] Le paragraphe 2 de l'Indemnité de 1985 exige que Great Lakes ou Reed avisent rapidement l'Ontario de toute réclamation pour pollution, telle qu'elle est définie au par. 1, et l'Ontario peut alors se charger du litige ou y participer. Great Lakes et Reed doivent collaborer avec l'Ontario à l'enquête sur toute réclamation pour pollution (par. 3). L'Indemnité de 1985 n'est [TRADUCTION] « assujettie à aucune limite de temps » (par. 4). La clause d'extension des bénéfices contenue au par. 6 prévoit ce qui suit : « L'indemnité lie les successeurs et ayants droit respectifs de l'Ontario, de Reed, d'International et de Great Lakes et bénéficie à ceux-ci, à condition toutefois que l'Ontario ne soit pas autorisé à céder l'indemnité sans le consentement préalable écrit des autres parties » (d.a., vol. IV, p. 191-192).

[16] In accordance with the Memorandum of Agreement, Reed and Great Lakes released Ontario from its obligations under the 1979 and 1982 Indemnities. The settlement of the Grassy Narrows Litigation was approved by the Supreme Court of Ontario on June 26, 1986.

[16] Conformément au protocole d'entente, Reed et Great Lakes ont déchargé l'Ontario de ses obligations en vertu des Indemnités de 1979 et de 1982. Le règlement du litige de Grassy Narrows a été approuvé par la Cour suprême de l'Ontario le 26 juin 1986.

[17] In subsequent years, both Reed and Great Lakes underwent corporate changes. After amalgamating with other corporations, Reed's successor corporation dissolved in 1993. In 1998, Great Lakes became Bowater which, in 2010, became part of Abitibi-Consolidated Inc. In 2012, it became Resolute.

[17] Au cours des années suivantes, Reed et Great Lakes ont subi des changements organisationnels. Après avoir fusionné avec d'autres sociétés, la société ayant succédé à Reed a été dissoute en 1993. En 1998, Great Lakes est devenue Bowater, qui a été intégrée à Abitibi-Consolidated Inc. en 2010. En 2012, la société a pris le nom de Résolu.

[18] In August 1998, Weyerhaeuser entered into an agreement with Bowater, Great Lakes' corporate successor, to purchase certain assets used in the Dryden pulp and paper business. Given the potential environmental liabilities, Weyerhaeuser initially sought to exclude the waste disposal site from the purchased assets. However, this exclusion required severing the waste disposal site from title, which could not be effected before the closing of the sale. As a result, when the transaction closed, Bowater conveyed title to the waste disposal site to Weyerhaeuser, which then immediately leased it back to Bowater. When severance finally occurred some two years later, Weyerhaeuser reconveyed the waste disposal site to Bowater. Title was registered in Weyerhaeuser's name from September 30, 1998, to August 25, 2000. In 2007, Weyerhaeuser sold the Dryden paper plant to Domtar Inc.

[19] In April 2009, Bowater and its related companies filed for protection under the *Companies' Creditors Arrangement Act*, R.S.C. 1985, c. C-36 ("*CCAA*"). In the course of the *CCAA* proceedings, with court approval, the waste disposal site was abandoned in April 2011.

[20] On August 25, 2011, the Ministry of the Environment issued a Director's Order to Weyerhaeuser (as a former owner of the waste disposal site) and Bowater, Resolute's corporate predecessor. This order imposed three main obligations: (1) to repair certain site erosion, perform specific groundwater and surface water testing, and file annual reports containing specified information; (2) to deliver to the Ministry of the Environment the sum of $273,063 as financial assurance in respect of the waste disposal site; and (3) to "take all reasonable measures to ensure that any discharge of a contaminant to the natural environment is prevented and any adverse effect that may result from such a discharge is dealt with according to all legal requirements" (A.R., vol. IV, at p. 27).

[18] En août 1998, Weyerhaeuser a conclu une entente avec Bowater, la société ayant succédé à Great Lakes, en vue de l'achat de certains actifs utilisés dans l'entreprise de pâtes et papiers de Dryden. Étant donné les responsabilités environnementales possibles, Weyerhaeuser a d'abord cherché à exclure le lieu d'élimination des déchets des actifs visés par l'achat. Toutefois, pour procéder à cette exclusion, il fallait séparer ce lieu du titre, ce qui ne pouvait s'effectuer avant la clôture de la vente. En conséquence, à la clôture de l'opération, Bowater a transféré le titre de propriété du lieu d'élimination des déchets à Weyerhaeuser, qui a immédiatement loué celui-ci à Bowater. Lorsque la séparation en question a finalement eu lieu quelque deux années plus tard, Weyerhaeuser a rétrocédé le site à Bowater. Le titre a été enregistré au nom de Weyerhaeuser du 30 septembre 1998 au 25 août 2000. En 2007, Weyerhaeuser a vendu l'usine de pâtes et papiers de Dryden à Domtar Inc.

[19] En avril 2009, Bowater et ses sociétés affiliées ont demandé à être placées sous la protection de la *Loi sur les arrangements avec les créanciers des compagnies*, L.R.C. 1985, c. C-36 (« *LACC* »). Dans le cadre des procédures fondées sur la *LACC*, et avec l'approbation du tribunal, le lieu d'élimination des déchets a été abandonné en avril 2011.

[20] Le 25 août 2011, le ministère de l'Environnement a pris un arrêté du directeur adressé à Weyerhaeuser (à titre d'ancienne propriétaire du lieu d'élimination des déchets) et à Bowater, la société ayant précédé Résolu. Cet arrêté imposait trois obligations principales : (1) réparer une certaine érosion du site, effectuer une analyse déterminée d'eaux souterraines et d'eaux de surface, et déposer des rapports annuels contenant des renseignements déterminés; (2) remettre au ministère de l'Environnement la somme de 273 063 $ à titre de garantie financière pour le lieu d'élimination des déchets; et (3) [TRADUCTION] « prendre toutes les mesures raisonnables pour éviter le rejet d'un contaminant dans l'environnement naturel et pour remédier aux conséquences préjudiciables pouvant résulter d'un tel rejet conformément à toutes les exigences légales » (d.a., vol. IV, p. 27).

[21] Weyerhaeuser filed a notice of appeal to the Environmental Review Tribunal, seeking to revoke or amend the Director's Order.

[22] In May 2013, Weyerhaeuser commenced an action in Superior Court seeking a declaration that the terms of the 1985 Indemnity required Ontario to compensate it for the cost of complying with the Director's Order. Resolute sought leave to intervene. Ontario submitted it was not responsible for the costs of complying with the Director's Order. All three parties moved for summary judgment.

[23] The motion judge held that the 1985 Indemnity clearly applied to a statutory claim or proceeding brought by an agent of the Province and that *both* Resolute and Weyerhaeuser were entitled to indemnification under the 1985 Indemnity for their costs of complying with the Director's Order. He therefore granted summary judgment in favour of Resolute and Weyerhaeuser (2016 ONSC 4652, 60 B.L.R. (5th) 237).

[24] Ontario appealed. The majority at the Court of Appeal for Ontario agreed with the motion judge with respect to the scope of the 1985 Indemnity, namely that it applied to the Director's Order. The majority concluded, however, that Resolute was not entitled to indemnification and remitted the issue of Weyerhaeuser's entitlement to indemnification to the Superior Court.

[25] Justice Laskin, dissenting, would have allowed Ontario's appeal. In his view, the motion judge made reversible errors in his interpretation of the 1985 Indemnity. Properly construed, the 1985 Indemnity was intended to cover *only* pollution claims brought by third parties. First party regulatory claims, such as the Director's Order, did not fall within the scope of the 1985 Indemnity.

[21] Weyerhaeuser a déposé un avis d'appel auprès du Tribunal de l'environnement afin de demander la révocation ou la modification de l'arrêté du directeur.

[22] En mai 2013, Weyerhaeuser a intenté une action devant la Cour supérieure et sollicité un jugement déclaratoire portant que, selon les modalités de l'Indemnité de 1985, l'Ontario était tenu de l'indemniser pour les frais engagés pour se conformer à l'arrêté du directeur. Résolu a demandé l'autorisation d'intervenir. L'Ontario a fait valoir qu'elle n'était pas responsable des frais engagés pour se conformer à l'arrêté du directeur. Les trois parties ont présenté une motion en jugement sommaire.

[23] Le juge des motions a conclu que l'Indemnité de 1985 s'appliquait clairement aux réclamations ou procédures prévues par la loi présentées par un agent de la province, et que Résolu et Weyerhaeuser avaient *toutes deux* droit à une indemnisation au titre de l'Indemnité de 1985 pour les frais engagés pour se conformer à l'arrêté du directeur. Il a donc rendu un jugement sommaire en faveur de Résolu et de Weyerhaeuser (2016 ONSC 4652, 60 B.L.R. (5th) 237).

[24] L'Ontario a interjeté appel. Les juges majoritaires de la Cour d'appel de l'Ontario ont souscrit à l'opinion du juge des motions en ce qui a trait au champ d'application de l'Indemnité de 1985, à savoir qu'elle visait l'arrêté du directeur. Ils ont toutefois conclu que Résolu n'avait pas droit à une indemnisation et ils ont renvoyé à la Cour supérieure la question du droit de Weyerhaeuser à une indemnité.

[25] Le juge Laskin, dissident, aurait fait droit à l'appel interjeté par l'Ontario. À son avis, le juge des motions a commis des erreurs justifiant infirmation dans son interprétation de l'Indemnité de 1985. Interprétée comme il se doit, celle-ci devait s'appliquer *seulement* aux réclamations pour pollution présentées par des tiers. Les réclamations réglementaires de première partie, tel l'arrêté du directeur, n'entraient pas dans le champ d'application de l'Indemnité de 1985.

Analysis

[26] The overriding issue in this case is the scope of the 1985 Indemnity. We would, with respect, allow Ontario's appeal substantially for the reasons of Laskin J.A. We conclude, as he did, that the motion judge made palpable and overriding errors of fact and failed to give sufficient regard to the factual matrix when interpreting the scope of the 1985 Indemnity justifying appellate intervention. We find it difficult to improve on his reasons, and would add only the following brief comments.

[27] Both Laskin J.A. and the majority at the Court of Appeal agreed that the motion judge erred when he found that the waste disposal site continues to discharge mercury into the environment. In the words of Laskin J.A.:

> The motion judge's mistaken finding that discharges of mercury from the [waste disposal site] were an ongoing source of "serious environmental liability" undoubtedly drove his conclusion that these discharges could give rise to "pollution claims", and that unless the 1985 Indemnity covered first party claims, the respondents would be exposed to significant financial liability. His conclusion is wrong.
>
> The motion judge misconstrued the purpose and effect of the [waste disposal site]. The [waste disposal site] was not a source of ongoing mercury contamination or environmental liability. Its creation would not give rise to a pollution claim. Quite the opposite. The [waste disposal site] was created and used as a solution to the mercury pollution problem, effectively as a burial site for mercury-contaminated waste. Again, there was no evidence of mercury-contaminated waste being discharged from the [waste disposal site]. Neither respondent submitted otherwise. [paras. 233-34]

[28] We agree that this erroneous factual finding was key to the motion judge's conclusion that the

Analyse

[26] La question primordiale en l'espèce concerne le champ d'application de l'Indemnité de 1985. En toute déférence, nous sommes d'avis d'accueillir le pourvoi formé par l'Ontario, essentiellement pour les motifs énoncés par le juge Laskin. Nous concluons, comme il l'a fait, que le juge des motions a commis des erreurs de fait manifestes et déterminantes et n'a pas tenu suffisamment compte du fondement factuel dans son interprétation du champ d'application de l'Indemnité de 1985, ce qui justifie une intervention en appel. Il nous paraît difficile d'améliorer ses motifs; aussi nous contenterons-nous de formuler les brèves remarques qui suivent.

[27] Le juge Laskin et les juges majoritaires de la Cour d'appel ont convenu que le juge des motions s'était trompé en concluant que le lieu d'élimination des déchets continuait de rejeter du mercure dans l'environnement. Pour reprendre les propos du juge Laskin :

> [TRADUCTION] La conclusion erronée du juge des motions suivant laquelle les rejets de mercure depuis le [lieu d'élimination des déchets] constituaient une source constante de « lourde responsabilité environnementale » l'a sans nul doute amené à conclure que les rejets en question pourraient donner lieu à des « réclamations pour pollution », et qu'à moins que l'Indemnité de 1985 ne s'applique aux réclamations de première partie, les intimées seraient exposées à une responsabilité financière considérable. Sa conclusion est erronée.
>
> Le juge des motions a mal interprété l'objet et l'effet du [lieu d'élimination des déchets]. Celui-ci n'était pas une source constante de contamination par le mercure ou de responsabilité environnementale. Sa création n'était pas susceptible de donner lieu à une réclamation pour pollution. Bien au contraire. Le [lieu d'élimination des déchets] a été créé et utilisé en tant que solution au problème de pollution au mercure, c'est-à-dire, dans les faits, en tant que site d'enfouissement pour les déchets contaminés par le mercure. Encore une fois, rien ne prouvait que des déchets contaminés par le mercure étaient rejetés du [lieu d'élimination des déchets]. Aucune des intimées n'a fait valoir le contraire. [par. 233-234]

[28] Nous convenons que cette conclusion de fait erronée a joué un rôle déterminant dans la conclusion

Director's Order, which imposed maintenance and monitoring obligations, was a "Pollution Claim" within the meaning of the 1985 Indemnity.

[29] Yet, as Laskin J.A. noted, the 1985 Indemnity was a schedule to the broader Memorandum of Agreement settling the Grassy Narrows Litigation. The scope of the 1985 Indemnity was limited to the issues defined in that agreement, namely, "[t]he discharge by Reed and its predecessors of mercury and any other pollutants into the English and Wabigoon and related river systems, and the continu[ed] presence of any such pollutants discharged by Reed and its predecessors . . . in the related ecosystems" (A.R., vol. IV, at p. 140). The motion judge failed to consider this context when interpreting the scope of the 1985 Indemnity. We agree with Laskin J.A. that, properly interpreted, the 1985 Indemnity was intended to cover only proceedings arising from the discharge or continued presence of mercury *in the related ecosystems*, not those related to the mere presence of mercury contained in the waste disposal site.

[30] We also agree with Laskin J.A. that the 1985 Indemnity must be read in the context of the 1979 and 1982 Indemnities. Indeed, the 1985 Indemnity was given in partial consideration for Great Lakes and Reed releasing Ontario from its obligations under those prior indemnities. It is clear that the 1979 and 1982 Indemnities were in response to the ongoing Grassy Narrows Litigation, which involved claims brought by *third parties*, not by Ontario directly. As Laskin J.A. observed, there is no language in those indemnities that would imply Ontario intended to provide protection against the costs of regulatory compliance.

[31] Although the motion judge concluded that the addition of the phrase "statutory or otherwise" in the 1985 Indemnity expanded the scope of protection beyond that provided previously, we agree

du juge des motions selon laquelle l'arrêté du directeur, qui imposait des obligations en matière d'entretien et de surveillance, constituait une [TRADUCTION] « réclamation pour pollution » au sens de l'Indemnité de 1985.

[29] Pourtant, comme l'a souligné le juge Laskin, l'Indemnité de 1985 constituait une annexe au protocole d'entente plus large réglant le litige de Grassy Narrows. Le champ d'application de l'Indemnité de 1985 se limitait aux points en litige définis dans cette entente, à savoir : [TRADUCTION] « [l]e rejet par Reed et ses prédécesseurs de mercure et de tout autre polluant dans le réseau hydrographique English-Wabigoon, ainsi que la présence continue de ces polluants [. . .] dans les écosystèmes connexes » (d.a., vol. IV, p. 140). Le juge des motions n'a pas tenu compte de ce contexte lorsqu'il a interprété le champ d'application de l'Indemnité de 1985. Nous sommes d'accord avec le juge Laskin pour dire qu'interprétée comme il se doit, l'Indemnité de 1985 était censée s'appliquer seulement aux procédures découlant du rejet ou de la présence continue de mercure *dans les écosystèmes connexes*, et non à celles liées à la simple présence de mercure dans le lieu d'élimination des déchets.

[30] Nous souscrivons également à l'opinion du juge Laskin selon laquelle l'Indemnité de 1985 doit être interprétée à la lumière des Indemnités de 1979 et de 1982. En fait, l'Indemnité de 1985 a été accordée en contrepartie partielle du fait que Great Lakes et Reed avaient déchargé l'Ontario de ses obligations en vertu de ces précédentes indemnités. Il est clair que les Indemnités de 1979 et de 1982 ont été consenties en réponse au litige de Grassy Narrows qui était en instance, et qui concernait des réclamations présentées par des *tiers*, et non par l'Ontario directement. Comme l'a fait observer le juge Laskin, rien dans le libellé de ces indemnités ne tend à indiquer que l'Ontario avait l'intention d'offrir une protection à l'égard des frais engagés pour se conformer à la réglementation.

[31] Bien que le juge des motions ait conclu que l'ajout des mots [TRADUCTION] « prévue par la loi ou autrement » dans l'Indemnité de 1985 élargissait l'étendue de la protection au-delà de ce qui était

with Laskin J.A. that the motion judge's view of the importance of that phrase and *why* the parties entered into the 1985 Indemnity was materially affected by a palpable and overriding factual error. The motion judge found that the 1985 Indemnity was provided in consideration for commitments from Great Lakes to make significant financial investments in the Dryden plant. Given what he found to be the rationale for entering into the 1985 Indemnity, the motion judge concluded that it would be commercially absurd if Ontario could still impose remediation costs. However, Great Lakes' financial commitments were actually provided as part of the prior 1979 Indemnity. Later, Great Lakes gave no new commitments to modernize in consideration for the 1985 Indemnity. The motion judge thus premised his interpretation of the 1985 Indemnity on an incorrect factual basis — one that, as Laskin J.A. noted, led him to place too much emphasis on a change in language and misconstrue the bargain actually struck in the 1985 Indemnity.

prévu auparavant, nous sommes d'accord avec le juge Laskin pour dire que l'opinion que s'est formée le juge des motions sur l'importance de ces mots ainsi que sur les *raisons* pour lesquelles les parties ont conclu l'Indemnité de 1985 a été entachée de manière importante par une erreur de fait manifeste et déterminante. Le juge des motions a estimé que l'Indemnité de 1985 avait été accordée en contrepartie des engagements pris par Great Lakes de procéder à des investissements financiers considérables dans l'usine de Dryden. Étant donné ce qui, à son avis, constituait la raison d'être de l'Indemnité de 1985, le juge des motions a conclu qu'il serait absurde sur le plan commercial que l'Ontario puisse toujours imposer des frais de remédiation. Cependant, les engagements financiers de Great Lakes étaient en réalité prévus dans la précédente Indemnité de 1979. Par la suite, Great Lakes n'a pris aucun nouvel engagement de modernisation en contrepartie de l'Indemnité de 1985. Le juge des motions a donc fait reposer son interprétation de cette indemnité sur un fondement factuel erroné, lequel, comme l'a souligné le juge Laskin, l'a amené à accorder trop d'importance à la modification au libellé et à mal interpréter la transaction réellement intervenue dans l'Indemnité de 1985.

[32] Moreover, as Laskin J.A. found, the motion judge erred by failing to consider the 1985 Indemnity as a whole when determining whether or not the Director's Order fell within its scope. Paragraphs 2 and 3 of the 1985 Indemnity are critical in this regard. Paragraph 2 provides that, in "any Pollution Claim . . . Ontario shall have the right to elect to either take carriage of the defence or to participate in the defence and/or settlement of the Pollution Claim and any proceeding relating thereto as Ontario deems appropriate" (A.R., vol. IV, at p. 190). Paragraph 3 of the 1985 Indemnity also requires the parties to cooperate with Ontario in the defence of a claim. We agree with Laskin J.A. that these clauses would be "utterly meaningless for first party claims".

[32] De plus, comme l'a conclu le juge Laskin, le juge des motions a eu tort de ne pas considérer l'Indemnité de 1985 globalement au moment de déterminer si l'arrêté du directeur entrait ou non dans son champ d'application. Les paragraphes 2 et 3 de l'Indemnité de 1985 revêtent une importance cruciale à cet égard. Le paragraphe 2 dispose que, dans [TRADUCTION] « toute réclamation pour pollution [. . .], l'Ontario a le droit de choisir d'assumer la défense ou de participer à la défense et/ou au règlement de la réclamation pour pollution et de toute procédure y afférente, selon ce qu'il estime approprié » (d.a., vol. IV, p. 190). Le paragraphe 3 de l'Indemnité de 1985 exige également des parties qu'elles collaborent avec l'Ontario à la défense d'une réclamation. Nous sommes d'accord avec le juge Laskin pour dire que ces clauses seraient [TRADUCTION] « dénuées de tout sens en ce qui a trait aux réclamations de première partie ».

[33] Indeed, the inclusion of paras. 2 and 3 in the 1985 Indemnity is completely inconsistent with the

[33] De fait, l'inclusion des par. 2 et 3 à l'Indemnité de 1985 est tout à fait incompatible avec l'idée

notion that para. 1 contemplates first party claims. Nothing in the 1985 Indemnity suggests that pollution claims included both first and third party claims, but that the requirements of paras. 2 and 3 would apply only to the *subset* of pollution claims brought by third parties. To the contrary, para. 2 applies in "*any* Pollution Claim" (emphasis added). The fact that the requirements of paras. 2 and 3 would be "utterly meaningless" in first party claims implies that pollution claims encompass *only* those brought by third parties. It follows that we agree with Laskin J.A. that the motion judge erred by failing to read the 1985 Indemnity as a whole. Properly interpreted, the 1985 Indemnity only applies to third party claims.

[34] In sum, we agree with Laskin J.A.'s conclusion that the 1985 Indemnity does not cover the Director's Order and we would allow Ontario's appeal on that basis. As a result, we find it unnecessary to address the remaining arguments raised in these appeals.

Conclusion

[35] We would allow Ontario's appeal and grant summary judgment in its favour, with costs throughout. Resolute and Weyerhaeuser's appeals are dismissed.

The reasons of Côté, Brown and Rowe JJ. were delivered by

CÔTÉ AND BROWN JJ. (dissenting in part) —

I. Overview

[36] During the 1960s, the owner of a pulp mill in Dryden, Ontario (the corporate predecessor of Reed Ltd.), stemmed the discharge of untreated mercury waste into a nearby river system by burying the waste at an adjacent disposal site. In 1979, Reed — by then the owner — sold the entire property (including the

selon laquelle le par. 1 vise les réclamations de première partie. Rien dans l'Indemnité de 1985 ne tend à indiquer que les réclamations pour pollution comprenaient aussi bien les réclamations de première partie que celles de tiers, mais que les exigences des par. 2 et 3 s'appliqueraient seulement au *sous-ensemble* des réclamations pour pollution présentées par des tiers. Au contraire, le par. 2 s'applique à « *toute* réclamation pour pollution » (italiques ajoutés). Le fait que les exigences des par. 2 et 3 soient [TRADUCTION] « dénuées de tout sens » en ce qui a trait aux réclamations de première partie signifie que les réclamations pour pollution englobent *seulement* celles présentées par des tiers. Nous sommes donc d'accord avec le juge Laskin pour dire que le juge des motions a commis une erreur en n'interprétant pas globalement l'Indemnité de 1985. Interprétée comme il se doit, cette indemnité s'applique seulement aux réclamations de tiers.

[34] En somme, nous souscrivons à la conclusion du juge Laskin selon laquelle l'Indemnité de 1985 ne s'applique pas à l'arrêté du directeur et nous sommes d'avis d'accueillir le pourvoi de l'Ontario pour ce motif. Nous n'estimons donc pas nécessaire de traiter des autres arguments soulevés dans les présents pourvois.

Conclusion

[35] Nous sommes d'avis d'accueillir le pourvoi de l'Ontario et de rendre un jugement sommaire en sa faveur, avec dépens dans toutes les cours. Les pourvois de Résolu et de Weyerhaeuser sont rejetés.

Version française des motifs des juges Côté, Brown et Rowe rendus par

LES JUGES CÔTÉ ET BROWN (dissidents en partie) —

I. Aperçu

[36] Au cours des années 1960, le propriétaire d'une usine de pâtes et papiers située à Dryden, en Ontario (la société ayant précédé Reed Ltd.), a mis fin au rejet de déchets mercuriels non traités dans un réseau hydrographique voisin en enterrant ces déchets dans un lieu d'élimination adjacent. En 1979,

waste disposal site) and the pulp and paper operation to Great Lakes Forest Products Limited. As part of a settlement of claims related to the earlier mercury waste discharge, the Province of Ontario granted an environmental liability indemnity to both Reed and Great Lakes (the "Ontario Indemnity"). This indemnity was to inure to the benefit of those corporations' successors and assigns.

[37] Our reasons address three appeals. At issue in the appeal brought by the Province is whether the scope of the Ontario Indemnity covers the costs of compliance with first party regulatory orders, including those made under legislation enacted after the execution of the agreement. The appeals brought by Weyerhaeuser Company Limited and Resolute FP Canada Inc. go to whether either or both of those corporations can benefit from the Ontario Indemnity as successors and assigns of Great Lakes.

[38] These appeals also present an opportunity for this Court to apply the principles of contractual interpretation articulated in *Sattva Capital Corp. v. Creston Moly Corp.*, 2014 SCC 53, [2014] 2 S.C.R. 633, and *Ledcor Construction Ltd. v. Northbridge Indemnity Insurance Co.*, 2016 SCC 37, [2016] 2 S.C.R. 23, to a series of complex commercial arrangements. The Province's appeal also invites us to consider the doctrine of fettering as it applies to the legislature's law-making powers.

[39] For the reasons that follow, we would dismiss the appeals brought by the Province and Weyerhaeuser, and allow the appeal brought by Resolute.

II. Factual Background

A. *Mercury Contamination of the English and Wabigoon Rivers in the 1960s and 1970s*

[40] During the 1960s and 1970s, Dryden Chemicals Limited and Dryden Paper Company Limited operated

Reed — alors propriétaire — a vendu l'ensemble de la propriété (y compris le lieu d'élimination des déchets) ainsi que l'exploitation de pâtes et papiers à Great Lakes Forest Products Limited. Dans le cadre d'un règlement des réclamations liées au rejet des déchets mercuriels, la province d'Ontario a accordé à Reed et à Great Lakes une indemnité au titre de la responsabilité environnementale (l'« Indemnité de l'Ontario »). Cette indemnité devait bénéficier aux successeurs et ayants droit de ces sociétés.

[37] Les présents motifs visent trois pourvois. Dans le pourvoi interjeté par la province, nous sommes appelés à déterminer si l'Indemnité de l'Ontario couvre les frais engagés pour se conformer aux ordonnances réglementaires de première partie, y compris celles prises en vertu d'une loi adoptée après la signature de l'entente. Les pourvois interjetés par la Compagnie Weyerhaeuser Limitée et Produits forestiers Résolu se rapportent à la question de savoir si l'une ou l'autre des sociétés, ou les deux, peuvent bénéficier de l'Indemnité de l'Ontario à titre de successeurs et ayants droit de Great Lakes.

[38] Les présents pourvois offrent aussi à notre Cour l'occasion d'appliquer les principes d'interprétation contractuelle énoncés dans les arrêts *Sattva Capital Corp. c. Creston Moly Corp.*, 2014 CSC 53, [2014] 2 R.C.S. 633, et *Ledcor Construction Ltd. c. Société d'assurance d'indemnisation Northbridge*, 2016 CSC 37, [2016] 2 R.C.S. 23, à un ensemble d'ententes commerciales complexes. Dans le pourvoi interjeté par la province, nous sommes aussi invités à nous pencher sur l'application de la doctrine de l'entrave aux pouvoirs de légiférer de la législature.

[39] Pour les motifs qui suivent, nous sommes d'avis de rejeter les pourvois interjetés par la province et Weyerhaeuser, et d'accueillir celui de Résolu.

II. Contexte factuel

A. *La contamination par le mercure des rivières English et Wabigoon dans les années 1960 et 1970*

[40] Au cours des années 1960 et 1970, Dryden Chemicals Limited et Dryden Paper Company Limited

a mercury cathode chlor-alkali plant and a pulp and paper mill, respectively, on property located in Dryden (the "Dryden Property"). Together, their operations produced various pollutants, including untreated mercury waste, which they released into the nearby English and Wabigoon rivers, harming the health and industry of those nearby, including members of the Grassy Narrows and Islington First Nations. To dispose of these environmental contaminants, Dryden Paper constructed a waste disposal site on the Dryden Property in 1971. Since 1977, the waste disposal site has been subject to compliance requirements imposed by the Province.

[41] In 1976, Dryden Paper and Dryden Chemicals amalgamated to form Reed.

[42] In 1977, the Grassy Narrows and Islington First Nations sued Reed, Dryden Paper and Dryden Chemicals for damage they say was caused by the contamination of the rivers (the "Grassy Narrows Litigation").

B. *The Sale of the Dryden Property to Great Lakes in 1979*

[43] In 1979, Reed entered into negotiations to sell the operations at the Dryden Property to Great Lakes. Great Lakes was reluctant to proceed with the purchase, however, due to potential liabilities relating to the mercury contamination, including the Grassy Narrows Litigation. At the same time, the Province was anxious to see a successful sale, to ensure the continuing viability of Dryden's local economy. It therefore agreed to indemnify both Reed and Great Lakes for any environmental damages caused by Reed in excess of $15 million (the "1979 Indemnity"). In exchange, Great Lakes and Reed agreed to spend around $200 million to modernize and expand the pulp mill. The terms of this agreement were set out in a letter dated November 6, 1979, from the Treasurer of Ontario to the President of Great Lakes. The relevant portion of this letter reads as follows:

The continued viability of the Dryden facilities and the undertaking of major modernization expenditures with

ont exploité, respectivement, une usine de chlore et de soude caustique utilisant le procédé à cathode de mercure et une usine de pâtes et papiers sur une propriété située à Dryden (la « propriété de Dryden »). Ensemble, elles ont produit divers polluants, dont des déchets mercuriels non traités, qu'elles ont rejeté dans les rivières English et Wabigoon situées à proximité, nuisant à la santé et aux entreprises de la population environnante, y compris des membres des Premières Nations de Grassy Narrows et d'Islington. Pour éliminer ces contaminants environnementaux, Dryden Paper a, en 1971, construit un lieu d'élimination des déchets sur la propriété de Dryden. Depuis 1977, ce site est assujetti à des exigences provinciales en matière de conformité.

[41] En 1976, Dryden Paper et Dryden Chemicals ont fusionné pour former Reed.

[42] En 1977, les Premières Nations de Grassy Narrows et d'Islington ont poursuivi Reed, Dryden Paper et Dryden Chemicals pour le préjudice que leur avait causé, selon elles, la contamination des rivières (le « litige de Grassy Narrows »).

B. *La vente de la propriété de Dryden à Great Lakes en 1979*

[43] En 1979, Reed a entamé des négociations en vue de vendre à Great Lakes ses opérations sur la propriété de Dryden. Great Lakes était toutefois réticente à procéder à cet achat en raison des responsabilités susceptibles de découler de la contamination par le mercure, dont celles en cause dans le litige de Grassy Narrows. Par ailleurs, la province tenait à ce que la vente se conclue afin d'assurer la viabilité économique locale de Dryden. La province a donc convenu d'indemniser Reed et Great Lakes pour tout dommage environnemental causé par Reed excédant 15 millions de dollars (l'« Indemnité de 1979 »). En retour, Great Lakes et Reed ont accepté de dépenser environ 200 millions de dollars pour la modernisation et l'agrandissement de l'usine de pâtes et papiers. Les modalités de cette entente ont été énoncées dans une lettre datée du 6 novembre 1979 du trésorier de l'Ontario au président de Great Lakes. Voici le passage pertinent de la lettre en question :

[TRADUCTION] La viabilité des installations de Dryden et l'engagement de dépenses majeures pour leur

respect to them are of considerable importance to the people of this Province. The substantial and beneficial employment and economic effects that the operation of a modernized facility will have on the population and economy of Dryden is of real significance.

In the event that Great Lakes negotiations with the Reed group of companies are successful then in the event that Great Lakes is required to pay any monies as a result of any final decision of a court against Great Lakes, Reed Ltd. or any other person prior to the year 2010 in respect of pollution caused by Reed Ltd. or any of its predecessor companies in the Dryden area prior to the date upon which Great Lakes acquires the assets and undertaking of the Dryden complex of Reed Ltd. or in the event that any settlement with any claimant is made the amount of which settlement has been approved by the Attorney General of Ontario, I have been authorized by the Executive Council of Ontario to advise you that I will make a Recommendation to the Executive Council of Ontario that the Government of Ontario take effective steps to ensure that Great Lakes Forest Products Limited will not be required to pay any monies in excess of the maximum amount of $15 million referred to in paragraph 2 of this letter, provided that over the next three to four years Great Lakes expends in the order of $200 million for the modernization and expansion of the Dryden facilities.

(A.R., vol. IV, at pp. 135-36)

[44] Great Lakes purchased the pulp mill in December 1979 by way of an asset purchase agreement (the "1979 Dryden Agreement"). That agreement addressed, among other things, environmental responsibilities respecting the Dryden Property. In particular, clause 5.3 of the 1979 Dryden Agreement created a regime for the sharing of costs arising from pollution claims, pursuant to which Reed and Great Lakes were to share the costs of environmental liabilities up to $15 million, leaving Great Lakes exclusively responsible for anything exceeding that amount. Clause 11.4 carves out of this regime the costs of compliance with a control order that the Province had issued in 1979 (the "Control Order"), making Great Lakes solely responsible for those costs.

modernisation revêtent une importance considérable pour les gens de cette province. Les effets bénéfiques marqués qu'aura l'exploitation d'une installation modernisée sur l'emploi et l'économie de Dryden sont d'une grande importance.

Si les négociations entre Great Lakes et le groupe d'entreprises Reed aboutissent, et que Great Lakes est tenue de verser une quelconque somme d'argent par suite d'une décision judiciaire définitive rendue avant 2010 contre Great Lakes, Reed Ltd. ou toute autre personne relativement à la pollution causée par Reed Ltd. ou l'une des sociétés qui l'ont précédée dans la région de Dryden avant la date d'acquisition par Great Lakes des actifs et de l'entreprise du complexe de Reed Ltd. situé à Dryden, ou qu'un règlement est conclu avec un demandeur, règlement dont le montant aura été approuvé par le procureur général de l'Ontario, j'ai été autorisé par le Conseil exécutif de l'Ontario à vous aviser que je recommanderai au Conseil exécutif de l'Ontario de faire en sorte que le gouvernement de l'Ontario prenne les mesures nécessaires pour que Great Lakes Forest Products Limited ne soit pas tenue de verser une somme qui dépasse le montant maximal de 15 millions de dollars dont il est question au paragraphe 2 de la présente lettre, pourvu que Great Lakes consacre une somme de l'ordre de 200 millions de dollars à la modernisation et à l'agrandissement des installations de Dryden au cours des trois ou quatre prochaines années.

(d.a., vol. IV, p. 135-136)

[44] Great Lakes a acheté l'usine de pâtes et papiers en décembre 1979 aux termes d'une convention d'achat d'actifs (la « convention de Dryden de 1979 »). Cette convention portait entre autres sur les responsabilités environnementales relatives à la propriété de Dryden. Plus particulièrement, la clause 5.3 de la convention créait un régime de partage des frais découlant des réclamations pour pollution, en vertu duquel Reed et Great Lakes devaient partager les frais liés aux responsabilités environnementales jusqu'à concurrence de 15 millions de dollars, laissant ainsi à Great Lakes l'entière responsabilité de tous les frais excédant ce montant. La clause 11.4 excluait de ce régime les frais engagés pour se conformer à un arrêté d'intervention pris par la province en 1979 (l'« arrêté d'intervention »), de sorte que Great Lakes en assumait seule la responsabilité.

C. *The Settlement of the Grassy Narrows Litigation in 1985*

[45] The Governments of Canada and Ontario initiated a mediation process with the Islington and Grassy Narrows First Nations to address the problems regarding the mercury contamination and to settle the Grassy Narrows Litigation. Great Lakes was reluctant to participate in any such settlement without releases from liability in relation to the mercury pollution caused by Reed and its predecessors. To overcome this impasse, Ontario's Provincial Secretary for Resources Development, the Honourable R. H. Ramsay, wrote to Great Lakes on January 28, 1982 (the "1982 Ramsay Letter"), stating that the Province would indemnify Great Lakes against any claims related to mercury pollution:

> The purpose of this letter is to facilitate a settlement of the current negotiations . . . .
>
> The Government of Ontario recognizes the distinct advantage of the Indian people obtaining a settlement in the very near future. Accordingly, the Government is prepared to indemnify Great Lakes Forest Products Limited against any claims related to mercury pollution such that the Company's total payments to all claimants in respect of damages awarded by any court or for any settlement approved by the Attorney General of Ontario attributable to the operations of Reed Paper Ltd. or any of its predecessor companies in the Dryden area will be limited to $15 million. The Government of Ontario will assume responsibility for any damages awarded by any court or for any settlement approved by the Attorney General of Ontario, after $15 million has been paid by the Great Lakes Forest Products Limited, Reed Ltd., Reed International Ltd., Dryden Chemicals Ltd. and Dryden Paper Co. Ltd. in connection with the above mentioned mercury pollution claims. Such claims include personal injury, property damage and economic claims of any claimants, including adults, minors and those yet unborn, related to mercury pollution.

C. *Le règlement du litige de Grassy Narrows en 1985*

[45] Les gouvernements du Canada et de l'Ontario ont amorcé un processus de médiation avec les Premières Nations d'Islington et de Grassy Narrows dans le but de résoudre les problèmes liés à la contamination par le mercure et de régler le litige de Grassy Narrows. Great Lakes était réticente à l'idée de participer à un règlement de litige de ce genre sans avoir obtenu de décharges de responsabilité pour la pollution au mercure causée par Reed et ses prédécesseurs. Pour sortir de cette impasse, le secrétaire provincial du Développement des ressources de l'Ontario, l'honorable R. H. Ramsay, a écrit à Great Lakes le 28 janvier 1982 (la « lettre de 1982 de Ramsay ») pour l'informer que la province l'indemniserait pour toute réclamation relative à la pollution au mercure :

> [TRADUCTION] La présente lettre vise à faciliter le dénouement des négociations en cours . . .
>
> Le gouvernement de l'Ontario reconnaît que le fait de parvenir à un règlement dans un avenir très rapproché représente un net avantage pour les peuples autochtones. Par conséquent, le gouvernement est prêt à indemniser Great Lakes Forest Products Limited pour toute réclamation relative à la pollution au mercure de sorte que le total des sommes versées par l'entreprise à titre de dommages-intérêts octroyés par un tribunal ou versées par l'entreprise dans le cadre d'un règlement approuvé par le procureur général de l'Ontario pour des dommages imputables aux activités de Reed Paper Ltd. ou de l'une des sociétés l'ayant précédée dans la région de Dryden sera limité à 15 millions de dollars. Le gouvernement de l'Ontario assumera la responsabilité de toute somme accordée à titre de dommages-intérêts par un tribunal ou de tout règlement approuvé par le procureur général de l'Ontario une fois que les 15 millions de dollars auront été payés par Great Lakes Forest Products Limited, Reed Ltd., Reed International Ltd., Dryden Chemicals Ltd. et Dryden Paper Co. Ltd. en ce qui touche les réclamations relatives à la pollution au mercure dont il est question précédemment. Ces réclamations incluent les réclamations relatives à la pollution au mercure fondées sur des dommages corporels, des dommages matériels et des pertes économiques, peu importe le demandeur, qu'il s'agisse d'un adulte, d'un mineur ou d'un enfant à naître.

It must be understood that any legal proceedings which could result in the Government of Ontario becoming liable to make payments pursuant to this undertaking must be brought to the attention of the Government of Ontario immediately upon such proceedings being launched, and the Government of Ontario shall have the right either to take carriage of or to participate in the defence and/or settlement of the litigation. Failure to give such notification or to allow the Government of Ontario to either take carriage of or to participate in the defence and/or settlement of the litigation will preclude the making of any payments by the Province with regard to the action in question.

(A.R., vol. III, at pp. 175-76)

[46] The Grassy Narrows Litigation was settled on terms formalized in a Memorandum of Agreement (the "Settlement Agreement") executed on November 22, 1985, by Canada, the Province, the Grassy Narrows and Islington First Nations, Reed, and Great Lakes. Its terms were approved by the Supreme Court of Ontario in 1986 (*Mandamin v. Reed Ltd.*, No. 14716/77, June 26, 1986), and were given effect by both Parliament and the Ontario Legislature (*Grassy Narrows and Islington Indian Bands Mercury Pollution Claims Settlement Act*, S.C. 1986, c. 23; *English and Wabigoon River Systems Mercury Contamination Settlement Agreement Act, 1986*, S.O. 1986, c. 23).

[47] The Settlement Agreement provides that "[t]he parties agree, without admission of liability by any party and subject to the terms of this Agreement, that the settlement is to settle all claims and causes of action, past, present and future, arising out of the issues" (A.R., vol. IV, at p. 141 (emphasis added)). The "issues" were defined in the recitals as follows:

The discharge by Reed and its predecessors of mercury and any other pollutants into the English and Wabigoon and related river systems, and the continuing presence of any such pollutants discharged by Reed and its predecessors, including the continuing but now diminishing presence of methylmercury in the related ecosystems since its initial identification in 1969, and governmental actions taken in consequence thereof, may have had and may continue to have effects and raise concerns in respect of the

Il est entendu que toute procédure judiciaire à l'issue de laquelle le gouvernement de l'Ontario pourrait être tenu de verser des sommes d'argent conformément à cet engagement doit être portée à l'attention dudit gouvernement dès qu'elle est introduite et celui-ci a le droit d'assumer la défense ou de participer à la défense et/ou au règlement du litige. Le fait de ne pas donner cet avis ou de ne pas permettre au gouvernement de l'Ontario d'assumer la défense ou de participer à la défense et/ou au règlement du litige fera obstacle au versement par la province de toute somme d'argent en ce qui concerne l'action en question.

(d.a., vol. III, p. 175-176)

[46] Le litige de Grassy Narrows fut réglé suivant des modalités officialisées dans un protocole d'entente (la « Convention de règlement ») signé le 22 novembre 1985 par le Canada, la province, les Premières Nations de Grassy Narrows et d'Islington, Reed et Great Lakes. Ces modalités furent approuvées par la Cour suprême de l'Ontario en 1986 (*Mandamin c. Reed Ltd.*, n° 14716/77, 26 juin 1986), et furent mises en œuvre par le Parlement et par la législature ontarienne (*Loi sur le règlement des revendications des bandes indiennes de Grassy Narrows et d'Islington (pollution par le mercure)*, L.C. 1986, c. 23; *Loi de 1986 sur la convention de règlement relative à la contamination par le mercure du réseau hydrographique English-Wabigoon*, L.O. 1986, c. 23).

[47] La Convention de règlement prévoit que [TRADUCTION] « [l]es parties conviennent, sans pour autant admettre leur responsabilité et sous réserve des modalités de la présente convention, que le règlement vise à régler toute réclamation et tout droit d'action, passés, présents et futurs, découlant des points en litige » (d.a., vol. IV, p. 141 (nous soulignons)). Les « points en litige » sont définis comme suit dans les attendus :

[TRADUCTION] Le rejet par Reed et ses prédécesseurs de mercure et de tout autre polluant dans le réseau hydrographique English-Wabigoon, ainsi que la présence continue de ces polluants, ce qui inclut la présence continue mais en voie de diminution de mercure méthylé dans les écosystèmes connexes depuis qu'on a constaté sa présence en 1969, et les mesures gouvernementales prises à cet égard, peuvent avoir eu des incidences et continuer d'en avoir et de soulever des préoccupations en ce qui concerne

social and economic circumstances and the health of the present and future members of the Bands ("the issues").

(A.R., vol. IV, at p. 140)

[48] The Settlement Agreement also required the Province to indemnify Great Lakes and Reed "in respect of the issues" (para. 2.4(a)), which led to the Ontario Indemnity (A.R., vol. IV, at p. 6). That indemnity was incorporated into Schedule F of the Settlement Agreement. In return, Great Lakes and Reed released the Province from any obligations under the 1979 Indemnity and the 1982 Ramsay Letter (para. 2.4(b); A.R., vol. IV, at p. 6).

[49] Paragraph 1 of the Ontario Indemnity — the meaning of which lies at the heart of this appeal — reads, in part, as follows:

Ontario hereby covenants and agrees to indemnify Great Lakes, Reed, International and any company which was at the Closing Date [December 17, 1979] a subsidiary or affiliate company (whether directly or indirectly) of International, harmless from and against any obligation, liability, damage, loss, costs or expenses incurred by any of them after the date hereof as a result of any claim, action or proceeding, whether statutory or otherwise, existing at December 17, 1979 or which may arise or be asserted thereafter (including those arising or asserted after the date of this agreement), whether by individuals, firms, companies, governments (including the Federal Government of Canada and any province or municipality thereof or any agency, body or authority created by statutory or other authority) or any group or groups of the foregoing, because of or relating to any damage, loss, event or circumstances, caused or alleged to be caused by or with respect to, either in whole or in part, the discharge or escape or presence of any pollutant by Reed or its predecessors, including mercury or any other substance, from or in the plant or plants or lands or premises forming part of the Dryden assets sold by Reed Ltd. to Great Lakes under the [1979] Dryden Agreement (hereinafter referred to as "Pollution Claims").

(A.R., vol. IV, at pp. 189-90)

la conjoncture économique et sociale ainsi que la santé des membres actuels et futurs des bandes en question (« les points en litige »).

(d.a., vol. IV, p. 140)

[48] Aux termes de la Convention de règlement, la province devait aussi indemniser Great Lakes et Reed [TRADUCTION] « à l'égard des points en litige » (par. 2.4(a)), ce qui a mené à l'Indemnité de l'Ontario (d.a., vol. IV, p. 6). Cette indemnité a été incorporée à l'annexe F de la Convention de règlement. En retour, Great Lakes et Reed ont libéré la province de toutes les obligations découlant de l'Indemnité de 1979 et de la lettre de 1982 de Ramsay (par. 2.4(b); d.a., vol. IV, p. 6).

[49] Le paragraphe 1 de l'Indemnité de l'Ontario — dont le sens est au cœur du présent pourvoi — est, en partie, ainsi libellé :

[TRADUCTION] L'Ontario s'engage et consent à tenir Great Lakes, Reed, International et toute société qui, à la date de clôture [soit le 17 décembre 1979], était (directement ou indirectement) une filiale ou une société affiliée d'International, à couvert de l'ensemble des obligations, responsabilités, dommages, pertes, frais ou dépenses qu'est susceptible d'entraîner pour l'une ou l'autre d'entre elles, après la date des présentes, toute réclamation, action ou procédure, qu'elle soit prévue par loi ou autrement, qui existait au 17 décembre 1979 ou qui était susceptible de prendre naissance ou d'être présentée par la suite (y compris celles ayant pris naissance ou ayant été présentées après la date des présentes), par des particuliers, des firmes, des sociétés, des gouvernements (y compris le gouvernement fédéral du Canada et toute province ou municipalité du Canada, ou tout organisme ou autorité créé en vertu d'un pouvoir légal, ou d'un autre pouvoir) ou un ou plusieurs groupes de ceux-ci, du fait ou à l'égard des dommages, pertes, événements ou circonstances dus ou présumés dus ou en ce qui a trait, en tout ou en partie, au rejet ou à la fuite de polluants, notamment le mercure ou toute autre substance, par Reed ou ses prédécesseurs, à partir des usines, des terrains ou des lieux faisant partie des actifs de Dryden que Reed Ltd. a vendus à Great Lakes en vertu de la convention de Dryden [de 1979], ou encore à la présence de tels polluants dans ces usines, terrains ou lieux (ci-après appelées les « réclamations pour pollution »).

(d.a., vol. IV, p. 189-190)

[50] Paragraph 2 of the Ontario Indemnity requires the party seeking indemnification to promptly notify the Province of the receipt of any notice of "Pollution Claims" (defined in para. 1), and gives the Province the right either to take carriage of the defence, or to participate in the pollution claim's defence and settlement; para. 3 requires Great Lakes to cooperate with the Province in the investigation, defence and settlement of a pollution claim; para. 4 states that the indemnity shall be valid without limitation as to time; and para. 6 provides that the indemnity enures to the benefit of the parties' respective successors and assigns. That provision reads as follows:

> The indemnity shall be binding upon and enure to the benefit of the respective successors and assigns of Ontario, Reed, International and Great Lakes, provided however that Ontario shall not be entitled to assign this indemnity without the prior written consent of the other parties hereto.

(A.R., vol. IV, at pp. 191-92)

[51] Great Lakes provided an indemnity to Reed in respect of environmental liabilities contemporaneously, as part of the Settlement Agreement. The parties contemplated that these two indemnities (this indemnity and the Ontario Indemnity) would operate in tandem; to the extent that Reed claimed on its indemnity against Great Lakes, Great Lakes would be indemnified under the Ontario Indemnity. This linkage was expressly recognized in the closing words of para. 1 of the Ontario Indemnity:

> It is hereby expressly acknowledged and agreed that in respect of Ontario's covenant and agreement hereunder to indemnify Great Lakes that the term "Pollution Claims" shall include any obligation, liability, damage, loss, costs or expenses incurred by Great Lakes as a result of any claim, action or proceeding resulting from or in connection with the indemnity agreement of even date herewith made between Great Lakes, Reed and International.

(A.R., vol. IV, at p. 190)

[50] Le paragraphe 2 de l'Indemnité de l'Ontario oblige la partie qui demande une indemnisation à aviser rapidement la province de la réception d'un avis de « réclamations pour pollution » (définies au par. 1), et donne à la province le droit d'assumer la défense, ou encore de participer à la défense et au règlement de la réclamation pour pollution. Aux termes du par. 3, Great Lakes doit collaborer avec la province à l'enquête, à la défense et au règlement d'une réclamation pour pollution. Le paragraphe 4 précise que l'indemnité n'est assujettie à aucune limite de temps, et le par. 6 prévoit que l'indemnité bénéficie aux successeurs et ayants droit respectifs des parties. Cette disposition est ainsi libellée :

> [TRADUCTION] L'indemnité lie les successeurs et ayants droit respectifs de l'Ontario, de Reed, d'International et de Great Lakes et bénéficie à ceux-ci, à condition toutefois que l'Ontario ne soit pas autorisé à céder l'indemnité sans le consentement préalable écrit des autres parties.

(d.a., vol. IV, p. 191-192)

[51] En même temps, dans le cadre de la Convention de règlement, Great Lakes accordait une indemnité à Reed pour ses responsabilités environnementales. Les parties envisageaient que ces deux indemnités (cette indemnité et celle de l'Ontario) s'appliqueraient de concert; si Reed demandait à Great Lakes de l'indemniser, Great Lakes serait indemnisée en vertu de l'Indemnité de l'Ontario. Ce lien a été expressément reconnu à la toute fin du par. 1 de l'Indemnité de l'Ontario :

> [TRADUCTION] Il est expressément reconnu et convenu par les présentes qu'en ce qui concerne l'engagement et le consentement de l'Ontario à indemniser Great Lakes, l'expression « réclamations pour pollution » comprend l'ensemble des obligations, responsabilités, dommages, pertes, frais ou dépenses qu'est susceptible d'entraîner pour Great Lakes toute réclamation, action ou procédure qui découle de l'entente d'indemnisation conclue à la même date que les présentes entre Great Lakes, Reed et International, ou qui y est liée.

(d.a., vol. IV, p. 190)

[52] After the parties executed the Settlement Agreement but before they signed the Ontario Indemnity, the *Environmental Protection Act*, R.S.O. 1980, c. 141, was amended to confer a statutory right of action on the Province and third parties against certain polluters. The amendments arose out of *An Act to amend The Environmental Protection Act, 1971*, S.O. 1979, c. 91, also known as the "Spills Bill". Although the Spills Bill never came into force, elements of it were incorporated into the 1980 *Environmental Protection Act*. The relevant provisions came into force in November 1985. For convenience, those amendments will be referred to as the "Spills Bill".

D. *The Changes in Corporate Status Between 1985 and 1998*

[53] Reed subsequently amalgamated with other corporations, and its successor corporation was dissolved in 1993. For its part, Great Lakes became Bowater Pulp and Paper Canada Inc. in July 1998.

E. *Weyerhaeuser's Purchase of the Dryden Property in 1998*

[54] On September 30, 1998, Weyerhaeuser bought the Dryden Property from Bowater, along with certain assets used in the pulp and paper operation. This sale was recorded in the "1998 Asset Purchase Agreement". Because of possible environmental liabilities associated with the waste disposal site, Weyerhaeuser initially sought to exclude the parcel of land on which it was constructed from the transaction, and Bowater agreed to this. This parcel could not be severed from the property before the closing date, however, and the deal was therefore restructured such that Bowater conveyed title to the entire Dryden Property — including the waste disposal site — to Weyerhaeuser. Weyerhaeuser then immediately leased the waste disposal site back to Bowater. Once title to the waste disposal site was severed from the rest of the Dryden Property, it was to be transferred back to Bowater.

[52] Après que les parties eurent signé la Convention de règlement, mais avant qu'elles signent l'Indemnité de l'Ontario, la *Loi sur la protection de l'environnement*, L.R.O. 1980, c. 141, a été modifée afin de conférer à la province et aux tiers un droit d'action contre certains pollueurs. Les modifications découlaient d'une loi intitulée *An Act to amend The Environmental Protection Act, 1971*, S.O. 1979, c. 91, et étaient également connues sous le nom de « loi sur les déversements ». Bien que la loi sur les déversements ne soit jamais entrée en vigueur, certains de ses éléments ont été incorporés dans la *Loi sur la protection de l'environnement* de 1980. Les dispositions pertinentes sont entrées en vigueur en novembre 1985. Par souci de commodité, ces modifications seront appelées « loi sur les déversements » dans les présents motifs.

D. *Les modifications apportées au statut de la société entre 1985 et 1998*

[53] Reed a subséquemment fusionné avec d'autres sociétés et la société qui lui a succédé a été dissoute en 1993. Pour sa part, Great Lakes est devenue Bowater Pâtes et papiers Canada Inc. en juillet 1998.

E. *L'achat par Weyerhaeuser de la propriété de Dryden en 1998*

[54] Le 30 septembre 1998, Weyerhaeuser a acheté de Bowater la propriété de Dryden ainsi que certains actifs utilisés dans l'exploitation de pâtes et papiers. Cette vente a été constatée dans la « convention d'achat d'actifs de 1998 ». En raison des responsabilités environnementales pouvant être associées au lieu d'élimination des déchets, Weyerhaeuser a voulu au départ exclure de l'opération la parcelle de terrain sur laquelle se trouvait le lieu en question, ce à quoi Bowater a consenti. Cette parcelle ne pouvait cependant pas être séparée de la propriété avant la date de clôture; l'accord a donc été restructuré de telle sorte que Bowater a transféré le titre de l'ensemble de la propriété de Dryden — y compris le lieu d'élimination des déchets — à Weyerhaeuser, et cette dernière a ensuite immédiatement loué ce site à Bowater. Une fois le titre du lieu d'élimination des déchets séparé du reste de la propriété de Dryden, ce lieu devait être rétrocédé à Bowater.

[55] The lease agreement between Bowater and Weyerhaeuser in respect of the waste disposal site (the "Lease Agreement") required Bowater to indemnify Weyerhaeuser for, among other things, "the presence or release of mercury and any other contaminant, substance or waste on or in the Lands" (A.R., vol. V, at p. 126). This indemnity was to survive the term of the lease.

[56] Bowater and Weyerhaeuser acknowledged that they had entered into the Lease Agreement "solely as an interim agreement pending severance approval under the *Planning Act*", at which time title to the waste disposal site was to be transferred back to Bowater (*ibid.*, at p. 123). Approval of the severance was obtained around two years later, and Weyerhaeuser re-conveyed the waste disposal site to Bowater on August 25, 2000.

[57] In 2007, Weyerhaeuser sold the Dryden pulp mill to Domtar Inc.

F. *Bowater's Corporate Restructuring*

[58] In April 2009, Bowater (which by then had become Bowater Canadian Forest Products Inc.) and a number of related companies filed for creditor protection under the *Companies' Creditors Arrangement Act*, R.S.C. 1985, c. C-36 ("*CCAA*"). At this point, Bowater still owned the waste disposal site. As part of the *CCAA* proceedings, Bowater was granted an order authorizing it to transfer the waste disposal site to 4513541 Canada Inc. in October 2010. Several months later, 4513541 Canada Inc.'s receiver obtained court approval to abandon the waste disposal site, with no associated liability.

[59] In 2012, Bowater became Resolute FP Canada Inc.

G. *The 2011 Director's Order*

[60] On August 25, 2011, the Province, through its Ministry of the Environment, issued a Director's

[55] Aux termes de la convention de bail conclue entre Bowater et Weyerhaeuser relativement au lieu d'élimination des déchets (la « Convention de bail »), Bowater devait entre autres indemniser Weyerhaeuser pour [TRADUCTION] « la présence ou le rejet de mercure et de tout autre contaminant, substance ou déchet sur ou dans les terres » (d.a., vol. V, p. 126). Cette clause d'indemnisation devait continuer de s'appliquer après la fin du bail.

[56] Bowater et Weyerhaeuser ont reconnu que la Convention de bail n'était [TRADUCTION] « qu'une entente provisoire en attendant que la séparation soit approuvée en vertu de la *Loi sur l'aménagement du territoire* », après quoi le titre du lieu d'élimination des déchets devait être rétrocédé à Bowater (*ibid.*, p. 123). La séparation a été approuvée environ deux ans plus tard et Weyerhaeuser a rétrocédé le lieu d'élimination des déchets à Bowater le 25 août 2000.

[57] En 2007, Weyerhaeuser a vendu l'usine de pâtes et papiers de Dryden à Domtar Inc.

F. *La restructuration de la société Bowater*

[58] En avril 2009, Bowater (qui était alors devenue Bowater Produits forestiers du Canada Inc.) et un certain nombre de sociétés affiliées déposaient une demande de protection contre les créanciers en vertu de la *Loi sur les arrangements avec les créanciers des compagnies*, L.R.C. 1985, c. C-36 (« *LACC* »). Bowater était alors toujours propriétaire du lieu d'élimination des déchets. Dans le cadre de la procédure fondée sur la *LACC*, Bowater a obtenu, en octobre 2010, une ordonnance l'autorisant à transférer le lieu d'élimination des déchets à 4513541 Canada Inc. Plusieurs mois plus tard, le séquestre de 4513541 Canada Inc. a obtenu du tribunal l'autorisation d'abandonner le lieu d'élimination des déchets, sans aucune responsabilité.

[59] En 2012, Bowater est devenue Produits forestiers Résolu.

G. *L'arrêté du directeur de 2011*

[60] Le 25 août 2011, la province, par l'entremise de son ministère de l'Environnement, a délivré

Order against 4513541 Canada Inc., Weyerhaeuser, Bowater, and several of Bowater's directors, requiring them:

> . . . to repair certain site erosion, perform specified groundwater and surface water testing, and file annual reports containing specified information; (ii) to deliver to the [Ministry of the Environment] the sum of $273,063 as financial assurance in respect of the [Waste Disposal Site]; and (iii) to "take all reasonable measures to ensure that any discharge of a contaminant to the natural environment is prevented and any adverse effect that may result from such a discharge is dealt with according to all legal requirements."

(C.A. reasons, at para. 50, citing the Director's Order, A.R., vol. IV, at p. 27.)

Paragraph 3.1 of the Director's Order described these requirements as "minimum requirements only", adding that their discharge would not relieve the named parties from "complying with any other applicable Order, Statute or Regulation", or from "obtaining any approvals or consents not specified in [the Director's] Order" (A.R., vol. IV, at p. 28).

[61] The Director's Order was issued under the *Environmental Protection Act*, R.S.O. 1990, c. E.19. That statute had been amended in 1990 to empower the Director to impose certain obligations upon *former* owners and those who *previously* held management or control of a given undertaking or property (see *Environmental Protection Statute Law Amendment Act, 1990*, S.O. 1990, c. 18, ss. 18(1) and 21 to 23).

[62] Both Weyerhaeuser and Resolute appealed the Director's Order to the Environmental Review Tribunal. The Province says that these appeals are in abeyance. Weyerhaeuser also filed a proof of claim in Bowater's *CCAA* proceedings (which were still ongoing at the time) for indemnification under the Lease Agreement for the present value of the work required by the Director's Order and estimated legal costs, amounting to approximately $373,063. In settlement of its claim, Weyerhaeuser received shares in a company that emerged from

un arrêté du directeur contre 4513541 Canada Inc., Weyerhaeuser, Bowater et plusieurs administrateurs de Bowater, les obligeant à faire ce qui suit :

> [TRADUCTION] . . . réparer une certaine érosion du site, effectuer une analyse déterminée d'eaux souterraines et d'eaux de surface, et déposer des rapports annuels contenant des renseignements déterminés; (ii) remettre au [ministère de l'Environnement] la somme de 273 063 $ à titre de garantie financière pour le [lieu d'élimination des déchets]; et (iii) « prendre toutes les mesures raisonnables pour éviter le rejet d'un contaminant dans l'environnement naturel et pour remédier aux conséquences préjudiciables pouvant résulter d'un tel rejet conformément à toutes les exigences légales. »

(Motifs de la C.A., par. 50, citant l'arrêté du directeur, d.a., vol. IV, p. 27.)

Aux termes du par. 3.1 de l'arrêté du directeur, ces exigences étaient [TRADUCTION] « des exigences minimales seulement » et le fait d'y satisfaire ne dispensait pas les parties désignées de « se conformer aux autres arrêtés, lois ou règlements applicables » ou d'« obtenir les approbations ou consentements non mentionnés dans [l'] arrêté [du directeur] » (d.a., vol. IV, p. 28).

[61] L'arrêté du directeur a été pris en vertu de la *Loi sur la protection de l'environnement*, L.R.O. 1990, c. E.19. Cette loi avait été modifiée en 1990 afin d'autoriser le directeur à imposer certaines obligations aux *anciens* propriétaires d'une entreprise ou d'un bien et aux personnes qui, *antérieurement*, en assuraient la gestion ou en avaient le contrôle (voir *Environmental Protection Statute Law Amendment Act, 1990*, S.O. 1990, c. 18, par. 18(1) et art. 21 à 23).

[62] Weyerhaeuser et Résolu ont interjeté appel de l'arrêté du directeur auprès du Tribunal de l'environnement. La province affirme que ces appels sont présentement suspendus. Weyerhaeuser a également déposé, dans le cadre de la procédure fondée sur la *LACC* introduite par Bowater (qui était toujours en cours à l'époque), une preuve de réclamation en vue d'être indemnisée, en vertu de la Convention de bail, pour la valeur actuelle des travaux exigés par l'arrêté du directeur et les frais juridiques estimés, soit environ 373 063 $. En règlement de sa réclamation,

CCAA protection, which shares were subsequently sold in May 2015.

III. Proceedings Below

[63] Shortly after being served with the Director's Order, counsel for Weyerhaeuser provided notice thereof to Ontario's Ministry of the Attorney General, invoking paras. 2 and 6 of the Ontario Indemnity, and claiming indemnity as a successor and assignee of Great Lakes. In response, the Attorney General denied that the costs of complying with the Director's Order fell within the scope of the Ontario Indemnity. Weyerhaeuser sued the Province for an order declaring that it is entitled to be indemnified under the terms of the Ontario Indemnity "for the costs that it has incurred and may incur as a result of [the] Director's Order made effective on September 6, 2011" (A.R., vol. II, at p. 3). Resolute was granted leave to intervene as a party to that proceeding.

A. *Decision of the Ontario Superior Court of Justice, 2016 ONSC 4652, 60 B.L.R. (5th) 237*

[64] All parties brought various motions for summary judgment before the Ontario Superior Court of Justice. At issue was whether the Ontario Indemnity covered the costs of complying with the Director's Order and, if so, whether Weyerhaeuser and Resolute are entitled to benefit thereunder.

[65] The motion judge found in favour of Weyerhaeuser and Resolute, holding that the scope of the Ontario Indemnity, as set out in its own first paragraph, covered first party regulatory orders. He further held that the Ontario Indemnity did not improperly fetter the Ontario Legislature's law-making powers.

[66] The motion judge also held that the enurement clause extended the rights and obligations under the Ontario Indemnity to Resolute and Weyerhaeuser — Resolute as a corporate successor to Great Lakes, and Weyerhaeuser as both a successor-in-title

Weyerhaeuser a reçu des actions d'une compagnie qui n'était plus sous la protection de la *LACC*, actions ayant par la suite été vendues en mai 2015.

III. Décisions des juridictions inférieures

[63] Peu après que l'arrêté du directeur lui eut été signifié, l'avocat de Weyerhaeuser en a avisé le ministère du Procureur général de l'Ontario, invoquant les par. 2 et 6 de l'Indemnité de l'Ontario et demandant que sa cliente soit indemnisée à titre de successeur et ayant droit de Great Lakes. En réponse, le procureur général a nié que les frais engagés pour se conformer à l'arrêté du directeur étaient couverts par l'Indemnité de l'Ontario. Weyerhaeuser a poursuivi la province afin d'obtenir une ordonnance déclarant qu'elle avait le droit d'être indemnisée en vertu de l'Indemnité de l'Ontario [TRADUCTION] « pour les frais qu'elle a engagés et qu'elle pourrait engager par suite de [l]'arrêté du directeur ayant pris effet le 6 septembre 2011 » (d.a., vol. II, p. 3). Résolu a obtenu l'autorisation d'intervenir à titre de partie à l'instance.

A. *La décision de la Cour supérieure de justice de l'Ontario, 2016 ONSC 4652, 60 B.L.R. (5th) 237*

[64] Les parties ont présenté diverses requêtes en jugement sommaire à la Cour supérieure de justice de l'Ontario. La question en litige était de savoir si l'Indemnité de l'Ontario couvrait les frais engagés pour se conformer à l'arrêté du directeur et, dans l'affirmative, si Weyerhaeuser et Résolu avaient le droit d'en bénéficier.

[65] Le juge des requêtes a donné gain de cause à Weyerhaeuser et à Résolu, et a conclu que, comme le prévoit son premier paragraphe, l'Indemnité de l'Ontario s'appliquait aux ordonnances réglementaires de première partie. Il a ajouté que l'Indemnité de l'Ontario n'entravait pas indûment les pouvoirs de légiférer de la législature ontarienne.

[66] Le juge des requêtes a également conclu que la clause d'extension des bénéfices faisait en sorte que les droits et obligations conférés par l'Indemnité de l'Ontario s'étendaient à Résolu et à Weyerhaeuser — Résolu à titre de successeur corporatif de Great Lakes

to the Dryden Property and an assignee of the Ontario Indemnity from Bowater pursuant to s. 3.1(xiv) of the 1998 Asset Purchase Agreement.

B. *Decision of the Court of Appeal, 2017 ONCA 1007, 77 B.L.R. (5th) 175*

[67] The Province appealed, arguing the motion judge erred in holding that the Ontario Indemnity covers the costs of complying with the Director's Order, and that Weyerhaeuser and Resolute enjoyed the benefit of indemnification thereunder.

[68] At the Court of Appeal, the majority found no error in the motion judge's finding that the Ontario Indemnity covered the costs of complying with first party claims, including the Director's Order. Nor did the majority disturb the finding that the 1998 Asset Purchase Agreement had the effect of transferring the full benefit of the Ontario Indemnity from Bowater to Weyerhaeuser. Given that Weyerhaeuser had subsequently sold the Dryden pulp mill to Domtar in 2007, however, the issue of what rights, if any, Weyerhaeuser possessed as an assignee of the Ontario Indemnity at the time the Director's Order was issued in 2011 was returned to the Ontario Superior Court of Justice for decision. The majority did, however, find palpable and overriding error in the motion judge's conclusion that Weyerhaeuser could claim the benefit of the enurement clause in the Ontario Indemnity, holding that this clause applies only to *corporate* successors.

[69] As to Resolute, the majority held that the motion judge erred in finding that Resolute could claim the benefit of the Ontario Indemnity as a corporate successor of Great Lakes, following the assignment of the Ontario Indemnity from Bowater to Weyerhaeuser under the 1998 Asset Purchase Agreement. The effect of this assignment was to extinguish Bowater's interest therein, such that Bowater could not then pass that interest on to Resolute as its corporate successor.

et Weyerhaeuser à titre de successeur en titre quant à la propriété de Dryden et de cessionnaire de l'Indemnité de l'Ontario de Bowater en vertu de l'art. 3.1(xiv) de la convention d'achat d'actifs de 1998.

B. *La décision de la Cour d'appel, 2017 ONCA 1007, 77 B.L.R. (5th) 175*

[67] La province a interjeté appel, soutenant que le juge des requêtes avait commis une erreur en concluant que l'Indemnité de l'Ontario couvrait les frais pour se conformer à l'arrêté du directeur, et que Weyerhaeuser et Résolu jouissaient du bénéfice de l'indemnisation qu'elle prévoyait.

[68] Les juges majoritaires de la Cour d'appel n'ont relevé aucune erreur dans la conclusion du juge des requêtes selon laquelle l'Indemnité de l'Ontario couvrait les frais engagés pour donner suite aux réclamations de première partie, y compris l'arrêté du directeur. Ils n'ont pas non plus modifié la conclusion selon laquelle la convention d'achat d'actifs de 1998 avait pour effet de transférer de Bowater à Weyerhaeuser le plein bénéfice de l'Indemnité de l'Ontario. Cependant, comme Weyerhaeuser avait vendu l'usine de pâtes et papiers de Dryden à Domtar en 2007, la question de savoir quels droits, s'il en est, détenait Weyerhaeuser à titre de cessionnaire de l'Indemnité de l'Ontario au moment où a été pris l'arrêté du directeur en 2011 a été renvoyée à la Cour supérieure de justice de l'Ontario pour décision. Les juges majoritaires ont toutefois relevé une erreur manifeste et déterminante dans la conclusion du juge des requêtes selon laquelle Weyerhaeuser pouvait se prévaloir de la clause d'extension des bénéfices prévue dans l'Indemnité de l'Ontario, affirmant que cette clause ne s'applique qu'aux successeurs *corporatifs*.

[69] Quant à Résolu, les juges majoritaires ont conclu que le juge des requêtes avait commis une erreur en statuant que Résolu pouvait réclamer l'Indemnité de l'Ontario à titre de successeur corporatif de Great Lakes après que Bowater eut cédé l'indemnité à Weyerhaeuser en vertu de la convention d'achat d'actifs de 1998. Cette cession a eu pour effet d'éteindre l'intérêt de Bowater dans l'indemnité de sorte que Bowater ne pouvait pas par la suite le transférer à Résolu à titre de successeur corporatif.

[70] In dissent, Laskin J.A. would have found that the Ontario Indemnity did not cover the Director's Order, because it was not intended to cover first party claims, and because the Director's Order does not constitute a "Pollution Claim" as defined in that document. Having so concluded, he found it unnecessary to address the question of whether Resolute and Weyerhaeuser (or either of them) could benefit from the Ontario Indemnity as successors and assignees.

IV. Issues and Positions of the Parties

[71] The Province, Resolute and Weyerhaeuser each appeal to this Court. Although they raise various interrelated issues, these appeals can be resolved by answering the following two questions:

1. Did the motion judge err in concluding that the Ontario Indemnity covers the costs of complying with the Director's Order?

2. Did the motion judge err in concluding that Resolute and Weyerhaeuser benefit from the Ontario Indemnity as successors and assigns of Great Lakes?

[72] The Province argues that the motion judge erred in both these respects and, further, that his interpretation of the Ontario Indemnity has the effect of impermissibly fettering the Ontario Legislature's law-making power. Resolute and Weyerhaeuser seek to uphold the motion judge on both questions, and further argue that the Province's obligation under the Ontario Indemnity does not impose an impermissible fetter upon the Ontario Legislature.

V. Analysis

A. *Principles of Contractual Interpretation*

[73] The Ontario Indemnity is a contract. Today's lawyers are fortunate to live in "an age when there is a galaxy of high appellate guidance on how to interpret contracts" (*Royal Devon and Exeter NHS Foundation*

[70] Dissident, le juge Laskin aurait conclu que l'Indemnité de l'Ontario ne s'appliquait pas à l'arrêté du directeur parce qu'elle ne devait pas viser les réclamations de première partie et que l'arrêté du directeur ne constituait pas une [TRADUCTION] « réclamation pour pollution » au sens de ce document. Vu cette conclusion, il a estimé inutile de trancher la question de savoir si Résolu et Weyerhaeuser (ou l'une d'entre elles) pouvaient bénéficier de l'Indemnité de l'Ontario à titre de successeurs et ayants droit.

IV. Questions en litige et positions des parties

[71] La province, Résolu et Weyerhaeuser se pourvoient toutes les trois en appel devant la Cour. Bien qu'elles soulèvent diverses questions interreliées, il est possible de trancher les présents pourvois en répondant aux deux questions suivantes :

1. Le juge des requêtes a-t-il commis une erreur en concluant que l'Indemnité de l'Ontario couvrait les frais engagés pour se conformer à l'arrêté du directeur?

2. Le juge des requêtes a-t-il commis une erreur en concluant que Résolu et Weyerhaeuser bénéficiaient de l'Indemnité de l'Ontario à titre de successeurs et ayants droit de Great Lakes?

[72] La province soutient que le juge des requêtes a commis une erreur à ces deux égards et que son interprétation de l'Indemnité de l'Ontario a pour effet d'entraver de manière inacceptable le pouvoir de légiférer de la législature ontarienne. Résolu et Weyerhaeuser demandent pour leur part que la décision du juge des requêtes soit confirmée sur ces deux questions. Elles font également valoir que l'obligation qu'a la province en vertu de l'Indemnité de l'Ontario n'impose aucune entrave inacceptable à la législature ontarienne.

V. Analyse

A. *Les principes d'interprétation contractuelle*

[73] L'Indemnité de l'Ontario est un contrat. Les avocats d'aujourd'hui ont de la chance de vivre à [TRADUCTION] « une époque où il existe une multitude de directives formulées par les tribunaux d'appel

Trust v. ATOS IT Services UK Ltd., [2017] EWCA Civ 2196, [2018] 2 All E.R. (Comm.) 535, at para. 45). While not wishing to add more gas and dark matter to the "galaxy", we do find it helpful here to stress certain first principles which we see as important in interpreting this particular contract.

[74] This Court has described the object of contractual interpretation as being to ascertain the objective intentions of the parties (*Sattva*, at para. 55). It has also described the object of contractual interpretation as discerning the parties' "reasonable expectations with respect to the meaning of a contractual provision" (*Ledcor*, at para. 65). In meeting these objects, the Court has signalled a shift away from an approach to contractual interpretation that is "dominated by technical rules of construction" to one that is instead rooted in "practical[ities and] common-sense" (*Sattva*, at para. 47). This requires courts to read a contract "as a whole, giving the words used their ordinary and grammatical meaning, consistent with the surrounding circumstances known to the parties at the time of formation of the contract" (*ibid.*).

[75] We recognize that this Court's references to the *objective intentions* of the parties at the time they entered into the contract, and to parties' *reasonable expectations*, may leave a degree of uncertainty respecting the objects of contractual interpretation (see A. Swan, J. Adamski and A. Y. Na, *Canadian Contract Law* (4th ed. 2018), at pp. 673-916). Since there is no suggestion here of a divergence between the parties' *intentions* and their *expectations*, we do not find it necessary to resolve this here, but we simply note the inconsistency.

[76] Contractual interpretation begins with reading the words of the contract. A legitimate interpretation will be consistent with the language that the parties employed to express their agreement (G. R. Hall, *Canadian Contractual Interpretation Law* (3rd ed. 2016), at p. 11). As this Court stated in *Sattva*, the meaning of a contract is rooted in the actual language used by the parties (para. 57). A

supérieurs sur la manière d'interpréter des contrats » (*Royal Devon and Exeter NHS Foundation Trust c. ATOS IT Services UK Ltd.*, [2017] EWCA Civ 2196, [2018] 2 All E.R. (Comm.) 535, par. 45). Sans vouloir ajouter à cette multitude de directives, nous estimons utile de souligner certains principes fondamentaux que nous jugeons importants pour l'interprétation du contrat dont il est question en l'espèce.

[74] Notre Cour a affirmé que l'objectif de l'interprétation contractuelle était de déterminer les intentions objectives des parties (*Sattva*, par. 55). Elle a aussi dit que cet objectif était de cerner les « attentes raisonnables des parties en ce qui concerne la signification d'une disposition contractuelle » (*Ledcor*, par. 65). Elle a signalé que, pour satisfaire à ces objectifs, les tribunaux avaient tendance à délaisser l'approche axée « sur des règles de forme en matière d'interprétation » et à appliquer une démarche fondée plutôt sur des « [considérations] pratique[s] [et] sur le bon sens » (*Sattva*, par. 47). Cela les oblige à interpréter le contrat « dans son ensemble, en donnant aux mots y figurant le sens ordinaire et grammatical qui s'harmonise avec les circonstances dont les parties avaient connaissance au moment de la conclusion du contrat » (*ibid.*).

[75] Nous reconnaissons qu'en parlant des *intentions objectives* des parties au moment de conclure le contrat et des *attentes raisonnables* des parties, la Cour peut avoir laissé planer une certaine incertitude quant aux objectifs de l'interprétation contractuelle (voir A. Swan, J. Adamski et A. Y. Na, *Canadian Contract Law* (4e éd. 2018), p. 673-916). Comme rien ne tend ici à indiquer qu'il y a une divergence entre les *intentions* et les *attentes* des parties, nous ne croyons pas qu'il soit nécessaire de régler cette question en l'espèce; nous soulignons simplement l'incohérence.

[76] L'interprétation contractuelle commence par la lecture des mots du contrat; une interprétation légitime sera compatible avec les termes employés par les parties pour exprimer leur accord (G. R. Hall, *Canadian Contractual Interpretation Law* (3e éd. 2016), p. 11). Comme la Cour l'a affirmé dans l'arrêt *Sattva*, la signification d'un contrat est fondée sur les termes mêmes utilisés par les parties (par. 57).

meaning that strays too far from the actual words fails to give effect to the way in which the parties chose to define their obligations (*Canadian Contractual Interpretation Law*, at p. 9).

[77] This is not to say that the words of the contract are to be read in isolation. This Court's direction in *Sattva* was that the words of the contract are to be read in light of the surrounding circumstances — sometimes referred to as the "factual matrix" — which consist of "objective evidence of the background facts at the time of the execution of the contract, that is, knowledge that was or reasonably ought to have been within the knowledge of both parties at or before the date of contracting" (para. 58 (citation omitted)). An interpretation that ignores the context in which the contract was formed will not accurately discern what the parties intended to achieve, even if the interpretation is "literally correct" (*Canadian Contractual Interpretation Law*, at p. 9; see also *Sattva*, at para. 57). Put simply, contractual text derives its meaning, in part, from the context.

[78] We stress that text derives its meaning from context *in part*. This leads to an important caveat: the context — that is, the factual matrix — cannot "overwhelm the words" of the contract or support an interpretation that "deviate[s] from the text such that the court effectively creates a new agreement" (*Sattva*, at para. 57). The factual matrix assists in *discerning the meaning* of the words that the parties chose to express their agreement; it is not a means by which to *change* the words of the contract in a manner that would modify the rights and obligations that the parties assumed thereunder (*Canadian Contractual Interpretation Law*, at pp. 33-34).

[79] As we will explain below, contractual interpretation also requires courts to consider the principle of commercial reasonableness and efficacy. Contracts ought therefore to be interpreted "in accordance with sound commercial principles and good business sense" (*Scanlon v. Castlepoint Development Corp.* (1992), 11 O.R. (3d) 744, at p. 770). As Lord Diplock explained in *Antaios Compania Naviera S.A. v. Salen Rederierna A.B.*, [1985] 1 A.C. 191 (H.L.), at p. 201, "if detailed semantic and syntactical analysis

Une interprétation qui s'écarte trop de ces termes ne donne pas effet à la façon dont les parties ont choisi de définir leurs obligations (*Canadian Contractual Interpretation Law*, p. 9).

[77] Cela ne veut pas dire que les mots employés dans le contrat doivent être lus isolément. La Cour a indiqué dans l'arrêt *Sattva* que les mots du contrat doivent être lus en tenant compte des circonstances — que l'on appelle parfois le « fondement factuel » — qui consistent en une « preuve objective du contexte factuel au moment de la signature du contrat, c'est-à-dire, les renseignements qui appartenaient ou auraient raisonnablement dû appartenir aux connaissances des deux parties à la date de signature ou avant celle-ci » (par. 58 (référence omise)). Une interprétation qui ne tient pas compte du contexte dans lequel le contrat a été conclu ne permettra pas de cerner les intentions des parties, même si l'interprétation est [TRADUCTION] « littéralement correcte » (*Canadian Contractual Interpretation Law*, p. 9; voir aussi *Sattva*, par. 57). En termes simples, le texte du contrat tire sa signification, en partie, du contexte.

[78] Nous tenons à souligner que le texte tire sa signification *en partie* du contexte. Une mise en garde importante s'impose donc : le contexte — c'est-à-dire le fondement factuel — ne peut pas « supplanter [les termes] » du contrat ou appuyer une interprétation qui « s'écarte [du texte] au point de créer dans les faits une nouvelle entente » (*Sattva*, par. 57). Le fondement factuel aide à *dégager le sens* des mots que les parties ont choisi d'employer pour exprimer leur accord; ce n'est pas un moyen pour *changer* les termes du contrat de manière à modifier les droits et les obligations des parties (*Canadian Contractual Interpretation Law*, p. 33-34).

[79] Comme nous l'expliquerons plus loin, l'interprétation contractuelle requiert aussi que les tribunaux tiennent compte du principe de la raisonnabilité et de l'efficacité commerciales. Les contrats doivent donc être interprétés [TRADUCTION] « conformément aux principes commerciaux reconnus et au bon sens en matière commerciale » (*Scanlon c. Castlepoint Development Corp.* (1992), 11 O.R. (3d) 744, p. 770). Comme l'a expliqué lord Diplock dans l'arrêt *Antaios Compania Naviera S.A. c. Salen Rederierna A.B.*,

of words in a commercial contract is going to lead to a conclusion that flouts business commonsense, it must be made to yield to business commonsense". The principle that requires contracts to be read in a commercially reasonable and efficient manner is therefore an important interpretive aid in construing contractual terms.

[80] Ultimately, contractual interpretation involves the application of various tools — including consideration of the factual matrix and the principle of commercial reasonableness — in order to properly understand the meaning of the words used by the parties to express their agreement.

B. *The Province's Appeal*

[81] At issue in the Province's appeal is whether the motion judge erred in concluding that the Province's obligation to indemnify under para. 1 of the Ontario Indemnity extends to the costs of compliance with first party regulatory orders, such as the Director's Order. In so finding, the motion judge placed considerable emphasis on the text of para. 1, which referred to "any claim, action or proceeding, whether statutory or otherwise . . . whether by individuals, firms, companies, governments (including the Federal Government of Canada and any province or municipality thereof or any agency, body or authority created by statutory or other authority)" (A.R., vol. IV, at p. 189 (emphasis added)). In his view, neither a reading of the contract as a whole nor the surrounding circumstances supported reading the Ontario Indemnity as excluding from coverage the costs of compliance with first party regulatory orders.

[82] The Province sees it differently. It says that para. 1, properly interpreted, covers only "third party claims, whether statutory or at common law, in the nature of those settled in 1985" (Ontario A.F., at para. 3). Because the Director's Order was made in 2011 by the Province's Ministry of the Environment using provisions of the 1990 *Environmental*

[1985] 1 A.C. 191 (H.L.), à la p. 201, [TRADUCTION] « si l'analyse sémantique et syntaxique détaillée de mots contenus dans un contrat commercial mène à une conclusion qui va à l'encontre du bon sens en matière commerciale, c'est le bon sens en matière commerciale qui l'emporte ». Le principe selon lequel les contrats doivent être lus de manière commercialement raisonnable et efficace est donc important dans l'interprétation des modalités d'un contrat.

[80] En définitive, l'interprétation contractuelle implique l'application de divers outils — y compris un examen du fondement factuel et du principe de la raisonnabilité commerciale — pour bien comprendre la signification des mots employés par les parties pour exprimer leur accord.

B. *Le pourvoi de la province*

[81] La question en litige dans le pourvoi de la province est celle de savoir si le juge des requêtes a commis une erreur en concluant que l'obligation qu'avait la province de verser une indemnité en vertu du par. 1 de l'Indemnité de l'Ontario s'étendait aux frais engagés pour se conformer aux ordonnances réglementaires de première partie, comme l'arrêté du directeur. En arrivant à cette conclusion, le juge a accordé une importance considérable au texte du par. 1, où il est question de [TRADUCTION] « toute réclamation, action ou procédure, qu'elle soit prévue par la loi ou autrement, [. . .] par des particuliers, des firmes, des sociétés, des gouvernements (y compris le gouvernement fédéral du Canada et toute province ou municipalité du Canada, ou tout organisme ou autorité créé en vertu d'un pouvoir statutaire ou d'un autre pouvoir) » (d.a., vol. IV, p. 189 (nous soulignons)). À son avis, ni la lecture du contrat dans son ensemble ni les circonstances ne permettaient de considérer que l'Indemnité de l'Ontario excluait les frais engagés pour se conformer aux ordonnances réglementaires de première partie.

[82] La province voit les choses différemment. Elle affirme que, correctement interprété, le par. 1 vise seulement [TRADUCTION] « les réclamations de tiers, prévues par la loi ou par la common law, de la nature de celles réglées en 1985 » (m.a. Ontario, par. 3). Comme l'arrêté du directeur a été pris en 2011 par le ministère provincial de l'Environnement

Protection Act, which was enacted five years after the Settlement Agreement was executed, the Province says that the obligation to indemnify does not extend to the resulting compliance costs to Weyerhaeuser and Resolute.

[83] More specifically, the Province says the motion judge made four errors: (1) failing to consider the text of the Ontario Indemnity with reference to the factual matrix, which, the Province says, includes the 1979 Indemnity, the 1982 Ramsay Letter, the 1979 Dryden Agreement, the Settlement Agreement, and the Spills Bill; (2) failing to interpret para. 1 of the Ontario Indemnity in light of the remainder of the Ontario Indemnity; (3) making palpable and overriding errors in two factual findings; and (4) interpreting the Ontario Indemnity so as to impermissibly fetter the Legislature's law-making powers, thereby rendering the Ontario Indemnity altogether unenforceable.

[84] Like the majority at the Court of Appeal, we reject each of these arguments, and would dismiss the Province's appeal. The motion judge made no error in interpreting the Ontario Indemnity as covering the costs imposed on the successors and assigns of Great Lakes by the Director's Order. Although his analysis on this point was rooted primarily in the wording of para. 1 of the Ontario Indemnity, the motion judge also considered para. 1's meaning in light of the agreement as a whole, and with reference to the circumstances surrounding its formation in 1985. Far from excluding the context of the agreement as a whole or the surrounding circumstances from consideration, he *considered* them, and then simply found that neither supported an interpretation of the Ontario Indemnity that would exclude coverage for first party claims.

(1) Did the Motion Judge Err in His Appreciation of the Factual Matrix?

[85] The Province submits that the motion judge erred by focusing on the text of the Ontario Indemnity

en vertu de dispositions de la *Loi sur la protection de l'environnement* de 1990, laquelle a été édictée cinq ans après la signature de la Convention de règlement, la province estime que l'obligation d'indemniser ne s'étend pas aux frais engagés par Weyerhaeuser et Résolu pour s'y conformer.

[83] Plus précisément, la province affirme que le juge des requêtes a commis quatre erreurs : (1) il n'a pas examiné le libellé de l'Indemnité de l'Ontario à la lumière du fondement factuel, qui, selon la province, comprend l'Indemnité de 1979, la lettre de 1982 de Ramsay, la convention de Dryden de 1979, la Convention de règlement et la loi sur les déversements; (2) il n'a pas interprété le par. 1 de l'Indemnité de l'Ontario à la lumière du reste de cette indemnité; (3) il a commis des erreurs manifestes et déterminantes dans deux conclusions de fait; et (4) il a interprété l'Indemnité de l'Ontario de manière à entraver de manière inacceptable les pouvoirs de légiférer de la législature, de sorte que l'Indemnité de l'Ontario est devenue complètement non exécutoire.

[84] À l'instar des juges majoritaires de la Cour d'appel, nous rejetons chacun de ces arguments et nous rejetterions le pourvoi de la province. Le juge des requêtes n'a commis aucune erreur en interprétant l'Indemnité de l'Ontario comme couvrant les frais que l'arrêté du directeur a imposés aux successeurs et ayants droit de Great Lakes. Bien que son analyse sur ce point ait reposé principalement sur le libellé du par. 1 de l'Indemnité de l'Ontario, le juge s'est aussi penché sur la signification de cette disposition à la lumière de l'entente dans son ensemble et des circonstances ayant entouré sa conclusion en 1985. Loin d'avoir exclu de son examen le contexte de l'entente dans son ensemble ou les circonstances entourant celle-ci, il en a *tenu compte* et il est tout simplement arrivé à la conclusion que ni l'une ni l'autre de ces considérations n'étayait une interprétation de l'Indemnité de l'Ontario qui exclurait les réclamations de première partie.

(1) Le juge des requêtes a-t-il commis une erreur dans son appréciation du fondement factuel?

[85] La province soutient que le juge des requêtes a commis une erreur en mettant l'accent sur le texte

and that, in so doing, he "failed to appreciate that events going back to 1979 significantly informed the meaning of the [Ontario] Indemnity" (Ontario A.F., at para. 71). He ought, the Province says, to have considered the interrelationship between the Ontario Indemnity and the 1979 Indemnity, the 1982 Ramsay Letter, the 1979 Dryden Agreement, the Settlement Agreement (inclusive of an escrow agreement and schedules), and the enactment of the Spills Bill.

[86] The motion judge's appreciation of the factual matrix in these circumstances is entitled to deference on appeal (*Sattva*, at para. 52). The Province bears the burden of showing that any error in this respect is of a palpable and overriding nature.

(a) *The 1979 Indemnity and the 1982 Ramsay Letter*

[87] The Province notes that the 1979 Indemnity, which can only be invoked in the case of a court decision requiring the payment of monies or a settlement approved by the Province, and the 1982 Ramsay Letter which contains similar terms, both evidence an intention, on its part, to indemnify only third party claims. A proper consideration of these elements of the factual matrix, it says, should have led the motion judge to find that the Ontario Indemnity likewise extends only to costs associated with third party obligations arising from court orders or settlements in respect of mercury contamination claims, and does not cover the costs of compliance with first party regulatory orders.

[88] Although he did not specifically refer to the 1982 Ramsay Letter in his analysis, the motion judge did reject any comparison between the Ontario Indemnity and the 1979 Indemnity on the basis that the former "is a separate agreement and must be interpreted by considering the words used by the parties in it, not a previous agreement" (para. 48). We see no error in this holding. While it is true that the three

de l'Indemnité de l'Ontario et que, ce faisant, il [TRADUCTION] « ne s'est pas rendu compte que des événements remontant à 1979 éclairaient considérablement le sens de l'indemnité [de l'Ontario] » (m.a. Ontario, par. 71). Selon elle, le juge aurait dû prendre en considération la corrélation entre, d'une part, l'Indemnité de l'Ontario et, d'autre part, l'Indemnité de 1979, la lettre de 1982 de Ramsay, la convention de Dryden de 1979, la Convention de règlement (y compris un contrat d'entiercement et des annexes) et l'adoption de la loi sur les déversements.

[86] L'appréciation que le juge des requêtes a faite du fondement factuel dans les circonstances de l'espèce commande la déférence en appel (*Sattva*, par. 52). Il incombe à la province de prouver que toute erreur commise à cet égard est une erreur de nature manifeste et déterminante.

a) *L'Indemnité de 1979 et la lettre de 1982 de Ramsay*

[87] La province souligne que l'Indemnité de 1979, qui ne peut être invoquée que si une décision judiciaire exige le paiement d'une somme d'argent ou si un règlement est approuvé par la province, et la lettre de 1982 de Ramsay, qui est rédigée en termes semblables, démontrent toutes deux qu'elle avait l'intention d'accorder une indemnité seulement pour les réclamations de tiers. Elle fait valoir qu'une prise en compte adéquate de ces éléments du fondement factuel aurait dû amener le juge des requêtes à conclure que l'Indemnité de l'Ontario ne s'étend de la même manière qu'aux frais associés aux obligations qu'ont les tiers en vertu d'ordonnances judiciaires ou de règlements de réclamations relatives à la contamination par le mercure et ne couvre pas les frais engagés pour se conformer aux ordonnances réglementaires de première partie.

[88] Bien qu'il n'ait pas fait précisément référence à la lettre de 1982 de Ramsay dans son analyse, le juge des requêtes a rejeté toute comparaison entre l'Indemnité de l'Ontario et l'Indemnité de 1979 au motif que la première [TRADUCTION] « est une entente distincte que l'on doit interpréter en tenant compte des mots employés par les parties à celle-ci et non d'une entente intervenue antérieurement »

indemnities address the same underlying problem (the mercury contamination), our colleagues in the majority do not recognize that they each represent *distinct* agreements given for *distinct* purposes in *distinct* sets of negotiations. Specifically, the 1979 Indemnity was given to encourage Great Lakes to purchase the Dryden Property; the indemnity in the 1982 Ramsay Letter was given to encourage Great Lakes to settle the Grassy Narrows Litigation; and the Ontario Indemnity was given as part of a final settlement of those claims.

[89] Significantly, the Ontario Indemnity — unlike the 1979 Indemnity or the 1982 Ramsay Letter — captures much more than just court orders and settlements relating to the Reed-era mercury contamination, applying to "any obligation, liability, damage, loss, costs or expenses incurred . . . as a result of any claim, action or proceeding, whether statutory or otherwise" (A.R., vol. IV, at p. 189). This breadth of scope, relative to the other indemnities, is significant to the interpretive exercise.

[90] Additionally, the fact that the parties replaced the 1979 Indemnity and the commitment in the 1982 Ramsay Letter with the Ontario Indemnity suggests that the parties *themselves* — whose intentions the motion judge was called upon to discern — did not view those earlier agreements as being co-extensive in scope with the Ontario Indemnity. Tellingly, there would have been no point served by Great Lakes and Reed releasing the Province of its obligations under the 1979 Indemnity and the 1982 Ramsay Letter in Schedule E of the Settlement Agreement, only then to bind the Province to the same terms by executing the Ontario Indemnity at Schedule F of that same agreement.

[91] We therefore see no palpable and overriding error in the motion judge's refusal to restrict the

(par. 48). Nous ne relevons aucune erreur dans cette conclusion. S'il est vrai que les trois indemnités visent à corriger le même problème sous-jacent (la contamination par le mercure), nos collègues de la majorité ne reconnaissent pas qu'il s'agit d'ententes *distinctes* conclues à des fins *distinctes* dans le cadre de négociations *distinctes*. Plus précisément, l'Indemnité de 1979 a été accordée pour inciter Great Lakes à acheter la propriété de Dryden, l'indemnité dont il est question dans la lettre de 1982 de Ramsay a été versée pour encourager Great Lakes à régler le litige de Grassy Narrows et l'Indemnité de l'Ontario a été accordée dans le cadre du règlement définitif de ces réclamations.

[89] Fait important, l'Indemnité de l'Ontario — contrairement à l'Indemnité de 1979 ou à la lettre de 1982 de Ramsay — englobe bien plus que les ordonnances judiciaires et les règlements relatifs à la contamination par le mercure remontant à l'époque de Reed; elle s'applique à [TRADUCTION] « l'ensemble des obligations, responsabilités, dommages, pertes, frais ou dépenses qu'est susceptible d'entraîner [. . .] toute réclamation, action ou procédure, qu'elle soit prévue par la loi ou autrement » (d.a., vol. IV, p. 189). Le champ d'application de cette indemnité, par rapport à celui des autres indemnités, est significatif pour l'exercice d'interprétation.

[90] En outre, le fait que les parties aient remplacé l'Indemnité de 1979 et l'engagement pris dans la lettre de 1982 de Ramsay par l'Indemnité de l'Ontario tend à indiquer que les parties *elles-mêmes* — dont le juge des requêtes devait cerner les intentions — ne considéraient pas que les ententes antérieures avaient le même champ d'application que l'Indemnité de l'Ontario. De toute évidence, il n'aurait servi à rien que Great Lakes et Reed libèrent la province des obligations qui lui incombaient en vertu de l'Indemnité de 1979 et de la lettre de 1982 de Ramsay figurant à l'annexe E de la Convention de règlement pour ensuite imposer à la province les mêmes conditions en signant l'Indemnité de l'Ontario contenue à l'annexe F de la même convention.

[91] Nous concluons donc que le juge des requêtes n'a commis aucune erreur manifeste et déterminante

scope of the Ontario Indemnity on the basis of the prior indemnities.

(b) *The 1979 Dryden Agreement*

[92] The scope of the Ontario Indemnity is substantially the same as the scope of the indemnity given to Reed by Great Lakes in clause 5.3 of the 1979 Dryden Agreement as part of its cost-sharing regime. As we have already explained, clause 11.4 of that agreement exempted the costs of complying with the Control Order issued by the Ministry of the Environment in 1979, making those costs the responsibility of Great Lakes exclusively. The motion judge found that the existence of this "specific provision that excluded the cost of regulatory compliance supports the conclusion that the Ontario Indemnity includes these costs because it does not contain a similar provision" (para. 48 (emphasis added)).[1]

[93] Before this Court, the Province observes that the 1979 Dryden Agreement "was a private contractual arrangement made between Reed and Great Lakes", such that the absence of any specific exemption in the Ontario Indemnity does not mean that the Province intended to cover regulatory costs (Ontario A.F., at para. 83). While it is true that the Province was not a party to the 1979 Dryden Agreement, it was aware of its terms when it agreed to the Ontario Indemnity (as para. 7 of the Ontario Indemnity makes clear). Moreover, the text used in the indemnity in clause 5.3 of the 1979 Dryden Agreement is almost identical to that used in para. 1 of the Ontario Indemnity. Given the term exempting the Control Order from the scope of the cost-sharing regime in the 1979 Dryden Agreement, the parties must have understood that this regulatory order would otherwise have constituted a "Pollution Claim" for

[1] The motion judge stated that the 1979 Indemnity contained that "specific provision", but given the context, it is clear that he misspoke and was instead referring to the 1979 Dryden Agreement. The Province does not take the position that this amounts to a palpable and overriding error of fact (Ontario A.F., at paras. 81-83).

en refusant de restreindre le champ d'application de l'Indemnité de l'Ontario sur le fondement des indemnités antérieures.

b) *La convention de Dryden de 1979*

[92] Le champ d'application de l'Indemnité de l'Ontario est essentiellement le même que celui de l'indemnité que Great Lakes a accordée à Reed à la clause 5.3 de la convention de Dryden de 1979 dans le cadre de son régime de partage des frais. Comme nous l'avons déjà expliqué, la clause 11.4 de cette convention soustrayait les frais engagés pour se conformer à l'arrêté d'intervention pris par le ministère de l'Environnement en 1979, et laissait à Great Lakes l'entière responsabilité de ces frais. Le juge des requêtes a conclu que l'existence de cette [TRADUCTION] « disposition particulière qui excluait les frais engagés pour se conformer à la réglementation étaye la conclusion selon laquelle l'Indemnité de l'Ontario englobe ces frais parce qu'elle ne renferme pas de disposition semblable » (par. 48 (nous soulignons))[1].

[93] Devant notre Cour, la province fait remarquer que la convention de Dryden de 1979 [TRADUCTION] « était une entente contractuelle privée conclue entre Reed et Great Lakes », de sorte que l'absence d'une exemption particulière dans l'Indemnité de l'Ontario ne signifie pas que la province voulait couvrir les frais engagés pour se conformer à la réglementation (m.a. Ontario, par. 83). Bien qu'il soit vrai que la province n'était pas partie à la convention de Dryden de 1979, elle en connaissait les modalités quand elle a consenti à l'Indemnité de l'Ontario (comme il ressort clairement du par. 7 de l'Indemnité de l'Ontario). En outre, le texte de l'indemnité prévue à la clause 5.3 de la convention de Dryden de 1979 est presque identique à celui utilisé au par. 1 de l'Indemnité de l'Ontario. Vu qu'il existe une disposition soustrayant l'arrêté d'intervention du champ d'application du régime de partage des frais dans la convention de Dryden

[1] Le juge des requêtes a affirmé que l'Indemnité de 1979 renfermait cette [TRADUCTION] « disposition particulière », mais, vu le contexte, il est clair qu'il s'est mal exprimé et qu'il renvoyait plutôt à la convention de Dryden de 1979. La province ne prétend pas qu'il s'agit là d'une erreur de fait manifeste et déterminante (m.a. Ontario, par. 81-83).

the purpose of clause 5.3. And, because para. 1 of the Ontario Indemnity defines the term "Pollution Claim" in near-identical terms, the motion judge did not err in placing weight on the absence of a similar exemption in the Ontario Indemnity as supporting the conclusion that regulatory orders — like the Director's Order — would fall within the scope of that indemnity.

[94] In his dissenting reasons, Laskin J.A. says that "similar carve out language was not needed" in the Ontario Indemnity, since by 1985, neither Reed nor Great Lakes had any obligations under the Control Order (para. 256). But, and with respect, the parties must have been aware that a new regulatory order could easily have been made subsequent to the execution of the Ontario Indemnity. Nothing prevented them from expressly providing — as did the parties to the 1979 Dryden Agreement — that such orders would not fall within the scope of the indemnity.

(c) *The Settlement Agreement*

[95] Under paragraph 2.4(a) of the Settlement Agreement, the Province was to indemnify Reed and Great Lakes in respect of "the issues" — a term that was defined in the recitals to the Settlement Agreement as follows:

> The discharge by Reed and its predecessors of mercury and any other pollutants into the English and Wabigoon and related river systems, and the continuing presence of any such pollutants discharged by Reed and its predecessors, including the continuing but now diminishing presence of methylmercury in the related ecosystems since its initial identification in 1969, and governmental actions taken in consequence thereof, may have had and may continue to have effects and raise concerns in respect of the social and economic circumstances and the health of the present and future members of the Bands (the "issues"). [Emphasis added.]

(A.R., vol. IV, at p. 140)

de 1979, les parties devaient avoir compris que cette ordonnance réglementaire aurait autrement constitué une [TRADUCTION] « réclamation pour pollution » pour l'application de la clause 5.3. De plus, comme le par. 1 de l'Indemnité de l'Ontario définit l'expression « réclamation pour pollution » dans des termes quasi identiques, le juge des requêtes n'a commis aucune erreur en considérant que l'absence d'une exemption semblable dans l'Indemnité de l'Ontario étayait la conclusion que les ordonnances réglementaires — comme l'arrêté du directeur — étaient visées par cette indemnité.

[94] Dans ses motifs dissidents, le juge Laskin affirme qu'un [TRADUCTION] « libellé d'exclusion semblable n'était pas nécessaire » dans l'Indemnité de l'Ontario puisqu'en 1985, ni Reed ni Great Lakes n'avait d'obligation en vertu de l'arrêté d'intervention (par. 256). Cependant, avec égards, les parties devaient savoir qu'une nouvelle ordonnance réglementaire pouvait facilement être rendue après la signature de l'Indemnité de l'Ontario. Rien ne les empêchait de prévoir expressément — comme l'avaient fait les parties à la convention de Dryden de 1979 — que de telles ordonnances ne seraient pas visées par l'indemnité.

c) *La Convention de règlement*

[95] Aux termes du par. 2.4(a) de la Convention de règlement, la province était tenue d'indemniser Reed et Great Lakes relativement aux [TRADUCTION] « points en litige », expression qui était définie comme suit dans les attendus de la convention :

> [TRADUCTION] Le rejet par Reed et ses prédécesseurs de mercure et de tout autre polluant dans le réseau hydrographique English-Wabigoon, ainsi que la présence continue de ces polluants, ce qui inclut la présence continue mais en voie de diminution de mercure méthylé dans les écosystèmes connexes depuis qu'on a constaté sa présence en 1969, et les mesures gouvernementales prises à cet égard, peuvent avoir eu et continuer d'avoir des incidences en ce qui concerne la conjoncture économique et sociale ainsi que la santé des membres actuels et futurs des bandes en question (les « points en litige »). [Nous soulignons.]

(d.a., vol. IV, p. 140)

[96] The Province says the motion judge failed to appreciate the importance of these portions of the Settlement Agreement to the interpretation of para. 1 of the Ontario Indemnity. Preventative orders — like the Director's Order — do not fall within the scope of "the issues" that the Settlement Agreement was intended to address, the Province says, since the waste disposal site was not a source of the discharge. We note, however, that among those "issues" are "governmental actions taken in consequence" of the mercury contamination by Reed and its predecessors. The record provides ample indication that the Province was aware of Dryden Paper's construction of the waste disposal site for the purpose of containing mercury waste, and that it had been the subject of oversight by governmental agencies since 1977 (A.R., vol. IV, at pp. 35-36; A.R., vol. VI, at pp. 2-3). It follows that such oversight falls well within the scope of the "issues" which the Settlement Agreement was intended to address.

[97] In any event, the Ontario Indemnity expressly applies in respect of (among other things) the "presence of any pollutant . . . including mercury or any other substance . . . in the plant or plants or lands or premises forming part of the Dryden assets sold by Reed Ltd. to Great Lakes under the [1979] Dryden Agreement" (A.R., vol. IV, at p. 190). Irrespective, then, of how one understands the scope of the issues set out in the Settlement Agreement, that element of the factual matrix cannot "overwhelm" or be used to "deviate from" the text of the Ontario Indemnity (*Sattva*, at para. 57).

(d) *The Spills Bill*

[98] Paragraph 1 of the Ontario Indemnity closely tracks the language of the indemnity given by Great Lakes to Reed as part of the cost-sharing regime in clause 5.3 of the 1979 Dryden Agreement, with one important difference: while the scope of the former expressly covers claims, actions and proceedings, "whether statutory or otherwise", the latter does not. The Province explains this specific reference to statutory claims in the Ontario Indemnity as reflecting

[96] La province soutient que le juge des requêtes n'a pas bien compris l'importance de ces passages de la Convention de règlement pour l'interprétation du par. 1 de l'Indemnité de l'Ontario. Selon elle, les ordonnances préventives — comme l'arrêté du directeur — ne font pas partie des [TRADUCTION] « points en litige » que la Convention de règlement visait à régler puisque le lieu d'élimination des déchets n'était pas une source du rejet. Nous constatons toutefois que parmi ces « points en litige » se trouvent les « mesures gouvernementales prises à [l']égard » de la contamination par le mercure causée par Reed et ses prédécesseurs. Le dossier montre amplement que la province savait que Dryden Paper avait construit un lieu d'élimination des déchets qui était destiné à contenir les déchets mercuriels et qui était surveillé par des organismes gouvernementaux depuis 1977 (d.a., vol. IV, p. 35-36; d.a., vol. VI, p. 2-3). Il s'ensuit que cette surveillance fait entièrement partie des « points en litige » que la Convention de règlement visait à régler.

[97] Quoi qu'il en soit, l'Indemnité de l'Ontario s'applique expressément (entre autres) à la présence de « polluants, notamment le mercure ou toute autre substance, [. . .] [dans] [l]es usines, [l]es terrains ou [l]es lieux faisant partie des actifs de Dryden que Reed Ltd. a vendus à Great Lakes en vertu de la convention de Dryden [de 1979] » (d.a., vol. IV, p. 190). En conséquence, peu importe la compréhension que l'on peut avoir de la portée des points en litige énoncés dans la Convention de règlement, cet élément du fondement factuel ne saurait « supplanter » le texte de l'Indemnité de l'Ontario ou être utilisé pour « s'écarte[r] » de ce dernier (*Sattva*, par. 57).

d) *La loi sur les déversements*

[98] Le paragraphe 1 de l'Indemnité de l'Ontario suit de très près le libellé de l'indemnité que Great Lakes a accordée à Reed à la clause 5.3 de la convention de Dryden de 1979 dans le cadre du régime de partage des frais, mais il existe une différence importante entre ces deux indemnités : la première s'applique expressément aux réclamations, actions et procédures, [TRADUCTION] « qu'elle[s] soi[ent] prévue[s] par la loi ou autrement », mais

the enactment of the Spills Bill, which created a new statutory right of action against polluters in favour of both the government and private parties, and which was proclaimed only two weeks before the parties executed the Settlement Agreement and the Ontario Indemnity. This language, it says, "addressed a significant new statutory cause of action created by the Spills Bill, along with other third party statutory claims which could have been brought at that time" (Ontario A.F., at para. 88). The Province's submission is therefore that the courts below erred by construing those terms as capturing the costs of compliance with (a) first party regulatory claims made under statutory powers, and (b) other kinds of claims arising from legislation enacted *after* the closing date in 1985 — like the Director's Order, which was made under provisions of the *Environmental Protection Act* that came into force in 1990.

pas la deuxième. La province explique que ce renvoi exprès aux réclamations prévues par la loi dans l'Indemnité de l'Ontario reflète l'adoption de la loi sur les déversements, qui a créé en faveur du gouvernement et des particuliers un nouveau droit d'action statutaire contre les pollueurs, et qui a été promulguée seulement deux semaines avant que les parties signent la Convention de règlement et l'Indemnité de l'Ontario. Ce libellé, affirme-t-elle, [TRADUCTION] « traitait d'une nouvelle cause d'action statutaire importante créée par la loi sur les déversements ainsi que des autres réclamations statutaires qui auraient pu être présentées par des tiers à ce moment-là » (m.a. Ontario, par. 88). La province soutient donc que les tribunaux d'instance inférieure ont commis une erreur en considérant que les termes en question englobaient les frais engagés pour donner suite a) aux réclamations réglementaires de première partie présentées en vertu de pouvoirs conférés par la loi et b) aux autres types de réclamations découlant d'une loi adoptée *après* la date de clôture en 1985 — comme l'arrêté du directeur, qui a été pris en vertu des dispositions de la *Loi sur la protection de l'environnement* entrées en vigueur en 1990.

[99] The motion judge did not consider the Spills Bill. (Neither, for that matter, do our colleagues in the majority.) He did, however, rely on the text of para. 1 of the Ontario Indemnity in concluding that it applies to "a statutory claim or proceeding brought by an agency of the Province such as the [Director's Order] issued by the [Ministry of the Environment]" (para. 47). The majority at the Court of Appeal saw no error in this: "it was not open to the motion judge to consider evidence of the parties' specific intentions or negotiations, including whether they discussed the Spills Bill during the negotiations that culminated in the execution of the Ontario Indemnity" (para. 112). This, the majority explained, was rooted in the principle that evidence of the parties' specific negotiations is inadmissible for the purpose of contractual interpretation. Justice Laskin, however, instead characterized the enactment of the Spills Bill as an objective fact that the parties would have or reasonably ought to have known about when entering into their agreement, and concluded that "[t]he timing of the Spills Bill relative to the [Ontario] Indemnity demonstrates that

[99] Le juge des requêtes n'a pas tenu compte de la loi sur les déversements. (Nos collègues de la majorité ne l'ont d'ailleurs pas fait non plus.) Il s'est toutefois fondé sur le libellé du par. 1 de l'Indemnité de l'Ontario pour conclure qu'elle s'applique [TRADUCTION] « aux réclamations ou procédures prévues par la loi présentées par un organisme de la province, comme [l'arrêté du directeur] pris par le [ministère de l'Environnement] » (par. 47). Les juges majoritaires de la Cour d'appel n'ont relevé aucune erreur à cet égard : [TRADUCTION] « il n'appartenait pas au juge des requêtes de prendre en considération la preuve relative aux intentions particulières des parties ou aux négociations particulières intervenues entre elles, et notamment de se demander si elles ont parlé de la loi sur les déversements pendant les négociations qui ont mené à la signature de l'Indemnité de l'Ontario » (par. 112). Comme ils l'ont expliqué, cette approche repose sur le principe selon lequel la preuve relative aux négociations particulières menées par les parties est inadmissible aux fins de l'interprétation contractuelle. Cependant, le juge Laskin a plutôt qualifié l'adoption de la loi

the Spills Bil[l] was undoubtedly the reason why the [Ontario] Indemnity contained the added words relied on by the motion judge and the respondents" (para. 249).

[100] We note that the "general rule" that renders evidence of the parties' specific negotiations and subjective intentions inadmissible sits uneasily next to the rule that the circumstances surrounding the formation of the agreement inform contractual interpretation. As was noted in *Canadian Contract Law*:

> The difficulty in Canada in now giving content to or even acknowledging the continued existence of the rule stems from Rothstein J.'s statement in *Sattva Capital* that a court must look at the surrounding circumstances or "factual matrix". It seems very difficult to separate what happened during the negotiations from the "surrounding circumstances"; in fact and notwithstanding the decision of the House of Lords in *Chartbrook Ltd. v. Persimmon Homes Ltd.* [[2009] UKHL 38], it is hard to imagine where or how the line could be drawn. [Footnote omitted; p. 746.]

The majority of the Court of Appeal may have been alluding to this difficulty when it suggested that the rule may be in need of change "as a matter of policy" (para. 112). Although we recognize the uncertainty surrounding this point of law, we would leave its resolution for another day, where it is both necessary to the disposition of the appeal and more directly addressed by the courts below and the parties in their submissions.

[101] Even accepting that the proclamation of the Spills Bill in November 1985 is objective and admissible evidence of what the parties did or ought to have had in contemplation when entering into the

sur les déversements de fait objectif que les parties connaissaient ou auraient raisonnablement dû connaître au moment de conclure leur entente, et il a conclu que [TRADUCTION] « [l]e moment où la loi sur les déversements a été adoptée par rapport à celui où l'Indemnité [de l'Ontario] a été conclue démontre que cette loi est sans aucun doute la raison pour laquelle l'Indemnité [de l'Ontario] contenait les termes supplémentaires sur lesquels se sont appuyés le juge des requêtes et les intimées » (par. 249).

[100] Soulignons que la « règle générale » qui rend inadmissible la preuve relative aux négociations particulières intervenues entre les parties et aux intentions subjectives particulières de ces dernières s'accorde mal avec la règle selon laquelle les circonstances entourant la conclusion d'un contrat en guident l'interprétation. Comme il a été souligné dans *Canadian Contract Law* :

> [TRADUCTION] Au Canada, la difficulté à maintenant déterminer le contenu de la règle ou même à reconnaître le maintien de son existence découle de la déclaration du juge Rothstein dans l'arrêt *Sattva Capital* selon qui un tribunal doit tenir compte des circonstances ou du « fondement factuel ». Il semble très difficile de distinguer ce qui s'est passé lors des négociations des « circonstances »; en fait, et malgré l'arrêt de la Chambre des lords, *Chartbrook Ltd. c. Persimmon Homes Ltd.* [[2009] UKHL 38], il est difficile d'imaginer où ou encore comment tracer la ligne. [Note en bas de page omise; p. 746.]

Les juges majoritaires de la Cour d'appel faisaient peut-être allusion à cette difficulté lorsqu'ils ont laissé entendre que la règle pourrait devoir être modifiée [TRADUCTION] « pour des raisons de politique générale » (par. 112). Bien que nous soyons conscients de l'incertitude qui entoure cette question de droit, nous sommes d'avis d'en reporter la résolution à une autre occasion, lorsqu'il sera nécessaire de le faire pour trancher le pourvoi, et lorsque les juridictions inférieures se seront prononcées plus directement sur celle-ci et que les parties en auront traité plus directement dans leur argumentation.

[101] Même en acceptant que la promulgation de la loi sur les déversements en novembre 1985 soit une preuve objective et admissible de ce que les parties avaient envisagé ou auraient dû envisager au moment

Ontario Indemnity, it is a far leap from that premise to the conclusion that they would have understood "statutory or otherwise" to refer solely to claims brought under the Spills Bill, or "other third party statutory claims which could have been brought at that time" (Ontario A.F., at para. 88). This element of the factual matrix does not support the position that the indemnity excludes claims, actions or proceedings brought under legislation enacted following the execution of the Ontario Indemnity — particularly given that it is expressly said to cover those "existing at December 17, 1979 or which may arise or be asserted thereafter" (A.R., vol. IV, at p. 189 (emphasis added)).

[102] Moreover, the proposition that the enactment of the Spills Bill as a surrounding circumstance supports reading the Ontario Indemnity narrowly — as excluding the costs of first party claims — cannot be reconciled with the Spills Bill's creation of a right of action for private persons *and for the Province of Ontario*. On this point, s. 68*i*(2) of the Spills Bill states:

(2) Her Majesty in right of Ontario or in right of Canada or any other person has the right to compensation,

(*a*) for loss or damage incurred as a direct result of,

(i) the spill of a pollutant that causes or is likely to cause adverse effects,

(ii) the exercise of any authority under subsection 1 of section 68*j* or the carrying out of or attempting to carry out a duty imposed or an order or direction made under this Part, or

de conclure l'Indemnité de l'Ontario, il est difficile de conclure à partir de cette prémisse que les parties comprenaient que les mots [TRADUCTION] « prévue par la loi ou autrement » renvoyaient seulement aux réclamations présentées en vertu de la loi sur les déversements ou aux « autres réclamations statutaires qui auraient pu être présentées par des tiers à ce moment-là » (m.a. Ontario, par. 88). Cet élément du fondement factuel n'étaye pas la thèse selon laquelle l'indemnité exclut les réclamations, actions ou procédures présentées en vertu d'une loi adoptée après la signature de l'Indemnité de l'Ontario — surtout qu'il est expressément indiqué qu'elle vise les réclamations, actions ou procédures « qui existai[ent] au 17 décembre 1979 ou qui étai[ent] susceptible[s] de prendre naissance ou d'être présentée[s] par la suite » (d.a., vol. IV, p. 189 (nous soulignons)).

[102] De plus, la thèse selon laquelle l'adoption de la loi sur les déversements, à titre de circonstance, appuie une interprétation restreinte de l'Indemnité de l'Ontario — interprétation selon laquelle cette indemnité exclut les frais liés aux réclamations de première partie — n'est pas conciliable avec le fait que la loi sur les déversements crée un droit d'action en faveur des particuliers *et de la province de l'Ontario*. À cet égard, le par. 68*i*(2) de la loi sur les déversements prévoit ce qui suit :

[TRADUCTION]

(2) Sa Majesté du chef de l'Ontario ou du chef du Canada ou toute autre personne a le droit d'obtenir une indemnisation du propriétaire du polluant et de la personne qui exerce un contrôle sur le polluant :

a) en ce qui concerne une perte ou un dommage subis directement à la suite :

(i) du déversement d'un polluant qui a ou aura vraisemblablement des conséquences préjudiciables,

(ii) de l'exercice de tout pouvoir en vertu du paragraphe 1 de l'article 68*j* ou de l'exécution d'une obligation imposée, de l'application d'un arrêté pris, ou d'une directive donnée dans le cadre de la présente partie, ou de la tentative qui est faite à cette fin,

(iii) neglect or default in carrying out a duty imposed or an order or direction made under this Part;

(*b*) for all reasonable cost and expense incurred in respect of carrying out or attempting to carry out an order or direction under this Part,

from the owner of the pollutant and the person having control of the pollutant.

(iii) du défaut, notamment par négligence, d'exécuter une obligation imposée ou d'appliquer un arrêté pris ou une directive donnée dans le cadre de la présente partie;

b) en ce qui concerne les frais et les dépenses raisonnables engagés en vue de faire appliquer ou de tenter de faire appliquer un arrêté pris ou une directive donnée dans le cadre de la présente partie.

Indeed, if the parties had (or, at least, ought to have had) the Spills Bill in contemplation when executing the Ontario Indemnity, they would have known that it created first *and* third party liability.

En fait, si les parties avaient (ou, du moins, devaient avoir) envisagé la loi sur les déversements lorsqu'elles ont signé l'Indemnité de l'Ontario, elles auraient su qu'elle créait une responsabilité à l'égard des premières parties *et* des tiers.

[103] In a similar vein, the Province also advances the curious argument that first party claims should be excluded from the scope of the Ontario Indemnity because its reference to claims, actions and proceedings brought by any "province" does not include those brought by the Government of Ontario (Ontario A.F., at paras. 43 and 93). With respect, the notion that the parties would not have understood the reference to "any province" as including the province in which the Dryden Property is located, and which clearly has the constitutional authority to enact and pursue statutory claims in circumstances such as these, is simply absurd (see motion judge's reasons, at para. 48). Indeed, Ontario may be *the only "province"* to which this provision could apply since, in *Interprovincial Co-operatives Ltd. v. The Queen*, [1976] 1 S.C.R. 477, this Court held that Manitoba lacked the constitutional jurisdiction to enact and pursue a statutory claim against Dryden Chemicals in respect of the mercury contamination into the rivers.

[103] Dans le même ordre d'idées, la province avance aussi l'argument pour le moins étrange selon lequel les réclamations de première partie devraient être exclues du champ d'application de l'Indemnité de l'Ontario parce que les réclamations, actions et procédures présentées par [TRADUCTION] « toute province » auxquelles elle fait référence n'englobent pas celles présentées par le gouvernement de l'Ontario (m.a. Ontario, par. 43 et 93). Avec égards, l'idée selon laquelle les parties n'auraient pas saisi que les termes « toute province » incluaient la province dans laquelle la propriété de Dryden est située et qui a clairement le pouvoir constitutionnel d'édicter et de faire valoir des réclamations statutaires en pareilles circonstances est simplement absurde (voir motifs du juge des requêtes, par. 48). En effet, l'Ontario est peut-être *la seule « province »* à laquelle pourrait s'appliquer cette disposition puisque dans l'arrêt *Interprovincial Co-operatives Ltd. c. La Reine*, [1976] 1 R.C.S. 477, notre Cour a conclu que le Manitoba n'avait pas le pouvoir constitutionnel d'édicter et de faire valoir une réclamation statutaire contre Dryden Chemicals relativement à la contamination par le mercure des rivières.

[104] Finally, the suggestion that the scope of the indemnity excludes the costs of complying with first party regulatory orders is further undermined by its express application to claims, actions and proceedings

[104] Enfin, l'idée selon laquelle le champ d'application de l'indemnité exclut les frais engagés pour se conformer aux ordonnances réglementaires de première partie est affaiblie davantage par le fait

brought by "any agency, body or authority created by statutory or other authority" (A.R., vol. IV, at p. 189). The role of such agencies, bodies or authorities is to act under the authority of Ontario statutes or regulations by, in this case, issuing regulatory orders such as that at issue in this appeal.

[105] In light of the foregoing, we see no reversible error in the motion judge's consideration of the factual matrix, nor, therefore, in his interpretation of the Province's obligation under para. 1 of the Ontario Indemnity as extending to first party claims, including those brought under subsequently-enacted legislation.

(2) Did the Motion Judge Err in Failing to Read Paragraph 1 of the Ontario Indemnity in Light of the Agreement as a Whole?

[106] In support of its second argument, the Province submits that paras. 2 and 3 of the Ontario Indemnity, which give Ontario the right to take carriage of a pollution claim and oblige the companies to cooperate with Ontario in relation to a pollution claim, are typical of third party indemnities, such that it should be clear that the Ontario Indemnity was not meant to address first party claims as well. Those two provisions read as follows:

2. Upon the receipt of notice of any Pollution Claim directed to Great Lakes or Reed or any predecessor in title of Reed, Great Lakes or Reed or failing Reed, International, as the case may be, shall promptly notify Ontario in writing of receipt of such notice giving reasonable particulars thereof, and Ontario shall have the right to elect to either take carriage of the defence or to participate in the defence and/or settlement of the Pollution Claim and any proceeding relating thereto as Ontario deems appropriate.

. . .

que l'indemnité s'applique expressément aux réclamations, actions et procédures intentées par [TRADUCTION] « tout organisme ou autorité créé en vertu d'un pouvoir statutaire ou d'un autre pouvoir » (d.a., vol. IV, p. 189). Le rôle de tels organismes ou autorités est d'agir en vertu des lois ou des règlements de l'Ontario en rendant des ordonnances réglementaires comme celle en cause en l'espèce.

[105] Compte tenu de ce qui précède, nous ne voyons aucune erreur révisable dans l'examen que le juge des requêtes a fait du fondement factuel et nous n'en voyons donc aucune dans son interprétation de l'obligation qu'a la province en vertu du par. 1 de l'Indemnité de l'Ontario, interprétation selon laquelle cette indemnité s'étend aux réclamations de première partie, y compris celles présentées en vertu d'une loi adoptée subséquemment.

(2) Le juge des requêtes a-t-il commis une erreur en ne lisant pas le par. 1 de l'Indemnité de l'Ontario à la lumière de l'entente dans son ensemble?

[106] À l'appui de son deuxième argument, la province soutient que les par. 2 et 3 de l'Indemnité de l'Ontario, lesquels confèrent à l'Ontario le droit de prendre en charge une réclamation pour pollution et obligent les sociétés à collaborer avec cette province dans le contexte d'une réclamation pour pollution, sont typiques des indemnités de tiers, de sorte qu'il devrait être clair que l'Indemnité de l'Ontario n'était pas censée viser également les réclamations de première partie. Ces deux dispositions sont rédigées en ces termes :

[TRADUCTION]

2. Sur réception d'un avis de toute réclamation pour pollution adressé à Great Lakes, à Reed ou à tout prédécesseur en titre de Reed, Great Lakes, Reed, ou à défaut de Reed, International, selon le cas, avise rapidement, par écrit, l'Ontario de la réception de cet avis et en donne des détails raisonnables; l'Ontario a le droit de choisir d'assumer la défense ou de participer à la défense et/ou au règlement de la réclamation pour pollution et de toute procédure y afférente, selon ce qu'il estime approprié.

. . .

3. Where a Pollution Claim is brought against any of the companies referred to in paragraph 1 hereof, the said companies shall fully cooperate with Ontario in the investigation and defence and settlement of any such Pollution Claim and shall use their best efforts to obtain the cooperation of all personnel having any knowledge or information relevant to any such Pollution Claim and shall make available to Ontario all information . . . .

3. Lorsqu'une réclamation pour pollution est présentée contre l'une ou l'autre des sociétés dont il est question au paragraphe 1 des présentes, lesdites sociétés doivent pleinement collaborer avec l'Ontario à l'enquête, à la défense et au règlement de la réclamation. Elles doivent également mettre tout en œuvre pour obtenir la collaboration de tout le personnel ayant des connaissances ou des informations pertinentes relativement à la réclamation pour pollution et communiquer à l'Ontario tous les renseignements dont elles disposent . . .

[107] We agree with Laskin J.A. that these provisions "are meaningful only for third party claims" against the indemnified parties, and are "utterly meaningless" in the context of first party claims and orders, such as the Director's Order (para. 268). Nor did this escape the motion judge. Rather, he viewed the notification requirement in para. 2 as being "not inconsistent with the Province's obligation to indemnify Weyerhaeuser and Resolute for their costs of complying with the [Director's Order]" (para. 48). In other words, while para. 2 does not provide for first party indemnity, it did not exclude it either, and does not oust the language in para. 1 which clearly includes it. As Weyerhaeuser points out, "[t]he fact that some procedural provisions may be unnecessary or redundant in the case of certain types of claims does not mean that a [c]ourt should ignore clear language confirming that those claims are covered by the [Ontario] Indemnity" (Weyerhaeuser R.F. (Ontario Appeal), at para. 55). (This reasoning would also apply to para. 3, given its similarity to para. 2.) Again, we see no reversible error here.

[107] Nous convenons avec le juge Laskin que ces dispositions [TRADUCTION] « n'ont de sens qu'à l'égard des réclamations de tiers » présentées à l'encontre des parties indemnisées, et qu'elles sont « dénuées de tout sens » dans le contexte de réclamations et d'ordonnances de première partie, tel l'arrêté du directeur (par. 268). Cela n'a pas non plus échappé au juge des requêtes. Celui-ci a plutôt estimé que l'obligation d'aviser imposée par le par. 2 n'était [TRADUCTION] « pas incompatible avec l'obligation qui incombe à la province d'indemniser Weyerhaeuser et Résolu pour les frais engagés pour se conformer à l'[arrêté du directeur] » (par. 48). Autrement dit, s'il ne prévoit pas d'indemnisation de première partie, le par. 2 ne l'exclut pas non plus, et il n'écarte pas le libellé du par. 1 qui la prévoit clairement. Comme le souligne Weyerhaeuser, [TRADUCTION] « [c]e n'est pas parce que certaines dispositions procédurales peuvent être inutiles ou redondantes pour certains types de réclamations qu'un tribunal ne doit pas prendre en considération un texte clair qui confirme que ces réclamations sont visées par l'indemnité [de l'Ontario] » (m.i. Weyerhaeuser (pourvoi de l'Ontario), par. 55). (Ce raisonnement s'appliquerait aussi au par. 3, étant donné sa ressemblance avec le par. 2.) Là encore, nous ne voyons aucune erreur révisable.

(3) Did the Motion Judge Commit Palpable and Overriding Errors of Fact in His Findings of Fact?

[108] The Province's third submission relies upon what it says were two palpable and overriding errors of fact by the motion judge. It points, first, to the motion judge's suggestion that Great Lakes "continued to spend significant amounts of money to modernize

(3) Le juge des requêtes a-t-il commis des erreurs manifestes et déterminantes dans ses conclusions de fait?

[108] Le troisième argument de la province repose sur ce qu'elle affirme être deux erreurs de fait manifestes et déterminantes commises par le juge des requêtes. La province renvoie d'abord à la déclaration de ce dernier que Great Lakes a [TRADUCTION] « continué

the pulp and paper operation in Dryden" as part of the Settlement Agreement (para. 48). This statement shows, the Province says, that he failed to appreciate that such modernization efforts were given in exchange for the 1979 Indemnity, and that they formed no part of the consideration given by Great Lakes for the Ontario Indemnity. The second putative error is said to be found in the motion judge's conclusion, unsupported by evidence, that the waste disposal site was the source of the mercury contamination into the English and Wabigoon rivers.

[109] We begin by rejecting the proposition that the motion judge erred when he stated that the Ontario Indemnity "replaced the 1979 Indemnity and was part of the settlement of the lawsuit in which Great Lakes agreed to pay millions of dollars, and also continued to spend significant amounts of money to modernize the pulp and paper operation in Dryden" (para. 48). Specifically, and contrary to the position taken by our colleagues in the majority, the motion judge did not actually find that the modernization commitment was given to the Province *as part of the settlement in 1985*. Rather, he simply observed that Great Lakes continued to invest in the Dryden pulp and paper mill through to 1985, as it was required to do in exchange for the 1979 Indemnity (which, as the motion judge properly found, was subsequently replaced by the Ontario Indemnity). We agree with the Court of Appeal that there is ample evidence in the record supporting these findings, and that no basis for appellate intervention is disclosed.

[110] In any event, and to the extent that either of these are "errors", or even "palpable" errors, we again agree with the majority at the Court of Appeal that they could not possibly have had an overriding effect on the conclusion reached by the motion judge. In our respectful view, neither the Province nor our colleagues remotely justify the exaggerated claim that such minor and collateral findings of fact somehow acquired an overriding significance so as to determine the outcome of the case (*Benhaim*

de dépenser beaucoup d'argent à la modernisation de l'exploitation de pâtes et papiers de Dryden », conformément à la Convention de règlement (par. 48). Selon elle, cette déclaration montre que le juge n'a pas compris que ces efforts de modernisation étaient consentis en contrepartie de l'Indemnité de 1979, et qu'ils ne faisaient pas partie de la contrepartie donnée par Great Lakes en échange de l'Indemnité de l'Ontario. La deuxième erreur soi-disant commise par le juge se trouverait dans sa conclusion, non étayée par la preuve, que le lieu d'élimination des déchets était la source de la contamination par le mercure des rivières English et Wabigoon.

[109] Nous commençons par rejeter la proposition selon laquelle le juge des requêtes a commis une erreur en disant que l'Indemnité de l'Ontario [TRADUCTION] « a remplacé l'Indemnité de 1979 et faisait partie du règlement de la poursuite dans le cadre duquel Great Lakes a consenti à verser des millions des dollars, en plus de continuer de dépenser beaucoup d'argent à la modernisation de l'exploitation de pâtes et papiers de Dryden » (par. 48). Plus précisément, et contrairement à la position adoptée par nos collègues de la majorité, le juge des requêtes n'a pas vraiment conclu que la promesse de modernisation avait été faite à la province *dans le cadre du règlement de 1985*. Il a plutôt simplement fait observer que Great Lakes avait continué à investir dans l'usine de pâtes et papiers située à Dryden jusqu'en 1985, comme elle était tenue de le faire en contrepartie de l'Indemnité de 1979 (qui, comme l'a conclu à juste titre le juge des requêtes, a par la suite été remplacée par l'Indemnité de l'Ontario). Nous convenons avec la Cour d'appel que la preuve au dossier étaye amplement ces conclusions et qu'il n'y a aucune raison d'intervenir en appel.

[110] Quoi qu'il en soit, et dans la mesure où il s'agit dans l'un ou l'autre cas d'« erreurs », ou même d'erreurs « manifestes », nous convenons aussi avec les juges majoritaires de la Cour d'appel que ces soi-disant erreurs ne sauraient avoir eu d'effet déterminant sur la conclusion du juge des requêtes. À notre humble avis, ni la province ni nos collègues n'ont un tant soit peu justifié la prétention exagérée voulant que des conclusions de fait mineures et accessoires de la sorte aient acquis une importance primordiale

v. St-Germain, 2016 SCC 48, [2016] 2 S.C.R. 352, at para. 38, quoting *South Yukon Forest Corp. v. R.*, 2012 FCA 165, 4 B.L.R. (5th) 31, at para. 46) — particularly where the motion judge's ultimate conclusion on the scope of the indemnity rested on *different* factual and contextual considerations. This ground of appeal must fail.

(4) Did the Motion Judge's Interpretation of the Ontario Indemnity Render the Agreement Unenforceable as an Impermissible Fetter on the Legislature's Law-Making Powers?

[111] The Province's argument here is that the motion judge's interpretation of the Ontario Indemnity — that it extends to the cost of compliance with first party statutory claims made under legislation enacted *after* the indemnity was given to Great Lakes and Reed in 1985 — has the impermissible effect of indirectly fettering the legislature's law-making power. *Ex hypothesi*, the expense that the Province would incur by indemnifying Great Lakes and Reed for compliance with such statutory claims would deter the legislature from enacting the enabling legislation in the first place. Based on the "presumption of law in favour of a legal, enforceable interpretation of a contract", the Province says that the motion judge's interpretation should be rejected and the Ontario Indemnity should instead be read as excluding the costs of complying with the Director's Order and other first party statutory claims based on legislation enacted post-1985 (Ontario A.F., at para. 132).

[112] This argument rests on two key premises. The first is that the motion judge "implied a term into [the Ontario Indemnity] under which [the Province] is required to compensate for costs incurred to comply with an order made under future legislation" (Ontario A.F., at para. 116 (emphasis added)). The second is that a contract that *implicitly* discourages legislative action is invalid and unenforceable. As to this second point, the Province says that an indirect fetter of legislative power — which occurs where a

au point de déterminer l'issue de l'affaire (*Benhaim c. St-Germain*, 2016 CSC 48, [2016] 2 R.C.S. 352, par. 38, citant *South Yukon Forest Corp. c. R.*, 2012 CAF 165, 4 B.L.R. (5th) 31, par. 46) — en particulier lorsque la conclusion finale du juge des requêtes sur le champ d'application de l'indemnité reposait sur des considérations factuelles et contextuelles *différentes*. Ce moyen d'appel doit être rejeté.

(4) L'interprétation donnée par le juge des requêtes à l'Indemnité de l'Ontario a-t-elle pour effet de rendre l'entente non exécutoire parce qu'elle constitue une entrave inacceptable aux pouvoirs de légiférer de la législature?

[111] L'argument ici avancé par la province est que l'interprétation que le juge des requêtes a faite de l'Indemnité de l'Ontario — interprétation selon laquelle elle s'étend aux frais engagés pour donner suite aux réclamations de première partie faites en vertu d'une loi adoptée *après* que l'indemnité ait été consentie à Great Lakes et à Reed en 1985 — a comme effet inacceptable d'entraver indirectement le pouvoir de légiférer de la législature. Suivant cette hypothèse, la dépense qu'engagerait la province pour indemniser Great Lakes et Reed afin qu'elles puissent donner suite à de telles réclamations aurait pour effet de dissuader la législature d'adopter la loi habilitante. Compte tenu de la [TRADUCTION] « présomption de droit favorisant une interprétation contractuelle qui soit légale et exécutoire », la province affirme que l'interprétation du juge des requêtes devrait être rejetée et que l'Indemnité de l'Ontario devrait plutôt être interprétée comme excluant les frais engagés pour se conformer à l'arrêté du directeur et pour donner suite à d'autres réclamations de première partie fondées sur une loi adoptée après 1985 (m.a. Ontario, par. 132).

[112] Cet argument repose sur deux prémisses clés. La première est que le juge des requêtes [TRADUCTION] « a introduit comme modalité implicite à [l'Indemnité de l'Ontario] que [la province] devait verser une indemnité pour les frais engagés pour se conformer à une ordonnance prise en vertu d'une loi future » (m.a. Ontario, par. 116 (nous soulignons)). La deuxième est qu'un contrat qui décourage *implicitement* une action législative est invalide et non exécutoire. À ce sujet, la province affirme qu'une entrave indirecte au pouvoir

contract imposes an obligation on the government to compensate the other contracting party in the event of future legislative action or inaction — "should only be permitted where there is an express intention to allocate commercial risk" in this manner (Ontario A.F., at para. 115).

[113] We agree with the majority at the Court of Appeal. The Province's argument rests on a mischaracterization of the terms of the Ontario Indemnity, and a significant misunderstanding of the doctrine of fettering.

(a) *The Motion Judge Did Not Imply Any Terms Into the Ontario Indemnity Regarding the Effect of Orders Pursuant to Subsequently-Enacted Legislation*

[114] We begin by rejecting the Province's stated but unelaborated premise that the motion judge's conclusion rested on the implication of terms. Rather, his conclusion was drawn from a straightforward interpretation of the scope of the Province's obligation, expressly stated in para. 1 of the Ontario Indemnity as extending to "any obligation, liability, damage, loss, costs or expenses incurred . . . as a result of any claim, action or proceeding . . . existing at December 17, 1979 or which may arise or be asserted thereafter" (A.R., vol. IV, at p. 189 (emphasis added)). The motion judge's conclusion is fortified by para. 4, which provides that the indemnity is valid "without limitation as to time" (*ibid.*, at p. 191). These provisions contemplate that Reed and Great Lakes are to be indemnified in respect of *all* Pollution Claims, as defined, *whenever asserted*. Neither the text nor the surrounding circumstances support the restriction that the Province would seek to have recognized.

[115] The majority at the Court of Appeal was correct. There was no error — let alone a palpable and overriding error — in the motion judge's conclusion that the Ontario Indemnity requires the Province to indemnify the costs of compliance with an order

législatif — qui se produit lorsqu'un contrat impose au gouvernement l'obligation d'indemniser l'autre partie contractante en cas d'action ou d'inaction législative future — [TRADUCTION] « ne devrait être permise que s'il existe une intention expresse de répartir [ainsi] le risque commercial » (m.a. Ontario, par. 115).

[113] Nous partageons l'avis des juges majoritaires de la Cour d'appel. L'argument de la province repose sur une interprétation erronée des modalités de l'Indemnité de l'Ontario et sur une très mauvaise compréhension de la doctrine de l'entrave.

a) *Le juge des requêtes n'a introduit aucune modalité implicite à l'Indemnité de l'Ontario en ce qui a trait à l'effet des ordonnances prises en vertu d'une loi adoptée subséquemment*

[114] Nous commençons par rejeter la prémisse mise de l'avant sans plus d'explication par la province que la conclusion du juge des requêtes reposait sur l'introduction de modalités implicites. Sa conclusion reposait plutôt sur une interprétation simple de la portée de l'obligation de la province, explicitement énoncée au par. 1 de l'Indemnité de l'Ontario, selon laquelle celle-ci s'étendait à [TRADUCTION] « l'ensemble des obligations, responsabilités, dommages, pertes, frais ou dépenses qu'est susceptible d'entraîner [. . .] toute réclamation, action ou procédure [. . .] qui existait au 17 décembre 1979 ou qui était susceptible de prendre naissance ou d'être présentée par la suite » (d.a., vol. IV, p. 189 (nous soulignons)). La conclusion du juge des requêtes est renforcée par le par. 4, qui prévoit que l'indemnité n'est assujettie [TRADUCTION] « à aucune limite de temps » (*ibid.*, p. 191). Il ressort de ces dispositions que Reed et Great Lakes doivent être indemnisées à l'égard de *toute* réclamation pour pollution, tel que cette expression est définie, *peu importe le moment où elle est présentée*. Ni le libellé du texte ni les circonstances n'appuient la restriction que la province souhaiterait voir reconnue.

[115] Les juges majoritaires de la Cour d'appel ont raison. Il n'y a aucune erreur — et encore moins une erreur manifeste et déterminante — dans la conclusion du juge des requêtes selon laquelle l'Indemnité de l'Ontario oblige la province à verser une

made under subsequently-enacted legislation. More to the point, the motion judge implied no term into the agreement.

(b) *The Fettering Doctrine Does Not Render Unenforceable Any Contract That Discourages Legislative Action or Inaction, Whether Implicitly or Explicitly*

[116] As a matter of constitutional law, the executive of the Canadian state cannot bind or restrict the legislature's sovereign law-making power, whether by contract or otherwise. As this Court affirmed in *Reference re Canada Assistance Plan (B.C.)*, [1991] 2 S.C.R. 525, "Ministers of State cannot . . . by means of contractual obligations entered into on behalf of the State fetter their own freedom, or the freedom of their successors or the freedom of other members of parliament, to propose, consider and, if they think fit, vote for laws, even laws which are inconsistent with the contractual obligations" (p. 560, quoting *West Lakes Ltd. v. South Australia* (1980), 25 S.A.S.R. 389, at p. 390). Similarly, this Court recently explained in *Reference re Pan-Canadian Securities Regulation*, 2018 SCC 48, [2018] 3 S.C.R. 189, that "the executive is incapable of interfering with the legislature's power to enact, amend and repeal legislation", with the result being that "[a]n executive agreement that purports to bind the parties' respective legislatures cannot, therefore, have any such effect" (para. 53).

[117] It follows that a contract entered into by the executive that purports to require that a certain law be enacted, amended or repealed cannot be enforced by way of injunction or specific performance. The legislature's sovereign power to "make or unmake any law whatever" means that it can never be bound by such an order (P. W. Hogg, P. J. Monahan and W. K. Wright, *Liability of the Crown* (4th ed. 2011), at p. 324). This is sometimes referred to as the rule against "direct fettering".

indemnité pour les frais engagés pour se conformer à une ordonnance prise en vertu d'une loi adoptée subséquemment. Plus précisément, le juge des requêtes n'a introduit aucune modalité implicite dans l'entente.

b) *La doctrine de l'entrave ne rend pas non exécutoire le contrat qui décourage, implicitement ou explicitement, une action ou une inaction législative*

[116] Sur le plan constitutionnel canadien, le pouvoir exécutif ne peut lier l'exercice souverain du pouvoir législatif ni restreindre celui-ci, que ce soit par contrat ou autrement. Comme la Cour l'a affirmé dans le *Renvoi relatif au Régime d'assistance publique du Canada (C.-B.)*, [1991] 2 R.C.S. 525, [TRADUCTION] « [l]es ministres d'État ne sauraient [. . .] au moyen d'obligations contractées pour le compte de l'État, imposer des restrictions à leur propre liberté, à celle de leurs successeurs ou à celle d'autres députés, de proposer, d'étudier et, s'ils le jugent opportun, de voter des lois, fussent-elles incompatibles avec les obligations contractuelles » (p. 560, citant *West Lakes Ltd. c. South Australia* (1980), 25 S.A.S.R. 389, p. 390). De même, notre Cour a récemment expliqué dans le *Renvoi relatif à la réglementation pancanadienne des valeurs mobilières*, 2018 CSC 48, [2018] 3 R.C.S. 189, que « le pouvoir exécutif est incapable de restreindre le pouvoir de la législature d'adopter, de modifier et d'abroger des lois », de sorte qu'« [u]n accord conclu par différents exécutifs et censé lier les législatures respectives des parties ne peut donc avoir un tel effet » (par. 53).

[117] Il s'ensuit qu'un contrat conclu par le pouvoir exécutif qui vise à obliger à ce qu'une certaine loi soit adoptée, modifiée ou abrogée ne peut faire l'objet d'une exécution par injonction ou en nature. Le pouvoir souverain de la législature [TRADUCTION] « de faire ou d'abroger quelque loi que ce soit » signifie que l'exercice de ce pouvoir ne peut être lié par une telle prescription (P. W. Hogg, P. J. Monahan et W. K. Wright, *Liability of the Crown* (4e éd. 2011), p. 324). C'est ce qu'on appelle parfois la règle interdisant l'« entrave directe ».

[118] At the same time — and this is the point that eludes the Province — there is an important difference between a contract that impermissibly *fetters* the legislature's power to enact, amend and repeal legislation, and a contract whose breach by the Crown exposes it to *liability*. Where the legislature exercises its law-making power in a manner inconsistent with the terms of a contract, the Crown may still face consequences in the form of liability in damages. While the possibility of such liability may deter the legislature from acting in a manner that runs contrary to the Crown's contractual promises — sometimes referred to as an "indirect fetter" — the legislature is not thereby truly *fettered*. Its freedom of action in these circumstances "is not diminished by holding that the enactment of a particular piece of legislation gives rise to an action for damages for breach of contract" (S. M. Waddams, *The Law of Contracts* (7th ed. 2017), at p. 453; see also K. Horsman and G. Morley, eds., *Government Liability: Law and Practice* (loose-leaf), at p. 2-10). As is explained in *Liability of the Crown*:

> While a contract entered into by the Crown (or anyone else) cannot validly impose a *direct* fetter on legislative power, an exercise of legislative power in breach of contract will give rise to an obligation on the Crown to compensate the private contracting party for any loss suffered by the breach of contract. That obligation is an *indirect* fetter on legislative power, but it is not forbidden by the rule against fettering; on the contrary, it is required by the rule of law. [Emphasis in original; p. 325.]

[119] We say nothing new here: the same point emerges from *Wells v. Newfoundland*, [1999] 3 S.C.R. 199. There, the claimant Wells served as a commissioner on a statutory board, under a contract which entitled him to hold office during good behaviour until the age of 70. By legislation, the board was restructured and Wells' office was abolished. When he was not reappointed to the new board, he sued for breach of contract.

[118] Par ailleurs — et c'est le point qui échappe à la province —, il y a une différence importante entre un contrat qui *entrave* de façon inacceptable le pouvoir de la législature d'adopter, de modifier et d'abroger une loi, et un contrat dont une violation par la Couronne expose celle-ci à une *responsabilité*. Si la législature exerce son pouvoir de légiférer d'une manière incompatible avec les modalités d'un contrat, la Couronne peut quand même être exposée à des conséquences prenant la forme d'une responsabilité pour dommages. Bien que l'éventualité d'une telle responsabilité puisse dissuader la législature d'agir d'une manière qui va à l'encontre des promesses contractuelles de la Couronne, ce qu'on appelle parfois une « entrave indirecte », la législature n'est pas de ce fait véritablement *entravée*. Sa liberté d'action dans les circonstances [TRADUCTION] « n'est pas réduite du fait que l'on affirme que l'édiction d'une mesure législative en particulier donne ouverture à une action en dommages-intérêts pour violation de contrat » (S. M. Waddams, *The Law of Contracts* (7e éd. 2017), p. 453; voir aussi K. Horsman et G. Morley, dir., *Government Liability : Law and Practice* (feuilles mobiles), p. 2-10). Comme il est expliqué dans l'ouvrage *Liability of the Crown* :

> [TRADUCTION] Bien qu'un contrat conclu par la Couronne (ou par n'importe qui d'autre) ne puisse valablement imposer d'entrave *directe* au pouvoir législatif, l'exercice de ce pouvoir en violation dudit contrat donnera naissance à une obligation pour la Couronne d'indemniser la partie contractante privée pour toute perte subie en conséquence de cette violation. Cette obligation est une entrave *indirecte* au pouvoir législatif, mais elle n'est pas interdite par la règle interdisant l'entrave; au contraire, elle est requise par la primauté du droit. [En italique dans l'original; p. 325.]

[119] Il n'y a rien de nouveau dans ce que nous venons de dire : la même chose se dégage de l'arrêt *Wells c. Terre-Neuve*, [1999] 3 R.C.S. 199. Dans cette affaire, le demandeur, M. Wells, était commissaire au sein d'un organisme établi par la loi, en vertu d'un contrat qui lui permettait d'occuper son poste à titre inamovible jusqu'à l'âge de 70 ans. La commission a été restructurée et le poste de M. Wells aboli par voie législative. N'ayant pas été nommé à la nouvelle commission, il a intenté une poursuite pour violation de contrat.

[120] While accepting that the legislature had throughout retained *unfettered* authority to restructure the Board and eliminate Wells' office, this Court nonetheless found for Wells by applying the "crucial distinction . . . between the Crown legislatively avoiding a contract, and altogether escaping the legal consequences of doing so" (para. 41). The Court went on to explain that:

> In a nation governed by the rule of law, we assume that the government will honour its obligations unless it explicitly exercises its power not to. In the absence of a clear express intent to abrogate rights and obligations — rights of the highest importance to the individual — those rights remain in force. To argue the opposite is to say that the government is bound only by its whim, not its word. In Canada this is unacceptable, and does not accord with the nation's understanding of the relationship between the state and its citizens. [para. 46]

[121] *Wells* therefore affirms the distinction between *fettering* and *exposure to liability*. A legislature must be free — that is, *unfettered* — to exercise its law-making powers as it sees fit, within constitutional bounds. But where the legislature exercises its powers in such a way as to breach a government contract (that is, a contract between the executive and a counterparty), the Crown is, as a general rule, liable, unless the legislature also expressly and unambiguously extinguished the counterparty's rights of action or excluded Crown liability.

[122] *Even if*, therefore (to return to the facts of this appeal), the Ontario Indemnity has the effect of imposing liability upon the Province to indemnify against first party claims — or even of deterring or otherwise discouraging the legislature from exercising its law-making power in a certain way — *Wells* makes it clear that these effects do not render the agreement unenforceable at law. *Wells* also undermines the proposition, advanced by the Province, that indirect fettering "should only be permitted where there is an express intention to allocate commercial

[120] Bien qu'elle ait reconnu que la législature avait toujours conservé le pouvoir *libre de toute entrave* de restructurer la Commission et d'éliminer le poste occupé par M. Wells, notre Cour a néanmoins conclu en faveur de ce dernier en appliquant la « distinction fondamentale [qui existe] entre le fait pour la Couronne de se soustraire à l'exécution d'un contrat au moyen d'une loi, et le fait d'échapper entièrement aux conséquences juridiques d'une telle mesure » (par. 41). La Cour a ensuite expliqué :

> Dans un pays régi par la primauté du droit, nous présumons que le gouvernement respectera ses obligations, à moins qu'il n'exerce expressément son pouvoir de ne pas le faire. Faute d'une intention expresse et claire d'abroger des droits et des obligations — droits de la plus haute importance pour l'individu — ces droits demeurent en vigueur. Prétendre le contraire signifierait que le gouvernement n'est lié que par son caprice, non par sa parole. Au Canada, cela est inacceptable et ne concorde pas avec la façon dont on envisage la relation entre l'État et ses citoyens. [par. 46]

[121] L'arrêt *Wells* confirme donc la distinction entre l'*entrave* et le *fait de s'exposer à une responsabilité*. Une législature doit être libre — c'est-à-dire *n'être soumise à aucune entrave* — d'exercer ses pouvoirs de légiférer comme elle le juge indiqué, dans les limites fixées par la Constitution. Cependant, si elle exerce ses pouvoirs d'une façon telle qu'elle viole un contrat gouvernemental (c'est-à-dire un contrat entre le pouvoir exécutif et une partie cocontractante), la Couronne est, en règle générale, responsable, à moins que la législature ait aussi, expressément et sans équivoque, éteint les droits d'action de la partie cocontractante ou exclu la responsabilité de la Couronne.

[122] *Même si*, par conséquent (pour revenir aux faits du présent pourvoi), l'Indemnité de l'Ontario a pour effet d'imposer à la province une obligation de couvrir les réclamations de première partie — ou même de dissuader ou autrement décourager la législature d'exercer son pouvoir de légiférer d'une certaine façon —, l'arrêt *Wells* établit clairement que ces effets ne rendent pas l'entente non exécutoire en droit. L'arrêt *Wells* mine également la thèse, avancée par la province, selon laquelle l'entrave indirecte [TRADUCTION] « ne devrait être permise que s'il

risk" (Ontario A.F., at para. 115), since there was no such express allocation in that case. Even though Wells' employment contract was silent on the point of compensation in the event of abolition of his office, this Court had no difficulty finding that "[t]he most plausible interpretation of the respondent's terms of employment is that while his position, and the authority flowing from it, could be eliminated, he could not be deprived of the benefits of the job except by virtue of age or bad behaviour" (para. 36).

[123] For its part, the Province relies heavily on this Court's decision in *Pacific National Investments Ltd. v. Victoria (City)*, 2000 SCC 64, [2000] 2 S.C.R. 919 ("*Pacific National No. 1*"). At issue in that case was a contract between Pacific National Investments ("PNI") and the City of Victoria, which required PNI to redevelop a seaside neighbourhood and required the City to pass the necessary zoning and to grant subdivision. Bowing to public pressure, the City subsequently down-zoned to limit further development, thereby scuttling PNI's redevelopment. PNI sued, arguing that its contract implicitly prohibited the City from re-zoning the lands until the expiry of a reasonable amount of time, and that the City breached this implicit term when it re-zoned the land.

[124] In finding for the City, this Court explained that, as a creature of statute, the City could only agree to the implied term posited by PNI if it had the statutory authority to do so. And even accepting that such a term might be read into the contract, such a term would nevertheless have been invalid as "an illegal fetter on [the City's] discretionary legislative powers" (para. 66). Indeed, the Court went as far as to reject the distinction between direct and indirect fettering, stating that "an agreement to compensate for a legislative decision . . . is no more acceptable than an outright restriction on the legislative power" (para. 63). Here, the Court was responding to an argument that a "duty to compensate . . . along these lines would necessarily make that legislative choice subject to considerations other than an objective

existe une intention expresse de répartir le risque commercial » (m.a. Ontario, par. 115), puisqu'aucune répartition expresse de ce genre n'a été faite en l'espèce. Même si le contrat d'emploi de M. Wells était muet sur la question de l'indemnisation en cas d'abolition de son poste, notre Cour n'a eu aucune difficulté à conclure que « [l]'interprétation la plus vraisemblable des conditions d'emploi de l'intimé est que même si son poste et le pouvoir qui en découle pouvaient être abolis, il ne pouvait pas être privé des avantages de l'emploi sauf en raison de son âge ou d'une inconduite » (par. 36).

[123] Pour sa part, la province s'appuie fortement sur l'arrêt de notre Cour *Pacific National Investments Ltd. c. Victoria (Ville)*, 2000 CSC 64, [2000] 2 R.C.S. 919 (« *Pacific National n^o 1* »). Cette affaire portait sur un contrat intervenu entre Pacific National Investments (« PNI ») et la Ville de Victoria, aux termes duquel PNI devait réaménager un quartier situé au bord de la mer alors que la Ville devait adopter le zonage nécessaire et approuver le lotissement. S'inclinant devant la pression publique, la Ville a par la suite modifié le zonage afin de limiter l'aménagement ultérieur, torpillant ainsi le plan de réaménagement de PNI. Cette dernière a engagé des poursuites, soutenant que son contrat interdisait implicitement à la Ville de modifier le zonage des terrains avant l'expiration d'un délai raisonnable et que la Ville avait contrevenu à cette clause implicite en modifiant le zonage des terrains.

[124] En concluant en faveur de la Ville, notre Cour a expliqué qu'en tant que création statutaire, la Ville ne pouvait consentir à une clause implicite comme celle invoquée par PNI que si la loi lui conférait le pouvoir de le faire. Et, même en admettant qu'une telle clause puisse être considérée comme faisant partie du contrat, elle aurait été invalide puisqu'elle aurait constitué « une entrave illicite aux pouvoirs de réglementation discrétionnaires de la [Ville] » (par. 66). En fait, la Cour est même allée jusqu'à rejeter la distinction entre l'entrave directe et indirecte, affirmant qu'« une entente d'indemnisation pour une décision en matière de réglementation [. . .] n'est pas plus acceptable qu'une restriction catégorique du pouvoir de réglementation » (par. 63). La Cour répondait alors à l'argument voulant qu'une

examination of what is best for the community of which [PNI] is undoubtedly also a part" (para. 64).

[125] The difficulty is that this reasoning is irreconcilable with the Court's decision only one year earlier in *Wells*. If the law commands that Wells be entitled to compensation for the breach of his employment contract that resulted from legislative action, we struggle to explain why the law would not operate similarly so as to entitle PNI to compensation for the breach of its development contract with the City when the City Council decided to "downzone" the seaside lands. We note that the reasoning in *Pacific National No. 1* has been the subject of heavy criticism on this very issue of fettering. The authors of *Liability of the Crown* take the view that "the decision is wrong, even if it is limited to the exercise of municipal legislative powers" (p. 328 (emphasis added); see also *Government Liability*, at p. 2-10; and *Andrews v. Canada (Attorney General)*, 2014 NLCA 32, 354 Nfld. & P.E.I.R. 42, at paras. 34-41). Likewise, Perell J. in *Rio Algom Ltd. v. Canada (Attorney General)*, 2012 ONSC 550, said there is "a very strong argument that *Pacific National No. 1* is wrong and inconsistent with other equally binding and authoritative Supreme Court of Canada's decisions" (para. 153 (CanLII) (emphasis added); see also *Ontario First Nations (2008) Limited Partnership v. Ontario (Minister of Aboriginal Affairs)*, 2013 ONSC 7141, 118 O.R. (3d) 356, at paras. 53-59).

[126] Significantly, this Court in *Pacific National No. 1* did not purport to overrule *Wells*, and instead distinguished it on two bases. First, the majority observed that *Wells* "did not deal with a contract governing the exercise of municipal legislative powers" (para. 61). The logic appears to be that, unlike a province, a municipality cannot indirectly fetter its law-making powers in the absence of "legislation

« obligation d'indemniser [. . .] de ce genre [. . .] assujettirait nécessairement cette décision [en matière de réglementation] à des considérations autres que l'examen objectif du meilleur intérêt de la collectivité [dont PNI fait indubitablement aussi partie] » (par. 64).

[125] Le problème tient à ce que ce raisonnement est inconciliable avec l'arrêt *Wells* que notre Cour a rendu seulement un an plus tôt. Si le droit exige que M. Wells ait droit à une indemnité pour la violation de son contrat d'emploi résultant d'une action législative, il nous est difficile d'expliquer pourquoi le droit ne s'appliquerait pas de la même manière afin de permettre à PNI d'être indemnisée pour la violation de son contrat d'aménagement avec la Ville lorsque le conseil municipal a décidé de « modifier le zonage » des terrains situés au bord de la mer. Soulignons que le raisonnement suivi dans l'arrêt *Pacific National n^o^ 1* a été fortement critiqué sur la question précise de l'entrave. Les auteurs de l'ouvrage *Liability of the Crown* estiment que [TRADUCTION] « la décision est erronée, même si elle se limite à l'exercice des pouvoirs de réglementation municipaux » (p. 328 (nous soulignons); voir aussi *Government Liability*, p. 2-10; et *Andrews c. Canada (Attorney General)*, 2014 NLCA 32, 354 Nfld. & P.E.I.R. 42, par. 34-41). De même, le juge Perell a dit, dans la décision *Rio Algom Ltd. c. Canada (Attorney General)*, 2012 ONSC 550, que [TRADUCTION] « des raisons solides permettent d'avancer que l'arrêt *Pacific National n^o^ 1* est erroné et qu'il est incompatible avec d'autres arrêts de la Cour suprême du Canada dont la force obligatoire et la valeur de précédent sont équivalentes » (par. 153 (CanLII) (nous soulignons); voir aussi *Ontario First Nations (2008) Limited Partnership c. Ontario (Minister of Aboriginal Affairs)*, 2013 ONSC 7141, 118 O.R. (3d) 356, par. 53-59).

[126] Fait important, dans *Pacific National n^o^ 1*, notre Cour n'entendait pas écarter l'arrêt *Wells*, et elle a plutôt établi une distinction entre celui-ci et l'affaire dont elle était saisie pour deux raisons. Premièrement, les juges majoritaires ont fait observer que, dans l'affaire *Wells*, « [i]l n'était pas question [. . .] d'un contrat régissant l'exercice de pouvoirs de réglementation municipaux » (par. 61). Le raisonnement

expressing a public policy permitting it to do so" (para. 65). With great respect, and while the failing may well be ours, this distinction eludes us. As Bastarache J. observed in dissent, public policy would tend to work the other way — there is no reason why the principle that the government should honour its commitments unless its legislature explicitly exercises the power not to (as was stated in *Wells*, at para. 46) should not apply with equal force in the context of municipalities (see *Pacific National No. 1*, at para. 112). In any event, this distinction would not assist the Province here, since it — and not a municipality — agreed to the Ontario Indemnity. Meaning, the circumstances of this appeal are analogous to *Wells*, and not to *Pacific National No. 1*.

[127] The second way that the majority in *Pacific National No. 1* distinguished *Wells* was to describe Wells' employment agreement as "a business contract in relation to the hiring of senior civil servants" (para. 61). In other words, a distinction was drawn between "business contracts" which *can* have the effect of indirectly fettering law-making powers, and other kinds of contracts which *cannot*. Again with great respect, we do not see the significance of this distinction — particularly since the contract in *Pacific National No. 1* for land redevelopment could hardly have been seen as less of a "business contract" than Wells' employment contract. In any event, if the principle that the government should honour its commitments unless its legislature explicitly exercises the power not to is to be cast aside, we see no reason for doing so in respect of one kind of contract and not another.

[128] We also note that the statements in *Pacific National No. 1* regarding fettering were called into question only four years later when that dispute found its way back to this Court in *Pacific National*

semble être que, contrairement à une province, une municipalité ne peut indirectement entraver ses pouvoirs de réglementation à moins « qu'une mesure législative n'énonce une politique officielle l'autorisant à le faire » (par. 65). Avec égards, et bien que la faute puisse fort bien nous en incomber, cette distinction nous échappe. Comme l'a fait remarquer le juge Bastarache en dissidence, cette politique tend plutôt vers l'autre sens; il n'y a aucune raison pour laquelle le principe selon lequel le gouvernement devrait honorer ses engagements à moins que sa législature n'exerce expressément son pouvoir de ne pas le faire (ainsi qu'il a été déclaré dans *Wells*, au par. 46) ne devrait pas s'appliquer avec la même force dans le contexte municipal (voir *Pacific National n^o 1*, par. 112). Quoi qu'il en soit, cette distinction ne serait pas utile à la province en l'espèce, puisque c'est elle — et non une municipalité — qui a consenti à l'Indemnité de l'Ontario. Ainsi, les circonstances du présent pourvoi sont analogues à celles de l'affaire *Wells*, et non à celles de l'affaire *Pacific National n^o 1*.

[127] Deuxièmement, les juges majoritaires dans *Pacific National n^o 1* ont établi une distinction d'avec l'arrêt *Wells* en décrivant le contrat d'emploi de M. Wells comme un « contrat d'affaire[s] portant sur l'engagement de hauts fonctionnaires » (par. 61). Autrement dit, une distinction a été établie entre les « contrats d'affaires » qui *peuvent* avoir pour effet d'entraver indirectement les pouvoirs de légiférer et les autres types de contrats qui *ne le peuvent pas*. Là encore, et avec égards, nous ne voyons pas l'importance de cette distinction — d'autant plus que, dans l'affaire *Pacific National n^o 1*, on pouvait difficilement considérer que le contrat de réaménagement des terrains était moins un « contrat d'affaires » que le contrat d'emploi de M. Wells. De toute façon, s'il faut écarter le principe selon lequel le gouvernement devrait honorer ses engagements à moins que la législature n'exerce expressément son pouvoir de ne pas le faire, nous ne voyons aucune raison de l'écarter à l'égard d'un type de contrat et non d'un autre.

[128] Soulignons également que les déclarations relatives à l'entrave faites par la Cour dans l'arrêt *Pacific National n^o 1* ont été mises en doute seulement quatre ans plus tard alors que la Cour a de

Investments Ltd. v. Victoria (City), 2004 SCC 75, [2004] 3 S.C.R. 575 ("*Pacific National No. 2*"). In its action against the City, PNI had also claimed in unjust enrichment for the $1.08 million that it had spent on improvements made in performing the failed development contract. In finding for PNI, a unanimous Court rejected the City's argument that the obligation to make restitution in those circumstances would constitute an indirect fetter on the City's, legislative power, explaining that "[t]he power to down-zone in the public interest does not immunize the City against claims for unjust enrichment" (para. 52). Commenting on this case, the authors of *Liability of the Crown* had the following to say:

> [In *Pacific National No. 2*], Binnie J. said: "Municipalities are subject to the law of unjust enrichment in the same way as other individuals or entities". We would add: what a shame that the same cannot be said of the law of contract! [Footnote omitted; p. 329.]

[129] Bearing all of this in mind, and to the extent that *Pacific National No. 1* can be taken as holding that the Crown will not be liable in damages for the breach of a governmental contract where that breach was caused by legislative action (or inaction), we are of the respectful view that it does not state the law as it relates to the fettering doctrine. On this point, we consider ourselves bound by *Wells*, and not *Pacific National No. 1*.

(c) *Conclusion on the Fettering Issue*

[130] It follows that we reject the Province's arguments that invoke the doctrine of fettering. Even if the Ontario Indemnity was to be interpreted as deterring the legislature from enacting new first party statutory claims, which would then be covered by the Province's obligation under para. 1 when asserted against Great Lakes and Reed, such an effect does not render the contract unenforceable or invalid such

nouveau été saisie du litige dans *Pacific National Investments Ltd. c. Victoria (Ville)*, 2004 CSC 75, [2004] 3 R.C.S. 575 (« *Pacific National nº 2* »). Dans son action contre la Ville, PNI avait également soulevé l'enrichissement sans cause pour le 1,08 million de dollars qu'elle avait dépensé pour les améliorations apportées dans l'exécution du contrat d'aménagement qui a échoué. Concluant en faveur de PNI, la Cour a unanimement rejeté l'argument de la Ville selon lequel l'obligation de restitution dans les circonstances constituerait une entrave indirecte au pouvoir de réglementation de la Ville, expliquant que « [l]e pouvoir de modifier le zonage dans l'intérêt public ne met pas la Ville à l'abri d'une action fondée sur l'enrichissement sans cause » (par. 52). Commentant cette affaire, les auteurs de l'ouvrage *Liability of the Crown* ont affirmé ce qui suit :

> [TRADUCTION] [Dans l'arrêt *Pacific National nº 2*], le juge Binnie a dit : « L'enrichissement sans cause s'applique à une municipalité comme à toute personne physique ou morale ». Nous tenons à ajouter ce qui suit : quel dommage que l'on ne puisse en dire autant du droit des contrats! [Note en bas de page omise; p. 329.]

[129] Compte tenu de tout ce qui précède, et dans la mesure où l'arrêt *Pacific National nº 1* peut être interprété comme établissant que la Couronne ne sera pas responsable des dommages causés par la violation d'un contrat gouvernemental si cette violation résulte d'une action (ou d'une inaction) législative, nous croyons respectueusement que cet arrêt n'énonce pas le droit applicable en ce qui concerne la doctrine de l'entrave. Sur ce point, nous considérons que nous sommes liés par l'arrêt *Wells*, et non par l'arrêt *Pacific National nº 1*.

c) *Conclusion sur la question de l'entrave*

[130] Nous rejetons donc les arguments avancés par la province au sujet de la doctrine de l'entrave. Même s'il fallait considérer que l'Indemnité de l'Ontario a pour effet de dissuader la législature d'édicter des mesures permettant de nouvelles réclamations de première partie, réclamations qui, après avoir été présentées contre Great Lakes et Reed, relèveraient ensuite de l'obligation imposée à la province par le

that the legislature was fettered. This accords with the authority of this Court's judgment in *Wells*.

[131] It also follows that we do not view the motion judge's interpretation of the Ontario Indemnity — as requiring the Province to indemnify the cost of complying with orders made under subsequent legislation — as impermissibly fettering the Ontario Legislature's law-making power. While the enactment of new statutory claims might expose the Province to greater liability under the Ontario Indemnity (which might therefore discourage such enactments in the first place), the Ontario Indemnity, as interpreted by the motion judge, in no way prevents the legislature from exercising its sovereign authority to "make or unmake any law whatever" (A. V. Dicey, *Introduction to the Study of the Law of the Constitution* (10th ed. 1959), at p. 40, cited in *Reference re Pan-Canadian Securities Regulation*, at para. 54).

C. *The Resolute and Weyerhaeuser Appeals*

[132] The appeals brought by Resolute and Weyerhaeuser ask whether either or both of them enjoy the benefit of the Ontario Indemnity by operation of the enurement clause (para. 6) of that agreement. That clause states that the indemnity "shall be binding upon and enure to the benefit of the respective successors and assigns of Ontario, Reed, International and Great Lakes" (A.R., vol. IV, at p. 191 (emphasis added)).

[133] The parties' submissions on this question are directed to three separate, but related, issues, which we will address below, in turn. The first is whether the benefit of the Ontario Indemnity extends to all of Great Lakes' successors and assigns, in perpetuity, irrespective of whether those successors and assigns had themselves assigned their benefits thereunder to third parties. Resolute and Weyerhaeuser say it does, while the Province (like the Court of Appeal) says that the assignor of a chose in action — such as

par. 1, un tel effet ne rend pas le contrat non exécutoire ou invalide de sorte qu'il y a eu entrave au pouvoir législatif. Cela est compatible avec l'arrêt de notre Cour dans l'affaire *Wells*.

[131] Il s'ensuit également que nous ne considérons pas que l'interprétation donnée à l'Indemnité de l'Ontario par le juge des requêtes — selon laquelle la province doit verser une indemnité pour les frais engagés pour se conformer aux ordonnances prises en vertu d'une loi subséquente — entrave de façon inacceptable le pouvoir de légiférer de la législature ontarienne. Bien qu'il soit possible que l'édiction de mesures permettant de nouvelles réclamations statutaires expose la province à une plus grande responsabilité en vertu de l'Indemnité de l'Ontario (ce qui pourrait en conséquence décourager de telles édictions), cette indemnité, telle qu'interprétée par le juge des requêtes, n'empêche nullement la législature d'exercer son droit souverain [TRADUCTION] « de faire ou d'abroger quelque loi que ce soit » (A. V. Dicey, *Introduction to the Study of the Law of the Constitution* (10e éd. 1959), p. 40, cité dans le *Renvoi relatif à la réglementation pancanadienne des valeurs mobilières*, par. 54).

C. *Les pourvois de Résolu et de Weyerhaeuser*

[132] Les pourvois formés par Résolu et Weyerhaeuser soulèvent la question de savoir si l'une ou l'autre, ou les deux, jouissent du bénéfice de l'Indemnité de l'Ontario par l'effet de la clause d'extension des bénéfices (par. 6) de cette entente. Cette clause stipule que l'indemnité [TRADUCTION] « lie les successeurs et ayants droit respectifs de l'Ontario, de Reed, d'International et de Great Lakes et bénéficie à ceux-ci » (d.a., vol. IV, p. 191 (nous soulignons)).

[133] Les arguments invoqués par les parties sur cette question portent sur trois questions distinctes, mais connexes, que nous examinerons tour à tour ci-après. La première vise à déterminer si le bénéfice de l'Indemnité de l'Ontario s'étend à tous les successeurs et ayants droit de Great Lakes, à perpétuité, que ces successeurs et ayants droit aient ou non eux-mêmes cédé à des tiers les bénéfices qu'elle leur confère. Résolu et Weyerhaeuser affirment que c'est le cas, alors que la province (à l'instar de la

a right to indemnity — loses the benefit thereunder upon assignment (see C.A. reasons, at paras. 194 and 196-98).

[134] The second issue is whether Bowater actually assigned the benefit of the Ontario Indemnity to Weyerhaeuser under the 1998 Asset Purchase Agreement. Resolute says it did not, and that both the motion judge and the majority of the Court of Appeal erred in concluding otherwise. Weyerhaeuser and the Province both say no such error was made by the courts below.

[135] The final issue is whether Weyerhaeuser may benefit under the Ontario Indemnity as Great Lakes' successor-in-title to the Dryden Property, independently of whether it can also benefit as an assignee of the rights thereunder. Weyerhaeuser says the motion judge correctly interpreted the term "successors" in the enurement clause as extending to Great Lakes' corporate successors (like Resolute) *and* to successors-in-title to the Dryden Property.

(1) Can an Indemnified Party Continue to Enjoy the Benefit of the Ontario Indemnity After It Assigns Its Rights Thereunder Absolutely to a Third Party?

[136] Resolute and Weyerhaeuser say that all of Great Lakes' successors and assigns may continue to benefit in perpetuity from the Ontario Indemnity, even where they have assigned the benefit of the indemnity to third parties. In other words, they say that the enurement clause contemplates (1) Resolute's continued enjoyment of the benefit of the Ontario Indemnity as a corporate successor of Great Lakes, *even if* it had assigned its interest thereunder to Weyerhaeuser under to the 1998 Asset Purchase Agreement, and (2) Weyerhaeuser's continued enjoyment of the same as a successor-in-title to the Dryden Property and assignee of the Ontario Indemnity, *even*

Cour d'appel) affirme que le cédant d'une chose non possessoire — tel un droit à une indemnité — en perd le bénéfice en cas de cession (voir motifs de la C.A., par. 194 et 196-198).

[134] La deuxième question est de savoir si Bowater a en fait cédé le bénéfice de l'Indemnité de l'Ontario à Weyerhaeuser en vertu de la convention d'achat d'actifs de 1998. Résolu dit que Bowater ne l'a pas cédé et que le juge des requêtes et les juges majoritaires de la Cour d'appel ont commis une erreur en concluant autrement. Weyerhaeuser et la province affirment toutes les deux que les juridictions inférieures n'ont pas commis une telle erreur.

[135] La dernière question consiste à décider si Weyerhaeuser peut bénéficier de l'Indemnité de l'Ontario en tant que successeur en titre de Great Lakes quant à la propriété de Dryden, peu importe qu'elle puisse ou non également en bénéficier en tant que cessionnaire des droits conférés par cette indemnité. Weyerhaeuser affirme que le juge des requêtes a correctement interprété le terme [TRADUCTION] « successeurs » employé dans la clause d'extension des bénéfices en l'étendant aux successeurs corporatifs de Great Lakes (comme Résolu) *et* aux successeurs en titre quant à la propriété de Dryden.

(1) Une partie indemnisée peut-elle continuer à jouir du bénéfice de l'Indemnité de l'Ontario après avoir consenti à un tiers une cession absolue des droits qu'elle lui confère?

[136] Résolu et Weyerhaeuser affirment que tous les successeurs et ayants droit de Great Lakes peuvent continuer à bénéficier à perpétuité de l'Indemnité de l'Ontario, même s'ils ont cédé le bénéfice de cette indemnité à des tiers. En d'autres mots, elles affirment que la clause d'extension des bénéfices prévoit que (1) Résolu continue à jouir du bénéfice de l'Indemnité de l'Ontario en tant que successeur corporatif de Great Lakes, *même si* elle a, en vertu de la convention d'achat d'actifs de 1998, cédé l'intérêt que cette indemnité lui confère à Weyerhaeuser, et que (2) Weyerhaeuser continue à jouir du bénéfice de ladite indemnité en tant que successeur en titre quant à la propriété de

if it had subsequently assigned its interest thereunder to a third party. According to Resolute:

> There is no legal principle that required the Court of Appeal to apply [a] "hot potato" theory, in which only the singular legal owner of an indemnity may rely on it. This Court relaxed the requirement of privity more than 25 years ago. Rather, the relevant question is what the parties to the Ontario Indemnity objectively intended. The only reasonable interpretation of the indemnity is that the parties intended to protect Great Lakes and its successors *and* assigns, in perpetuity. Any other interpretation is fundamentally inconsistent with the nature of the environmental liability that the Ontario Indemnity was given to protect against. [Emphasis in original.]

(Resolute A.F., at para. 64)

[137] We disagree. Our starting position is that of the majority of the Court of Appeal: the effect of an absolute assignment of contractual right is to extinguish the assignor's right to call upon the obligation for him or herself, and to place that right in the hands of the assignee:

> The party making the assignment was a promisee but became an assignor who assigned the contract right he had against a promisor. Unless the assignment is made to secure the payment of a debt, it extinguishes the contract right in the assignor (former promisee) and the right is recreated in the assignee to whom the party with the correlative duty (the promisor) made no promise. There is no longer any promisee since the former promisee has surrendered the right previously created by his promise by becoming an assignor.

(J. E. Murray, Jr., *Corbin on Contracts* (rev. ed. 2007), vol. 9, at p. 130)

See also C.A. reasons, at para. 194; G. Tolhurst, *The Assignment of Contractual Rights* (2nd ed. 2016), at § 3.10.

[138] The enurement clause alters none of this. By referring to "successors and assigns", it simply

Dryden et en tant que cessionnaire de l'Indemnité de l'Ontario, *même si* elle a par la suite cédé l'intérêt que cette indemnité lui confère à un tiers. Selon Résolu :

> [TRADUCTION] Aucun principe juridique n'obligeait la Cour d'appel à appliquer une théorie de la « question délicate », selon laquelle seul le particulier qui est propriétaire en droit d'une indemnité peut en bénéficier. Cette Cour a assoupli l'exigence de la connexité d'intérêts il y a plus de 25 ans. La question pertinente est plutôt celle de savoir quelle était l'intention objective des parties à l'Indemnité de l'Ontario. La seule interprétation raisonnable de l'indemnité consiste à considérer que les parties entendaient protéger Great Lakes ainsi que ses successeurs *et* ayants droit à perpétuité. Toute autre interprétation est fondamentalement incompatible avec la nature de la responsabilité environnementale contre laquelle l'Indemnité de l'Ontario est censée protéger. [En italique dans l'original.]

(m.a. Résolu, par. 64)

[137] Nous ne sommes pas d'accord. Notre position de départ est celle des juges majoritaires de la Cour d'appel : la cession absolue d'un droit contractuel a pour effet d'éteindre le droit du cédant d'exiger en sa faveur l'exécution de l'obligation en question, et de placer ce droit entre les mains du cessionnaire :

> [TRADUCTION] La partie qui consent la cession était un destinataire de promesse, mais elle est devenue un cédant qui a cédé le droit contractuel qu'elle avait à l'encontre du promettant. À moins que la cession soit faite pour garantir le paiement d'une dette, elle éteint le droit contractuel détenu par le cédant (l'ancien destinataire de promesse), lequel droit est recréé en faveur du cessionnaire à qui la partie à qui incombe l'obligation corrélative (le promettant) n'a fait aucune promesse. Il n'y a plus aucun destinataire de promesse puisque l'ancien destinataire de promesse a cédé le droit antérieurement créé par la promesse qui lui a été faite en devenant cédant.

(J. E. Murray, Jr., *Corbin on Contracts* (éd. rév. 2007), vol. 9, p. 130)

Voir aussi les motifs de la C.A., par. 194; G. Tolhurst, *The Assignment of Contractual Rights* (2e éd. 2016), § 3.10.

[138] La clause d'extension des bénéfices ne change rien à cela. En faisant référence aux [TRADUCTION]

affirms that the rights and obligations thereunder continue to the benefit of successors and assigns. We see nothing in either the text of para. 6 or its surrounding circumstances, and Resolute and Weyerhaeuser direct our attention to nothing in this respect that would allow the indemnity to apply to those who have alienated their interest. We therefore find no error in the conclusion of the Court of Appeal on this point.

(2) Did Bowater Transfer the Benefit of the Ontario Indemnity to Weyerhaeuser Under the 1998 Asset Purchase Agreement?

[139] On this issue, Resolute says that a proper consideration of the context in which the 1998 Asset Purchase Agreement was made by the parties, in accordance with the modern approach to contractual interpretation rather than a purely textual reading of the relevant provisions, should have led the motion judge to conclude that Bowater did not absolutely assign the Ontario Indemnity to Weyerhaeuser under that agreement. We agree with Resolute. By failing to read the impugned contractual term in light of the factual matrix and in a commercially sensible way, the motion judge erred in holding that Bowater assigned the Ontario Indemnity to Weyerhaeuser under the 1998 Asset Purchase Agreement. We would therefore allow Resolute's appeal. Resolute is entitled to rely on the Ontario Indemnity to cover past and future costs incurred in complying with the Director's Order.

(a) *The Motion Judge Erred in Principle in His Approach to Interpreting the 1998 Asset Purchase Agreement*

[140] Generally, the interpretation of negotiated contracts involves questions of mixed fact and law, such that appellate review is confined to seeking out palpable and overriding error. Extricable questions of law, however, are reviewed for correctness (see *Sattva*, at para. 53). Such questions include "the application of an incorrect principle, the failure to consider a required element of a legal test, . . . the

« successeurs et ayants droit », elle ne fait que confirmer que les droits et obligations découlant de l'entente continuent de bénéficier à ceux-ci. Nous ne voyons rien dans le libellé du par. 6 ou dans les circonstances, et Résolu et Weyerhaeuser n'ont rien fait valoir à cet égard qui permettrait que l'indemnité s'applique à ceux qui ont aliéné leur intérêt. Nous ne décelons donc aucune erreur dans la conclusion que la Cour d'appel a tirée sur ce point.

(2) Bowater a-t-elle transféré le bénéfice de l'Indemnité de l'Ontario à Weyerhaeuser en vertu de la convention d'achat d'actifs de 1998?

[139] Sur cette question, Résolu affirme qu'un examen approprié du contexte dans lequel la convention d'achat d'actifs de 1998 a été conclue par les parties, examen fait selon la méthode moderne d'interprétation contractuelle — plutôt que selon une interprétation purement textuelle des dispositions pertinentes —, aurait dû amener le juge des requêtes à conclure que Bowater n'a pas cédé de façon absolue l'Indemnité de l'Ontario à Weyerhaeuser en vertu de cette convention. Nous sommes d'accord avec Résolu. Nous estimons qu'en ne lisant pas la clause contractuelle contestée à la lumière du fondement factuel et d'une manière qui a du sens sur le plan commercial, le juge des requêtes a commis une erreur lorsqu'il a conclu que Bowater a cédé l'Indemnité de l'Ontario à Weyerhaeuser en vertu de la convention d'achat d'actifs de 1998. Nous serions donc d'avis d'accueillir le pourvoi de Résolu. Résolu a le droit de bénéficier de l'Indemnité de l'Ontario pour couvrir les frais passés et futurs engagés pour se conformer à l'arrêté du directeur.

a) *Le juge des requêtes a commis une erreur de principe dans sa façon d'interpréter la convention d'achat d'actifs de 1998*

[140] De façon générale, l'interprétation de contrats négociés soulève des questions mixtes de fait et de droit, de sorte que le contrôle en appel se limite à la recherche d'une erreur manifeste et déterminante. Les questions de droit isolables sont toutefois contrôlées selon la norme de la décision correcte (voir *Sattva*, par. 53). Ces questions comprennent le fait [TRADUCTION] d'« appliquer le mauvais principe[, de] négliger

failure to consider a relevant factor", or questions with respect to substantive legal rules of contract (*Sattva*, at para. 53, quoting *King v. Operating Engineers Training Institute of Manitoba Inc.*, 2011 MBCA 80, 341 D.L.R. (4th) 520, at para. 21).

[141] We accept Resolute's submission that the motion judge erred *in law* by failing to properly apply the rules of contractual interpretation in determining whether Bowater assigned the Ontario Indemnity to Weyerhaeuser under the 1998 Asset Purchase Agreement. Indeed, the motion judge gave no reasons in support of his conclusion on this point, which was stated in a somewhat peremptory manner, and grounded solely on an analysis of the text of the relevant provisions of the 1998 Asset Purchase Agreement (motion judge reasons, at paras. 20 and 64). In our respectful view, he was required to consider both the context and circumstances surrounding the formation of the 1998 Asset Purchase Agreement, as well as the commercial reasonableness of any purported assignment. As he failed to apply the proper approach to contractual interpretation, his conclusion that the Ontario Indemnity was assigned from Bowater to Weyerhaeuser is entitled to no appellate deference.

(b) *Bowater Did Not Assign the Benefit of the Ontario Indemnity to Weyerhaeuser Under the 1998 Asset Purchase Agreement*

(i) Contracts Must Be Interpreted With a View to Commercial Reasonableness

[142] As we have already observed, commercial reasonableness is a crucial consideration in interpreting a contract (see *Canadian Contractual Interpretation Law*, at p. 55). This is simply a corollary of the object of discerning the parties' intentions: when interpreting commercial contracts, courts seek to reach a commercially sensible interpretation, since doing so is more likely than not to give effect to the intention of the parties (see *ibid.*, at p. 57; *Nickel Developments Ltd. v. Canada Safeway Ltd.*, 2001 MBCA 79, 156 Man. R. (2d) 170, at para. 34). Simply put, courts safely assume that those who enter

un élément essentiel d'un critère juridique[,] un facteur pertinent », ou encore les questions relatives aux règles de droit substantif en matière contractuelle (*Sattva*, par. 53, citant *King c. Operating Engineers Training Institute of Manitoba Inc.*, 2011 MBCA 80, 341 D.L.R. (4th) 520, par. 21).

[141] Nous acceptons l'argument de Résolu selon lequel le juge des requêtes a commis une erreur *de droit* en n'appliquant pas correctement les règles d'interprétation contractuelle au moment de déterminer si Bowater avait cédé l'Indemnité de l'Ontario à Weyerhaeuser en vertu de la convention d'achat d'actifs de 1998. Le juge n'a d'ailleurs pas motivé sa conclusion sur ce point, laquelle a été exposée de manière quelque peu péremptoire et reposait exclusivement sur une analyse du libellé des dispositions pertinentes de la convention en question (motifs du juge des requêtes, par. 20 et 64). À notre humble avis, il devait prendre en considération à la fois le contexte et les circonstances entourant la conclusion de la convention d'achat d'actifs de 1998, ainsi que la raisonnabilité commerciale d'une quelconque cession. Comme il n'a pas appliqué la bonne méthode d'interprétation contractuelle, sa conclusion suivant laquelle Bowater a cédé l'Indemnité de l'Ontario à Weyerhaeuser ne commande aucune déférence en appel.

b) *Bowater n'a pas cédé le bénéfice de l'Indemnité de l'Ontario à Weyerhaeuser en vertu de la convention d'achat d'actifs de 1998*

(i) Les contrats doivent être interprétés à la lumière de la raisonnabilité commerciale

[142] Comme nous l'avons déjà mentionné, la raisonnabilité commerciale est une considération cruciale dans l'interprétation d'un contrat (voir *Canadian Contractual Interpretation Law*, p. 55). Il s'agit simplement d'un corollaire de l'objectif visant à cerner les intentions des parties : dans l'interprétation de contrats commerciaux, les tribunaux cherchent à parvenir à une interprétation sensée sur le plan commercial, puisque ce faisant, il est plus probable qu'ils donnent effet à l'intention des parties (voir *ibid.*, p. 57; *Nickel Developments Ltd. c. Canada Safeway Ltd.*, 2001 MBCA 79, 156 Man. R. (2d) 170, par. 34). En

into commercial contracts intend for their contracts to "work" (*Humphries v. Lufkin Industries Canada Ltd.*, 2011 ABCA 366, 68 Alta. L.R. (5th) 175, at para. 15).

[143] Discerning commercial reasonableness entails, like all contractual interpretation, an objective analysis (see *Canadian Contractual Interpretation Law*, at p. 57). Courts should therefore read commercial contracts in a "positive and purposive manner", seeking to understand the structure of the agreement reached by the parties, the purpose of the transaction and the business context in which the contract was intended to operate (*Humphries*, at para. 15). As Lord Wilberforce said in *Reardon Smith Line Ltd. v. Hansen-Tangen*, [1976] 3 All E.R. 570, and as quoted with approval by this Court in *Sattva*, at para. 47:

> No contracts are made in a vacuum: there is always a setting in which they have to be placed. . . . In a commercial contract it is certainly right that the court should know the commercial purpose of the contract and this in turn presupposes knowledge of the genesis of the transaction, the background, the context, the market in which the parties are operating.

[144] Given, then, the choice between an interpretation that allows the contract to function in furtherance of its commercial purpose and one that does not, it is generally the former interpretation that should prevail (see *Humphries*, at para. 15). While a party cannot avoid its contractual obligations simply because the bargain that they entered into was undesirable or unusual, commercially absurd interpretations should be avoided (see *Canadian Contractual Interpretation Law*, at pp. 61-63). As this Court said in *Guarantee Co. of North America v. Gordon Capital Corp.*, [1999] 3 S.C.R. 423, at para. 61, "[i]f a given construction of the contract would lead to an absurd result, the assumption is that this result could not have been intended by rational commercial actors in making their bargain, absent some explanation to the contrary". See also *City of Toronto v. W.H. Hotel Ltd.*, [1966] S.C.R. 434, at p. 440.

termes simples, les tribunaux assument que les parties qui concluent un contrat commercial veulent que leur contrat [TRADUCTION] « fonctionne » (*Humphries c. Lufkin Industries Canada Ltd.*, 2011 ABCA 366, 68 Alta. L.R. (5th) 175, par. 15).

[143] La détermination de la raisonnabilité commerciale nécessite, comme toute interprétation contractuelle, une analyse objective (voir *Canadian Contractual Interpretation Law*, p. 57). Les tribunaux devraient donc interpréter les contrats commerciaux de [TRADUCTION] « manière positive et téléologique », et chercher à comprendre la structure de l'entente conclue par les parties, l'objet de l'opération et le contexte commercial dans lequel le contrat doit être exécuté (*Humphries*, par. 15). Comme lord Wilberforce l'a dit dans l'arrêt *Reardon Smith Line Ltd. c. Hansen-Tangen*, [1976] 3 All E.R. 570, cité avec approbation par notre Cour au par. 47 de l'arrêt *Sattva* :

> [TRADUCTION] Aucun contrat n'est conclu dans l'abstrait : les contrats s'inscrivent toujours dans un contexte. [. . .] Lorsqu'un contrat commercial est en cause, le tribunal devrait certes connaître son objet sur le plan commercial, ce qui présuppose d'autre part une connaissance de l'origine de l'opération, de l'historique, du contexte, du marché dans lequel les parties exercent leurs activités.

[144] Étant donné, donc, le choix entre une interprétation qui permet au contrat de servir son objectif commercial et une qui n'a pas cet effet, c'est généralement la première interprétation qui devrait l'emporter (voir *Humphries*, par. 15). Bien qu'une partie ne puisse échapper à ses obligations contractuelles simplement parce que la transaction qu'elle a conclue est non souhaitable ou inhabituelle, il convient d'éviter les interprétations absurdes sur le plan commercial (voir *Canadian Contractual Interpretation Law*, p. 61-63). Comme notre Cour l'a affirmé dans l'arrêt *Guarantee Co. of North America c. Gordon Capital Corp.*, [1999] 3 R.C.S. 423, par. 61, « [s]i une interprétation donnée du contrat menait à un résultat absurde, on supposerait qu'en l'absence d'explication contraire des acteurs commerciaux rationnels ne peuvent pas avoir voulu un tel résultat en concluant leur contrat ». Voir également *City of Toronto c. W.H. Hotel Ltd.*, [1966] R.C.S. 434, p. 440.

(ii) It Was Not Commercially Reasonable for Bowater to Transfer the Ontario Indemnity to Weyerhaeuser

[145] In light of the foregoing — and, in particular, based on an interpretation of the 1998 Asset Purchase Agreement that properly reflects the factual matrix and which is consistent with the principle of commercial reasonableness — we find ourselves in respectful disagreement with the conclusions reached by the courts below. We would instead hold that the Ontario Indemnity was *not* assigned by Bowater to Weyerhaeuser as part of the 1998 Asset Purchase Agreement. The manner in which the parties structured the transfer of the Dryden Property from Bowater to Weyerhaeuser reveals an intention that Bowater would both continue to bear the risk associated with the waste disposal site and indemnify Weyerhaeuser in respect of any environmental liabilities that the latter may incur in relation to the Reed-era mercury contamination.

[146] Section 3.1(vii) and (xiv) of the 1998 Asset Purchase Agreement recorded Bowater's agreement to sell certain intangible assets forming part of the Dryden Property to Weyerhaeuser. As already noted, the motion judge relied on both provisions in concluding that the benefit of the Ontario Indemnity was assigned to Bowater as part of the asset sale. The majority at the Court of Appeal agreed, citing the "plain and unambiguous language of s. 3.1(xiv)", and the commercial reasonableness of Weyerhaeuser's seeking to "maximize its protection against environmental liabilities associated with the [waste disposal site]" (paras. 156 and 159).

[147] But s. 3.1(xiv) of the 1998 Asset Purchase Agreement cannot be read in isolation. Instead, as we have stressed throughout these reasons, contractual text must be interpreted in light of the surrounding circumstances and with a view to commercial reasonableness, taking into account the commercial purpose and the structure of the agreement.

(ii) Il n'était pas commercialement raisonnable pour Bowater de transférer l'Indemnité de l'Ontario à Weyerhaeuser

[145] À la lumière de ce qui précède — et nous fondant, en particulier, sur une interprétation de la convention d'achat d'actifs de 1998 qui reflète adéquatement le fondement factuel et qui s'accorde avec le principe de la raisonnabilité commerciale —, nous ne partageons pas les conclusions tirées par les juridictions inférieures. Nous estimons plutôt que l'Indemnité de l'Ontario *n'*a *pas* été cédée par Bowater à Weyerhaeuser dans le cadre de la convention d'achat d'actifs de 1998. La façon dont les parties ont structuré le transfert de la propriété de Dryden de Bowater à Weyerhaeuser révèle l'intention que Bowater continue d'assumer le risque posé par le lieu d'élimination des déchets et indemnise Weyerhaeuser à l'égard de toute responsabilité environnementale qui pourrait incomber à cette dernière en ce qui a trait à la contamination par le mercure remontant à l'époque de Reed.

[146] Les articles 3.1(vii) et (xiv) de la convention d'achat d'actifs de 1998 constatent le fait que Bowater a consenti à vendre à Weyerhaeuser certains actifs incorporels faisant partie de la propriété de Dryden. Comme nous l'avons déjà souligné, le juge des requêtes s'est fondé sur ces deux dispositions pour conclure que le bénéfice de l'Indemnité de l'Ontario avait été cédé à Bowater dans le cadre de la vente d'actifs. Les juges majoritaires de la Cour d'appel ont souscrit à cette conclusion, invoquant les [TRADUCTION] « termes clairs et non équivoques de l'art. 3.1(xiv) », et la raisonnabilité commerciale de la volonté de Weyerhaeuser de « maximiser sa protection contre les responsabilités environnementales liées au [lieu d'élimination des déchets] » (par. 156 et 159).

[147] Cependant, l'art. 3.1(xiv) de la convention d'achat d'actifs de 1998 ne saurait être interprété isolément. Comme nous l'avons souligné tout au long des présents motifs, un libellé contractuel doit plutôt être interprété à la lumière des circonstances et de la raisonnabilité commerciale, eu égard à l'objectif commercial et à la structure de l'entente.

[148] Further, commercial reasonableness must be assessed *from the perspective of both parties*. After all, a commercial arrangement that makes sense for one party but no sense for another makes no sense as a commercial arrangement at all. As the Court of Appeal for Ontario explained in *Kentucky Fried Chicken Canada v. Scott's Food Services Inc.* (1998), 114 O.A.C. 357, at para. 27:

> Where . . . the document to be construed is a negotiated commercial document, the court should avoid an interpretation that would result in a commercial absurdity. Rather, the document should be construed in accordance with sound commercial principles and good business sense. Care must be taken, however, to do this objectively rather than from the perspective of one contracting party or the other, since what might make good business sense to one party would not necessarily do so for the other. [Emphasis added; citations omitted.]

[149] This point looms large in considering the text of s. 3.1(xiv), which, at first glance, appears to transfer to Weyerhaeuser the full benefit of *all* of the intangible rights that Bowater enjoys under the representations, warranties, guarantees, indemnities, undertakings, certificates, covenants, agreements and security that it has received upon the acquisition of the Dryden Property or "otherwise". Read literally, "otherwise" suggests that Bowater would be stripped of all of its contractual benefits by operation of s. 3.1(xiv) *even if* those benefits were unconnected to the Dryden Property. This simply could not have been the intention of the parties: Weyerhaeuser could not reasonably have expected to enjoy rights unrelated to the assets it was purchasing. Such an arrangement would be commercially absurd.

[150] The meaning of the term "otherwise" in s. 3.1(xiv) — and, specifically, whether it captures the benefit of the Ontario Indemnity — becomes evident, however, once the structure of the agreement between Bowater and Weyerhaeuser, and how they chose to allocate risk as between them is understood. The latter is a key consideration, since the allocation of contractual risk is an attempt by one party to shape

[148] En outre, la raisonnabilité commerciale doit être évaluée *du point de vue des deux parties*. Après tout, une entente commerciale qui est sensée pour une partie, mais qui ne l'est pas pour une autre, n'est en aucun cas une entente sensée sur le plan commercial. Comme l'a expliqué la Cour d'appel de l'Ontario dans l'arrêt *Kentucky Fried Chicken Canada c. Scott's Food Services Inc.* (1998), 114 O.A.C. 357, par. 27 :

> [TRADUCTION] Lorsque [. . .] le document à interpréter est un document commercial négocié, le tribunal devrait éviter toute interprétation qui mènerait à une absurdité sur le plan commercial. Il convient plutôt d'interpréter le document conformément aux principes commerciaux reconnus et au bon sens en matière commerciale. Il faut prendre soin, cependant, de le faire objectivement plutôt que du point de vue d'une partie contractante ou de l'autre, puisque ce qui peut être sensé sur le plan commercial pour l'une ne l'est pas nécessairement pour l'autre. [Nous soulignons; références omises.]

[149] Ce point revêt une grande importance dans l'examen du libellé de l'art. 3.1(xiv), qui, à première vue, semble transférer à Weyerhaeuser le plein bénéfice de *l'ensemble* des droits incorporels dont jouit Bowater à l'égard des déclarations, garanties, indemnités, engagements, certificats, conventions, ententes et sûretés qu'elle a reçus lors de l'acquisition de la propriété de Dryden [TRADUCTION] ou « autrement ». Interprété littéralement, le mot « autrement » donne à penser que Bowater aurait été dépouillée de tous ses bénéfices contractuels par application de l'art. 3.1(xiv) *même si* ces bénéfices n'étaient pas liés à la propriété de Dryden. Cela ne peut tout simplement pas avoir été l'intention des parties : Weyerhaeuser ne peut raisonnablement s'être attendue à jouir de droits qui n'ont aucun rapport avec les actifs qu'elle achetait. Un tel arrangement serait absurde sur le plan commercial.

[150] Le sens du terme « autrement » à l'art. 3.1(xiv) — et, plus précisément, la question de savoir s'il englobe le bénéfice de l'Indemnité de l'Ontario — devient évident, cependant, lorsqu'on comprend la structure de l'entente intervenue entre Bowater et Weyerhaeuser, et la façon dont ces sociétés ont choisi de répartir le risque entre elles. Cette deuxième considération joue un rôle clé, car la répartition du risque contractuel

the other's expectations in light of what they are prepared to do (see *Canadian Contract Law*, at p. 731).

[151] Here, the parties structured the 1998 Asset Purchase Agreement in a way that imposed *all risk* in relation to environmental liabilities — especially in relation to the waste disposal site — *on Bowater*, and not on Weyerhaeuser. First and foremost, as part of the deal, Bowater provided to Great Lakes a broad environmental indemnity in respect of the entire Dryden Property, in the following terms:

10.7 Environmental Indemnity

The Vendor shall indemnify the Purchaser from and against any Claim wherein the Claimant alleges that any Loss, or any damages of any nature whatsoever, was suffered or incurred as a result of a release or discharge of any Hazardous Substance that occurred prior to the Time of Closing, which Hazardous Substance leaves or left the Purchased Assets prior to the Time of Closing and which originated from the Purchased Assets (the "Claim"). For purposes of this paragraph, Claimant shall not include the Purchaser. The carriage and defence of the Claim shall be conducted in accordance with Section 18.4. There shall be no limitation period and no maximum amount for the Indemnity under this Section 10.7.

(A.R., vol. V, at p. 70)

[152] Further, by s. 9.01 of the 1998 Lease Agreement, Bowater also provided to Weyerhaeuser a separate indemnity for *all claims* relating to the presence or release of mercury in relation to the waste disposal site:

9.01 **Tenant's Indemnity**

[Bowater] covenants to indemnify and save harmless [Weyerhaeuser] from all claims, actions, costs and losses of every nature arising during the Term or thereafter relating to or arising in any way from this lease of the Lands

est une tentative par une partie d'orienter les attentes de l'autre partie en fonction de ce qu'elle est disposée à faire (voir *Canadian Contract Law*, p. 731).

[151] En l'espèce, les parties ont structuré la convention d'achat d'actifs de 1998 de façon à ce que *tous les risques* en matière de responsabilités environnementales — en particulier ceux ayant trait au lieu d'élimination des déchets — *incombent à Bowater*, et non à Weyerhaeuser. D'abord et avant tout, Bowater a consenti à Great Lakes, dans le cadre de l'entente qu'elles ont conclue, une indemnité environnementale considérable en ce qui concerne l'ensemble de la propriété de Dryden :

[TRADUCTION]

10.7 Indemnité environnementale

Le vendeur s'engage à indemniser l'acheteur quant à toute réclamation dans laquelle le réclamant allègue avoir subi une perte ou des dommages de quelque nature qu'ils soient par suite du rejet d'une substance dangereuse antérieur à l'heure de clôture, laquelle substance dangereuse doit être évacuée ou avoir été évacuée des actifs visés par l'achat avant l'heure de clôture et doit provenir des actifs visés par l'achat (la « réclamation »). Pour l'application du présent paragraphe, le terme « réclamant » n'englobe pas l'acheteur. La conduite et la défense de la réclamation se feront conformément à l'article 18.4. Aucun délai de prescription ni aucun montant maximal ne s'appliqueront à l'indemnité prévue au présent article 10.7.

(d.a., vol. V, p. 70)

[152] Par ailleurs, aux termes de l'art. 9.01 de la Convention de bail de 1998, Bowater a également consenti à Weyerhaeuser une indemnité distincte à l'égard de *l'ensemble des réclamations* portant sur la présence ou le rejet de mercure en ce qui concerne le lieu d'élimination des déchets :

[TRADUCTION]

9.01 **Indemnité du locataire**

[Bowater] s'engage à indemniser [Weyerhaeuser] et à la tenir à couvert de l'ensemble des réclamations, actions, frais et pertes de quelconque nature ayant pris naissance pendant la durée du présent bail ou après l'expiration de

and the Access Area except to the extent caused by the Landlord's negligence or wilful misconduct. The foregoing indemnity extends without limitation to all claims, actions, costs or losses arising out of or relating to:

(1) the presence or release of mercury and any other contaminant, substance or waste on or in the Lands;

. . .

The obligations of the Tenant to indemnify the Landlord under the provisions of this section are to survive the termination or expiry of this lease.

(A.R., vol. V, at pp. 126-27)

[153] These two broadly-worded indemnities reveal with absolute clarity the risk allocation structure that Bowater and Weyerhaeuser intended to achieve. Once the indemnity in the 1998 Lease Agreement was provided, Weyerhaeuser was protected from any and all environmental liability resulting from its temporary ownership of the waste disposal site, in addition to the protection that it enjoyed in relation to the rest of the Dryden Property. The parties clearly intended that any claim against Weyerhaeuser in respect of the presence or release of the mercury waste would be covered by either the indemnity in s. 10.7 of the 1998 Asset Purchase Agreement or in s. 9.01 of the Lease Agreement (assuming, of course, that any such claim falls within the scope of either provision).

[154] This risk-allocation structure makes commercial sense, however, if *and only if* Bowater's interests remained protected by the Ontario Indemnity. The Province acknowledged as much during the hearing in this Court and in its factum in the Superior Court of Justice (see hearing transcript, at p. 121; A.R., vol. VIII, at p. 24). As Resolute says, such an interpretation of the 1998 Asset Purchase Agreement makes sense because "Weyerhaeuser would have

celui-ci, et qui ont trait ou sont consécutives de quelque manière que ce soit au présent bail sur les terres et la zone d'accès sauf dans la mesure où il est question de négligence ou d'inconduite délibérée de la part du locateur. L'indemnité susmentionnée s'étend notamment à l'ensemble des réclamations, actions, frais ou pertes consécutives ou ayant trait à ce qui suit :

(1) la présence ou le rejet de mercure et de tout autre contaminant, substance ou déchet sur ou dans les terres;

. . .

Les obligations d'indemnisation du locateur qui incombent au locataire en vertu des dispositions du présent article continuent de s'appliquer après la résiliation ou l'expiration du présent bail.

(d.a., vol. V, p. 126-127)

[153] Ces deux indemnités, rédigées en termes larges, révèlent avec une clarté absolue la structure de répartition du risque que Bowater et Weyerhaeuser entendaient établir. Une fois l'indemnité de la Convention de bail de 1998 accordée, Weyerhaeuser était protégée contre toute responsabilité environnementale découlant de son droit de propriété temporaire sur le lieu d'élimination des déchets, en plus de bénéficier d'une protection à l'égard du reste de la propriété de Dryden. Les parties ont clairement voulu que toute réclamation visant Weyerhaeuser en ce qui a trait à la présence ou au rejet de déchets mercuriels soit visée soit par l'indemnité prévue à l'art. 10.7 de la convention d'achat d'actifs de 1998 ou par celle prévue à l'art. 9.01 de la Convention de bail (en supposant, bien sûr, qu'une telle réclamation entre dans le champ d'application de l'une ou l'autre de ces dispositions).

[154] Toutefois, cette structure de répartition du risque n'a de sens sur le plan commercial que si, *et seulement si*, l'Indemnité de l'Ontario continuait à protéger les intérêts de Bowater. La province l'a reconnu à l'audience devant notre Cour ainsi que dans le mémoire qu'elle a déposé devant la Cour supérieure de justice (voir transcription de l'audience, p. 121; d.a., vol. VIII, p. 24). Comme le dit Résolu, cette façon d'interpréter la convention d'achat d'actifs de 1998

recourse against Bowater, and Bowater would have recourse against [the Province]", the result being that "[e]veryone would be protected" (Resolute A.F., at para. 101).

[155] Weyerhaeuser also conceded that "it would have been commercially absurd for Bowater to assign the indemnity if, by doing so, Bowater (and its successor, Resolute) would lose the benefit of the Indemnity" (Weyerhaeuser R.F. (Resolute Appeal), at para. 28). It argues, however — and the majority at the Court of Appeal accepted — that it was "perfectly reasonable" for Weyerhaeuser to seek both an assignment of the Ontario Indemnity *and* a separate indemnity from Bowater under the Lease Agreement (*ibid.*, at para. 27; see also C.A. reasons, at para. 159). While this is undoubtedly so, this submission views the commercial reasonableness of the transaction exclusively from the standpoint of Weyerhaeuser. But, again, commercial reasonableness has to be assessed from the standpoint of *each party*, and not just one of them. And, as Weyerhaeuser concedes, from the standpoint of *Bowater*, this arrangement would be ridiculous, leaving Bowater (and its successors) responsible for *two* contractual indemnities vis-à-vis Weyerhaeuser, and completely exposed to all environmental liabilities in respect of both the Dryden Property and the waste disposal site.

[156] It follows that, in our view, for the purpose of applying s. 3.1(xiv) of the 1998 Asset Purchase Agreement, the contractual rights and indemnities "otherwise" received by Bowater and its corporate predecessors must not be read so as to confer on Weyerhaeuser *all* the rights and indemnities enjoyed by Bowater. Both the factual matrix (which includes the indemnities in the 1998 Asset Purchase Agreement and in the Lease Agreement) and the principle of commercial reasonableness indicate that this provision did not effect a transfer of Bowater's rights under the Ontario Indemnity to Weyerhaeuser. The parties could not reasonably have intended that Bowater would be obliged to indemnify Weyerhaeuser for all environmental liabilities in relation to the Dryden Property and the

est sensée parce que [TRADUCTION] « Weyerhaeuser pourrait poursuivre Bowater, et cette dernière pourrait poursuivre [la province] », de sorte que « [t]out le monde serait protégé » (m.a. Résolu, par. 101).

[155] Weyerhaeuser a également concédé qu'il [TRADUCTION] « aurait été absurde sur le plan commercial que Bowater cède l'indemnité si, ce faisant, Bowater (et son successeur, Résolu) en avait perdu le bénéfice » (m.i. Weyerhaeuser (pourvoi de Résolu), par. 28). Elle soutient cependant — et les juges majoritaires de la Cour d'appel en conviennent — qu'il était [TRADUCTION] « parfaitement raisonnable » pour elle de vouloir à la fois une cession de l'Indemnité de l'Ontario *et* l'octroi par Bowater d'une indemnité distincte en vertu de la Convention de bail (*ibid.*, par. 27; voir aussi motifs de la C.A., par. 159). Bien que ce soit indubitablement le cas, cet argument envisage la raisonnabilité commerciale de l'opération uniquement du point de vue de Weyerhaeuser. Cependant, nous le répétons, la raisonnabilité commerciale doit être appréciée du point de vue de *chacune des parties*, et non seulement de l'une d'elles. De plus, comme le concède Weyerhaeuser, du point de vue de *Bowater*, cet arrangement serait ridicule en ce que Bowater (et ses successeurs) assumerait la responsabilité de *deux* indemnités contractuelles à l'égard de Weyerhaeuser, et qu'elle serait complètement exposée à toute responsabilité environnementale afférente à la propriété de Dryden et au lieu d'élimination des déchets.

[156] C'est pourquoi nous estimons que, pour l'application de l'art. 3.1(xiv) de la convention d'achat d'actifs de 1998, les droits et indemnités contractuels « autrement » reçus par Bowater et les sociétés qui l'ont précédée ne doivent pas être interprétés de façon à conférer à Weyerhaeuser *tous* les droits et indemnités dont bénéficiait Bowater. Tant le fondement factuel (qui comprend les indemnités prévues dans la convention d'achat d'actifs de 1998 et la Convention de bail) que le principe de la raisonnabilité commerciale indiquent que cette disposition n'a pas eu pour effet de transférer à Weyerhaeuser les droits de Bowater en vertu de l'Indemnité de l'Ontario. Les parties ne pouvaient raisonnablement vouloir que Bowater soit tenue d'indemniser Weyerhaeuser pour toute responsabilité environnementale

waste disposal site, while relinquishing its own protection.

[157] We would therefore allow Resolute's appeal.

(3) Is Weyerhaeuser a "Successor" of Great Lakes for the Purpose of the Enurement Clause at Paragraph 6 of the Ontario Indemnity?

[158] While Weyerhaeuser is not an assignee of the benefit of the Ontario Indemnity, it also says that it may still benefit thereunder as a successor owner of the Dryden Property. In its submission, the term "successor" in para. 6 of the Ontario Indemnity includes both corporate successors of Great Lakes *and* successors-in-title to the Dryden Property. Relying on *Brown v. Belleville (City)*, 2013 ONCA 148, 114 O.R. (3d) 561, Weyerhaeuser argues that the enurement clause extends the benefit of the Ontario Indemnity to a *class* of beneficiaries, all of whom may simultaneously benefit from the agreement.

[159] Like the majority at the Court of Appeal, we are of the respectful view that the motion judge made a palpable and overriding error in concluding that the enurement clause extended the benefit of the Ontario Indemnity to successor owners of the Dryden Property (i.e., successors-*in-title*). In our view, the term "successors" clearly refers only to *corporate* successors. It is worth noting that this clause is a standard contractual term — that is, "boilerplate" — that solicitors use in order to protect their clients' interests and expectations (see *Canadian Contract Law*, at pp. 741-42). Certainty in commercial transactions is best protected where courts give effect to the common understanding and inclusion of such terms in contracts, absent any indication that the parties intended them to have a different effect.

afférente à la propriété de Dryden et au lieu d'élimination des déchets tout en renonçant à sa propre protection.

[157] Nous accueillerions donc le pourvoi de Résolu.

(3) Weyerhaeuser est-elle un « successeur » de Great Lakes pour les besoins de la clause d'extension des bénéfices contenue au par. 6 de l'Indemnité de l'Ontario?

[158] Bien que Weyerhaeuser ne soit pas cessionnaire du bénéfice de l'Indemnité de l'Ontario, elle affirme par ailleurs qu'elle peut quand même en bénéficier en tant que propriétaire successeur de la propriété de Dryden. Elle soutient que le terme [TRADUCTION] « successeurs » au par. 6 de l'Indemnité de l'Ontario vise à la fois les successeurs corporatifs de Great Lakes *et* les successeurs en titre quant à la propriété de Dryden. Invoquant l'arrêt *Brown c. Belleville (City)*, 2013 ONCA 148, 114 O.R. (3d) 561, Weyerhaeuser fait valoir que la clause d'extension des bénéfices étend le bénéfice de l'Indemnité de l'Ontario à une *classe* de bénéficiaires, tous susceptibles de bénéficier simultanément de l'entente.

[159] À l'instar des juges majoritaires de la Cour d'appel, nous sommes d'avis que le juge des requêtes a commis une erreur manifeste et déterminante en concluant que la clause d'extension des bénéfices étendait le bénéfice de l'Indemnité de l'Ontario aux propriétaires successeurs de la propriété de Dryden (c.-à-d. aux successeurs *en titre*). Selon nous, le terme [TRADUCTION] « successeurs » ne renvoie clairement qu'aux successeurs *corporatifs*. Il convient de souligner que cette clause est une clause contractuelle type, c.-à-d. [TRADUCTION] « standard », que les avocats utilisent pour protéger les intérêts et les attentes de leurs clients (voir *Canadian Contract Law*, p. 741-742). La certitude en matière d'opérations commerciales est mieux protégée lorsque les tribunaux donnent effet au sens courant et à l'inclusion de telles clauses figurant dans les contrats, en l'absence d'indication que les parties ont voulu que celles-ci aient un effet différent.

[160] In *National Trust Co. v. Mead*, [1990] 2 S.C.R. 410, this Court observed that, "[w]hen used in reference to corporations, a 'successor' generally denotes another corporation which, through merger, amalgamation or some other type of legal succession, assumes the burdens and becomes vested with the rights of the first corporation" (p. 423). Indeed, this common understanding of the term "successor" has been recognized in considering enurement clauses like the one at issue here (see C. L. Elderkin and J. S. Shin Doi, *Behind and Beyond Boilerplate: Drafting Commercial Agreements* (1998), at pp. 250-51; M. H. Ogilvie, "Re-defining Privity of Contract: *Brown v. Belleville (City)*" (2015), 52 *Alta. L. Rev.* 731, at p. 736). Again, bearing in mind that the object of contractual interpretation is to discern the parties' objective *intentions*, the commonly accepted meaning of that term provides a helpful starting point to considering what the parties understood the words in the enurement clause to mean.

[161] We agree with the majority at the Court of Appeal that, in these particular circumstances, "nothing in the language of the Ontario Indemnity or in the circumstances surrounding the formation of the contract" supports Weyerhaeuser's interpretation of the enurement clause (para. 184). To the contrary, in reading the enurement clause together with the rest of the Ontario Indemnity, it becomes clear that the parties intended to restrict the term "successors" to *corporate* successors. Paragraph 2 of the Ontario Indemnity refers to Reed's "predecessor[s] in title", while para. 6 uses the term "successors" without any such qualification. As this Court remarked in *Heritage Capital Corp. v. Equitable Trust Co.*, 2016 SCC 19, [2016] 1 S.C.R. 306, at para. 47, "[m]eaning must be given to the choice to use one term in one clause and a different term in a different clause of the same agreement". Had the parties to the Ontario Indemnity intended the enurement clause to apply to all successors-in-title over the Dryden Property, they could have made those intentions clear.

[160] Dans l'arrêt *National Trust Co. c. Mead*, [1990] 2 R.C.S. 410, notre Cour a fait observer qu'« [e]mployé à l'égard de sociétés, le terme "successeur" désigne généralement une autre société qui, par fusion ou une autre forme de succession juridique, assume les obligations et acquiert les droits de la première société » (p. 423). En fait, ce sens courant du terme « successeur » a été reconnu à l'occasion de l'examen de clauses d'extension des bénéfices comme celle en cause en l'espèce (voir C. L. Elderkin et J. S. Shin Doi, *Behind and Beyond Boilerplate : Drafting Commercial Agreements* (1998), p. 250-251; M. H. Ogilvie, « Re-defining Privity of Contract : *Brown v. Belleville (City)* » (2015), 52 *Alta. L. Rev.* 731, p. 736). Encore là, étant donné que l'interprétation contractuelle a pour objectif de cerner les *intentions* objectives des parties, le sens communément reconnu de ce terme constitue un point de départ utile pour déterminer comment les parties ont interprété les mots employés dans la clause d'extension des bénéfices.

[161] Nous sommes d'accord avec les juges majoritaires de la Cour d'appel pour dire que, dans les circonstances particulières de l'espèce, [TRADUCTION] « rien dans le libellé de l'Indemnité de l'Ontario ou dans les circonstances entourant la conclusion du contrat » n'appuie l'interprétation donnée par Weyerhaeuser à la clause d'extension des bénéfices (par. 184). Au contraire, lorsqu'on lit cette clause conjointement avec le reste de l'Indemnité de l'Ontario, il apparaît clairement que les parties ont voulu restreindre le sens du terme [TRADUCTION] « successeurs » aux successeurs *corporatifs*. Le paragraphe 2 de l'Indemnité de l'Ontario renvoie aux « prédécesseur[s] en titre » de Reed, alors que le par. 6 emploie le terme « successeurs » sans aucun qualificatif de la sorte. Comme la Cour l'a fait remarquer dans l'arrêt *Heritage Capital Corp. c. Équitable, Cie de fiducie*, 2016 CSC 19, [2016] 1 R.C.S. 306, par. 47, « [i]l faut donner un sens à la décision d'employer un terme donné dans une clause et un terme différent dans une autre clause figurant dans le même contrat ». Si les parties à l'Indemnité de l'Ontario voulaient que la clause d'extension des bénéfices s'applique à tous les successeurs en titre quant à la propriété de Dryden, elles auraient pu l'exprimer clairement.

[162] This is not to say that our conclusion with respect to the word "successors" in this specific enurement clause sets out a universal definition of that term. It may be possible, in other circumstances, for the term "successors" to refer to successors-in-title (e.g. *Belleville*).

[163] For these reasons, Weyerhaeuser is neither an assignee of the benefit of the Ontario Indemnity nor a corporate successor of either Great Lakes or Reed. Notwithstanding its rights under the 1998 Asset Purchase Agreement and the Lease Agreement, it has no entitlement to benefit under the Ontario Indemnity, and we would dismiss its appeal.

[164] Given this conclusion, it is unnecessary for us to decide whether the enurement clause operates to the benefit of a class of beneficiaries (being Great Lakes' successors *and* assigns).

VI. Conclusion

[165] We would dismiss the appeals of the Province and of Weyerhaeuser. We would allow Resolute's appeal and declare that Weyerhaeuser enjoys no benefit under the Ontario Indemnity. Resolute is entitled to its costs in this Court and throughout, including costs before the motion judge on the terms he ordered (*Weyerhaeuser Company Limited v. Ontario (Attorney General)*, 2017 ONSC 1814).

Appeal of Resolute FP Canada Inc. dismissed, CÔTÉ, BROWN *and* ROWE JJ. *dissenting.*

Appeal of Her Majesty The Queen as represented by the Ministry of the Attorney General allowed with costs throughout, CÔTÉ, BROWN *and* ROWE JJ. *dissenting.*

Appeal of Weyerhaeuser Company Limited dismissed.

Solicitors for the appellant/respondent Resolute FP Canada Inc.: Torys, Toronto.

[162] Cela ne signifie pas que notre conclusion sur le mot [TRADUCTION] « successeurs » figurant dans cette clause particulière d'extension des bénéfices donne à ce terme une définition universelle. Il se peut que dans d'autres circonstances, le terme « successeurs » renvoie aux successeurs en titre (p. ex. *Belleville*).

[163] Pour ces motifs, Weyerhaeuser n'est ni cessionnaire du bénéfice de l'Indemnité de l'Ontario ni un successeur corporatif de Great Lakes ou de Reed. Malgré les droits que lui confèrent la convention d'achat d'actifs de 1998 et la Convention de bail, elle n'a pas droit au bénéfice de l'Indemnité de l'Ontario et nous rejetterions son pourvoi.

[164] Étant donné cette conclusion, il n'est pas nécessaire que nous décidions si la clause d'extension des bénéfices s'applique au profit d'une classe de bénéficiaires (qui sont les successeurs *et* ayants droit de Great Lakes).

VI. Conclusion

[165] Nous rejetterions les pourvois de la province et de Weyerhaeuser. Nous accueillerions le pourvoi de Résolu et déclarerions que Weyerhaeuser ne jouit pas du bénéfice de l'Indemnité de l'Ontario. Résolu a droit à ses dépens devant toutes les cours, y compris les dépens aux conditions ordonnées par le juge des requêtes (*Weyerhaeuser Company Limited c. Ontario (Attorney General)*, 2017 ONSC 1814).

Pourvoi de Produits forestiers Résolu rejeté, les juges CÔTÉ, BROWN *et* ROWE *sont dissidents.*

Pourvoi de Sa Majesté la Reine représentée par le ministère du procureur général accueilli avec dépens dans toutes les cours, les juges CÔTÉ, BROWN *et* ROWE *sont dissidents.*

Pourvoi de Compagnie Weyerhaeuser Limitée rejeté.

Procureurs de l'appelante/intimée Produits forestiers Résolu : Torys, Toronto.

Solicitor for the appellant/respondent Her Majesty The Queen as represented by the Ministry of the Attorney General: Ministry of the Attorney General, Toronto.

Solicitors for the appellant/respondent Weyerhaeuser Company Limited: Borden Ladner Gervais, Toronto.

Solicitor for the intervener the Attorney General of British Columbia: Attorney General of British Columbia, Victoria.

Procureur de l'appelante/intimée Sa Majesté la Reine représentée par le ministère du procureur général : Ministère du procureur général, Toronto.

Procureurs de l'appelante/intimée Compagnie Weyerhaeuser Limitée : Borden Ladner Gervais, Toronto.

Procureur de l'intervenant le procureur général de la Colombie-Britannique : Procureur général de la Colombie-Britannique, Victoria.

TAB 19

In the Court of Appeal of Alberta

Citation: Royal Bank of Canada v Swartout, 2011 ABCA 362

Date: 20111208
Docket: 1001-0307-AC
Registry: Calgary

Between:

Royal Bank of Canada

Respondent (Plaintiff)

- and -

Hank Swartout, Keith MacPhail and Grant Fagerheim

Appellants (Defendants)

The Court:

The Honourable Madam Justice Marina Paperny
The Honourable Mr. Justice J. D. Bruce McDonald
The Honourable Mr. Justice Brian O'Ferrall

Memorandum of Judgment

Appeal from the Order by
The Honourable Mr. Justice G. H. Poelman
Dated the 2nd day of September, 2010
Filed on the 7th day of December, 2010
(Docket: 0901-09798)

Memorandum of Judgment

The Court:

Introduction

[1] The appellants had a letter agreement with the respondent Royal Bank of Canada (the respondent) for loans to finance the construction of a condominium complex. The construction project failed and the respondent sued the appellants for damages for failing to fund the cost overruns and ensure completion of the project. The chambers judge dismissed the appellants' application to dismiss the respondent's claim against them and granted the respondent's application to dismiss the appellants' defences based on the *Guarantees Acknowledgment Act*, RSA 2000, c G-11 (the *Act*).

Background Facts

[2] The three individual appellants were directors, officers and substantial shareholders of The Resort at Copper Point Ltd. (the Resort), a single purpose company formed to develop a condominium project in Invermere, British Columbia (the Project). The appellants were described as successful businessmen. The appellants were involved in the planning and supervision of fundamental aspects of the Project. Construction commenced with funding by the appellants even before financing was obtained in 2007 by way of a loan facility from the respondent. There were significant cost overruns and the Project went ultimately into receivership on February 26, 2009.

[3] Throughout the loan arrangements, the respondent, the appellants and the Resort were represented by counsel. Two relevant documents were created for the loan transaction: a letter agreement dated August 27, 2007 setting out the terms of the loan facilities (the Letter Agreement), and a form of identical guarantee to be granted by each of the appellants (the guarantee). Under the terms of the guarantee, each appellant severally guaranteed the loan for the Project for up to a total of $3,000,000. Each guarantee had a properly completed certificate of notary public pursuant to the *Act*. There is no dispute with respect to the appellants' legal obligations under the guarantees and indeed those obligations have been honoured.

[4] The respondent asserts that by the terms of the Letter Agreement, the appellants agreed to pay all cost overruns by paying the funds necessary to complete the Project and as a result, the respondent commenced an action against the appellants claiming indemnity for the cost overruns. The chambers judge described the respondent's claim as seeking "damages for the alleged breaches of the individuals in not ensuring that the Project was completed on schedule and within budget, and in not funding cost overruns and the like." In contrast, the guarantees related to a shortfall in recovery of the loans.

[5] The appellants applied for summary judgment dismissing the respondent's claim against them on the basis that their obligations under the Letter Agreement are guarantees within the

meaning of the *Act*, and the requirements of the *Act* were not satisfied. The respondent brought a cross-application to dismiss those parts of the appellants' statement of defence that are based on a failure of the Letter Agreement to comply with the provisions of the *Act*.

Decision of the Chambers Judge

[6] The chambers judge held that the obligations of the appellants under the Letter Agreement were not in the nature of a guarantee, but rather were primary obligations. He dismissed the appellants' application for summary judgment and granted the respondent's application instead.

[7] The chambers judge described the issue as follows: Are the appellants' obligations under the Cost Over-Run Provision of the Letter Agreement those of guarantors of the Resort's obligations, or do they constitute primary obligations of the individual appellants themselves?

[8] The Letter Agreement provided for three loan facilities. The first facility, the primary loan, was described as a $45,978,000 non-revolving term facility. The appellants are referred to and individually identified in the Letter Agreement as "Guarantors" and the Resort is referred to and defined as "Borrower". The respondent is defined as the "Bank".

[9] The key provisions of the Letter Agreement were reviewed by the chambers judge. These include the following:

> Availability
> Facility (1)
> The Borrower may borrow up to the amount of this facility provided:
> . . .
> (b) an Event of Default shall not have occurred and be continuing at the time of any Borrowing
>
> (c) . . . the maximum total loan amount available will be determined as follows:
>
> > (i) Actual costs to date . . . must be greater than or equal to the aggregate borrowing advanced to date . . .
> > (ii) Costs to complete the Project . . . must be less than or equal to the un-utilized portion of this facility . . .
>
> (e) the Bank will be under no obligation to advance further borrowings if at any time the condition outlined in (c)(ii) above is not met. The Borrower and the Guarantors will be severally liable to immediately cover any such deficiency as soon as it arises or is identified by the Bank or the Project Monitor.
> . . .

> Repayment
> Facility (1)
> Borrowings are to be repaid from 100% of the Net Sales Proceeds received on the closings of sales of units in the Project. . . .
> . . .
> Security
> The security for the Borrowings and all other obligations of the Borrower to the Bank shall include:
> . . .
> (b) Guarantee and postponement of claim on the Bank's form 812 in the amount of $3,000,000 signed by Grant Fagerheim;
>
> (c) Guarantee and postponement of claim on the Bank's form 812 in the amount of $3,000,000 signed by Keith MacPhail;
>
> (d) Guarantee and postponement of claim on the Bank's form 812 in the amount of $3,000,000 signed by Hank Swartout;
> . . .
>
> General Covenants
> The Borrower covenants and agrees with the Bank, while this agreement is in effect:
>
> (a) to pay all sums of money when due by it under this agreement;
> . . .
>
> (m) to diligently and continuously proceed with the Project, once commenced, in accordance with the Project Budget and Project Schedule and not to abandon the Project;
> . . .
>
> (q) to immediately fund from resources outside the Project, any cost overruns, margin deficiencies or debt servicing shortfalls as they may occur or be identified by the Bank or Project Monitor; . . .

[10] The main provision of the Letter Agreement at issue in this appeal was headed "Cost Over-Runs" (Cost Over-Run Provision), which reads as follows:

> Each of the Guarantors, for the consideration set forth in this agreement, severally undertakes with the Bank, knowing the Bank will be relying upon such undertaking in making credit available to the Borrower under this agreement, as follows:

> (i) that the Project will be completed in accordance with the Project Schedule and within the Project Budget; and
> (ii) that, should the Project not be completed within the Project Budget, all cost overruns in excess of the aggregate costs set out in the Project Budget, any margin deficiencies or any debt servicing shortfalls, as they may occur or be identified by the Bank or the Project Monitor, shall forthwith be funded from those resources of the Guarantors, or any one of them, that are not already committed to the Project in accordance with this agreement.
>
> Each of the Guarantors acknowledges that the Borrower will not be eligible for further advances from the Bank until such costs overruns, deficiencies or debt servicing shortfalls are fully funded.
>
> Failure by the Borrower to complete the Project in accordance with the Project Schedule or to comply with the first paragraph above shall constitute an Event of Default under this agreement.

[11] Additionally, under the heading "Events of Default", the chambers judge specifically noted the following:

> (a) the Borrower fails to pay when due any principal, interest, fees or other amounts due under this agreement;
>
> (b) the Borrower or any Guarantor breaches any provision of this agreement or any security or other agreement with the Bank or any subsidiary or affiliate of the Bank;

[12] The Letter Agreement also includes the following preamble before the appellants' signatures:

> We acknowledge and confirm our agreement with the foregoing terms and conditions, as Guarantors, as of August 31, 2007, and we specifically acknowledge and confirm our agreement with the provisions of the Cost Over-runs section of this Agreement.

[13] The chambers judge interpreted the Cost Over-Run Provision as, in essence, providing that each appellant (or "Guarantor" as they are defined) severally undertakes with the respondent (a) that the Project will be completed on schedule and within budget, and (b) that if not within budget, all cost overruns, any margin deficiencies or debt servicing shortfalls will forthwith be funded by the appellants, from resources not already committed to the Project. Those commitments, he held are expressed as being obligations of the appellants alone.

[14] The chambers judge reviewed authorities dealing with the distinction between primary and secondary obligations, or indemnities and guarantees respectively, and concluded that based upon the plain meaning of the Letter Agreement and the guidance of the case authorities, the appellants' obligations in the Cost Over-Run Provision are not guarantees within the meaning of the *Act* but are clearly expressed as primary undertakings of the appellants to the respondent and separately confirmed again on the execution page.

[15] He asked whether the appellants promised to answer for an act or default of another, or covenant on their own behalf? He held that the plain words in the Cost Over-Run Provision are that the appellants gave their own undertakings. The fact that the Resort may be in default, coincident with the appellants being in breach, or called upon to fund, does not mean the appellants answer only for the Resort's default.

[16] The chambers judge concluded the Cost Over-Run Provision imposes performance obligations and funding obligations directly on, and only on, the appellants. Although they were referred throughout the Letter Agreement as "Guarantors", the use of the defined term did nothing more than identify the three individual appellants. The label did not determine the substance of their legal obligations.

[17] The chambers judge further held this interpretation was consistent with the context of the transaction as the Project would not have proceeded expeditiously and economically without the involvement of the appellants and it was not surprising that their financial commitments went beyond the $3,000,000 guarantees.

[18] The chambers judge held the Letter Agreement was not ambiguous, therefore, *contra proferentum* did not apply.

Issues on Appeal

[19] The appellants take no issue with the chambers judge's findings of fact. The sole issue on appeal is whether the chambers judge erred in law by determining that the obligations imposed on the appellants by the Letter Agreement were indemnities rather than guarantees.

[20] The appellants submit that their obligations under the Letter Agreement are guarantees for four reasons. Firstly, interpreting the substance of the Letter Agreement, their obligations are secondary, rather than primary obligations and therefore are at law guarantees. Secondly, the appellants signed as "Guarantors". Thirdly, the appellants are referred to as "Guarantors" throughout the Letter Agreement, a term which has a specific legal meaning. Fourthly, in the alternative, the Letter Agreement is ambiguous and the doctrine of *contra proferentum* applies in their favour.

[21] The respondent submits the chambers judge considered and correctly rejected each of the four arguments.

Standard of Review

[22] The parties agree the issue of whether the Cost Over-Run Provision is an indemnity or guarantee is a question of law and therefore is to be reviewed on a standard of correctness. We agree that correctness is the proper standard of review for this issue.

[23] The standard of review for factual inferences is overriding and palpable error: *Housen v Nikolaisen*, 2002 SCC 33, [2002] 2 SCR 235 at para 19. Even where, as in this case, the fact findings are not based on *viva voce* evidence nor linked to the credibility of witnesses, the rule remains that appellate interference requires overriding and palpable error as there are numerous policy reasons supporting deference to all factual conclusions of a trial judge: *Housen* at paras 24 - 25.

Analysis

Indemnity or guarantee

[24] The chambers judge correctly stated the law distinguishing the difference between indemnities and guarantees as the former is a primary, direct obligation which is not conditional upon default by another. An indemnity is not within the jurisdiction of the *Act* which defines "guarantee" at section 1(a) as:

> (a) "guarantee" means a deed or written agreement whereby a person, not being a corporation, enters into an obligation to answer for an act or default or omission of another, but does not include
>
> (i) a bill of exchange, cheque or promissory note,
>
> (ii) a partnership agreement,
>
> (iii) a bond or recognizance given to the Crown or to a court or pursuant to a statute, or
>
> (iv) a guarantee given on the sale of an interest in land or an interest in goods or chattels;

[25] The appellants submit that the provisions of the Letter Agreement support the conclusion that the primary obligations are those of the Resort, and the appellants have only secondary obligations in the event of the Resort's default.

[26] In the Letter Agreement, the Resort, as Borrower, covenanted to complete the Project and to fund any cost overruns as set out under the General Covenants heading in the agreement at clauses (m) and (q):

> (m) to diligently and continuously proceed with the Project, once commenced, in accordance with the Project Budget and Project Schedule and not to abandon the Project
>
> (q) to immediately fund from resources outside the Project, any cost overruns, margin deficiencies or debt servicing shortfalls as they may occur or be identified by the Bank or Project Monitor

[27] Failure to comply with any of the provisions, including the above, constituted a default by the Borrower under the heading "Events of Default". The appellants submit that those provisions impose upon the Borrower, i.e. the Resort, the primary obligation. The obligation of the Guarantors is therefore a secondary obligation.

[28] The Cost Over-Run Provision, provides that each of the "Guarantors", "for the consideration set forth in this agreement, severally undertakes with the respondent" to (i) complete the Project on time and on budget, and (ii) to fund cost overruns. The consequences of failing to do either (i) or (ii) are also set out in the Cost Over-Run Provision as follows:

> Failure by the Borrower to complete the Project in accordance with the Project Schedule or to comply with the first paragraph above shall constitute an Event of Default under this agreement.

The appellants submit the above provision clearly states the default is that of the Borrower, not the Guarantors. The appellants submit that if they were to be indemnitors, this paragraph would not have been included in the agreement.

[29] The respondent argues that the Cost Over-Run Provision in the Letter Agreement and the separate guarantees signed by each of the appellants were drafted by the respondent to protect the respondent from two separate and distinct risks.

[30] With respect to the Cost-Over Run Provision, it is designed to compel the appellants to ensure that the Project was finished on time and within budget. This is not a surprising requirement given the fact that the Resort was a single purpose company with no assets beyond the Project in question. The Cost Over-Run Provision was designed to protect the respondent from the "construction cost risk".

[31] On the other hand, the three guarantees were designed to protect the respondent from the "market risk" i.e. in the event that the total sale proceeds realized from the sale of the Project was insufficient to retire the Bank loan in full.

[32] In looking at the terms of the Letter Agreement, the context must be kept in mind. The Letter Agreement is unusual in including references to the appellants as "Guarantors" throughout. In this case, it is explained that funding for the Project initially relied on the appellants and at later stages they infused additional funds. The appellants were totally involved in and had the ability to control the Project. The respondent was well aware that in order to complete construction of the Project, there was only the bank loan and personal funding from the appellants available to do so.

[33] Despite the very able argument of appellants' counsel, we are unable to agree with his submission. In our view the Cost Over-Run Provision contained in the Letter Agreement imposes primary obligations on the appellants.

[34] As the chambers judge noted, it is not surprising that the financial commitments of the appellants went beyond their $3,000,000 guarantees. The context thus explains the provision for any cost overruns which provided:

> Each of the Guarantors, [the appellants] for the consideration set forth in this agreement, severally undertakes with the Bank, knowing the Bank will be relying upon such undertaking in making credit available to the Borrower under this agreement, as follows:
>
> > (i) that the Project will be completed in accordance with the Project Schedule and within the Project Budget; and
> >
> > (ii) that, should the Project not be completed within the Project Budget, all cost overruns in excess of the aggregate costs set out in the Project Budget, any margin deficiencies or any debt servicing shortfalls, as they may occur or be identified by the Bank or the Project Monitor, shall forthwith be funded from those resources of the Guarantors, or any one of them, that are not already committed to the Project in accordance with this agreement.

[35] The Cost Over-Run Provision is expressed solely as an obligation of the appellants (being described as "Guarantors"). It is not conditional upon failure or default of the Borrower. The provision goes on to explain the consequences of failing to complete the Project or fund cost overruns will constitute a default by the Borrower. As the chambers judge explained, there are many reasons why lenders deem certain events to be acts of default including preserving the ability to stop advances and realize upon security. But even where the Borrower may be in default, the obligation

of the appellants does not change. The provision does not state that the appellants are obligated only for the Borrower's default. The appellants could also be in breach or called upon to fund the cost overruns.

[36] Additionally, the Letter Agreement provides that if the costs to complete exceed the undrawn loans, "The Borrower and the Guarantors [the appellants] will be severally liable to immediately cover any such deficiency as soon as it arises or is identified by the respondent or the Project Monitor." Being severally liable does not describe a guarantor.

[37] A plain reading of both of the above provisions shows that they impose obligations directly on the appellants. They are not secondary obligations in the event of the Borrower's default.

[38] The case authorities have held that if the language of the agreement does not make the obligation conditional upon failure of another, the obligation is direct and not a guarantee: *32262 BC Ltd v Pataki Enterprises*, 1998 ABCA 90, 216 AR 78 at para 11. Nor is it the case that where individuals are jointly and severally liable with a corporation, the obligations are conditional. Similarly, in *Standard Trust v Steel* (1991), 117 AR 241, 83 DLR (4th) 130 at page 142, this court stated:

> The appellant promised to perform. He did not promise to perform only if the corporation did not. As the trial judge stated, he cannot therefore rely upon the technical provisions of the *Guarantees Acknowledgement Act* to relieve him of the obligation to pay the debt.

[39] Here, having both a secondary and a primary obligation is explained by the separate rationales for the covenants given in the Letter Agreement and in the guarantees. In the Letter Agreement, the respondent intended that the Guarantors assume the risk of any cost overruns for completion of the Project. Once the Project was complete, the loan to the respondent was to be repaid by sales of the condominium units. The guarantees were intended to cover the risk that the market for sales of the condominiums would be insufficient to repay the respondent after the condominium units had been sold. In the case of this market risk, the appellants as guarantors had their respective liability limited to $3,000,000. each (being a total of $9,000,000 to the respondent).

[40] That there may be more than one obligation is recognized in the Letter Agreement under the provision for non-merger of obligations stating:

> The provisions of this agreement shall not merge with any security provided to the Bank, but shall continue in full force for the benefit of the parties hereto.

Preamble to the signatures

[41] The recognition that there are two separate obligations also helps interpret the preamble to the signatures of the individuals, which stated:

> We acknowledge and confirm our agreement with the foregoing terms and conditions, as Guarantors, as of August 31, 2007, and we specifically acknowledge and confirm our agreement with the provisions of the Cost Over-runs section of this Agreement.

[42] The first part of the preamble, "We acknowledge and confirm our agreement with the foregoing terms and conditions, as Guarantors" acknowledges the basis upon which the respondent would lend money and thus, put the appellants at risk for their guarantees. The second part, "... we specifically acknowledge and confirm our agreement with the provisions of the Cost Over-runs section of this Agreement", confirms their earlier obligations, not as guarantors of the Borrower's obligation, but to their agreement with the Cost Over-Run Provision.

[43] Indeed, that there were two separate obligations of the appellants was underscored by the signature page in the amending letter agreement dated September 23, 2008 which expressly stated:

> We acknowledge and consent to the foregoing, as Guarantors, as of September 23, 2008 and we confirm that, both our guarantee as well as our agreement to cost overruns as detailed in the Cost Overruns section of the Letter Agreement, remain in full force and effect.

Guarantors as a term of art

[44] The appellants submit that "as Guarantors" in the preamble to the signatures indicates their obligations throughout the agreement were only in the nature of guarantees. They submit that "Guarantors" is a term of art with a specific legal meaning and should be read as such. The agreement could have described them otherwise, but did not.

[45] In this case, the label is not determinative of the appellants' obligations. Under the Letter Agreement, "Guarantors" was specifically defined as being the three individual appellants. It is a term which collectively labels the three individuals. The chambers judge acknowledged that the choice of label was "ill-advised" where the individuals were intended to have primary obligations as well as secondary, and the parties agree that the drafting of the Letter Agreement was not well done. But in any event, it is the substance of the obligation, not the label, that determines whether or not it is a guarantee: *CIBC v Morgan* (1993), 143 AR 36, [1993] 7 WWR 171 at para 32.

[46] In this case, the Cost Over-Run Provision of the Letter Agreement imposed direct obligations, not guarantees, upon the individuals collectively described as the "Guarantors" (ie. the appellants). This label does not alter the reality that the appellants had agreed with the respondent that the Project would be completed on schedule and within budget, and that they would fund cost

overruns if such were required. The need to fund the cost overruns was to ensure that the Project would be completed and be in a condition to ultimately sell.

[47] The chambers judge considered the respondent's requests for increased guarantees in 2008. He rejected the appellants' submission that the later requests suggest that the guarantees were the respondent's only recourse as he found the requests were equally consistent with a recognition by the respondent that unit sales to repay the loan might leave a shortfall. The chambers judge's factual inferences are to be afforded deference, and in any case, as he emphasized, the interpretation of the Letter Agreement does not depend on such evidence.

Contra proferentum

[48] For the reasons above, we agree with the chambers judge that the agreement was not ambiguous, therefore, *contra proferentum* has no application. Moreover, as this court has stated, the *contra proferentum* rule should not be invoked where there are sophisticated parties, represented by lawyers and each had a meaningful opportunity to participate in the negotiation of the instrument: *Ironside v Smith*, 1998 ABCA 366, 223 AR 379 at paras 66-67.

Conclusion

[49] The appellants have not shown that the chambers judge erred in his interpretation of the Letter Agreement and in particular, the Cost Over-Run Provision, and therefore this appeal is dismissed.

Appeal heard on November 10, 2011

Memorandum filed at Calgary, Alberta
this 8th day of December, 2011

Paperny J.A.

McDonald J.A.

O'Ferrall J.A.

Appearances:

C. Jensen, Q.C.
M.E. McCarty-Cameron
for the Appellants

M. Andrews, Q.C.
J. Francis
A. Kotkas
for the Respondent

TAB 20

Sattva Capital Corporation (formerly Sattva Capital Inc.) *Appellant*

v.

Creston Moly Corporation (formerly Georgia Ventures Inc.) *Respondent*

and

Attorney General of British Columbia and BCICAC Foundation *Interveners*

Sattva Capital Corporation (anciennement Sattva Capital Inc.) *Appelante*

c.

Creston Moly Corporation (anciennement Georgia Ventures Inc.) *Intimée*

et

Procureur général de la Colombie-Britannique et BCICAC Foundation *Intervenants*

Indexed as: Sattva Capital Corp. *v.* Creston Moly Corp.

2014 SCC 53

File No.: 35026.

2013: December 12; 2014: August 1.

Present: McLachlin C.J. and LeBel, Abella, Rothstein, Moldaver, Karakatsanis and Wagner JJ.

Répertorié : Sattva Capital Corp. *c.* Creston Moly Corp.

2014 CSC 53

N° du greffe : 35026.

2013 : 12 décembre; 2014 : 1er août.

Présents : La juge en chef McLachlin et les juges LeBel, Abella, Rothstein, Moldaver, Karakatsanis et Wagner.

ON APPEAL FROM THE COURT OF APPEAL FOR BRITISH COLUMBIA

Arbitration — Appeals — Commercial arbitration awards — Parties entering into agreement providing for payment of finder's fee in shares — Parties disagreeing as to date on which to price shares for payment of finder's fee and entering into arbitration — Leave to appeal arbitral award sought pursuant to s. 31(2) of the Arbitration Act — Leave to appeal denied but granted on appeal to Court of Appeal — Appeal of award dismissed but dismissal reversed by Court of Appeal — Whether Court of Appeal erred in granting leave to appeal — What is appropriate standard of review to be applied to commercial arbitral decisions made under Arbitration Act — Arbitration Act, R.S.B.C. 1996, c. 55, s. 31(2).

Contracts — Interpretation — Parties entering into agreement providing for payment of finder's fee in shares — Parties disagreeing as to date on which to price the shares for payment of finder's fee and entering into arbitration — Whether arbitrator reasonably construed contract

EN APPEL DE LA COUR D'APPEL DE LA COLOMBIE-BRITANNIQUE

Arbitrage — Appels — Sentences arbitrales commerciales — Conclusion d'une entente entre les parties prévoyant le versement en actions des honoraires d'intermédiation — Désaccord des parties sur la date applicable à l'évaluation du cours de l'action aux fins du versement des honoraires d'intermédiation et recours à l'arbitrage — Autorisation d'appel de la sentence arbitrale demandée en application de l'art. 31(2) de l'Arbitration Act — Rejet initial de la demande d'autorisation d'appel, qui est accueillie à l'issue d'un appel devant la Cour d'appel — Rejet de l'appel interjeté de la sentence infirmé par la Cour d'appel — La Cour d'appel a-t-elle accordé à tort l'autorisation d'appel? — Quelle est la norme de contrôle applicable aux sentences arbitrales commerciales rendues sous le régime de l'Arbitration Act? — Arbitration Act, R.S.B.C. 1996, ch. 55, art. 31(2).

Contrats — Interprétation — Conclusion d'une entente entre les parties prévoyant le versement en actions des honoraires d'intermédiation — Désaccord des parties sur la date applicable à l'évaluation du cours de l'action aux fins du versement des honoraires d'intermédiation

as a whole — Whether contractual interpretation is question of law or of mixed fact and law.

S and C entered into an agreement that required C to pay S a finder's fee in relation to the acquisition of a molybdenum mining property by C. The parties agreed that under this agreement, S was entitled to a finder's fee of US$1.5 million and was entitled to be paid this fee in shares of C. However, they disagreed on which date should be used to price the shares and therefore the number of shares to which S was entitled. S argued that the share price was dictated by the date set out in the Market Price definition in the agreement and therefore that it should receive approximately 11,460,000 shares priced at $0.15. C claimed that the agreement's "maximum amount" proviso prevented S from receiving shares valued at more than US$1.5 million on the date the fee was payable, and therefore that S should receive approximately 2,454,000 shares priced at $0.70. The parties entered into arbitration pursuant to the B.C. *Arbitration Act* and the arbitrator found in favour of S. C sought leave to appeal the arbitrator's decision pursuant to s. 31(2) of the *Arbitration Act*, but leave was denied on the basis that the question on appeal was not a question of law. The Court of Appeal reversed the decision and granted C's application for leave to appeal, finding that the arbitrator's failure to address the meaning of the agreement's "maximum amount" proviso raised a question of law. The superior court judge on appeal dismissed C's appeal, holding that the arbitrator's interpretation of the agreement was correct. The Court of Appeal allowed C's appeal, finding that the arbitrator reached an absurd result. S appeals the decisions of the Court of Appeal that granted leave and that allowed the appeal.

Held: The appeal should be allowed and the arbitrator's award reinstated.

Appeals from commercial arbitration decisions are narrowly circumscribed under the *Arbitration Act*. Under s. 31(1), they are limited to questions of law, and leave to appeal is required if the parties do not consent to the appeal. Section 31(2)(a) sets out the requirements for leave at issue in the present case: the court may grant leave if it determines that the result is important to the parties and

et recours à l'arbitrage — L'arbitre a-t-il donné une interprétation raisonnable de l'entente dans son ensemble? — L'interprétation contractuelle constitue-t-elle une question de droit ou une question mixte de fait et de droit?

S et C ont conclu une entente selon laquelle C devait payer à S des honoraires d'intermédiation relativement à l'acquisition d'une propriété minière de molybdène par C. Les parties reconnaissaient qu'en vertu de l'entente, S a droit à des honoraires d'intermédiation de 1,5 million $US, versés en actions de C. Cependant, elles ne s'entendaient pas sur la date qui devrait être retenue pour évaluer le cours de l'action et, par conséquent, sur le nombre d'actions que S doit recevoir. S prétendait que la valeur de l'action était dictée par la date établie dans la définition du cours prévue dans l'entente et, par conséquent, qu'elle devait recevoir environ 11 460 000 actions, à raison de 0,15 $ l'unité. C prétendait que la stipulation relative au « plafond », qui figure dans l'entente, empêchait S de recevoir des actions d'une valeur supérieure à 1,5 million $US à la date du versement des honoraires et donc que S devait obtenir environ 2 454 000 actions, à raison de 0,70 $ l'unité. Les parties ont soumis le différend à l'arbitrage conformément à l'*Arbitration Act* de la Colombie-Britannique et l'arbitre a statué en faveur de S. C a demandé l'autorisation d'interjeter appel de la sentence arbitrale en vertu du par. 31(2) de l'*Arbitration Act*. La demande a été rejetée au motif que la question soulevée n'était pas une question de droit. La Cour d'appel a infirmé la décision et accueilli la demande, présentée par C, en autorisation d'interjeter appel, jugeant que l'omission par l'arbitre d'examiner la signification de la stipulation de l'entente relative au « plafond » soulevait une question de droit. Le juge de la cour supérieure saisi de l'appel a rejeté l'appel de C et conclu que l'interprétation de l'entente par l'arbitre était correcte. La Cour d'appel a accueilli l'appel de C, concluant que l'interprétation de l'arbitre menait à un résultat absurde. S interjette appel des décisions de la Cour d'appel ayant accordé l'autorisation d'appel et ayant accueilli l'appel.

Arrêt : Le pourvoi est accueilli et la sentence arbitrale est rétablie.

L'appel d'une sentence arbitrale commerciale est étroitement circonscrit par l'*Arbitration Act*. Aux termes du par. 31(1), il ne peut être interjeté appel que sur une question de droit, et l'autorisation d'appel est requise lorsque les parties ne consentent pas à l'appel. L'alinéa 31(2)(a) énonce les critères d'autorisation sur lesquels porte le présent litige, à savoir que le tribunal peut accorder

the determination of the point of law may prevent a miscarriage of justice.

In the case at bar, the Court of Appeal erred in finding that the construction of the finder's fee agreement constituted a question of law. Such an exercise raises a question of mixed fact and law, and therefore, the Court of Appeal erred in granting leave to appeal.

The historical approach according to which determining the legal rights and obligations of the parties under a written contract was considered a question of law should be abandoned. Contractual interpretation involves issues of mixed fact and law as it is an exercise in which the principles of contractual interpretation are applied to the words of the written contract, considered in light of the factual matrix of the contract.

It may be possible to identify an extricable question of law from within what was initially characterized as a question of mixed fact and law; however, the close relationship between the selection and application of principles of contractual interpretation and the construction ultimately given to the instrument means that the circumstances in which a question of law can be extricated from the interpretation process will be rare. The goal of contractual interpretation, to ascertain the objective intentions of the parties, is inherently fact specific. Accordingly, courts should be cautious in identifying extricable questions of law in disputes over contractual interpretation. Legal errors made in the course of contractual interpretation include the application of an incorrect principle, the failure to consider a required element of a legal test, or the failure to consider a relevant factor. Concluding that C's application for leave to appeal raised no question of law is sufficient to dispose of this appeal; however, the Court found it salutary to continue with its analysis.

In order to rise to the level of a miscarriage of justice for the purposes of s. 31(2)(a), an alleged legal error must pertain to a material issue in the dispute which, if decided differently, would affect the result of the case. According to this standard, a determination of a point of law "may prevent a miscarriage of justice" only where the appeal itself has some possibility of succeeding. An appeal with no chance of success will not meet the threshold of "may prevent a miscarriage of justice" because there would be no chance that the outcome of the appeal would cause a change in the final result of the case.

l'autorisation s'il estime que, selon le cas, l'issue est importante pour les parties et que le règlement de la question de droit peut permettre d'éviter une erreur judiciaire.

En l'espèce, la Cour d'appel a assimilé à tort l'interprétation de l'entente relative aux honoraires d'intermédiation à une question de droit. Un tel exercice soulève une question mixte de fait et de droit, et la Cour d'appel a donc commis une erreur en accueillant la demande d'autorisation d'appel.

Il faut rompre avec l'approche historique selon laquelle la détermination des droits et obligations juridiques des parties à un contrat écrit ressortit à une question de droit. L'interprétation contractuelle soulève des questions mixtes de fait et de droit, car il s'agit d'en appliquer les principes aux termes figurant dans le contrat écrit, à la lumière du fondement factuel de ce dernier.

Il peut se révéler possible de dégager une pure question de droit de ce qui paraît au départ constituer une question mixte de fait et de droit, mais le rapport étroit qui existe entre, d'une part, le choix et l'application des principes d'interprétation contractuelle et, d'autre part, l'interprétation que recevra l'instrument juridique en dernière analyse fait en sorte que rares seront les circonstances dans lesquelles il sera possible d'isoler une question de droit au cours de l'exercice d'interprétation. Le but de l'interprétation contractuelle — déterminer l'intention objective des parties — est, de par sa nature même, axé sur les faits. Par conséquent, le tribunal doit faire preuve de prudence avant d'isoler une question de droit dans un litige portant sur l'interprétation contractuelle. L'interprétation contractuelle peut occasionner des erreurs de droit, notamment appliquer le mauvais principe ou négliger un élément essentiel d'un critère juridique ou un facteur pertinent. Conclure que la demande d'autorisation d'appel présentée par C ne soulevait aucune question de droit suffit à trancher le présent pourvoi; toutefois, la Cour juge salutaire de poursuivre l'analyse.

Pour que l'erreur de droit reprochée soit une erreur judiciaire pour l'application de l'al. 31(2)(a), elle doit se rapporter à une question importante en litige qui, si elle était tranchée différemment, aurait une incidence sur le résultat. Suivant cette norme, le règlement d'un point de droit « peut permettre d'éviter une erreur judiciaire » seulement lorsqu'il existe une certaine possibilité que l'appel soit accueilli. Un appel qui est voué à l'échec ne saurait « permettre d'éviter une erreur judiciaire » puisque les possibilités que l'issue d'un tel appel joue sur le résultat final du litige sont nulles.

At the leave stage, it is not appropriate to consider the full merits of a case and make a final determination regarding whether an error of law was made. However, some preliminary consideration of the question of law by the leave court is necessary to determine whether the appeal has the potential to succeed and thus to change the result in the case. The appropriate threshold for assessing the legal question at issue under s. 31(2) is whether it has arguable merit, meaning that the issue raised by the applicant cannot be dismissed through a preliminary examination of the question of law.

Assessing whether the issue raised by an application for leave to appeal has arguable merit must be done in light of the standard of review on which the merits of the appeal will be judged. This requires a preliminary assessment of the standard of review. The leave court's assessment of the standard of review is only preliminary and does not bind the court which considers the merits of the appeal.

The words "may grant leave" in s. 31(2) of the *Arbitration Act* confer on the court residual discretion to deny leave even where the requirements of s. 31(2) are met. Discretionary factors to consider in a leave application under s. 31(2)(a) include: conduct of the parties, existence of alternative remedies, undue delay and the urgent need for a final answer. These considerations could be a sound basis for declining leave to appeal an arbitral award even where the statutory criteria have been met. However, courts should exercise such discretion with caution.

Appellate review of commercial arbitration awards is different from judicial review of a decision of a statutory tribunal, thus the standard of review framework developed for judicial review in *Dunsmuir v. New Brunswick*, 2008 SCC 9, [2008] 1 S.C.R. 190, and the cases that followed it, is not entirely applicable to the commercial arbitration context. Nevertheless, judicial review of administrative tribunal decisions and appeals of arbitration awards are analogous in some respects. As a result, aspects of the *Dunsmuir* framework are helpful in determining the appropriate standard of review to apply in the case of commercial arbitration awards.

Ce n'est pas à l'étape de l'autorisation qu'il convient d'examiner exhaustivement le fond du litige et de se prononcer définitivement sur l'absence ou l'existence d'une erreur de droit. Cependant, le tribunal saisi de la demande d'autorisation doit procéder à un examen préliminaire de la question de droit pour déterminer si l'appel a une chance d'être accueilli et, par conséquent, de modifier l'issue du litige. Ce qu'il faut démontrer, pour l'application du par. 31(2), c'est que la question de droit invoquée a un fondement défendable, à savoir que l'argument soulevé par le demandeur ne peut être rejeté à l'issue d'un examen préliminaire de la question de droit.

L'examen visant à décider si la question soulevée dans la demande d'autorisation d'appel a un fondement défendable doit se faire à la lumière de la norme de contrôle applicable à l'analyse du bien-fondé de l'appel. Il faut donc procéder à un examen préliminaire ayant pour objet cette norme. Le tribunal saisi de la demande d'autorisation ne procède qu'à un examen préliminaire à l'égard de la norme de contrôle, qui ne lie pas celui qui se penchera sur le bien-fondé de l'appel.

Les termes « peut accorder l'autorisation » figurant au par. 31(2) de l'*Arbitration Act* confèrent au tribunal un pouvoir discrétionnaire résiduel qui lui permet de refuser l'autorisation même quand les critères prévus par la disposition sont respectés. Les facteurs à prendre en considération dans l'exercice du pouvoir discrétionnaire à l'égard d'une demande d'autorisation présentée en vertu de l'al. 31(2)(a) comprennent : la conduite des parties, l'existence d'autres recours, un retard indu et le besoin urgent d'obtenir un règlement définitif. Ces facteurs pourraient justifier le rejet de la demande sollicitant l'autorisation d'interjeter appel d'une sentence arbitrale même dans le cas où il est satisfait aux critères légaux. Cependant, les tribunaux devraient faire preuve de prudence dans l'exercice de ce pouvoir discrétionnaire.

L'examen en appel des sentences arbitrales commerciales diffère du contrôle judiciaire d'une décision rendue par un tribunal administratif, de sorte que le cadre relatif à la norme de contrôle judiciaire établi dans l'arrêt *Dunsmuir c. Nouveau-Brunswick*, 2008 CSC 9, [2008] 1 R.C.S. 190, et les arrêts rendus depuis, ne peut être tout à fait transposé dans le contexte de l'arbitrage commercial. Il demeure que le contrôle judiciaire d'une décision rendue par un tribunal administratif et l'appel d'une sentence arbitrale se ressemblent dans une certaine mesure. Par conséquent, certains éléments du cadre établi dans l'arrêt *Dunsmuir* aident à déterminer le degré de déférence qu'il convient d'accorder aux sentences arbitrales commerciales.

In the context of commercial arbitration, where appeals are restricted to questions of law, the standard of review will be reasonableness unless the question is one that would attract the correctness standard, such as constitutional questions or questions of law of central importance to the legal system as a whole and outside the adjudicator's expertise. The question at issue here does not fall into one of those categories and thus the standard of review in this case is reasonableness.

En matière d'arbitrage commercial, la possibilité d'interjeter appel étant subordonnée à l'existence d'une question de droit, la norme de contrôle est celle de la décision raisonnable, à moins que la question n'appartienne à celles qui entraînent l'application de la norme de la décision correcte, comme les questions constitutionnelles ou les questions de droit qui revêtent une importance capitale pour le système juridique dans son ensemble et qui sont étrangères au domaine d'expertise du décideur. La question dont nous sommes saisis n'appartient pas à l'une ou l'autre de ces catégories; la norme de la décision raisonnable s'applique donc à la présente affaire.

In the present case, the arbitrator reasonably construed the contract as a whole in determining that S is entitled to be paid its finder's fee in shares priced at $0.15. The arbitrator's decision that the shares should be priced according to the Market Price definition gives effect to both that definition and the "maximum amount" proviso and reconciles them in a manner that cannot be said to be unreasonable. The arbitrator's reasoning meets the reasonableness threshold of justifiability, transparency and intelligibility.

En l'espèce, l'arbitre a donné une interprétation raisonnable de l'entente considérée dans son ensemble en déterminant que S était en droit de recevoir ses honoraires d'intermédiation en actions, à raison de 0,15 $ l'action. La sentence arbitrale, selon laquelle l'action devrait être évaluée en fonction de la définition du cours, donne effet à cette dernière et à la stipulation relative au « plafond » en les conciliant d'une manière qui ne peut être considérée comme déraisonnable. Le raisonnement de l'arbitre satisfait à la norme du caractère raisonnable dont les attributs sont la justification, la transparence et l'intelligibilité.

A court considering whether leave should be granted is not adjudicating the merits of the case. It decides only whether the matter warrants granting leave, not whether the appeal will be successful, even where the determination of whether to grant leave involves a preliminary consideration of the question of law at issue. For this reason, comments by a leave court regarding the merits cannot bind or limit the powers of the court hearing the actual appeal.

Le tribunal chargé de statuer sur une demande d'autorisation ne tranche pas l'affaire sur le fond. Il détermine uniquement s'il est justifié d'accorder l'autorisation, et non si l'appel sera accueilli, même lorsque l'étude de la demande d'autorisation appelle un examen préliminaire de la question de droit en cause. C'est pourquoi les remarques sur le bien-fondé de l'affaire formulées par le tribunal saisi de la demande d'autorisation ne sauraient lier le tribunal chargé de statuer sur l'appel ni restreindre ses pouvoirs.

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Michael A. Feder and *Tammy Shoranick*, for the appellant.

Darrell W. Roberts, *Q.C.*, and *David Mitchell*, for the respondent.

Jonathan Eades and *Micah Weintraub*, for the intervener the Attorney General of British Columbia.

David Wotherspoon and *Gavin R. Cameron*, for the intervener the BCICAC Foundation.

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Michael A. Feder et *Tammy Shoranick*, pour l'appelante.

Darrell W. Roberts, *c.r.*, et *David Mitchell*, pour l'intimée.

Jonathan Eades et *Micah Weintraub*, pour l'intervenant le procureur général de la Colombie-Britannique.

David Wotherspoon et *Gavin R. Cameron*, pour l'intervenante BCICAC Foundation.

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I. Facts

[2] The issues in this case arise out of the obligation of Creston Moly Corporation (formerly Georgia Ventures Inc.) to pay a finder's fee to Sattva Capital

Version française du jugement de la Cour rendu par

[1] Le juge Rothstein — Dans quelles circonstances l'interprétation contractuelle est-elle une question mixte de fait et de droit et dans quelles circonstances est-elle une question de droit? Comment établir l'équilibre entre le caractère révisable et l'irrévocabilité des sentences arbitrales commerciales prononcées sous le régime de la *Commercial Arbitration Act*, R.S.B.C. 1996, ch. 55 (maintenant l'*Arbitration Act*, ci-après l'« *AA* »)? Les conclusions relatives au bien-fondé de l'appel tirées par le tribunal qui autorise l'appel peuvent-elles lier celui qui est appelé à trancher l'appel? Voilà trois questions qui sont soulevées dans le présent pourvoi.

I. Faits

[2] Les questions soulevées dans le présent pourvoi découlent de l'obligation de Creston Moly Corporation (anciennement Georgia Ventures Inc.) de

Corporation (formerly Sattva Capital Inc.). The parties agree that Sattva is entitled to a finder's fee of US$1.5 million and is entitled to be paid this fee in shares of Creston, cash or a combination thereof. They disagree on which date should be used to price the Creston shares and therefore the number of shares to which Sattva is entitled.

[3] Mr. Hai Van Le, a principal of Sattva, introduced Creston to the opportunity to acquire a molybdenum mining property in Mexico. On January 12, 2007, the parties entered into an agreement (the "Agreement") that required Creston to pay Sattva a finder's fee in relation to the acquisition of this property. The relevant provisions of the Agreement are set out in Appendix I.

[4] On January 30, 2007, Creston entered into an agreement to purchase the property for US$30 million. On January 31, 2007, at the request of Creston, trading of Creston's shares on the TSX Venture Exchange ("TSXV") was halted to prevent speculation while Creston completed due diligence in relation to the purchase. On March 26, 2007, Creston announced it intended to complete the purchase and trading resumed the following day.

[5] The Agreement provides that Sattva was to be paid a finder's fee equal to the maximum amount that could be paid pursuant to s. 3.3 of Policy 5.1 in the TSXV Policy Manual. Section 3.3 of Policy 5.1 is incorporated by reference into the Agreement at s. 3.1 and is set out in Appendix II of these reasons. The maximum amount pursuant to s. 3.3 of Policy 5.1 in this case is US$1.5 million.

[6] According to the Agreement, by default, the fee would be paid in Creston shares. The fee would only be paid in cash or a combination of shares and cash if Sattva made such an election. Sattva made no such election and was therefore entitled to be paid the fee in shares. The finder's fee was to be paid no later than five working days after the closing of the transaction purchasing the molybdenum mining property.

payer des honoraires d'intermédiation à Sattva Capital Corporation (anciennement Sattva Capital Inc.). Les parties reconnaissent que Sattva a droit à des honoraires d'intermédiation de 1,5 million $US, qui peuvent lui être versés en argent, en actions de Creston, ou en argent et en actions. Elles ne s'entendent pas sur la date qui devrait être retenue pour évaluer le cours de l'action et, par conséquent, sur le nombre d'actions que Sattva recevra.

[3] M. Hai Van Le, un directeur de Sattva, a fait part à Creston de la possibilité d'acquérir une propriété minière de molybdène au Mexique. Le 12 janvier 2007, les parties ont conclu une entente (l'« entente »), selon laquelle Creston devait payer à Sattva des honoraires d'intermédiation relativement à l'acquisition de cette propriété. Les dispositions pertinentes de l'entente sont énoncées à l'annexe I.

[4] Le 30 janvier 2007, Creston a conclu une convention d'achat de la propriété, le prix étant fixé à 30 millions $US. Le 31 janvier 2007, Creston a demandé que la négociation de ses actions à la Bourse de croissance TSX (la « Bourse ») soit suspendue afin d'empêcher la spéculation le temps d'achever le contrôle diligent préalable à l'achat. Le 26 mars 2007, Creston a annoncé qu'elle avait l'intention de conclure l'achat, et la négociation à la bourse a repris le lendemain.

[5] Aux termes de l'entente, Sattva doit recevoir des honoraires d'intermédiation correspondant au plafond autorisé par le point 3.3 de la politique 5.1 qui se trouve dans le Guide du financement des sociétés de la Bourse. Le point 3.3 est incorporé par renvoi à l'entente, à l'art. 3.1, et il est reproduit à l'annexe II des présents motifs. Dans le cas qui nous occupe, le plafond autorisé au point 3.3 de la politique 5.1 est de 1,5 million $US.

[6] Aux termes de l'entente, à moins d'indication contraire, les honoraires sont payés sous forme d'actions de Creston. Ils ne seraient versés en argent ou en argent et en actions que si Sattva avait indiqué avoir fait tel choix, ce qu'elle n'a pas fait. Ses honoraires devaient donc lui être versés sous forme d'actions au plus tard cinq jours ouvrables après la conclusion de l'achat de la propriété minière de molybdène.

[7] The dispute between the parties concerns which date should be used to determine the price of Creston shares and thus the number of shares to which Sattva is entitled. Sattva argues that the share price is dictated by the Market Price definition at s. 2 of the Agreement, i.e. the price of the shares "as calculated on close of business day before the issuance of the press release announcing the Acquisition". The press release announcing the acquisition was released on March 26, 2007. Prior to the halt in trading on January 31, 2007, the last closing price of Creston shares was $0.15. On this interpretation, Sattva would receive approximately 11,460,000 shares (based on the finder's fee of US$1.5 million).

[8] Creston claims that the Agreement's "maximum amount" proviso means that Sattva cannot receive cash or shares valued at more than US$1.5 million on the date the fee is payable. The shares were payable no later than five days after May 17, 2007, the closing date of the transaction. At that time, the shares were priced at $0.70 per share. This valuation is based on the price an investment banking firm valued Creston at as part of underwriting a private placement of shares on April 17, 2007. On this interpretation, Sattva would receive approximately 2,454,000 shares, some 9 million fewer shares than if the shares were priced at $0.15 per share.

[9] The parties entered into arbitration pursuant to the *AA*. The arbitrator found in favour of Sattva. Creston sought leave to appeal the arbitrator's decision pursuant to s. 31(2) of the *AA*. Leave was denied by the British Columbia Supreme Court (2009 BCSC 1079 (CanLII) ("SC Leave Court")). Creston successfully appealed this decision and was granted leave to appeal the arbitrator's decision by the British Columbia Court of Appeal (2010 BCCA 239, 7 B.C.L.R. (5th) 227 ("CA Leave Court")).

[10] The British Columbia Supreme Court judge who heard the merits of the appeal (2011 BCSC

[7] Le différend qui oppose les parties porte sur la date à retenir pour fixer le cours de l'action de Creston et, par conséquent, le nombre d'actions auquel Sattva a droit. Cette dernière prétend que la valeur de l'action est dictée par la définition du « cours », à l'art. 2 de l'entente, c.-à-d. la valeur de l'action [TRADUCTION] « le dernier jour ouvrable avant la publication du communiqué de presse annonçant l'acquisition ». Le communiqué de presse a été publié le 26 mars 2007. Avant la suspension de la négociation des actions le 31 janvier 2007, le dernier cours de clôture de l'action de Creston s'établissait à 0,15 $. Suivant cette interprétation, Sattva recevrait environ 11 460 000 actions (selon le calcul effectué en fonction des honoraires d'intermédiation de 1,5 million $US).

[8] Creston prétend que la stipulation relative au « plafond », qui figure dans l'entente, a pour effet de limiter à 1,5 million $US la somme d'argent ou la valeur des actions que peut recevoir Sattva à la date de versement des honoraires. Les actions devaient être cédées au plus tard cinq jours après le 17 mai 2007, date de conclusion de l'achat. À ce moment-là, l'action de Creston valait 0,70 $, selon les calculs effectués par une société bancaire d'investissement en vue d'un placement privé par voie de prise ferme le 17 avril 2007. Suivant cette interprétation, Sattva recevrait environ 2 454 000 actions, soit environ 9 millions d'actions de moins que si chacune valait 0,15 $.

[9] Les parties ont soumis le différend à l'arbitrage conformément à l'*AA*. L'arbitre a statué en faveur de Sattva. Creston a demandé l'autorisation d'interjeter appel de la sentence arbitrale en vertu du par. 31(2) de l'*AA*. La Cour suprême de la Colombie-Britannique a refusé l'autorisation (2009 BCSC 1079 (CanLII) (« formation de la CS saisie de la demande d'autorisation »)). Creston a appelé de cette décision et obtenu l'autorisation de la Cour d'appel de la Colombie-Britannique d'interjeter appel de la sentence arbitrale (2010 BCCA 239, 7 B.C.L.R. (5th) 227 (« formation de la CA saisie de la demande d'autorisation »)).

[10] Le juge de la Cour suprême de la Colombie-Britannique chargé de statuer sur le bien-fondé de

597, 84 B.L.R. (4th) 102 ("SC Appeal Court")) upheld the arbitrator's award. Creston appealed that decision to the British Columbia Court of Appeal (2012 BCCA 329, 36 B.C.L.R. (5th) 71 ("CA Appeal Court")). That court overturned the SC Appeal Court and found in favour of Creston. Sattva appeals the decisions of the CA Leave Court and CA Appeal Court to this Court.

II. Arbitral Award

[11] The arbitrator, Leon Getz, Q.C., found in favour of Sattva, holding that it was entitled to receive its US$1.5 million finder's fee in shares priced at $0.15 per share.

[12] The arbitrator based his decision on the Market Price definition in the Agreement:

> What, then, was the "Market Price" within the meaning of the Agreement? The relevant press release is that issued on March 26 . . . . Although there was no closing price on March 25 (the shares being on that date halted), the "last closing price" within the meaning of the definition was the $0.15 at which the [Creston] shares closed on January 30, the day before trading was halted "pending news" . . . . This conclusion requires no stretching of the words of the contractual definition; on the contrary, it falls literally within those words. [para. 22]

[13] Both the Agreement and the finder's fee had to be approved by the TSXV. Creston was responsible for securing this approval. The arbitrator found that it was either an implied or an express term of the Agreement that Creston would use its best efforts to secure the TSXV's approval and that Creston did not apply its best efforts to this end.

[14] As previously noted, by default, the finder's fee would be paid in shares unless Sattva made an election otherwise. The arbitrator found that

l'appel (2011 BCSC 597, 84 B.L.R. (4th) 102 (« formation de la CS saisie de l'appel »)) a confirmé la sentence arbitrale. Creston a interjeté appel de cette décision devant la Cour d'appel de la Colombie-Britannique (2012 BCCA 329, 36 B.C.L.R. (5th) 71 (« formation de la CA saisie de l'appel »)), laquelle a infirmé la décision de la formation de la CS saisie de l'appel et a donné gain de cause à Creston. Sattva interjette appel des décisions des deux formations de la CA, soit celle saisie de la demande d'autorisation et celle saisie de l'appel, devant la Cour.

II. Sentence arbitrale

[11] L'arbitre, Leon Getz, c.r., a donné gain de cause à Sattva, concluant qu'elle était en droit de recevoir des honoraires d'intermédiation de 1,5 million $US en actions, à raison de 0,15 $ l'action.

[12] L'arbitre a fondé sa décision sur la définition du « cours » figurant dans l'entente :

> [TRADUCTION] Qu'était donc le « cours » au sens de l'entente? Le communiqué de presse pertinent est celui qui a été publié le 26 mars [. . .] Il n'y avait pas de cours de clôture le 25 mars (la négociation des actions était suspendue à cette date). Par conséquent, le « dernier cours de clôture », au sens où cette expression est employée dans la définition, était de 0,15 $, soit le cours de clôture des actions de [Creston] le 30 janvier, le jour précédant la suspension des opérations « jusqu'à nouvel ordre » [. . .] Cette conclusion ne nécessite aucune extension de sens des mots employés dans la définition qui figure au contrat. Au contraire, elle concorde littéralement avec la définition. [par. 22]

[13] L'entente et les honoraires d'intermédiation devaient être approuvés par la Bourse. Creston était chargée d'obtenir cette approbation. L'arbitre a conclu qu'il était implicitement ou expressément prévu dans l'entente que Creston ferait de son mieux pour obtenir l'approbation de la Bourse. Selon lui, Creston n'avait pas fait de son mieux pour y arriver.

[14] Comme nous l'avons expliqué, les honoraires d'intermédiation se payaient en actions à moins d'avis contraire de la part de Sattva. L'arbitre a

Sattva never made such an election. Despite this, Creston represented to the TSXV that the finder's fee was to be paid in cash. The TSXV conditionally approved a finder's fee of US$1.5 million to be paid in cash. Sattva first learned that the fee had been approved as a cash payment in early June 2007. When Sattva raised this matter with Creston, Creston responded by saying that Sattva had the choice of taking the finder's fee in cash or in shares priced at $0.70.

[15] Sattva maintained that it was entitled to have the finder's fee paid in shares priced at $0.15. Creston asked its lawyer to contact the TSXV to clarify the minimum share price it would approve for payment of the finder's fee. The TSXV confirmed on June 7, 2007 over the phone and August 9, 2007 via email that the minimum share price that could be used to pay the finder's fee was $0.70 per share. The arbitrator found that Creston "consistently misrepresented or at the very least failed to disclose fully the nature of the obligation it had undertaken to Sattva" (para. 56(k)) and "that in the absence of an election otherwise, Sattva is entitled under that Agreement to have that fee paid in shares at $0.15" (para. 56(g)). The arbitrator found that the first time Sattva's position was squarely put before the TSXV was in a letter from Sattva's solicitor on October 9, 2007.

[16] The arbitrator found that had Creston used its best efforts, the TSXV could have approved the payment of the finder's fee in shares priced at $0.15 and such a decision would have been consistent with its policies. He determined that there was "a substantial probability that [TSXV] approval would have been given" (para. 81). He assessed that probability at 85 percent.

[17] The arbitrator found that Sattva could have sold its Creston shares after a four-month holding period at between $0.40 and $0.44 per share, netting proceeds of between $4,583,914 and $5,156,934.

conclu que Sattva n'avait pas manifesté de choix. Malgré cela, Creston a déclaré à la Bourse que les honoraires d'intermédiation seraient versés en argent. La Bourse a donc approuvé conditionnellement le versement d'une somme de 1,5 million $US en argent. Sattva a appris qu'un versement en argent de ses honoraires avait été approuvé au début du mois de juin 2007. Quand Sattva a abordé ce point avec Creston, cette dernière a répondu que Sattva avait le choix de percevoir ses honoraires en argent ou en actions, à raison de 0,70 $ l'action.

[15] Sattva a soutenu qu'elle avait droit au versement des honoraires d'intermédiation en actions, à raison de 0,15 $ l'action. Creston a demandé à ses avocats de communiquer avec la Bourse afin qu'elle indique la valeur minimale de l'action qu'elle approuverait pour le versement des honoraires d'intermédiation. La Bourse a confirmé, par téléphone le 7 juin 2007 et par courriel le 9 août de la même année, qu'un cours minimal de 0,70 $ l'action s'appliquait aux fins du calcul des honoraires d'intermédiation. Selon l'arbitre, Creston [TRADUCTION] « a constamment fait des déclarations inexactes quant à l'obligation qu'elle avait contractée envers Sattva ou, à tout le moins, omis d'en divulguer complètement la nature » (par. 56(k)) et qu'« à moins que Sattva n'en décide autrement, elle a le droit aux termes de l'entente de percevoir ces honoraires sous forme d'actions, à raison de 0,15 $ l'action » (par. 56(g)). Selon l'arbitre, la position de Sattva a été véritablement présentée à la Bourse pour la première fois dans la lettre de l'avocat de celle-ci datée du 9 octobre 2007.

[16] L'arbitre était d'avis que si Creston avait fait de son mieux, la Bourse aurait pu approuver le versement des honoraires d'intermédiation sous forme d'actions, à 0,15 $ l'action, et qu'une telle décision aurait été conforme à ses politiques. Il a affirmé que [TRADUCTION] « [la Bourse] aurait fort probablement donné son approbation » (par. 81) et il a évalué cette probabilité à 85 p. 100.

[17] Selon l'arbitre, Sattva aurait pu vendre ses actions de Creston après quatre mois à un prix variant entre 0,40 et 0,44 $ l'unité, ce qui aurait représenté un produit net situé dans une fourchette de

The arbitrator took the average of those two amounts, which came to $4,870,424, and then assessed damages at 85 percent of that number, which came to $4,139,860, and rounded it to $4,140,000 plus costs.

[18] After this award was made, Creston made a cash payment of US$1.5 million (or the equivalent in Canadian dollars) to Sattva. The balance of the damages awarded by the arbitrator was placed in the trust account of Sattva's solicitors.

III. Judicial History

A. *British Columbia Supreme Court — Leave to Appeal Decision, 2009 BCSC 1079*

[19] The SC Leave Court denied leave to appeal because it found the question on appeal was not a question of law as required under s. 31 of the *AA*. In the judge's view, the issue was one of mixed fact and law because the arbitrator relied on the "factual matrix" in coming to his conclusion. Specifically, determining how the finder's fee was to be paid involved examining "the TSX's policies concerning the maximum amount of the finder's fee payable, as well as the discretionary powers granted to the Exchange in determining that amount" (para. 35).

[20] The judge found that even had he found a question of law was at issue he would have exercised his discretion against granting leave because of Creston's conduct in misrepresenting the status of the finder's fee to the TSXV and Sattva, and "on the principle that one of the objectives of the [*AA*] is to foster and preserve the integrity of the arbitration system" (para. 41).

4 583 914 $ à 5 156 934 $. Établissant la moyenne de ces deux sommes d'argent à 4 870 424 $, l'arbitre a ensuite évalué les dommages-intérêts à 85 p. 100 de ce nombre, soit 4 139 860 $, qu'il a ensuite arrondis à la hausse, pour obtenir 4 140 000 $, plus les dépens.

[18] Après le prononcé de cette sentence arbitrale, Creston a versé 1,5 million $US (ou l'équivalent en dollars canadiens) à Sattva. Le solde des dommages-intérêts accordés par l'arbitre a été placé dans le compte en fiducie des avocats de Sattva.

III. Historique judiciaire

A. *Cour suprême de la Colombie-Britannique — décision sur la demande d'autorisation d'appel, 2009 BCSC 1079*

[19] La Cour suprême de la Colombie-Britannique a rejeté la demande d'autorisation d'appel parce qu'elle était d'avis que la question soulevée n'était pas une question de droit, un critère prévu à l'art. 31 de l'*AA*. Selon le juge, il s'agissait d'une question mixte de fait et de droit puisque l'arbitre avait appuyé sa conclusion sur le [TRADUCTION] « fondement factuel ». Plus précisément, pour déterminer sous quelle forme les honoraires d'intermédiation devaient être versés, il fallait examiner « les politiques de la TSX se rapportant au plafond applicable aux honoraires d'intermédiation, ainsi que les pouvoirs discrétionnaires dont dispose la Bourse pour déterminer le montant des honoraires » (par. 35).

[20] Le juge a conclu que, même s'il avait été d'avis que le litige soulevait une question de droit, il aurait exercé son pouvoir discrétionnaire pour refuser l'autorisation d'appel en raison des déclarations inexactes faites par Creston à propos des honoraires d'intermédiation à la Bourse et à Sattva, et par égard pour le [TRADUCTION] « principe selon lequel l'[*AA*] a notamment pour objectif de favoriser et de préserver l'intégrité du système d'arbitrage » (par. 41).

B. *British Columbia Court of Appeal — Leave to Appeal Decision, 2010 BCCA 239*

[21] The CA Leave Court reversed the SC Leave Court and granted Creston's application for leave to appeal the arbitral award. It found the SC Leave Court "err[ed] in failing to find that the arbitrator's failure to address the meaning of s. 3.1 of the Agreement (and in particular the 'maximum amount' provision) raised a question of law" (para. 23). The CA Leave Court decided that the construction of s. 3.1 of the Agreement, and in particular the "maximum amount" proviso, was a question of law because it did not involve reference to the facts of what the TSXV was told or what it decided.

[22] The CA Leave Court acknowledged that Creston was "less than forthcoming in its dealings with Mr. Le and the [TSXV]" but said that "these facts are not directly relevant to the question of law it advances on the appeal" (para. 27). With respect to the SC leave judge's reference to the preservation of the integrity of the arbitration system, the CA Leave Court said that the parties would have known when they chose to enter arbitration under the *AA* that an appeal on a question of law was possible. Additionally, while the finality of arbitration is an important factor in exercising discretion, when "a question of law arises on a matter of importance and a miscarriage of justice might be perpetrated if an appeal were not available, the integrity of the process requires, at least in the circumstances of this case, that the right of appeal granted by the legislation also be respected" (para. 29).

C. *British Columbia Supreme Court — Appeal Decision, 2011 BCSC 597*

[23] Armstrong J. reviewed the arbitrator's decision on a correctness standard. He dismissed the

B. *Cour d'appel de la Colombie-Britannique — décision sur la demande d'autorisation d'appel, 2010 BCCA 239*

[21] La Cour d'appel a infirmé la décision de la Cour suprême et a accueilli la demande, présentée par Creston, en autorisation d'interjeter appel de la sentence arbitrale. Selon elle, la Cour suprême avait [TRADUCTION] « commis une erreur en ne reconnaissant pas que l'omission par l'arbitre d'examiner la signification de l'art. 3.1 de l'entente (et plus particulièrement de la stipulation relative au "plafond") soulevait une question de droit » (par. 23). La Cour d'appel a conclu que l'interprétation de l'art. 3.1 de l'entente, et plus particulièrement de la stipulation relative au « plafond », constituait une question de droit parce qu'elle ne reposait pas sur les faits de l'affaire, à savoir les renseignements communiqués à la Bourse et la décision de cette dernière.

[22] La Cour d'appel a reconnu que Creston s'était montrée [TRADUCTION] « moins que franche dans ses démarches auprès de M. Le et de [la Bourse] », mais a déclaré que « ces faits n'intéressent pas directement la question de droit qu'elle soulève en appel » (par. 27). Au sujet de la remarque sur la préservation de l'intégrité du système d'arbitrage formulée par la formation de la CS saisie de la demande d'autorisation d'appel, la formation de la CA saisie de la demande d'autorisation a dit que les parties, quand elles ont choisi de soumettre leur différend à l'arbitrage en vertu de l'*AA*, savaient que l'appel d'une question de droit était possible. De plus, bien que l'irrévocabilité de la sentence arbitrale constitue un facteur important dans l'exercice du pouvoir discrétionnaire, lorsqu'« une question de droit importante est soulevée et qu'il y a risque d'erreur judiciaire en cas d'impossibilité d'interjeter appel, l'intégrité du processus exige, du moins dans les circonstances de l'espèce, que le droit d'appel conféré par la loi soit respecté » (par. 29).

C. *Cour suprême de la Colombie-Britannique — décision sur l'appel, 2011 BCSC 597*

[23] Le juge Armstrong a contrôlé la sentence arbitrale selon la norme de la décision correcte. Il

appeal, holding the arbitrator's interpretation of the Agreement was correct.

[24] Armstrong J. found that the plain and ordinary meaning of the Agreement required that the US$1.5 million fee be paid in shares priced at $0.15. He did not find the meaning to be absurd simply because the price of the shares at the date the fee became payable had increased in relation to the price determined according to the Market Price definition. He was of the view that changes in the price of shares over time are inevitable, and that the parties, as sophisticated business persons, would have reasonably understood a fluctuation in share price to be a reality when providing for a fee payable in shares. According to Armstrong J., it is indeed because of market fluctuations that it is necessary to choose a specific date to price the shares in advance of payment. He found that this was done by defining "Market Price" in the Agreement, and that the fee remained US$1.5 million in $0.15 shares as determined by the Market Price definition regardless of the price of the shares at the date that the fee was payable.

[25] According to Armstrong J., that the price of the shares may be more than the Market Price definition price when they became payable was foreseeable as a "natural consequence of the fee agreement" (para. 62). He was of the view that the risk was borne by Sattva, since the price of the shares could increase, but it could also decrease such that Sattva would have received shares valued at less than the agreed upon fee of US$1.5 million.

[26] Armstrong J. held that the arbitrator's interpretation which gave effect to both the Market Price definition and the "maximum amount" proviso should be preferred to Creston's interpretation of the agreement which ignored the Market Price definition.

[27] In response to Creston's argument that the arbitrator did not consider s. 3.1 of the Agreement

a rejeté l'appel et conclu que l'interprétation de l'entente proposée par l'arbitre était correcte.

[24] Le juge Armstrong estimait que, selon le sens ordinaire de l'entente, les honoraires de 1,5 million $US devaient être versés en actions, à raison de 0,15 $ l'unité. Il n'estimait pas une telle interprétation absurde du simple fait que le cours de l'action à la date du versement des honoraires était supérieur à celui déterminé suivant la définition du cours. Selon lui, avec le temps, la fluctuation des cours est inévitable, et dès lors qu'elles ont prévu la possibilité du versement des honoraires en actions, les parties, des entreprises averties, devaient raisonnablement s'attendre à la fluctuation du marché. De l'avis du juge Armstrong, c'est d'ailleurs à cause de cette fluctuation qu'il faut indiquer une date précise qui servira à déterminer la valeur de l'action avant le versement. Il est arrivé à la conclusion que pour ce faire, le « cours » était défini dans l'entente et que le montant des honoraires demeurait 1,5 million $US, à payer sous forme d'actions à raison de 0,15 $ l'unité, cette valeur étant établie suivant la définition du cours, sans égard à la valeur de l'action à la date du versement des honoraires.

[25] Selon le juge Armstrong, il était prévisible que le cours de l'action à la date du versement soit supérieur à celui établi conformément à la définition du cours et il s'agissait là d'une [TRADUCTION] « conséquence naturelle de l'entente relative aux honoraires d'intermédiation » (par. 62). Il était d'avis que le risque était assumé par Sattva, puisque le prix de l'action pouvait certes augmenter, mais il pouvait aussi diminuer, de sorte que Sattva aurait alors reçu un portefeuille d'actions d'une valeur inférieure au montant des honoraires (1,5 million $US) qui avait été convenu.

[26] Le juge Armstrong était d'avis que l'interprétation de l'arbitre, laquelle donnait effet à la définition du cours et à la stipulation relative au « plafond », était préférable à celle de Creston, qui faisait fi de la définition du cours.

[27] En réponse à l'argument de Creston selon lequel l'arbitre n'avait pas examiné l'art. 3.1 de

which contains the "maximum amount" proviso, Armstrong J. noted that the arbitrator explicitly addressed the "maximum amount" proviso at para. 23 of his decision.

D. *British Columbia Court of Appeal — Appeal Decision, 2012 BCCA 329*

[28] The CA Appeal Court allowed Creston's appeal, ordering that the payment of US$1.5 million that had been made by Creston to Sattva on account of the arbitrator's award constituted payment in full of the finder's fee. The court reviewed the arbitrator's decision on a standard of correctness.

[29] The CA Appeal Court found that both it and the SC Appeal Court were bound by the findings made by the CA Leave Court. There were two findings that were binding: (1) it would be anomalous if the Agreement allowed Sattva to receive US$1.5 million if it received its fee in cash, but shares valued at approximately $8 million if Sattva took its fee in shares; and (2) the arbitrator ignored this anomaly and did not address s. 3.1 of the Agreement.

[30] The Court of Appeal found that it was an absurd result to find that Sattva is entitled to an $8 million finder's fee in light of the fact that the "maximum amount" proviso in the Agreement limits the finder's fee to US$1.5 million. The court was of the view that the proviso limiting the fee to US$1.5 million "when paid" should be given paramount effect (para. 47). In its opinion, giving effect to the Market Price definition could not have been the intention of the parties, nor could it have been in accordance with good business sense.

IV. Issues

[31] The following issues arise in this appeal:

l'entente, qui contient la stipulation relative au « plafond », le juge Armstrong a souligné que l'arbitre avait fait expressément référence à cette stipulation au par. 23 de la sentence arbitrale.

D. *Cour d'appel de la Colombie-Britannique — décision sur l'appel, 2012 BCCA 329*

[28] La Cour d'appel a accueilli l'appel de Creston et a statué que la somme de 1,5 million $US versée par Creston en faveur de Sattva en exécution de la sentence arbitrale constituait le paiement intégral des honoraires d'intermédiation. La cour a contrôlé la sentence arbitrale suivant la norme de la décision correcte.

[29] La formation de la CA saisie de l'appel s'estimait liée, de même que la Cour suprême, par deux conclusions tirées par la formation de la CA saisie de la demande d'autorisation, à savoir : 1º il serait incongru que l'entente permette à Sattva, si elle opte pour le versement de ses honoraires en argent, de toucher 1,5 million $US alors que, si elle opte pour le versement sous forme d'actions, elle recevra un portefeuille valant environ 8 millions $ et 2º l'arbitre n'a pas tenu compte de cette anomalie et a fait fi de l'art. 3.1 de l'entente.

[30] Selon la Cour d'appel, conclure que Sattva avait droit à des honoraires d'intermédiation de 8 millions $ menait à un résultat absurde, étant donné la stipulation de l'entente relative au « plafond », qui limite le montant de tels honoraires à 1,5 million $US. La cour était d'avis qu'il faudrait donner l'effet prépondérant à cette stipulation qui limite à 1,5 million $US les honoraires [TRADUCTION] « à la date de leur versement » (par. 47). Elle était d'avis que donner effet à la définition du cours ne saurait avoir été l'intention des parties, et ce n'était pas non plus une décision sensée sur le plan commercial.

IV. Questions en litige

[31] Les questions suivantes sont soulevées dans le présent pourvoi :

(a) Is the issue of whether the CA Leave Court erred in granting leave under s. 31(2) of the *AA* properly before this Court?

(b) Did the CA Leave Court err in granting leave under s. 31(2) of the *AA*?

(c) If leave was properly granted, what is the appropriate standard of review to be applied to commercial arbitral decisions made under the *AA*?

(d) Did the arbitrator reasonably construe the Agreement as a whole?

(e) Did the CA Appeal Court err in holding that it was bound by comments regarding the merits of the appeal made by the CA Leave Court?

V. Analysis

A. *The Leave Issue Is Properly Before This Court*

[32] Sattva argues, in part, that the CA Leave Court erred in granting leave to appeal from the arbitrator's decision. In Sattva's view, the CA Leave Court did not identify a question of law, a requirement to obtain leave pursuant to s. 31(2) of the *AA*. Creston argues that this issue is not properly before this Court. Creston makes two arguments in support of this point.

[33] First, Creston argues that this issue was not advanced in Sattva's application for leave to appeal to this Court. This argument must fail. Unless this Court places restrictions in the order granting leave, the order granting leave is "at large". Accordingly, appellants may raise issues on appeal that were not set out in the leave application. However, the Court may exercise its discretion to refuse to deal with issues that were not addressed in the courts below, if there is prejudice to the respondent, or if for any other reason the Court considers it appropriate not to deal with a question.

a) La Cour a-t-elle été saisie à bon droit de la question de savoir si la Cour d'appel a commis une erreur en autorisant l'appel en vertu du par. 31(2) de l'*AA*?

b) La Cour d'appel a-t-elle commis une erreur en autorisant l'appel en vertu du par. 31(2) de l'*AA*?

c) Si l'autorisation a été accordée à bon droit, quelle norme de contrôle convient-il d'appliquer aux sentences arbitrales commerciales rendues sous le régime de l'*AA*?

d) L'arbitre a-t-il donné une interprétation raisonnable de l'entente dans son ensemble?

e) La Cour d'appel a-t-elle commis une erreur en s'estimant liée par les remarques formulées par la formation de la CA saisie de la demande d'autorisation au sujet du bien-fondé de l'appel?

V. Analyse

A. *Notre Cour est saisie à bon droit de la question de l'autorisation*

[32] Sattva prétend notamment que la Cour d'appel a commis une erreur en accordant l'autorisation d'interjeter appel de la sentence arbitrale. Selon elle, la Cour d'appel n'a cerné aucune question de droit, alors que l'autorisation est subordonnée à l'existence d'une telle question, aux termes du par. 31(2) de l'*AA*. Creston soutient que la Cour n'est pas saisie à bon droit de cette question et avance deux arguments à l'appui de sa position.

[33] Premièrement, Creston fait valoir que cette question n'était pas soulevée dans la demande d'autorisation d'appel que Sattva a présentée à la Cour. Cet argument ne saurait tenir. À moins que la Cour n'impose des restrictions dans l'ordonnance accordant l'autorisation, cette ordonnance est de « portée générale ». Par conséquent, l'appelant peut soulever en appel une question qui n'était pas énoncée dans la demande d'autorisation. La Cour peut toutefois exercer son pouvoir discrétionnaire et refuser de trancher une question qui n'a pas été abordée par les tribunaux d'instance inférieure, s'il en résulte un préjudice pour l'intimé, ou si, pour toute autre raison, elle juge opportun de ne pas la trancher.

[34] Here, this Court's order granting leave to appeal from both the CA Leave Court decision and the CA Appeal Court decision contained no restrictions (2013 CanLII 11315). The issue — whether the proposed appeal was on a question of law — was expressly argued before, and was dealt with in the judgments of, the SC Leave Court and the CA Leave Court. There is no reason Sattva should be precluded from raising this issue on appeal despite the fact it was not mentioned in its application for leave to appeal to this Court.

[35] Second, Creston argues that the issue of whether the CA Leave Court identified a question of law is not properly before this Court because Sattva did not contest this decision before all of the lower courts. Specifically, Creston states that Sattva did not argue that the question on appeal was one of mixed fact and law before the SC Appeal Court and that it conceded the issue on appeal was a question of law before the CA Appeal Court. This argument must also fail. At the SC Appeal Court, it was not open to Sattva to reargue the question of whether leave should have been granted. The SC Appeal Court was bound by the CA Leave Court's finding that leave should have been granted, including the determination that a question of law had been identified. Accordingly, Sattva could hardly be expected to reargue before the SC Appeal Court a question that had been determined by the CA Leave Court. There is nothing in the *AA* to indicate that Sattva could have appealed the leave decision made by a panel of the Court of Appeal to another panel of the same court. The fact that Sattva did not reargue the issue before the SC Appeal Court or CA Appeal Court does not prevent it from raising the issue before this Court, particularly since Sattva was also granted leave to appeal the CA Leave Court decision by this Court.

[34] En l'espèce, l'ordonnance accordant l'autorisation d'interjeter appel des deux décisions de la Cour d'appel, sur la demande d'autorisation d'appel et sur l'appel, ne comportait aucune restriction (2013 CanLII 11315). La question — à savoir si l'appel proposé soulevait une question de droit — a été expressément débattue devant les formations de la CS et de la CA saisies de la demande d'autorisation, qui l'ont tranchée. Rien n'empêche Sattva de soulever cette question en appel, même si elle ne l'a pas mentionnée dans la demande d'autorisation d'appel qu'elle a présentée à la Cour.

[35] Deuxièmement, Creston soutient que la Cour n'a pas été saisie à bon droit de la question de savoir si la formation de la CA saisie de la demande d'autorisation a cerné une question de droit parce que Sattva n'a pas contesté la décision rendue à ce sujet devant tous les tribunaux d'instance inférieure. Plus précisément, aux dires de Creston, Sattva n'aurait pas fait valoir devant la formation de la CS saisie de l'appel que l'appel soulevait une question mixte de fait et de droit et aurait reconnu devant la Cour d'appel que l'appel soulevait une question de droit. Un tel argument ne tient pas. Devant la formation de la CS saisie de l'appel, il n'était pas possible pour Sattva de débattre à nouveau de la question de savoir si l'autorisation aurait dû être accordée. La formation de la CS saisie de l'appel était liée par les conclusions tirées par la formation de la CA saisie de la demande d'autorisation, à savoir que l'autorisation était opportune et qu'une question de droit avait été cernée. Ainsi, Sattva ne pouvait guère plaider devant la formation de la CS saisie de l'appel un point sur lequel la formation de la CA saisie de la demande d'autorisation s'était déjà prononcée. Rien dans l'*AA* n'habilite Sattva à interjeter appel de la décision sur la demande d'autorisation d'appel rendue par une formation de la Cour d'appel à une autre formation de la même cour. Ce n'est pas parce que Sattva n'a pas plaidé à nouveau le point devant la formation de la CS saisie de l'appel ou devant la formation de la CA saisie de l'appel qu'elle ne peut le soulever devant notre Cour, tout particulièrement étant donné que Sattva a obtenu de notre Cour l'autorisation d'appeler de la décision rendue par la formation de la CA saisie de la demande d'autorisation.

[36] While this Court may decline to grant leave where an issue sought to be argued before it was not argued in the courts appealed from, that is not this case. Here, whether leave from the arbitrator's decision had been sought by Creston on a question of law or a question of mixed fact and law had been argued in the lower leave courts.

[37] Accordingly, the issue of whether the CA Leave Court erred in finding a question of law for the purposes of granting leave to appeal is properly before this Court.

B. *The CA Leave Court Erred in Granting Leave Under Section 31(2) of the AA*

(1) Considerations Relevant to Granting or Denying Leave to Appeal Under the *AA*

[38] Appeals from commercial arbitration decisions are narrowly circumscribed under the *AA*. Under s. 31(1), appeals are limited to either questions of law where the parties consent to the appeal or to questions of law where the parties do not consent but where leave to appeal is granted. Section 31(2) of the *AA*, reproduced in its entirety in Appendix III, sets out the requirements for leave:

(2) In an application for leave under subsection (1)(b), the court may grant leave if it determines that

(a) the importance of the result of the arbitration to the parties justifies the intervention of the court and the determination of the point of law may prevent a miscarriage of justice,

(b) the point of law is of importance to some class or body of persons of which the applicant is a member, or

(c) the point of law is of general or public importance.

[36] Ainsi, la Cour peut certes refuser l'autorisation si la question que l'on cherche à soulever devant elle n'a pas été plaidée devant les tribunaux d'instance inférieure, mais ce n'est pas le cas en l'espèce. En l'occurrence, les arguments sur le fondement de la demande d'autorisation d'appel de la sentence arbitrale présentée par Creston — à savoir si elle soulevait une question de droit ou une question mixte de fait et de droit — avaient été plaidés devant les formations saisies des demandes d'autorisation.

[37] Par conséquent, la Cour est saisie à bon droit de la question de savoir si la formation de la CA qui a accueilli la demande d'autorisation a conclu à tort que l'appel soulevait une question de droit.

B. *La Cour d'appel a commis une erreur en autorisant l'appel en vertu du par. 31(2) de l'AA*

(1) Facteurs qui entrent en ligne de compte dans l'analyse de la demande d'autorisation d'appel présentée au titre de l'*AA*

[38] L'appel d'une sentence arbitrale commerciale est étroitement circonscrit par l'*AA*. Aux termes du par. 31(1), il ne peut être interjeté appel que sur une question de droit dans le cas où les parties consentent à l'appel ou, en l'absence de consentement, dans les cas où l'autorisation d'appel est accordée. Le paragraphe 31(2) de l'*AA*, reproduit intégralement à l'annexe III, énonce les critères d'autorisation :

[TRADUCTION]

(2) Relativement à une demande d'autorisation présentée en vertu de l'alinéa (1)(b), le tribunal peut accorder l'autorisation s'il estime que, selon le cas :

(a) l'importance de l'issue de l'arbitrage pour les parties justifie son intervention et que le règlement de la question de droit peut permettre d'éviter une erreur judiciaire,

(b) la question de droit revêt de l'importance pour une catégorie ou un groupe de personnes dont le demandeur fait partie,

(c) la question de droit est d'importance publique.

[39] The B.C. courts have found that the words "may grant leave" in s. 31(2) of the *AA* give the courts judicial discretion to deny leave even where the statutory requirements have been met (*British Columbia Institute of Technology (Student Assn.) v. British Columbia Institute of Technology*, 2000 BCCA 496, 192 D.L.R. (4th) 122 ("*BCIT*"), at paras. 25-26). Appellate review of an arbitrator's award will only occur where the requirements of s. 31(2) are met and where the leave court does not exercise its residual discretion to nonetheless deny leave.

[40] Although Creston's application to the SC Leave Court sought leave pursuant to s. 31(2)(a), (b) and (c), it appears the arguments before that court and throughout focused on s. 31(2)(a). The SC Leave Court's decision quotes a lengthy passage from *BCIT* that focuses on the requirements of s. 31(2)(a). The SC Leave Court judge noted that both parties conceded the first requirement of s. 31(2)(a): that the issue be of importance to the parties. The CA Leave Court decision expressed concern that denying leave might give rise to a miscarriage of justice — a criterion only found in s. 31(2)(a). Finally, neither the lower courts' leave decisions nor the arguments before this Court reflected arguments about the question of law being important to some class or body of persons of which the applicant is a member (s. 31(2)(b)) or being a point of law of general or public importance (s. 31(2)(c)). Accordingly, the following analysis will focus on s. 31(2)(a).

(2) The Result Is Important to the Parties

[41] In order for leave to be granted from a commercial arbitral award, a threshold requirement must be met: leave must be sought on a question of law. However, before dealing with that issue, it will be convenient to quickly address another requirement of s. 31(2)(a) on which the parties agree: whether

[39] De l'avis des tribunaux de la C.-B., l'expression [TRADUCTION] « peut accorder l'autorisation » qui figure au par. 31(2) de l'*AA* confère au tribunal un pouvoir discrétionnaire qui l'habilite à refuser l'autorisation même lorsque les critères légaux sont respectés (*British Columbia Institute of Technology (Student Assn.) c. British Columbia Institute of Technology*, 2000 BCCA 496, 192 D.L.R. (4th) 122 (« *BCIT* »), par. 25-26). L'appel d'une sentence arbitrale n'est donc entendu que si les critères du par. 31(2) sont remplis et que le tribunal saisi de la demande d'autorisation ne refuse pas néanmoins l'autorisation en vertu de son pouvoir discrétionnaire résiduel.

[40] Bien que Creston ait présenté une demande d'autorisation à la Cour suprême sur le fondement des al. 31(2)(a), (b) et (c), il semble que les arguments invoqués devant elle et au cours des autres instances portaient sur l'al. 31(2)(a). La décision de la Cour suprême sur la demande d'autorisation reprend un long passage tiré de l'affaire *BCIT* axé sur les éléments de l'al. 31(2)(a). La Cour suprême y souligne que les deux parties reconnaissent qu'il est satisfait au premier élément de l'al. 31(2)(a), c'est-à-dire que la question est importante pour les parties. Dans sa décision sur la demande d'autorisation d'appel, la Cour d'appel a dit craindre que refuser l'autorisation ne donne lieu à une erreur judiciaire — un critère prévu seulement à l'al. 31(2)(a). Enfin, ni les décisions sur les demandes d'autorisation des tribunaux d'instance inférieure ni les arguments soulevés devant notre Cour ne traitent des autres critères, à savoir que la question de droit revêt de l'importance pour une catégorie ou un groupe de personnes dont le demandeur fait partie (al. 31(2)(b)) ou est d'importance publique (al. 31(2)(c)). Par conséquent, l'analyse qui suit porte principalement sur l'al. 31(2)(a).

(2) L'issue est importante pour les parties

[41] L'autorisation d'interjeter appel d'une sentence arbitrale commerciale est subordonnée au respect d'un critère minimal : l'appel doit porter sur une question de droit. Toutefois, avant d'aborder ce sujet, il convient d'examiner sommairement un autre élément requis par l'al. 31(2)(a) et sur lequel

the importance of the result of the arbitration to the parties justifies the intervention of the court. Justice Saunders explained this criterion in *BCIT* as requiring that the result of the arbitration be "sufficiently important", in terms of principle or money, to the parties to justify the expense and time of court proceedings (para. 27). The parties in this case have agreed that the result of the arbitration is of importance to each of them. In view of the relatively large monetary amount in dispute and in light of the fact that the parties have agreed that the result is important to them, I accept that the importance of the result of the arbitration to the parties justifies the intervention of the court. This requirement of s. 31(2)(a) is satisfied.

(3) The Question Under Appeal Is Not a Question of Law

(a) *When Is Contractual Interpretation a Question of Law?*

[42] Under s. 31 of the *AA*, the issue upon which leave is sought must be a question of law. For the purpose of identifying the appropriate standard of review or, as is the case here, determining whether the requirements for leave to appeal are met, reviewing courts are regularly required to determine whether an issue decided at first instance is a question of law, fact, or mixed fact and law.

[43] Historically, determining the legal rights and obligations of the parties under a written contract was considered a question of law (*King v. Operating Engineers Training Institute of Manitoba Inc.*, 2011 MBCA 80, 270 Man. R. (2d) 63, at para. 20, *per* Steel J.A.; K. Lewison, *The Interpretation of Contracts* (5th ed. 2011 & Supp. 2013), at pp. 173-76; and G. R. Hall, *Canadian Contractual Interpretation Law* (2nd ed. 2012), at pp. 125-26). This rule originated in England at a time when there were frequent civil jury trials and widespread illiteracy. Under those circumstances, the interpretation of written documents had to be considered questions of law because only the judge could be

s'entendent les parties, à savoir que l'importance de l'issue de l'arbitrage pour les parties doit justifier l'intervention du tribunal. Selon l'explication donnée par la juge Saunders de ce critère dans *BCIT*, il faut que l'issue de l'arbitrage soit [TRADUCTION] « suffisamment importante » aux yeux des parties, pour le principe ou les sommes d'argent en jeu, pour justifier le coût et la longueur d'une instance (par. 27). Les parties en l'espèce ont convenu que l'issue de l'arbitrage revêt de l'importance pour chacune. Étant donné la somme relativement considérable en litige et compte tenu du fait que les parties s'entendent pour dire que l'issue est importante pour elles, je conviens que l'importance de l'issue de l'arbitrage pour les parties justifie l'intervention du tribunal. Cette condition prévue à l'al. 31(2)(a) est remplie.

(3) La question soulevée n'est pas une question de droit

a) *Dans quelles circonstances l'interprétation contractuelle est-elle une question de droit?*

[42] Aux termes de l'art. 31 de l'*AA*, la demande d'autorisation d'appel doit porter sur une question de droit. Pour déterminer la norme de contrôle applicable ou, comme c'est le cas en l'espèce, pour déterminer si les critères d'autorisation sont respectés, le tribunal siégeant en révision est régulièrement appelé à décider si une question tranchée en première instance est une question de droit, une question de fait ou une question mixte de fait et de droit.

[43] Autrefois, la détermination des droits et obligations juridiques des parties à un contrat écrit ressortissait à une question de droit (*King c. Operating Engineers Training Institute of Manitoba Inc.*, 2011 MBCA 80, 270 Man. R. (2d) 63, par. 20, la juge Steel; K. Lewison, *The Interpretation of Contracts* (5e éd. 2011 et suppl. 2013), p. 173-176; G. R. Hall, *Canadian Contractual Interpretation Law* (2e éd. 2012), p. 125-126). Cette règle a pris naissance en Angleterre, à une époque où les procès civils devant jury étaient fréquents et l'analphabétisme courant. Dans de telles circonstances, l'interprétation des documents écrits devait être assimilée à une question de droit parce que le juge était le seul dont on

assured to be literate and therefore capable of reading the contract (Hall, at p. 126; and Lewison, at pp. 173-74).

[44] This historical rationale no longer applies. Nevertheless, courts in the United Kingdom continue to treat the interpretation of a written contract as always being a question of law (*Thorner v. Major*, [2009] UKHL 18, [2009] 3 All E.R. 945, at paras. 58 and 82-83; and Lewison, at pp. 173-77). They do this despite the fact that U.K. courts consider the surrounding circumstances, a concept addressed further below, when interpreting a written contract (*Prenn v. Simmonds*, [1971] 3 All E.R. 237 (H.L.); and *Reardon Smith Line Ltd. v. Hansen-Tangen*, [1976] 3 All E.R. 570 (H.L.)).

[45] In Canada, there remains some support for the historical approach. See for example *Jiro Enterprises Ltd. v. Spencer*, 2008 ABCA 87 (CanLII), at para. 10; *QK Investments Inc. v. Crocus Investment Fund*, 2008 MBCA 21, 290 D.L.R. (4th) 84, at para. 26; *Dow Chemical Canada Inc. v. Shell Chemicals Canada Ltd.*, 2010 ABCA 126, 25 Alta. L.R. (5th) 221, at paras. 11-12; and *Minister of National Revenue v. Costco Wholesale Canada Ltd.*, 2012 FCA 160, 431 N.R. 78, at para. 34. However, some Canadian courts have abandoned the historical approach and now treat the interpretation of written contracts as an exercise involving either a question of law or a question of mixed fact and law. See for example *WCI Waste Conversion Inc. v. ADI International Inc.*, 2011 PECA 14, 309 Nfld. & P.E.I.R. 1, at para. 11; *269893 Alberta Ltd. v. Otter Bay Developments Ltd.*, 2009 BCCA 37, 266 B.C.A.C. 98, at para. 13; *Hayes Forest Services Ltd. v. Weyerhaeuser Co.*, 2008 BCCA 31, 289 D.L.R. (4th) 230, at para. 44; *Bell Canada v. The Plan Group*, 2009 ONCA 548, 96 O.R. (3d) 81, at paras. 22-23 (majority reasons, *per* Blair J.A.) and paras. 133-35 (*per* Gillese J.A., in dissent, but not on this point); and *King*, at paras. 20-23.

[46] The shift away from the historical approach in Canada appears to be based on two developments. The first is the adoption of an approach to contractual interpretation which directs courts to have regard for the surrounding circumstances of the contract

pouvait être certain qu'il savait lire et écrire et, par conséquent, qu'il était en mesure de prendre connaissance du contrat (Hall, p. 126; Lewison, p. 173-174).

[44] Cette justification historique ne s'applique plus. Néanmoins, pour les tribunaux du Royaume-Uni, l'interprétation d'un contrat écrit ressortit toujours à une question de droit (*Thorner c. Major*, [2009] UKHL 18, [2009] 3 All E.R. 945, par. 58 et 82-83; Lewison, p. 173-177), et ce, même s'ils tiennent compte des circonstances — un concept que nous aborderons — dans l'interprétation du contrat écrit (*Prenn c. Simmonds*, [1971] 3 All E.R. 237 (H.L.); *Reardon Smith Line Ltd. c. Hansen-Tangen*, [1976] 3 All E.R. 570 (H.L.)).

[45] Au Canada, l'approche historique n'a pas perdu tous ses adeptes. Voir par exemple *Jiro Enterprises Ltd. c. Spencer*, 2008 ABCA 87 (CanLII), par. 10; *QK Investments Inc. c. Crocus Investment Fund*, 2008 MBCA 21, 290 D.L.R. (4th) 84, par. 26; *Dow Chemical Canada Inc. c. Shell Chemicals Canada Ltd.*, 2010 ABCA 126, 25 Alta. L.R. (5th) 221, par. 11-12; *Canada c. Costco Wholesale Canada Ltd.*, 2012 CAF 160 (CanLII), par. 34. Or, des tribunaux canadiens ont délaissé l'approche historique au profit d'une nouvelle démarche qui conçoit l'interprétation des contrats écrits soit comme une question de droit soit comme une question mixte de fait et de droit. Voir par exemple *WCI Waste Conversion Inc. c. ADI International Inc.*, 2011 PECA 14, 309 Nfld. & P.E.I.R. 1, par. 11; *269893 Alberta Ltd. c. Otter Bay Developments Ltd.*, 2009 BCCA 37, 266 B.C.A.C. 98, par. 13; *Hayes Forest Services Ltd. c. Weyerhaeuser Co.*, 2008 BCCA 31, 289 D.L.R. (4th) 230, par. 44; *Bell Canada c. The Plan Group*, 2009 ONCA 548, 96 O.R. (3d) 81, par. 22-23 (les juges majoritaires, sous la plume du juge Blair) et par. 133-135 (la juge Gillese, dissidente, mais pas sur ce point); *King*, par. 20-23.

[46] La tendance à délaisser l'approche historique au Canada semble s'expliquer par deux changements. Le premier est l'adoption d'une méthode d'interprétation contractuelle qui oblige le tribunal à tenir compte des circonstances — que l'on appelle

— often referred to as the factual matrix — when interpreting a written contract (Hall, at pp. 13, 21-25 and 127; and J. D. McCamus, *The Law of Contracts* (2nd ed. 2012), at pp. 749-51). The second is the explanation of the difference between questions of law and questions of mixed fact and law provided in *Canada (Director of Investigation and Research) v. Southam Inc.*, [1997] 1 S.C.R. 748, at para. 35, and *Housen v. Nikolaisen*, 2002 SCC 33, [2002] 2 S.C.R. 235, at paras. 26 and 31-36.

[47] Regarding the first development, the interpretation of contracts has evolved towards a practical, common-sense approach not dominated by technical rules of construction. The overriding concern is to determine "the intent of the parties and the scope of their understanding" (*Jesuit Fathers of Upper Canada v. Guardian Insurance Co. of Canada*, 2006 SCC 21, [2006] 1 S.C.R. 744, at para. 27, *per* LeBel J.; see also *Tercon Contractors Ltd. v. British Columbia (Transportation and Highways)*, 2010 SCC 4, [2010] 1 S.C.R. 69, at paras. 64-65, *per* Cromwell J.). To do so, a decision-maker must read the contract as a whole, giving the words used their ordinary and grammatical meaning, consistent with the surrounding circumstances known to the parties at the time of formation of the contract. Consideration of the surrounding circumstances recognizes that ascertaining contractual intention can be difficult when looking at words on their own, because words alone do not have an immutable or absolute meaning:

> No contracts are made in a vacuum: there is always a setting in which they have to be placed. . . . In a commercial contract it is certainly right that the court should know the commercial purpose of the contract and this in turn presupposes knowledge of the genesis of the transaction, the background, the context, the market in which the parties are operating.

(*Reardon Smith Line*, at p. 574, *per* Lord Wilberforce)

[48] The meaning of words is often derived from a number of contextual factors, including the purpose of the agreement and the nature of the relationship created by the agreement (see *Moore Realty Inc.*

souvent le fondement factuel — dans l'interprétation d'un contrat écrit (Hall, p. 13, 21-25 et 127; J. D. McCamus, *The Law of Contracts* (2e éd. 2012), p. 749-751). Le deuxième découle des explications formulées dans les arrêts *Canada (Directeur des enquêtes et recherches) c. Southam Inc.*, [1997] 1 R.C.S. 748, par. 35, et *Housen c. Nikolaisen*, 2002 CSC 33, [2002] 2 R.C.S. 235, par. 26 et 31-36, sur ce qui distingue la question de droit de la question mixte de fait et de droit.

[47] Relativement au premier changement, l'interprétation des contrats a évolué vers une démarche pratique, axée sur le bon sens plutôt que sur des règles de forme en matière d'interprétation. La question prédominante consiste à discerner « l'intention des parties et la portée de l'entente » (*Jesuit Fathers of Upper Canada c. Cie d'assurance Guardian du Canada*, 2006 CSC 21, [2006] 1 R.C.S. 744, par. 27, le juge LeBel; voir aussi *Tercon Contractors Ltd. c. Colombie-Britannique (Transports et Voirie)*, 2010 CSC 4, [2010] 1 R.C.S. 69, par. 64-65, le juge Cromwell). Pour ce faire, le décideur doit interpréter le contrat dans son ensemble, en donnant aux mots y figurant le sens ordinaire et grammatical qui s'harmonise avec les circonstances dont les parties avaient connaissance au moment de la conclusion du contrat. Par l'examen des circonstances, on reconnaît qu'il peut être difficile de déterminer l'intention contractuelle à partir des seuls mots, car les mots en soi n'ont pas un sens immuable ou absolu :

> [TRADUCTION] Aucun contrat n'est conclu dans l'abstrait : les contrats s'inscrivent toujours dans un contexte. [. . .] Lorsqu'un contrat commercial est en cause, le tribunal devrait certes connaître son objet sur le plan commercial, ce qui présuppose d'autre part une connaissance de l'origine de l'opération, de l'historique, du contexte, du marché dans lequel les parties exercent leurs activités.

(*Reardon Smith Line*, p. 574, le lord Wilberforce)

[48] Le sens des mots est souvent déterminé par un certain nombre de facteurs contextuels, y compris l'objet de l'entente et la nature des rapports créés par celle-ci (voir *Moore Realty Inc. c. Manitoba*

v. Manitoba Motor League, 2003 MBCA 71, 173 Man. R. (2d) 300, at para. 15, *per* Hamilton J.A.; see also Hall, at p. 22; and McCamus, at pp. 749-50). As stated by Lord Hoffmann in *Investors Compensation Scheme Ltd. v. West Bromwich Building Society*, [1998] 1 All E.R. 98 (H.L.):

> The meaning which a document (or any other utterance) would convey to a reasonable man is not the same thing as the meaning of its words. The meaning of words is a matter of dictionaries and grammars; the meaning of the document is what the parties using those words against the relevant background would reasonably have been understood to mean. [p. 115]

[49] As to the second development, the historical approach to contractual interpretation does not fit well with the definition of a pure question of law identified in *Housen* and *Southam*. Questions of law "are questions about what the correct legal test is" (*Southam*, at para. 35). Yet in contractual interpretation, the goal of the exercise is to ascertain the objective intent of the parties — a fact-specific goal — through the application of legal principles of interpretation. This appears closer to a question of mixed fact and law, defined in *Housen* as "applying a legal standard to a set of facts" (para. 26; see also *Southam*, at para. 35). However, some courts have questioned whether this definition, which was developed in the context of a negligence action, can be readily applied to questions of contractual interpretation, and suggest that contractual interpretation is primarily a legal affair (see for example *Bell Canada*, at para. 25).

[50] With respect for the contrary view, I am of the opinion that the historical approach should be abandoned. Contractual interpretation involves issues of mixed fact and law as it is an exercise in which the principles of contractual interpretation are applied to the words of the written contract, considered in light of the factual matrix.

[51] The purpose of the distinction between questions of law and those of mixed fact and law further

Motor League, 2003 MBCA 71, 173 Man. R. (2d) 300, par. 15, la juge Hamilton; voir aussi Hall, p. 22; McCamus, p. 749-750). Pour reprendre les propos du lord Hoffmann dans *Investors Compensation Scheme Ltd. c. West Bromwich Building Society*, [1998] 1 All E.R. 98 (H.L.) :

> [TRADUCTION] Le sens d'un document (ou toute autre déclaration) qui est transmis à la personne raisonnable n'équivaut pas au sens des mots qui le composent. Le sens des mots fait intervenir les dictionnaires et les grammaires; le sens du document représente ce qu'il est raisonnable de croire que les parties, en employant ces mots compte tenu du contexte pertinent, ont voulu exprimer. [p. 115]

[49] Relativement au deuxième changement, l'approche historique de l'interprétation contractuelle ne cadre pas bien avec la définition de la pure question de droit formulée dans les arrêts *Housen* et *Southam*. Les questions de droit « concernent la détermination du critère juridique applicable » (*Southam*, par. 35). Or, lorsqu'il s'agit d'interprétation contractuelle, le but de l'exercice consiste à déterminer l'intention objective des parties — un but axé sur les faits — par l'application des principes juridiques d'interprétation. Il me semble que cela se rapproche plutôt de la question mixte de fait et de droit, définie dans l'arrêt *Housen* comme supposant « l'application d'une norme juridique à un ensemble de faits » (par. 26; voir aussi *Southam*, par. 35). Toutefois, certains tribunaux ont émis des doutes sur l'application directe de cette définition, qui avait été établie à l'égard d'une action intentée pour négligence, à des questions d'interprétation contractuelle et laissent entendre que cette dernière est d'abord et avant tout une affaire de droit (voir par exemple *Bell Canada*, par. 25).

[50] Avec tout le respect que je dois aux tenants de l'opinion contraire, à mon avis, il faut rompre avec l'approche historique. L'interprétation contractuelle soulève des questions mixtes de fait et de droit, car il s'agit d'en appliquer les principes aux termes figurant dans le contrat écrit, à la lumière du fondement factuel.

[51] Cette conclusion est étayée par les raisons qui sous-tendent la distinction établie entre la

supports this conclusion. One central purpose of drawing a distinction between questions of law and those of mixed fact and law is to limit the intervention of appellate courts to cases where the results can be expected to have an impact beyond the parties to the particular dispute. It reflects the role of courts of appeal in ensuring the consistency of the law, rather than in providing a new forum for parties to continue their private litigation. For this reason, *Southam* identified the degree of generality (or "precedential value") as the key difference between a question of law and a question of mixed fact and law. The more narrow the rule, the less useful will be the intervention of the court of appeal:

> If a court were to decide that driving at a certain speed on a certain road under certain conditions was negligent, its decision would not have any great value as a precedent. In short, as the level of generality of the challenged proposition approaches utter particularity, the matter approaches pure application, and hence draws nigh to being an unqualified question of mixed law and fact. See R. P. Kerans, *Standards of Review Employed by Appellate Courts* (1994), at pp. 103-108. Of course, it is not easy to say precisely where the line should be drawn; though in most cases it should be sufficiently clear whether the dispute is over a general proposition that might qualify as a principle of law or over a very particular set of circumstances that is not apt to be of much interest to judges and lawyers in the future. [para. 37]

[52] Similarly, this Court in *Housen* found that deference to fact-finders promoted the goals of limiting the number, length, and cost of appeals, and of promoting the autonomy and integrity of trial proceedings (paras. 16-17). These principles also weigh in favour of deference to first instance decision-makers on points of contractual interpretation. The legal obligations arising from a contract are, in most cases, limited to the interest of the particular parties. Given that our legal system leaves broad scope to tribunals of first instance to resolve issues of limited application, this supports treating contractual interpretation as a question of mixed fact and law.

question de droit et la question mixte de fait et de droit. En distinguant ces deux catégories, on visait principalement à restreindre l'intervention de la juridiction d'appel aux affaires qui entraîneraient probablement des répercussions qui ne seraient pas limitées aux parties au litige. Ainsi, le rôle des cours d'appel, qui consiste à assurer la cohérence du droit, et non à offrir aux parties une nouvelle tribune leur permettant de poursuivre leur litige privé, est préservé. C'est pourquoi la Cour dans l'arrêt *Southam* reconnaît le degré de généralité (ou « la valeur comme précédents ») comme la principale différence entre la question de droit et la question mixte de fait et de droit. Plus la règle est stricte, moins l'intervention de la cour d'appel sera utile :

> Si une cour décidait que le fait d'avoir conduit à une certaine vitesse, sur une route donnée et dans des conditions particulières constituait de la négligence, sa décision aurait peu de valeur comme précédent. Bref, plus le niveau de généralité de la proposition contestée se rapproche de la particularité absolue, plus l'affaire prend le caractère d'une question d'application pure, et s'approche donc d'une question de droit et de fait parfaite. Voir R. P. Kerans, *Standards of Review Employed by Appellate Courts* (1994), aux pp. 103 à 108. Il va de soi qu'il n'est pas facile de dire avec précision où doit être tracée la ligne de démarcation; quoique, dans la plupart des cas, la situation soit suffisamment claire pour permettre de déterminer si le litige porte sur une proposition générale qui peut être qualifiée de principe de droit ou sur un ensemble très particulier de circonstances qui n'est pas susceptible de présenter beaucoup d'intérêt pour les juges et les avocats dans l'avenir. [par. 37]

[52] De même, la Cour dans l'arrêt *Housen* conclut que la retenue à l'égard du juge des faits contribue à réduire le nombre, la durée et le coût des appels tout en favorisant l'autonomie du procès et son intégrité (par. 16-17). Ces principes militent également en faveur de la déférence à l'endroit des décideurs de première instance en matière d'interprétation contractuelle. Les obligations juridiques issues d'un contrat se limitent, dans la plupart des cas, aux intérêts des parties au litige. Le vaste pouvoir de trancher les questions d'application limitée que notre système judiciaire confère aux tribunaux de première instance appuie la proposition selon laquelle l'interprétation contractuelle est une question mixte de fait et de droit.

[53] Nonetheless, it may be possible to identify an extricable question of law from within what was initially characterized as a question of mixed fact and law (*Housen*, at paras. 31 and 34-35). Legal errors made in the course of contractual interpretation include "the application of an incorrect principle, the failure to consider a required element of a legal test, or the failure to consider a relevant factor" (*King*, at para. 21). Moreover, there is no question that many other issues in contract law do engage substantive rules of law: the requirements for the formation of the contract, the capacity of the parties, the requirement that certain contracts be evidenced in writing, and so on.

[54] However, courts should be cautious in identifying extricable questions of law in disputes over contractual interpretation. Given the statutory requirement to identify a question of law in a leave application pursuant to s. 31(2) of the *AA*, the applicant for leave and its counsel will seek to frame any alleged errors as questions of law. The legislature has sought to restrict such appeals, however, and courts must be careful to ensure that the proposed ground of appeal has been properly characterized. The warning expressed in *Housen* to exercise caution in attempting to extricate a question of law is relevant here:

> Appellate courts must be cautious, however, in finding that a trial judge erred in law in his or her determination of negligence, as it is often difficult to extricate the legal questions from the factual. It is for this reason that these matters are referred to as questions of "mixed law and fact". Where the legal principle is not readily extricable, then the matter is one of "mixed law and fact" . . . . [para. 36]

[55] Although that caution was expressed in the context of a negligence case, it applies, in my opinion, to contractual interpretation as well. As mentioned above, the goal of contractual interpretation, to ascertain the objective intentions of the parties, is inherently fact specific. The close relationship between the selection and application of principles of

[53] Néanmoins, il peut se révéler possible de dégager une pure question de droit de ce qui paraît au départ constituer une question mixte de fait et de droit (*Housen*, par. 31 et 34-35). L'interprétation contractuelle peut occasionner des erreurs de droit, notamment [TRADUCTION] « appliquer le mauvais principe ou négliger un élément essentiel d'un critère juridique ou un facteur pertinent » (*King*, par. 21). En outre, il est indubitable que nombre d'autres questions se posant en droit des contrats mettent en jeu des règles de droit substantiel : les critères de formation du contrat, la capacité des parties, l'obligation que soient constatés par écrit certains types de contrat, etc.

[54] Le tribunal doit cependant faire preuve de prudence avant d'isoler une question de droit dans un litige portant sur l'interprétation contractuelle. Compte tenu de l'obligation, prévue au par. 31(2) de l'*AA*, que la demande d'autorisation soulève une question de droit, le demandeur et son représentant chercheront à qualifier de question de droit toute erreur qu'ils invoquent. Toutefois, le législateur a pris des mesures visant à limiter ce genre d'appels, et les tribunaux doivent examiner soigneusement le motif d'appel proposé pour déterminer s'il est bien caractérisé. La mise en garde exprimée dans *Housen* qui appelle à la prudence lorsqu'il s'agit d'isoler une question de droit s'applique dans le cas présent :

> Les cours d'appel doivent cependant faire preuve de prudence avant de juger que le juge de première instance a commis une erreur de droit lorsqu'il a conclu à la négligence, puisqu'il est souvent difficile de départager les questions de droit et les questions de fait. Voilà pourquoi on appelle certaines questions des questions « mixtes de fait et de droit ». Si le principe juridique n'est pas facilement isolable, il s'agit alors d'une « question mixte de fait et de droit » . . . [par. 36]

[55] Certes, cette mise en garde a été formulée dans le contexte d'une action pour négligence, mais elle s'applique également à mon avis à l'interprétation contractuelle. Comme je le mentionne précédemment, le but de l'interprétation contractuelle — déterminer l'intention objective des parties — est, de par sa nature même, axé sur les faits. Le rapport

contractual interpretation and the construction ultimately given to the instrument means that the circumstances in which a question of law can be extricated from the interpretation process will be rare. In the absence of a legal error of the type described above, no appeal lies under the *AA* from an arbitrator's interpretation of a contract.

étroit qui existe entre, d'une part, le choix et l'application des principes d'interprétation contractuelle et, d'autre part, l'interprétation que recevra l'instrument juridique en dernière analyse fait en sorte que rares seront les circonstances dans lesquelles il sera possible d'isoler une question de droit au cours de l'exercice d'interprétation. En l'absence d'une erreur de droit du genre de celles décrites plus haut, aucun droit d'appel de l'interprétation par un arbitre d'un contrat n'est prévu à l'*AA*.

(b) *The Role and Nature of the "Surrounding Circumstances"*

b) *Le rôle et la nature des « circonstances »*

[56] I now turn to the role of the surrounding circumstances in contractual interpretation and the nature of the evidence that can be considered. The discussion here is limited to the common law approach to contractual interpretation; it does not seek to apply to or alter the law of contractual interpretation governed by the *Civil Code of Québec*.

[56] Abordons le rôle des circonstances dans l'interprétation du contrat et la nature des éléments admis à l'examen. La présente analyse ne traite que de la démarche d'interprétation contractuelle fondée sur la common law; elle ne se veut ni une application ni une modification du droit relatif à l'interprétation contractuelle régi par le *Code civil du Québec*.

[57] While the surrounding circumstances will be considered in interpreting the terms of a contract, they must never be allowed to overwhelm the words of that agreement (*Hayes Forest Services*, at para. 14; and Hall, at p. 30). The goal of examining such evidence is to deepen a decision-maker's understanding of the mutual and objective intentions of the parties as expressed in the words of the contract. The interpretation of a written contractual provision must always be grounded in the text and read in light of the entire contract (Hall, at pp. 15 and 30-32). While the surrounding circumstances are relied upon in the interpretive process, courts cannot use them to deviate from the text such that the court effectively creates a new agreement (*Glaswegian Enterprises Inc. v. B.C. Tel Mobility Cellular Inc.* (1997), 101 B.C.A.C. 62).

[57] Bien que les circonstances soient prises en considération dans l'interprétation des termes d'un contrat, elles ne doivent jamais les supplanter (*Hayes Forest Services*, par. 14; Hall, p. 30). Le décideur examine cette preuve dans le but de mieux saisir les intentions réciproques et objectives des parties exprimées dans les mots du contrat. Une disposition contractuelle doit toujours être interprétée sur le fondement de son libellé et de l'ensemble du contrat (Hall, p. 15 et 30-32). Les circonstances sous-tendent l'interprétation du contrat, mais le tribunal ne saurait fonder sur elles une lecture du texte qui s'écarte de ce dernier au point de créer dans les faits une nouvelle entente (*Glaswegian Enterprises Inc. c. B.C. Tel Mobility Cellular Inc.* (1997), 101 B.C.A.C. 62).

[58] The nature of the evidence that can be relied upon under the rubric of "surrounding circumstances" will necessarily vary from case to case. It does, however, have its limits. It should consist only of objective evidence of the background facts at the time of the execution of the contract (*King*,

[58] La nature de la preuve susceptible d'appartenir aux « circonstances » variera nécessairement d'une affaire à l'autre. Il y a toutefois certaines limites. Il doit s'agir d'une preuve objective du contexte factuel au moment de la signature du contrat (*King*, par. 66 et 70), c'est-à-dire, les renseignements qui

at paras. 66 and 70), that is, knowledge that was or reasonably ought to have been within the knowledge of both parties at or before the date of contracting. Subject to these requirements and the parol evidence rule discussed below, this includes, in the words of Lord Hoffmann, "absolutely anything which would have affected the way in which the language of the document would have been understood by a reasonable man" (*Investors Compensation Scheme*, at p. 114). Whether something was or reasonably ought to have been within the common knowledge of the parties at the time of execution of the contract is a question of fact.

(c) *Considering the Surrounding Circumstances Does Not Offend the Parol Evidence Rule*

[59] It is necessary to say a word about consideration of the surrounding circumstances and the parol evidence rule. The parol evidence rule precludes admission of evidence outside the words of the written contract that would add to, subtract from, vary, or contradict a contract that has been wholly reduced to writing (*King*, at para. 35; and Hall, at p. 53). To this end, the rule precludes, among other things, evidence of the subjective intentions of the parties (Hall, at pp. 64-65; and *Eli Lilly & Co. v. Novopharm Ltd.*, [1998] 2 S.C.R. 129, at paras. 54-59, *per* Iacobucci J.). The purpose of the parol evidence rule is primarily to achieve finality and certainty in contractual obligations, and secondarily to hamper a party's ability to use fabricated or unreliable evidence to attack a written contract (*United Brotherhood of Carpenters and Joiners of America, Local 579 v. Bradco Construction Ltd.*, [1993] 2 S.C.R. 316, at pp. 341-42, *per* Sopinka J.).

[60] The parol evidence rule does not apply to preclude evidence of the surrounding circumstances. Such evidence is consistent with the objectives of finality and certainty because it is used as an interpretive aid for determining the meaning of the written words chosen by the parties, not to change or overrule the meaning of those words. The surrounding circumstances are facts known or facts

appartenaient ou auraient raisonnablement dû appartenir aux connaissances des deux parties à la date de signature ou avant celle-ci. Compte tenu de ces exigences et de la règle d'exclusion de la preuve extrinsèque que nous verrons, on entend par « circonstances », pour reprendre les propos du lord Hoffmann [TRADUCTION] « tout ce qui aurait eu une incidence sur la manière dont une personne raisonnable aurait compris les termes du document » (*Investors Compensation Scheme*, p. 114). La question de savoir si quelque chose appartenait ou aurait dû raisonnablement appartenir aux connaissances communes des parties au moment de la signature du contrat est une question de fait.

c) *Tenir compte des circonstances n'est pas contraire à la règle d'exclusion de la preuve extrinsèque*

[59] Quelques mots sur l'examen des circonstances et la règle d'exclusion de la preuve extrinsèque s'imposent. Cette règle empêche l'admission d'éléments de preuve autres que les termes du contrat écrit qui auraient pour effet de modifier ou de contredire un contrat qui a été entièrement consigné par écrit, ou d'y ajouter de nouvelles clauses ou d'en supprimer (*King*, par. 35; Hall, p. 53). À cette fin, la règle interdit notamment les éléments de preuve concernant les intentions subjectives des parties (Hall, p. 64-65; *Eli Lilly & Co. c. Novopharm Ltd.*, [1998] 2 R.C.S. 129, par. 54-59, le juge Iacobucci). La règle vise, premièrement, à donner un caractère définitif et certain aux obligations contractuelles et, deuxièmement, à empêcher qu'une partie puisse utiliser des éléments de preuve fabriqués ou douteux pour attaquer un contrat écrit (*Fraternité unie des charpentiers et menuisiers d'Amérique, section locale 579 c. Bradco Construction Ltd.*, [1993] 2 R.C.S. 316, p. 341-342, le juge Sopinka).

[60] La règle d'exclusion de la preuve extrinsèque n'interdit pas au tribunal de tenir compte des circonstances entourant le contrat. Cette preuve est compatible avec les objectifs relatifs au caractère définitif et certain puisqu'elle sert d'outil d'interprétation qui vient éclairer le sens des mots du contrat choisis par les parties, et non le changer ou s'y substituer. Les circonstances sont des faits connus

that reasonably ought to have been known to both parties at or before the date of contracting; therefore, the concern of unreliability does not arise.

[61] Some authorities and commentators suggest that the parol evidence rule is an anachronism, or, at the very least, of limited application in view of the myriad of exceptions to it (see for example *Gutierrez v. Tropic International Ltd.* (2002), 63 O.R. (3d) 63 (C.A.), at paras. 19-20; and Hall, at pp. 53-64). For the purposes of this appeal, it is sufficient to say that the parol evidence rule does not apply to preclude evidence of surrounding circumstances when interpreting the words of a written contract.

(d) *Application to the Present Case*

[62] In this case, the CA Leave Court granted leave on the following issue: "Whether the Arbitrator erred in law in failing to construe the whole of the Finder's Fee Agreement . . ." (A.R., vol. I, at p. 62).

[63] As will be explained below, while the requirement to construe a contract as a whole is a question of law that could — if extricable — satisfy the threshold requirement under s. 31 of the *AA*, I do not think this question was properly extricated in this case.

[64] I accept that a fundamental principle of contractual interpretation is that a contract must be construed as a whole (McCamus, at pp. 761-62; and Hall, at p. 15). If the arbitrator did not take the "maximum amount" proviso into account, as alleged by Creston, then he did not construe the Agreement as a whole because he ignored a specific and relevant provision of the Agreement. This is a question of law that would be extricable from a finding of mixed fact and law.

[65] However, it appears that the arbitrator did consider the "maximum amount" proviso. Indeed,

ou qui auraient raisonnablement dû l'être des deux parties à la date de signature du contrat ou avant celle-ci; par conséquent, le risque que des éléments d'une fiabilité douteuse soient invoqués ne se pose pas.

[61] Selon une certaine jurisprudence et des auteurs, la règle d'exclusion de la preuve extrinsèque serait un anachronisme ou, à tout le moins, d'application restreinte vu la myriade d'exceptions dont elle est assortie (voir par exemple *Gutierrez c. Tropic International Ltd.* (2002), 63 O.R. (3d) 63 (C.A.), par. 19-20; Hall, p. 53-64). Dans le cadre du présent pourvoi, il suffit de dire que la règle d'exclusion de la preuve extrinsèque ne s'oppose pas à la présentation d'une preuve des circonstances entourant le contrat pour l'interprétation de ce dernier.

d) *Application au présent pourvoi*

[62] En l'espèce, la Cour d'appel a accordé l'autorisation d'appel relativement à la question suivante : [TRADUCTION] « L'arbitre a-t-il commis une erreur de droit en n'interprétant pas l'entente relative aux honoraires d'intermédiation dans son ensemble . . . ? » (d.a., vol. I, p. 62)

[63] Comme nous le verrons, l'obligation d'interpréter le contrat dans son ensemble est une question de droit susceptible, si on pouvait l'isoler, de satisfaire au critère minimal exigé à l'art. 31 de l'*AA*. À mon avis, cette question n'a pas été isolée comme il se doit en l'espèce.

[64] Je reconnais qu'il est un principe fondamental de l'interprétation contractuelle selon lequel le contrat doit être interprété dans son ensemble (McCamus, p. 761-762; Hall, p. 15). Si l'arbitre n'a pas tenu compte de la stipulation relative au « plafond », comme le prétend Creston, il n'a alors pas interprété l'entente dans son ensemble, car il en a négligé une clause précise et pertinente. Voilà une question de droit qui pourrait être isolée de la conclusion mixte de fait et de droit.

[65] Or, il semble que l'arbitre a effectivement tenu compte de la stipulation relative au « plafond ».

the CA Leave Court acknowledges that the arbitrator had considered that proviso, since it notes that he turned his mind to the US$1.5 million maximum amount, an amount that can only be calculated by referring to the TSXV policy referenced in the "maximum amount" proviso in s. 3.1 of the Agreement. As I read its reasons, rather than being concerned with whether the arbitrator ignored the maximum amount proviso, which is what Creston alleges in this Court, the CA Leave Court decision focused on how the arbitrator construed s. 3.1 of the Agreement, which included the maximum amount proviso (paras. 25-26). For example, the CA Leave Court expressed concern that the arbitrator did not address the "incongruity" in the fact that the value of the fee would vary "hugely" depending on whether it was taken in cash or shares (para. 25).

En effet, selon la formation de la CA saisie de la demande d'autorisation, l'arbitre a examiné la stipulation, puisqu'elle signale qu'il a envisagé le plafond de 1,5 million $US, un nombre auquel il ne peut être arrivé que s'il a consulté la politique de la Bourse à laquelle renvoie la stipulation relative au « plafond » à l'art. 3.1 de l'entente. À la lumière de ses motifs, j'estime que la formation de la CA saisie de la demande d'autorisation, au lieu de se demander si l'arbitre a négligé la stipulation relative au plafond — ce que Creston prétend devant la Cour —, a axé sa décision sur l'interprétation qu'a donnée l'arbitre de l'art. 3.1 de l'entente, qui contient cette stipulation (par. 25-26). Par exemple, la formation de la CA saisie de la demande d'autorisation s'est dite préoccupée que l'arbitre n'ait pas abordé l'[TRADUCTION] « absurdité » de la variation « considérable » dans la valeur des honoraires selon qu'ils étaient versés en argent ou en actions (par. 25).

[66] With respect, the CA Leave Court erred in finding that the construction of s. 3.1 of the Agreement constituted a question of law. As explained by Justice Armstrong in the SC Appeal Court decision, construing s. 3.1 and taking account of the proviso required relying on the relevant surrounding circumstances, including the sophistication of the parties, the fluctuation in share prices, and the nature of the risk a party assumes when deciding to accept a fee in shares as opposed to cash. Such an exercise raises a question of mixed fact and law. There being no question of law extricable from the mixed fact and law question of how s. 3.1 and the proviso should be interpreted, the CA Leave Court erred in granting leave to appeal.

[66] Avec tout le respect que je lui dois, j'estime que la formation de la CA saisie de la demande d'autorisation a assimilé à tort l'interprétation de l'art. 3.1 de l'entente à une question de droit. Comme l'explique le juge Armstrong dans la décision de la CS sur l'appel, pour interpréter l'art. 3.1 et tenir compte de la stipulation, il fallait examiner les circonstances pertinentes, y compris le fait que les parties étaient des parties avisées, la fluctuation du cours de l'action et la nature du risque qu'une partie assume quand elle opte pour le versement de ses honoraires en actions plutôt qu'en argent. Un tel exercice soulève une question mixte de fait et de droit. Comme aucune question de droit ne peut être isolée de la question mixte de fait et de droit qui porte sur l'interprétation de l'art. 3.1 et de la stipulation, la Cour d'appel a commis une erreur en accueillant la demande d'autorisation d'appel.

[67] The conclusion that Creston's application for leave to appeal raised no question of law would be sufficient to dispose of this appeal. However, as this Court rarely has the opportunity to address appeals of arbitral awards, it is, in my view, useful to explain that, even had the CA Leave Court been correct in finding that construction of s. 3.1 of the Agreement constituted a question of law, it should have nonetheless denied leave to appeal as the

[67] Conclure que la demande d'autorisation d'appel présentée par Creston ne soulevait aucune question de droit suffirait à trancher le présent pourvoi. Toutefois, puisque la Cour a rarement l'occasion de se pencher sur l'appel d'une sentence arbitrale, il est à mon avis utile d'expliquer que même si la formation de la CA saisie de la demande d'autorisation avait conclu à bon droit que l'interprétation de l'art. 3.1 de l'entente constituait une question de

application also failed the miscarriage of justice and residual discretion stages of the leave analysis set out in s. 31(2)(a) of the *AA*.

droit, elle devait néanmoins rejeter la demande, car il n'était pas satisfait aux autres volets de l'analyse des demandes d'autorisation que requiert l'al. 31(2)(a) de l'*AA*, qui concernent l'erreur judiciaire et le pouvoir discrétionnaire résiduel.

(4) May Prevent a Miscarriage of Justice

(4) Le règlement de la question de droit peut permettre d'éviter une erreur judiciaire

(a) *Miscarriage of Justice for the Purposes of Section 31(2)(a) of the AA*

a) *L'erreur judiciaire pour l'application de l'al. 31(2)(a) de l'AA*

[68] Once a question of law has been identified, the court must be satisfied that the determination of that point of law on appeal "may prevent a miscarriage of justice" in order for it to grant leave to appeal pursuant to s. 31(2)(a) of the *AA*. The first step in this analysis is defining miscarriage of justice for the purposes of s. 31(2)(a).

[68] Une fois qu'il a cerné une question de droit, le tribunal doit être convaincu que le fait de statuer sur cette dernière [TRADUCTION] « peut permettre d'éviter une erreur judiciaire » avant d'accorder l'autorisation d'appel en vertu de l'al. 31(2)(a) de l'*AA*. La première étape de l'analyse consiste donc à définir l'erreur judiciaire pour l'application de cette disposition.

[69] In *BCIT*, Justice Saunders discussed the miscarriage of justice requirement under s. 31(2)(a). She affirmed the definition set out in *Domtar Inc. v. Belkin Inc.* (1989), 39 B.C.L.R. (2d) 257 (C.A.), which required the error of law in question to be a material issue that, if decided differently, would lead to a different result: ". . . if the point of law were decided differently, the arbitrator would have been led to a different result. In other words, was the alleged error of law material to the decision; does it go to its heart?" (*BCIT*, at para. 28). See also *Quan v. Cusson*, 2009 SCC 62, [2009] 3 S.C.R. 712, which discusses the test of whether "some substantial wrong or miscarriage of justice has occurred" in the context of a civil jury trial (para. 43).

[69] Dans *BCIT*, la juge Saunders traite du critère concernant l'erreur judiciaire prévu à l'al. 31(2)(a). Elle confirme la définition énoncée dans l'affaire *Domtar Inc. c. Belkin Inc.* (1989), 39 B.C.L.R. (2d) 257 (C.A.), selon laquelle l'erreur de droit doit toucher une question importante de sorte qu'une conclusion différente aurait abouti à un résultat différent : [TRADUCTION] « . . . si le point de droit avait été tranché différemment, l'arbitre aurait rendu une décision différente. Autrement dit, l'erreur de droit invoquée a-t-elle eu un effet déterminant sur la décision; touche-t-elle au cœur de la décision? » (*BCIT*, par. 28). Voir également l'arrêt *Quan c. Cusson*, 2009 CSC 62, [2009] 3 R.C.S. 712, où la Cour analyse le critère qui sert à déterminer s'il y a « préjudice grave ou [. . .] erreur judiciaire » dans le contexte des procès civils avec jury (par. 43).

[70] Having regard to *BCIT* and *Quan*, I am of the opinion that in order to rise to the level of a miscarriage of justice for the purposes of s. 31(2)(a) of the *AA*, an alleged legal error must pertain to a material issue in the dispute which, if decided differently, would affect the result of the case.

[70] Compte tenu des arrêts *BCIT* et *Quan*, je suis d'avis que, pour que l'erreur de droit reprochée soit une erreur judiciaire au sens où il faut l'entendre pour l'application de l'al. 31(2)(a) de l'*AA*, elle doit se rapporter à une question importante en litige qui, si elle était tranchée différemment, aurait une incidence sur le résultat.

[71] According to this standard, a determination of a point of law "may prevent a miscarriage of justice" only where the appeal itself has some possibility of succeeding. An appeal with no chance of success will not meet the threshold of "may prevent a miscarriage of justice" because there would be no chance that the outcome of the appeal would cause a change in the final result of the case.

[72] At the leave stage, it is not appropriate to consider the full merits of a case and make a final determination regarding whether an error of law was made. However, some preliminary consideration of the question of law is necessary to determine whether the appeal has the potential to succeed and thus to change the result in the case.

[73] *BCIT* sets the threshold for this preliminary assessment of the appeal as "more than an arguable point" (para. 30). With respect, once an arguable point has been made out, it is not apparent what more is required to meet the "more than an arguable point" standard. Presumably, the leave judge would have to delve more deeply into the arguments around the question of law on appeal than would be appropriate at the leave stage to find *more* than an arguable point. Requiring this closer examination of the point of law, in my respectful view, blurs the line between the function of the court considering the leave application and the court hearing the appeal.

[74] In my opinion, the appropriate threshold for assessing the legal question at issue under s. 31(2) is whether it has arguable merit. The arguable merit standard is often used to assess, on a preliminary basis, the merits of an appeal at the leave stage (see for example *Quick Auto Lease Inc. v. Nordin*, 2014 MBCA 32, 303 Man. R. (2d) 262, at para. 5; and *R. v. Fedossenko*, 2013 ABCA 164 (CanLII), at para. 7). "Arguable merit" is a well-known phrase whose meaning has been expressed in a variety of ways: "a reasonable prospect of success" (*Quick Auto Lease*, at para. 5; and *Enns v. Hansey*, 2013 MBCA 23 (CanLII), at para. 2); "some hope of success" and "sufficient merit" (*R. v. Hubley*, 2009 PECA 21, 289 Nfld. & P.E.I.R. 174, at para. 11); and "credible

[71] Suivant cette norme, le règlement d'un point de droit « peut permettre d'éviter une erreur judiciaire » seulement lorsqu'il existe une certaine possibilité que l'appel soit accueilli. Un appel qui est voué à l'échec ne saurait « permettre d'éviter une erreur judiciaire » puisque les possibilités que l'issue d'un tel appel joue sur le résultat final du litige sont nulles.

[72] Ce n'est pas à l'étape de l'autorisation qu'il convient d'examiner exhaustivement le fond du litige et de se prononcer définitivement sur l'absence ou l'existence d'une erreur de droit. Cependant, il faut procéder à un examen préliminaire de la question de droit pour déterminer si l'appel a une chance d'être accueilli et, par conséquent, de modifier le résultat du litige.

[73] Selon l'arrêt *BCIT*, le demandeur doit établir [TRADUCTION] « plus qu'un argument défendable » (par. 30) lors de cet examen préliminaire de l'appel. Pourtant, une fois un argument défendable soulevé, que faudrait-il démontrer de plus pour qu'il soit satisfait à cette norme? Vraisemblablement, le juge saisi de la demande d'autorisation devrait alors examiner les arguments se rapportant à la question de droit soulevée en appel de plus près que ce qui serait indiqué à cette étape pour trouver *plus* qu'un argument défendable. À mon humble avis, exiger un examen plus approfondi du point de droit brouille les rôles respectifs de la formation saisie de la demande d'autorisation et de celle saisie de l'appel.

[74] Selon moi, ce qu'il faut démontrer, pour l'application du par. 31(2), c'est que la question de droit invoquée a un fondement défendable. Ce critère s'applique souvent à l'étape de l'autorisation, pour établir sommairement le bien-fondé de l'appel (voir par exemple *Quick Auto Lease Inc. c. Nordin*, 2014 MBCA 32, 303 Man. R. (2d) 262, par. 5; *R. c. Fedossenko*, 2013 ABCA 164 (CanLII), par. 7). Il est bien connu et a été exprimé de diverses façons : [TRADUCTION] « une possibilité raisonnable d'être accueilli » (*a reasonable prospect of success*) (*Quick Auto Lease*, par. 5; *Enns c. Hansey*, 2013 MBCA 23 (CanLII), par. 2); une « certaine chance de succès » (*some hope of success*) et un « fondement suffisant » (*sufficient merit*) (*R. c. Hubley*, 2009 PECA

argument" (*R. v. Will*, 2013 SKCA 4, 405 Sask. R. 270, at para. 8). In my view, the common thread among the various expressions used to describe arguable merit is that the issue raised by the applicant cannot be dismissed through a preliminary examination of the question of law. In order to decide whether the award should be set aside, a more thorough examination is necessary and that examination is appropriately conducted by the court hearing the appeal once leave is granted.

[75] Assessing whether the issue raised by an application for leave to appeal has arguable merit must be done in light of the standard of review on which the merits of the appeal will be judged. This requires a preliminary assessment of the applicable standard of review. As I will later explain, reasonableness will almost always apply to commercial arbitrations conducted pursuant to the *AA*, except in the rare circumstances where the question is one that would attract a correctness standard, such as a constitutional question or a question of law of central importance to the legal system as a whole and outside the adjudicator's expertise. Therefore, the leave inquiry will ordinarily ask whether there is any arguable merit to the position that the arbitrator's decision on the question at issue is unreasonable, keeping in mind that the decision-maker is not required to refer to all the arguments, provisions or jurisprudence or to make specific findings on each constituent element, for the decision to be reasonable (*Newfoundland and Labrador Nurses' Union v. Newfoundland and Labrador (Treasury Board)*, 2011 SCC 62, [2011] 3 S.C.R. 708, at para. 16). Of course, the leave court's assessment of the standard of review is only preliminary and does not bind the court which considers the merits of the appeal. As such, this should not be taken as an invitation to engage in extensive arguments or analysis about the standard of review at the leave stage.

21, 289 Nfld. & P.E.I.R. 174, par. 11); un « argument plausible » (*credible argument*) (*R. c. Will*, 2013 SKCA 4, 405 Sask. R. 270, par. 8). À mon avis, les diverses appellations qui désignent le fondement défendable présentent un élément commun : l'argument soulevé par le demandeur ne peut être rejeté à l'issue d'un examen préliminaire de la question de droit. Pour déterminer s'il faut annuler la sentence arbitrale, un examen approfondi est nécessaire, et c'est au tribunal saisi de l'appel qu'il incombe, une fois l'autorisation accordée.

[75] L'examen visant à décider si la question soulevée dans la demande d'autorisation d'appel a un fondement défendable doit se faire à la lumière de la norme de contrôle applicable à l'analyse du bien-fondé de l'appel. Il faut donc procéder à un examen préliminaire ayant pour objet la norme applicable. Comme nous le verrons, la norme de la décision raisonnable s'appliquera presque toujours aux arbitrages commerciaux régis par l'*AA*, sauf dans les rares circonstances où l'application de la norme de la décision correcte s'imposera, notamment lorsqu'il s'agit d'une question constitutionnelle ou d'une question de droit qui revêt une importance capitale pour le système juridique dans son ensemble et qui est étrangère au domaine d'expertise du décideur administratif. Par conséquent, dans le cadre de l'examen préalable à l'autorisation le tribunal s'interrogera ordinairement quant à savoir si la prétention — selon laquelle la sentence arbitrale sur la question en litige était déraisonnable — a un fondement défendable, compte tenu du fait que le décideur n'est pas tenu de faire référence à tous les arguments, dispositions ou précédents ni de tirer une conclusion précise sur chaque élément constitutif du raisonnement pour que sa décision soit raisonnable (*Newfoundland and Labrador Nurses' Union c. Terre-Neuve-et-Labrador (Conseil du Trésor)*, 2011 CSC 62, [2011] 3 R.C.S. 708, par. 16). Certes, le tribunal saisi de la demande d'autorisation ne procède qu'à un examen préliminaire ayant pour objet la norme de contrôle, qui ne lie pas celui qui se penchera sur le bien-fondé de l'appel. Ainsi, il ne faudrait pas considérer qu'il s'agit d'une invitation à se perdre en analyses ou en arguments poussés à propos de la norme de contrôle à l'étape de la demande d'autorisation.

[76] In *BCIT*, Saunders J.A. considered the stage of s. 31(2)(a) of the *AA* at which an examination of the merits of the appeal should occur. At the behest of one of the parties, she considered examining the merits under the miscarriage of justice criterion. However, she decided that a consideration of the merits was best done at the residual discretion stage. Her reasons indicate that this decision was motivated by the desire to take a consistent approach across s. 31(2)(a), (b) and (c):

> Where, then, if anywhere, does consideration of the merits of the appeal belong? Mr. Roberts for the Student Association contends that any consideration of the merits of the appeal belongs in the determination of whether a miscarriage of justice may occur; that is, under the second criterion. I do not agree. In my view, the apparent merit or lack of merit of an appeal is part of the exercise of the residual discretion, and applies equally to all three subsections, (*a*) through (*c*). Just as an appeal woefully lacking in merit should not attract leave under (*b*) (of importance to a class of people including the applicant) or (*c*) (of general or public importance), so too it should not attract leave under (*a*). Consideration of the merits, for consistency in the section as a whole, should be made as part of the exercise of residual discretion. [para. 29]

[77] I acknowledge the consistency rationale. However, in my respectful opinion, the desire for a consistent approach to s. 31(2)(a), (b) and (c) cannot override the text of the legislation. Unlike s. 31(2)(b) and (c), s. 31(2)(a) requires an assessment to determine whether allowing leave to appeal "may prevent a miscarriage of justice". It is my opinion that a preliminary assessment of the question of law is an implicit component in a determination of whether allowing leave "may prevent a miscarriage of justice".

[78] However, in an application for leave to appeal pursuant to s. 31(2)(b) or (c), neither of which contain a miscarriage of justice requirement, I agree with Justice Saunders in *BCIT* that a preliminary

[76] Dans *BCIT*, la juge Saunders s'interroge sur l'étape à laquelle il convient d'examiner le bien-fondé de l'appel dans le cadre de l'analyse requise par l'al. 31(2)(a) de l'*AA*. Contrairement à ce que prétendait une partie, soit que l'évaluation du bien-fondé se rapporte au critère de l'erreur judiciaire, la juge détermine que cet examen se rattache plutôt à l'exercice du pouvoir discrétionnaire. Ses motifs révèlent que sa décision découle de sa volonté d'adopter une approche uniforme à l'égard des al. 31(2)(a), (b) et (c) :

> [TRADUCTION] À quel moment, le cas échéant, faut-il alors examiner le bien-fondé de l'appel? M. Roberts, qui représente l'Association étudiante, prétend qu'il convient de procéder à cet examen lorsqu'on se demande si une erreur judiciaire risque d'être commise, c'est-à-dire, à la deuxième étape. Je ne suis pas d'accord. À mon avis, l'appréciation du bien-fondé ou de l'absence de fondement apparent de l'appel s'inscrit dans l'exercice du pouvoir discrétionnaire résiduel et s'applique également aux trois alinéas, de (*a*) à (*c*). Tout comme un appel manifestement dénué de fondement ne devrait pas être autorisé en vertu de l'al. (*b*) (revêt de l'importance pour une catégorie ou un groupe de personnes dont le demandeur fait partie) ou de l'al. (*c*) (est d'importance publique), un tel appel ne devrait pas non plus être autorisé en vertu de l'al. (*a*). Dans un but d'uniformité à l'égard de l'article entier, l'appréciation du bien-fondé devrait être intégrée à l'exercice du pouvoir discrétionnaire résiduel. [par. 29]

[77] Je reconnais la validité du raisonnement axé sur l'uniformité. Cependant, à mon humble avis, cette volonté d'adopter une démarche semblable au regard des al. 31(2)(a), (b) et (c) ne saurait l'emporter sur le libellé de la disposition. Contrairement aux al. 31(2)(b) et (c), l'al. 31(2)(a) exige que le tribunal détermine si le fait d'autoriser l'appel « peut permettre d'éviter une erreur judiciaire ». J'estime qu'un examen préliminaire de la question de droit s'inscrit implicitement dans l'examen qui vise à déterminer si l'autorisation « peut permettre d'éviter une erreur judiciaire ».

[78] Cependant, lorsqu'il s'agit d'une demande d'autorisation d'appel présentée en vertu des al. 31(2)(b) ou (c) — puisque ces dispositions ne prévoient pas le risque d'erreur judiciaire comme

examination of the merits of the question of law should be assessed at the residual discretion stage of the analysis as considering the merits of the proposed appeal will always be relevant when deciding whether to grant leave to appeal under s. 31.

[79] In sum, in order to establish that "the intervention of the court and the determination of the point of law may prevent a miscarriage of justice" for the purposes of s. 31(2)(a) of the *AA*, an applicant must demonstrate that the point of law on appeal is material to the final result and has arguable merit.

(b) *Application to the Present Case*

[80] The CA Leave Court found that the arbitrator may have erred in law by not interpreting the Agreement as a whole, specifically in ignoring the "maximum amount" proviso. Accepting that this is a question of law for these purposes only, a determination of the question would be material because it could change the ultimate result arrived at by the arbitrator. The arbitrator awarded $4.14 million in damages on the basis that there was an 85 percent chance the TSXV would approve a finder's fee paid in $0.15 shares. If Creston's argument is correct and the $0.15 share price is foreclosed by the "maximum amount" proviso, damages would be reduced to US$1.5 million, a significant reduction from the arbitrator's award of damages.

[81] As s. 31(2)(a) of the *AA* is the relevant provision in this case, a preliminary assessment of the question of law will be conducted in order to determine if a miscarriage of justice could have occurred had Creston been denied leave to appeal. Creston argues that the fact that the arbitrator's conclusion results in Sattva receiving shares valued at considerably more than the US$1.5 million maximum dictated by the "maximum amount" proviso is

critère —, je souscris aux commentaires formulés par la juge Saunders dans *BCIT* selon lesquels l'examen préliminaire du bien-fondé de la question de droit devrait intervenir à l'étape de l'exercice du pouvoir discrétionnaire résiduel dans l'analyse, puisque l'examen du bien-fondé de l'appel proposé demeure pertinent dans la décision d'accorder ou non l'autorisation d'appel en vertu de l'art. 31.

[79] Bref, afin d'établir que l'intervention du tribunal est justifiée [TRADUCTION] « et que le règlement de la question de droit peut permettre d'éviter une erreur judiciaire » pour l'application de l'al. 31(2)(a) de l'*AA*, le demandeur doit prouver que le point de droit en appel aura une incidence sur le résultat final et qu'il est défendable.

b) *Application au présent pourvoi*

[80] La formation de la CA saisie de la demande d'autorisation a conclu à la possibilité d'une erreur de droit par l'arbitre qui n'aurait pas interprété l'entente dans son ensemble et, plus particulièrement, aurait fait fi de la stipulation relative au « plafond ». Admettons cette prétention comme question de droit uniquement pour les besoins de la cause. Le règlement de la question est déterminant parce qu'il pourrait avoir pour effet de modifier la sentence de l'arbitre, lequel a accordé 4,14 millions $ en dommages-intérêts au motif qu'il évaluait à 85 p. 100 la probabilité que la Bourse approuve des honoraires d'intermédiation payés en actions, à raison de 0,15 $ l'unité. Si l'argument invoqué par Creston est correct et que le cours de l'action ne peut s'établir à 0,15 $ en raison de la stipulation relative au « plafond », les dommages-intérêts seraient réduits à 1,5 million $US, une amputation considérable de la somme initiale accordée.

[81] Comme l'al. 31(2)(a) de l'*AA* est la disposition pertinente en l'espèce, il doit être procédé à un examen préliminaire de la question de droit pour déterminer le risque qu'une erreur judiciaire découle du rejet de la demande d'autorisation d'appel présentée par Creston. Cette dernière soutient que le fait que Sattva reçoive un portefeuille d'actions dont la valeur est très supérieure au plafond de 1,5 million $US en exécution de la sentence arbitrale

evidence of the arbitrator's failure to consider that proviso.

[82] However, the arbitrator did refer to s. 3.1, the "maximum amount" proviso, at two points in his decision: paras. 18 and 23(a). For example, at para. 23 he stated:

> In summary, then, as of March 27, 2007 it was clear and beyond argument that under the Agreement:
>
> (a) Sattva was entitled to a fee equal to the maximum amount payable pursuant to the rules and policies of the TSX Venture Exchange – section 3.1. It is common ground that the quantum of this fee is US$1,500,000.
>
> (b) The fee was payable in shares based on the Market Price, as defined in the Agreement, unless Sattva elected to take it in cash or a combination of cash and shares.
>
> (c) The Market Price, as defined in the Agreement, was $0.15. [Emphasis added.]

[83] Although the arbitrator provided no express indication that he considered how the "maximum amount" proviso interacted with the Market Price definition, such consideration is implicit in his decision. The only place in the contract that specifies that the amount of the fee is calculated as US$1.5 million is the "maximum amount" proviso's reference to s. 3.3 of the TSXV Policy 5.1. The arbitrator acknowledged that the quantum of the fee is US$1.5 million and awarded Sattva US$1.5 million in shares priced at $0.15. Contrary to Creston's argument that the arbitrator failed to consider the proviso in construing the Agreement, it is apparent on a preliminary examination of the question that the arbitrator did in fact consider the "maximum amount" proviso.

[84] Accordingly, even had the CA Leave Court properly identified a question of law, leave to appeal should have been denied. The requirement that there be arguable merit that the arbitrator's decision was unreasonable is not met and the miscarriage of justice threshold was not satisfied.

prouve que l'arbitre n'a pas tenu compte de la stipulation relative au « plafond ».

[82] Or, l'arbitre renvoie effectivement à l'art. 3.1, la stipulation relative au « plafond », à deux reprises dans sa décision, soit aux par. 18 et 23(a). Par exemple, il affirme ce qui suit au par. 23 :

> [TRADUCTION]
>
> Bref, à partir du 27 mars 2007, il était clair et incontestable qu'aux termes de l'entente :
>
> (a) Sattva avait le droit de recevoir des honoraires équivalant au plafond payable conformément aux règles et politiques de la Bourse de croissance TSX – article 3.1. Les parties conviennent que le montant des honoraires s'établit à 1 500 000 $US.
>
> (b) La commission était payable en actions, en fonction du cours, tel qu'il est défini dans l'entente, à moins que Sattva n'opte pour le versement des honoraires en argent ou en argent et en actions.
>
> (c) Le cours de l'action, tel qu'il est défini dans l'entente, s'établissait à 0,15 $. [Je souligne.]

[83] Ainsi, même si l'arbitre n'indique pas expressément avoir examiné le jeu de la stipulation relative au « plafond » et de la définition du cours, cet examen ressort implicitement de sa sentence. La seule clause de l'entente qui prévoit le montant des honoraires, soit 1,5 million $US, est la stipulation relative au « plafond », qui renvoie au point 3.3 de la politique 5.1 de la Bourse. Reconnaissant que le montant des honoraires s'élève à 1,5 million $US, l'arbitre a accordé à Sattva pareille somme, payable en actions, à raison de 0,15 $ l'unité. Contrairement à l'argument avancé par Creston, selon qui l'arbitre aurait négligé la stipulation dans son interprétation de l'entente, il ressort de l'examen préliminaire de la question que l'arbitre a effectivement tenu compte de la stipulation relative au « plafond ».

[84] Par conséquent, même si la Cour d'appel avait cerné à juste titre une question de droit, elle aurait dû rejeter la demande d'autorisation. Il n'était pas satisfait au critère qui exige que le caractère déraisonnable de la sentence arbitrale ait un fondement défendable, ni à celui de l'erreur judiciaire.

(5) Residual Discretion to Deny Leave

(a) *Considerations in Exercising Residual Discretion in a Section 31(2)(a) Leave Application*

[85] The B.C. courts have found that the words "may grant leave" in s. 31(2) of the *AA* confer on the court residual discretion to deny leave even where the requirements of s. 31(2) are met (*BCIT*, at paras. 9 and 26). In *BCIT*, Saunders J.A. sets out a non-exhaustive list of considerations that would be applicable to the exercise of discretion (para. 31):

1. "the apparent merits of the appeal";

2. "the degree of significance of the issue to the parties, to third parties and to the community at large";

3. "the circumstances surrounding the dispute and adjudication including the urgency of a final answer";

4. "other temporal considerations including the opportunity for either party to address the result through other avenues";

5. "the conduct of the parties";

6. "the stage of the process at which the appealed decision was made";

7. "respect for the forum of arbitration, chosen by the parties as their means of resolving disputes"; and

8. "recognition that arbitration is often intended to provide a speedy and final dispute mechanism, tailor-made for the issues which may face the parties to the arbitration agreement".

(5) Le pouvoir discrétionnaire résiduel qui habilite à refuser l'autorisation

a) *Éléments à examiner dans l'exercice du pouvoir discrétionnaire résiduel à l'égard d'une demande d'autorisation présentée en vertu de l'al. 31(2)(a)*

[85] Les tribunaux de la C.-B. ont conclu que les termes [TRADUCTION] « peut accorder l'autorisation » figurant au par. 31(2) de l'*AA* confèrent au tribunal un pouvoir discrétionnaire résiduel qui lui permet de refuser l'autorisation même quand les critères prévus par la disposition sont respectés (*BCIT*, par. 9 et 26). Dans *BCIT*, la juge Saunders énumère des facteurs à considérer dans l'exercice de ce pouvoir discrétionnaire (par. 31) :

1. [TRADUCTION] « le bien-fondé apparent de l'appel »;

2. « l'importance de la question pour les parties, les tiers et la société en général »;

3. « les circonstances qui sont à l'origine du différend et de l'arbitrage, y compris le besoin urgent d'obtenir un règlement définitif »;

4. « d'autres considérations temporelles, y compris la possibilité pour l'une ou l'autre des parties de remédier autrement aux conséquences »;

5. « la conduite des parties »;

6. « l'étape à laquelle la décision qui a été portée en appel avait été prise »;

7. « le respect du choix des parties d'avoir recours à l'arbitrage pour résoudre leurs différends »;

8. « la reconnaissance du fait que l'arbitrage constitue souvent un moyen expéditif et définitif de régler les différends, spécialement conçu pour traiter les enjeux susceptibles de toucher les parties à la convention d'arbitrage ».

[86] I agree with Justice Saunders that it is not appropriate to create what she refers to as an "immutable checklist" of factors to consider in exercising discretion under s. 31(2) (*BCIT*, at para. 32). However, I am unable to agree that all the listed considerations are applicable at this stage of the analysis.

[87] In exercising its statutorily conferred discretion to deny leave to appeal pursuant to s. 31(2)(a), a court should have regard to the traditional bases for refusing discretionary relief: the parties' conduct, the existence of alternative remedies, and any undue delay (*Immeubles Port Louis Ltée v. Lafontaine (Village)*, [1991] 1 S.C.R. 326, at pp. 364-67). Balance of convenience considerations are also involved in determining whether to deny discretionary relief (*MiningWatch Canada v. Canada (Fisheries and Oceans)*, 2010 SCC 2, [2010] 1 S.C.R. 6, at para. 52). This would include the urgent need for a final answer.

[88] With respect to the other listed considerations and addressed in turn below, it is my opinion that they have already been considered elsewhere in the s. 31(2)(a) analysis or are more appropriately considered elsewhere under s. 31(2). Once considered, these matters should not be assessed again under the court's residual discretion.

[89] As discussed above, in s. 31(2)(a), a preliminary assessment of the merits of the question of law at issue in the leave application is to be considered in determining the miscarriage of justice question. The degree of significance of the issue to the parties is covered by the "importance of the result of the arbitration to the parties" criterion in s. 31(2)(a). The degree of significance of the issue to third parties and to the community at large should not be considered under s. 31(2)(a) as the *AA* sets these out as separate grounds for granting leave to appeal under s. 31(2)(b) and (c). Furthermore, respect for the forum of arbitration chosen by the parties is a consideration that animates the legislation itself and

[86] Je conviens avec la juge Saunders pour dire qu'il n'est pas opportun de dresser ce qu'elle appelle une [TRADUCTION] « liste immuable » de facteurs à considérer dans l'exercice du pouvoir discrétionnaire prévu au par. 31(2) (*BCIT*, par. 32). Cependant, je ne peux convenir que tous les facteurs qui figurent sur la liste qu'elle a dressée sont applicables à cette étape de l'analyse.

[87] Dans l'exercice du pouvoir discrétionnaire que lui confère l'al. 31(2)(a) et qui l'habilite à rejeter la demande d'autorisation, le tribunal devrait examiner les motifs traditionnels justifiant le refus d'une réparation discrétionnaire : la conduite des parties, l'existence d'autres recours et tout retard indu (*Immeubles Port Louis Ltée c. Lafontaine (Village)*, [1991] 1 R.C.S. 326, p. 364-367). L'exercice du pouvoir discrétionnaire qui permet de refuser une réparation fait intervenir des considérations relatives à la prépondérance des inconvénients (*Mines Alerte Canada c. Canada (Pêches et Océans)*, 2010 CSC 2, [2010] 1 R.C.S. 6, par. 52). Parmi celles-ci se trouve le besoin urgent d'obtenir un règlement définitif.

[88] Quant aux autres facteurs mentionnés dans la liste et dont je traite successivement ci-après, j'estime qu'ils ont déjà été examinés dans le cadre de l'analyse fondée sur l'al. 31(2)(a) ou qu'il conviendrait mieux de les examiner à un autre volet du critère énoncé au par. 31(2). Une fois examinés, ces facteurs ne devraient pas être réexaminés par le tribunal au moment de l'exercice de son pouvoir discrétionnaire résiduel.

[89] Je le rappelle, dans l'analyse fondée sur l'al. 31(2)(a), il faut procéder à l'examen préliminaire du bien-fondé de la question de droit soulevée dans la demande d'autorisation pour déterminer s'il y a risque d'erreur judiciaire. La question de l'importance pour les parties se règle à l'al. 31(2)(a) : [TRADUCTION] « l'importance de l'issue de l'arbitrage pour les parties ». L'importance de la question pour les tiers et pour la société en général ne doit pas être examinée à l'al. 31(2)(a), car l'*AA* prévoit ces motifs à des dispositions distinctes, soit les al. 31(2)(b) et (c). En outre, le respect du choix des parties d'avoir recours à l'arbitrage sous-tend la loi elle-même, ce dont témoigne le seuil élevé auquel l'autorisation

can be seen in the high threshold to obtain leave under s. 31(2)(a). Recognition that arbitration is often chosen as a means to obtain a fast and final resolution tailor-made for the issues is already reflected in the urgent need for a final answer.

[90] As for the stage of the process at which the decision sought to be appealed was made, it is not a consideration relevant to the exercise of the court's residual discretion to deny leave under s. 31(2)(a). This factor seeks to address the concern that granting leave to appeal an interlocutory decision may be premature and result in unnecessary fragmentation and delay of the legal process (D. J. M. Brown and J. M. Evans, with the assistance of C. E. Deacon, *Judicial Review of Administrative Action in Canada* (loose-leaf), at pp. 3-67 to 3-76). However, any such concern will have been previously addressed by the leave court in its analysis of whether a miscarriage of justice may arise; more specifically, whether the interlocutory issue has the potential to affect the final result. As such, the above-mentioned concerns should not be considered anew.

[91] In sum, a non-exhaustive list of discretionary factors to consider in a leave application under s. 31(2)(a) of the *AA* would include:

- conduct of the parties;
- existence of alternative remedies;
- undue delay; and
- the urgent need for a final answer.

[92] These considerations could, where applicable, be a sound basis for declining leave to appeal an arbitral award even where the statutory criteria of s. 31(2)(a) have been met. However, courts should

est subordonnée aux termes de l'al. 31(2)(a). La reconnaissance du fait que l'arbitrage constitue souvent un moyen expéditif et définitif de régler les différends et spécialement conçu pour traiter les enjeux susceptibles de toucher les parties à la convention d'arbitrage s'inscrit dans le besoin urgent d'obtenir un règlement définitif.

[90] Quant à l'étape du processus à laquelle la décision dont on veut faire appel a été rendue, ce n'est pas un facteur pertinent pour l'exercice par le tribunal du pouvoir discrétionnaire résiduel conféré par l'al. 31(2)(a) qui lui permet de refuser l'autorisation. Ce facteur a été défini en réponse à des préoccupations selon lesquelles l'autorisation d'appeler d'une décision interlocutoire risque d'être prématurée et d'entraîner des retards indus ainsi qu'une fragmentation inutile du processus judiciaire (D. J. M. Brown et J. M. Evans, avec la collaboration de C. E. Deacon, *Judicial Review of Administrative Action in Canada* (feuilles mobiles), p. 3-67 à 3-76). Or, ces préoccupations auront été dissipées par la formation saisie de la demande d'autorisation lorsqu'elle se sera penchée sur le risque d'erreur judiciaire, et, plus précisément, sur la possibilité que la question interlocutoire ait une incidence sur le résultat final. Ainsi, les préoccupations mentionnées précédemment ne devraient donc pas être réexaminées.

[91] En résumé, une liste non exhaustive des facteurs à prendre en considération dans l'exercice du pouvoir discrétionnaire à l'égard d'une demande d'autorisation présentée en vertu de l'al. 31(2)(a) de l'*AA* comprendrait :

- la conduite des parties;
- l'existence d'autres recours;
- un retard indu;
- le besoin urgent d'obtenir un règlement définitif.

[92] Ces facteurs pourraient, le cas échéant, justifier le rejet de la demande sollicitant l'autorisation d'interjeter appel d'une sentence arbitrale même dans le cas où il est satisfait aux critères prévus à

exercise such discretion with caution. Having found an error of law and, at least with respect to s. 31(2)(a), a potential miscarriage of justice, these discretionary factors must be weighed carefully before an otherwise eligible appeal is rejected on discretionary grounds.

(b) *Application to the Present Case*

[93] The SC Leave Court judge denied leave on the basis that there was no question of law. Even had he found a question of law, the SC Leave Court judge stated that he would have exercised his residual discretion to deny leave for two reasons: first, because of Creston's conduct in misrepresenting the status of the finder's fee issue to the TSXV and Sattva; and second, "on the principle that one of the objectives of the [*AA*] is to foster and preserve the integrity of the arbitration system" (para. 41). The CA Leave Court overruled the SC Leave Court on both of these discretionary grounds.

[94] For the reasons discussed above, fostering and preserving the integrity of the arbitral system should not be a discrete discretionary consideration under s. 31(2)(a). While the scheme of s. 31(2) recognizes this objective, the exercise of discretion must pertain to the facts and circumstances of a particular case. This general objective is not a discretionary matter for the purposes of denying leave.

[95] However, conduct of the parties is a valid consideration in the exercise of the court's residual discretion under s. 31(2)(a). A discretionary decision to deny leave is to be reviewed with deference by an appellate court. A discretionary decision should not be interfered with merely because an appellate court would have exercised the discretion differently (*R. v. Bellusci*, 2012 SCC 44, [2012]

l'al. 31(2)(a). Cependant, les tribunaux devraient faire preuve de prudence dans l'exercice de ce pouvoir discrétionnaire. Après avoir conclu à l'existence d'une erreur de droit et, au moins en ce qui concerne l'al. 31(2)(a), d'un risque d'erreur judiciaire, le tribunal doit soupeser ces facteurs avec soin avant de décider s'il va rejeter ou non pour des motifs discrétionnaires une demande par ailleurs admissible.

b) *Application au présent pourvoi*

[93] Le juge de la CS saisi de la demande d'autorisation a rejeté cette dernière au motif qu'elle ne soulevait aucune question de droit. Il a indiqué que, même s'il avait conclu à l'existence d'une telle question, il aurait refusé l'autorisation en vertu de son pouvoir discrétionnaire résiduel, et ce, pour deux raisons : premièrement, à cause de la conduite de Creston qui a présenté inexactement les faits relatifs aux honoraires d'intermédiation à la Bourse et à Sattva; deuxièmement, [TRADUCTION] « par égard pour le principe selon lequel l'[*AA*] a notamment pour objectif de favoriser et de préserver l'intégrité du système d'arbitrage » (par. 41). La formation de la CA saisie de la demande d'autorisation a écarté la décision de la CS pour ces deux raisons discrétionnaires.

[94] Pour les motifs énoncés précédemment, l'objectif qui vise à favoriser et à préserver l'intégrité du système d'arbitrage ne devrait pas constituer une considération distincte dans l'analyse que requiert l'al. 31(2)(a) préalable à l'exercice du pouvoir discrétionnaire. Bien que le régime instauré par le par. 31(2) reconnaît cet objectif, l'exercice du pouvoir discrétionnaire doit se rapporter aux faits et aux circonstances de l'affaire. Cet objectif général ne fait pas partie des considérations susceptibles de justifier le refus discrétionnaire de l'autorisation.

[95] Toutefois, la conduite des parties est un facteur que le tribunal peut prendre en considération dans l'exercice du pouvoir discrétionnaire résiduel que lui confère l'al. 31(2)(a). La cour d'appel doit faire preuve de déférence lorsqu'elle contrôle la décision discrétionnaire de refuser l'autorisation d'interjeter appel. Elle doit se garder d'intervenir seulement parce qu'elle aurait exercé son pouvoir

2 S.C.R. 509, at paras. 18 and 30). An appellate court is only justified in interfering with a lower court judge's exercise of discretion if that judge misdirected himself or if his decision is so clearly wrong as to amount to an injustice (*R. v. Bjelland*, 2009 SCC 38, [2009] 2 S.C.R. 651, at para. 15; and *R. v. Regan*, 2002 SCC 12, [2002] 1 S.C.R. 297, at para. 117).

[96] Here, the SC Leave Court relied upon a well-accepted consideration in deciding to deny discretionary relief: the misconduct of Creston. The CA Leave Court overturned this decision on the grounds that Creston's conduct was "not directly relevant to the question of law" advanced on appeal (at para. 27).

[97] The CA Leave Court did not explain why misconduct need be directly relevant to a question of law for the purpose of denying leave. I see nothing in s. 31(2) of the *AA* that would limit a leave judge's exercise of discretion in the manner suggested by the CA Leave Court. My reading of the jurisprudence does not support the view that misconduct must be directly relevant to the question to be decided by the court.

[98] In *Homex Realty and Development Co. v. Corporation of the Village of Wyoming*, [1980] 2 S.C.R. 1011, at pp. 1037-38, misconduct by a party not directly relevant to the question at issue before the court resulted in denial of a remedy. The litigation in *Homex* arose out of a disagreement regarding whether the purchaser of lots in a subdivision, Homex, had assumed the obligations of the vendor under a subdivision agreement to provide "all the requirements, financial and otherwise" for the installation of municipal services on a parcel of land that had been subdivided (pp. 1015-16). This Court determined that Homex had not been accorded procedural fairness when the municipality passed a by-law related to the dispute (p. 1032). Nevertheless, discretionary relief to quash the by-law was denied because, among other things, Homex had sought "throughout all these proceedings to

discrétionnaire différemment (*R. c. Bellusci*, 2012 CSC 44, [2012] 2 R.C.S. 509, par. 18 et 30). La cour d'appel ne saurait intervenir à l'égard de l'exercice du pouvoir discrétionnaire par le juge de l'instance inférieure que si celui-ci s'est fondé sur des considérations erronées en droit ou si sa décision est erronée au point de créer une injustice (*R. c. Bjelland*, 2009 CSC 38, [2009] 2 R.C.S. 651, par. 15; *R. c. Regan*, 2002 CSC 12, [2002] 1 R.C.S. 297, par. 117).

[96] En l'espèce, la formation de la CS saisie de la demande d'autorisation a fondé sur un facteur reconnu sa décision de refuser la réparation discrétionnaire : l'inconduite de Creston. La formation de la CA saisie de la demande d'autorisation a infirmé cette décision au motif que [TRADUCTION] « ces faits [la conduite de Creston] n'intéressent pas directement la question de droit » soulevée en appel (par. 27).

[97] La formation de la CA saisie de la demande d'autorisation n'a pas expliqué pourquoi l'inconduite doit se rapporter directement à une question de droit pour que l'autorisation soit refusée. Rien dans le par. 31(2) de l'*AA* ne limite l'exercice du pouvoir discrétionnaire du juge saisi de la demande d'autorisation de la façon avancée par la Cour d'appel. Mon interprétation de la jurisprudence ne cadre pas avec le point de vue selon lequel l'inconduite d'une partie doit se rapporter directement à la question devant être tranchée par la cour.

[98] Dans l'arrêt *Homex Realty and Development Co. c. Corporation of the Village of Wyoming*, [1980] 2 R.C.S. 1011, p. 1037-1038, l'inconduite d'une partie ne se rapportait pas directement à la question en cause devant la Cour, mais cette dernière a néanmoins refusé d'accorder la réparation. Le litige tirait son origine d'un désaccord sur la question de savoir si l'acheteur de lots sur un lotissement, Homex, avait assumé les obligations du vendeur prévues à la convention de lotissement, c'est-à-dire de satisfaire à « toutes les exigences, financières ou autres » relativement à l'installation des services d'utilité publique sur un lotissement (p. 1015-1016). La Cour décide qu'Homex n'a pas bénéficié de l'équité procédurale lorsque la municipalité avait adopté un règlement se rapportant au litige (p. 1032). Néanmoins, la demande visant à obtenir l'annulation discrétionnaire du règlement a été rejetée notamment

avoid the burden associated with the subdivision of the lands" that it owned (p. 1037), even though the Court held that Homex knew this obligation was its responsibility (pp. 1017-19). This conduct was related to the dispute that gave rise to the litigation, but not to the question of whether the by-law was enacted in a procedurally fair manner. Accordingly, I read *Homex* as authority for the proposition that misconduct related to the dispute that gave rise to the proceedings may justify the exercise of discretion to refuse the relief sought, in this case refusing to grant leave to appeal.

[99] Here, the arbitrator found as a fact that Creston misled the TSXV and Sattva regarding "the nature of the obligation it had undertaken to Sattva by representing that the finder's fee was payable in cash" (para. 56(k)). While this conduct is not tied to the question of law found by the CA Leave Court, it is tied to the arbitration proceeding convened to determine which share price should be used to pay Sattva's finder's fee. The SC Leave Court was entitled to rely upon such conduct as a basis for denying leave pursuant to its residual discretion.

[100] In the result, in my respectful opinion, even if the CA Leave Court had identified a question of law and the miscarriage of justice test had been met, it should have upheld the SC Leave Court's denial of leave to appeal in deference to that court's exercise of judicial discretion.

[101] Although the CA Leave Court erred in granting leave, these protracted proceedings have nonetheless now reached this Court. In light of the fact that the true concern between the parties is the merits of the appeal — that is, how much the Agreement requires Creston to pay Sattva — and that the courts below differed significantly in their interpretation of the Agreement, it would be

parce que « [t]out au long de ces procédures, Homex a cherché à éviter les obligations qui se rattachent au lotissement des terrains » qu'elle détenait (p. 1037), même si Homex savait, de l'avis de la Cour, qu'elle devait assumer cette obligation (p. 1017-1019). Cette conduite se rapportait, non pas à la question de savoir si le règlement avait été adopté d'une manière équitable sur le plan de la procédure, mais au désaccord à l'origine dulitige. Par conséquent, je crois que l'arrêt *Homex* étaye la proposition selon laquelle une conduite répréhensible se rapportant au différend à l'origine du litige peut justifier le refus de la réparation discrétionnaire sollicitée, en l'occurrence l'autorisation d'interjeter appel.

[99] En l'espèce, l'arbitre a tiré la conclusion de fait suivante : Creston a induit la Bourse et Sattva en erreur en ce qui concerne [TRADUCTION] « la nature de l'obligation qu'elle avait contractée envers Sattva en affirmant que les honoraires d'intermédiation étaient payables en argent » (par. 56(k)). Bien que cette conduite ne soit pas reliée à la question de droit énoncée par la formation de la CA saisie de la demande d'autorisation, elle est reliée à l'arbitrage visant à déterminer le cours de l'action applicable aux fins du versement des honoraires d'intermédiation de Sattva. La Cour suprême pouvait à bon droit fonder sur une telle conduite sa décision de refuser l'autorisation, en vertu de son pouvoir discrétionnaire.

[100] Par conséquent, à mon humble avis, même si la formation de la CA saisie de la demande d'autorisation avait défini une question de droit et qu'il avait été satisfait au critère du risque d'erreur judiciaire, elle aurait dû confirmer la décision de la formation de la CS saisie de la demande d'autorisation de rejeter cette demande, par égard pour l'exercice du pouvoir discrétionnaire de cette cour.

[101] S'il est vrai que la formation de la CA saisie de la demande d'autorisation a commis une erreur en autorisant l'appel, ces interminables procédures ne s'en trouvent pas moins à l'heure actuelle devant nous. Puisque, par ailleurs, c'est la question de fond de l'appel — soit celle de savoir combien l'entente exige que Creston paie à Sattva — qui intéresse réellement les parties, et que les tribunaux d'instance

unsatisfactory not to address the very dispute that has given rise to these proceedings. I will therefore proceed to consider the three remaining questions on appeal as if leave to appeal had been properly granted.

C. *Standard of Review Under the AA*

[102] I now turn to consideration of the decisions of the appeal courts. It is first necessary to determine the standard of review of the arbitrator's decision in respect of the question on which the CA Leave Court granted leave: whether the arbitrator construed the finder's fee provision in light of the Agreement as a whole, particularly, whether the finder's fee provision was interpreted having regard for the "maximum amount" proviso.

[103] At the outset, it is important to note that the *Administrative Tribunals Act*, S.B.C. 2004, c. 45, which sets out standards of review of the decisions of many statutory tribunals in British Columbia (see ss. 58 and 59), does not apply in the case of arbitrations under the *AA*.

[104] Appellate review of commercial arbitration awards takes place under a tightly defined regime specifically tailored to the objectives of commercial arbitrations and is different from judicial review of a decision of a statutory tribunal. For example, for the most part, parties engage in arbitration by mutual choice, not by way of a statutory process. Additionally, unlike statutory tribunals, the parties to the arbitration select the number and identity of the arbitrators. These differences mean that the judicial review framework developed in *Dunsmuir v. New Brunswick*, 2008 SCC 9, [2008] 1 S.C.R. 190, and the cases that followed it, is not entirely applicable to the commercial arbitration context. For example, the *AA* forbids review of an arbitrator's factual findings. In the context of commercial arbitration, such a provision is absolute. Under the

inférieure ont considérablement divergé d'opinion quant à l'interprétation qu'il faut donner à l'entente, il serait bien peu satisfaisant que le véritable litige à l'origine de cette instance ne soit pas réglé. Je vais donc examiner les trois autres questions soulevées en appel comme si l'autorisation d'interjeter appel avait été accordée à bon droit.

C. *Norme de contrôle applicable aux affaires régies par l'AA*

[102] Abordons les décisions des tribunaux siégeant en appel. Tout d'abord, il est nécessaire de déterminer la norme applicable au contrôle de la sentence arbitrale en fonction de la question à l'égard de laquelle la formation de la CA saisie de la demande d'autorisation a accordé cette dernière : l'arbitre a-t-il interprété la disposition sur les honoraires d'intermédiation à la lumière de l'entente dans son ensemble? Plus particulièrement, l'a-t-il interprétée en tenant compte de la stipulation relative au « plafond »?

[103] D'entrée de jeu, il convient de souligner que l'*Administrative Tribunals Act*, S.B.C. 2004, ch. 45, laquelle prévoit les normes de contrôle applicables aux décisions rendues par de nombreux tribunaux administratifs de la Colombie-Britannique (art. 58 et 59), ne s'applique pas aux arbitrages régis par l'*AA*.

[104] L'examen en appel des sentences arbitrales commerciales s'inscrit dans un régime, strictement défini et adapté aux objectifs de l'arbitrage commercial, qui diffère du contrôle judiciaire d'une décision rendue par un tribunal administratif. Par exemple, la plupart du temps, les parties décident d'un commun accord de soumettre leur différend à l'arbitrage. Il ne s'agit pas d'un processus imposé par la loi. De plus, contrairement à la procédure devant un tribunal administratif, dans le cas d'un arbitrage les parties à la convention choisissent le nombre d'arbitres et l'identité de chacun. Ces différences révèlent que le cadre relatif au contrôle judiciaire établi dans l'arrêt *Dunsmuir c. Nouveau-Brunswick*, 2008 CSC 9, [2008] 1 R.C.S. 190, et les arrêts rendus depuis, ne peut être tout à fait transposé dans le contexte de l'arbitrage commercial. Par exemple, l'*AA* interdit

Dunsmuir judicial review framework, a privative clause does not prevent a court from reviewing a decision, it simply signals deference (*Dunsmuir*, at para. 31).

[105] Nevertheless, judicial review of administrative tribunal decisions and appeals of arbitration awards are analogous in some respects. Both involve a court reviewing the decision of a non-judicial decision-maker. Additionally, as expertise is a factor in judicial review, it is a factor in commercial arbitrations: where parties choose their own decision-maker, it may be presumed that such decision-makers are chosen either based on their expertise in the area which is the subject of dispute or are otherwise qualified in a manner that is acceptable to the parties. For these reasons, aspects of the *Dunsmuir* framework are helpful in determining the appropriate standard of review to apply in the case of commercial arbitration awards.

[106] *Dunsmuir* and the post-*Dunsmuir* jurisprudence confirm that it will often be possible to determine the standard of review by focusing on the nature of the question at issue (see for example *Alberta (Information and Privacy Commissioner) v. Alberta Teachers' Association*, 2011 SCC 61, [2011] 3 S.C.R. 654, at para. 44). In the context of commercial arbitration, where appeals are restricted to questions of law, the standard of review will be reasonableness unless the question is one that would attract the correctness standard, such as constitutional questions or questions of law of central importance to the legal system as a whole and outside the adjudicator's expertise (*Alberta Teachers' Association*, at para. 30). The question at issue here, whether the arbitrator interpreted the Agreement as a whole, does not fall into one of those categories. The relevant portions of the *Dunsmuir* analysis point to a standard of review of reasonableness in this case.

le contrôle des conclusions de fait tirées par l'arbitre. En matière d'arbitrage commercial, une telle disposition est absolue. Suivant le cadre établi dans *Dunsmuir*, l'existence d'une disposition d'inattaquabilité (aussi appelée clause privative) n'empêche pas le tribunal judiciaire de procéder au contrôle d'une décision administrative, elle signale simplement que la déférence est de mise (*Dunsmuir*, par. 31).

[105] Il demeure que le contrôle judiciaire d'une décision rendue par un tribunal administratif et l'appel d'une sentence arbitrale se ressemblent dans une certaine mesure. Dans les deux cas, le tribunal examine la décision rendue par un décideur administratif. En outre, l'expertise constitue un facteur tant en matière de contrôle judiciaire qu'en matière d'arbitrage commercial : quand les parties choisissent leur propre décideur, on peut présumer qu'elles fondent leur choix sur l'expertise de l'arbitre dans le domaine faisant l'objet du litige ou jugent sa compétence acceptable. Pour ces raisons, j'estime que certains éléments du cadre établi dans l'arrêt *Dunsmuir* aident à déterminer le degré de déférence qu'il convient d'accorder aux sentences rendues en matière d'arbitrage commercial.

[106] La jurisprudence depuis l'arrêt *Dunsmuir* vient confirmer qu'il est souvent possible de déterminer la norme de contrôle applicable suivant la nature de la question en litige (voir par exemple *Alberta (Information and Privacy Commissioner) c. Alberta Teachers' Association*, 2011 CSC 61, [2011] 3 R.C.S. 654, par. 44). En matière d'arbitrage commercial, la possibilité d'interjeter appel étant subordonnée à l'existence d'une question de droit, la norme de contrôle est celle de la décision raisonnable, à moins que la question n'appartienne à celles qui entraînent l'application de la norme de la décision correcte, comme les questions constitutionnelles ou les questions de droit qui revêtent une importance capitale pour le système juridique dans son ensemble et qui sont étrangères au domaine d'expertise du décideur (*Alberta Teachers' Association*, par. 30). La question dont nous sommes saisis, à savoir si l'arbitre a interprété l'entente dans son ensemble, n'appartient pas à l'une ou l'autre de ces catégories. Compte tenu des éléments pertinents de l'analyse établie dans l'arrêt *Dunsmuir*, la norme de la décision raisonnable s'applique en l'espèce.

D. *The Arbitrator Reasonably Construed the Agreement as a Whole*

[107] For largely the reasons outlined by Justice Armstrong in paras. 57-75 of the SC Appeal Court decision, in my respectful opinion, in determining that Sattva is entitled to be paid its finder's fee in shares priced at $0.15 per share, the arbitrator reasonably construed the Agreement as a whole. Although Justice Armstrong conducted a correctness review of the arbitrator's decision, his reasons amply demonstrate the reasonableness of that decision. The following analysis is largely based upon his reasoning.

[108] The question that the arbitrator had to decide was which date should be used to determine the price of the shares used to pay the finder's fee: the date specified in the Market Price definition in the Agreement or the date the finder's fee was to be paid?

[109] The arbitrator concluded that the price determined by the Market Price definition prevailed, i.e. $0.15 per share. In his view, this conclusion followed from the words of the Agreement and was "clear and beyond argument" (para. 23). Apparently, because he considered this issue clear, he did not offer extensive reasons in support of his conclusion.

[110] In *Newfoundland and Labrador Nurses' Union*, Abella J. cites Professor David Dyzenhaus to explain that, when conducting a reasonableness review, it is permissible for reviewing courts to supplement the reasons of the original decision-maker as part of the reasonableness analysis:

> "Reasonable" means here that the reasons do in fact or in principle support the conclusion reached. That is, even if the reasons in fact given do not seem wholly adequate to support the decision, the court must first seek to supplement them before it seeks to subvert them. For if it is right that among the reasons for deference are the appointment of the tribunal and not the court as the front line adjudicator, the tribunal's proximity to the dispute, its expertise, etc., then it is also the case that its decision should be presumed to be correct even if its reasons are in

D. *L'arbitre a donné une interprétation raisonnable de l'entente considérée dans son ensemble*

[107] Essentiellement pour les mêmes motifs que ceux exprimés par le juge Armstrong aux par. 57-75 de la décision de la CS sur l'appel, je suis d'avis que l'arbitre, en déterminant que Sattva était en droit de recevoir ses honoraires d'intermédiation en actions, à raison de 0,15 $ l'action, a donné une interprétation raisonnable de l'entente considérée dans son ensemble. Le juge Armstrong a contrôlé la décision de l'arbitre selon la norme de la décision correcte, mais ses motifs démontrent amplement le caractère raisonnable de cette décision. L'analyse qui suit est largement fondée sur son raisonnement.

[108] La question que devait trancher l'arbitre portait sur la date qui doit être retenue pour évaluer le cours de l'action aux fins du versement des honoraires d'intermédiation : la date établie selon la définition du cours qui figure dans l'entente ou la date du versement des honoraires d'intermédiation.

[109] L'arbitre a conclu que la valeur calculée selon la définition du cours l'emportait, soit 0,15 $ l'action. Selon lui, tel constat découlait des termes de l'entente et était [TRADUCTION] « clair et incontestable » (par. 23). Apparemment, comme il estimait que ce point était clair, il ne l'a pas motivé abondamment.

[110] Dans l'arrêt *Newfoundland and Labrador Nurses' Union*, la juge Abella cite le professeur David Dyzenhaus pour expliquer que les tribunaux siégeant en révision peuvent compléter les motifs du décideur de première ligne dans le cadre de l'analyse du caractère raisonnable :

> [TRADUCTION] Le « caractère raisonnable » s'entend ici du fait que les motifs étayent, effectivement ou en principe, la conclusion. Autrement dit, même si les motifs qui ont en fait été donnés ne semblent pas tout à fait convenables pour étayer la décision, la cour de justice doit d'abord chercher à les compléter avant de tenter de les contrecarrer. Car s'il est vrai que parmi les motifs pour lesquels il y a lieu de faire preuve de retenue on compte le fait que c'est le tribunal, et non la cour de justice, qui a été désigné comme décideur de

some respects defective. [Emphasis added by Abella J.; para. 12.]

(Quotation from D. Dyzenhaus, "The Politics of Deference: Judicial Review and Democracy", in M. Taggart, ed., *The Province of Administrative Law* (1997), 279, at p. 304)

Accordingly, Justice Armstrong's explanation of the interaction between the Market Price definition and the "maximum amount" proviso can be considered a supplement to the arbitrator's reasons.

[111] The two provisions at issue here are the Market Price definition and the "maximum amount" proviso:

2. DEFINITIONS

"Market Price" for companies listed on the TSX Venture Exchange shall have the meaning as set out in the Corporate Finance Manual of the TSX Venture Exchange as calculated on close of business day before the issuance of the press release announcing the Acquisition. For companies listed on the TSX, Market Price means the average closing price of the Company's stock on a recognized exchange five trading days immediately preceding the issuance of the press release announcing the Acquisition.

And:

3. FINDER'S FEE

3.1 . . . the Company agrees that on the closing of an Acquisition introduced to Company by the Finder, the Company will pay the Finder a finder's fee (the "Finder's Fee") based on Consideration paid to the vendor equal to the maximum amount payable pursuant to the rules and policies of the TSX Venture Exchange. Such finder's fee is to be paid in shares of the Company based on Market Price or, at the option of the Finder, any combination of shares and cash, provided the amount does not exceed the maximum amount as set out in the Exchange Policy 5.1, Section 3.3 Finder's Fee Limitations. [Emphasis added.]

première ligne, la connaissance directe qu'a le tribunal du différend, son expertise, etc., il est aussi vrai qu'on doit présumer du bien-fondé de sa décision même si ses motifs sont lacunaires à certains égards. [Soulignement ajouté par la juge Abella; par. 12.]

(Citation de D. Dyzenhaus, « The Politics of Deference : Judicial Review and Democracy », dans M. Taggart, dir., *The Province of Administrative Law* (1997), 279, p. 304)

Par conséquent, on peut supposer que l'explication donnée par le juge Armstrong du jeu de la définition du cours et de la stipulation relative au « plafond » complète les motifs de l'arbitre.

[111] Les deux clauses en cause sont la définition du cours et la stipulation relative au « plafond » :

[TRADUCTION]

2. DÉFINITIONS

« cours », pour les sociétés dont les titres sont inscrits à la cote de la Bourse de croissance TSX, a le sens qui lui est attribué dans le Guide du financement des sociétés de la Bourse de croissance TSX, c'est-à-dire qu'il s'entend du cours de clôture des actions le dernier jour ouvrable avant la publication du communiqué de presse annonçant l'acquisition. Pour les sociétés cotées à la Bourse TSX, le cours s'entend du cours de clôture moyen des actions de la société à une bourse reconnue cinq jours de bourse avant la publication du communiqué de presse annonçant l'acquisition.

Et :

3. HONORAIRES D'INTERMÉDIATION

3.1 . . . la société convient qu'à la conclusion d'une acquisition qui lui a été présentée par l'intermédiaire, elle verse à l'intermédiaire des honoraires (des « honoraires d'intermédiation »), calculés en fonction de la contrepartie versée au vendeur, dont le montant est égal au plafond payable conformément aux règles et politiques de la Bourse de croissance TSX. Ces honoraires d'intermédiation sont versés en actions de la société en fonction du cours ou, au choix de l'intermédiaire, en actions et en argent, dans la mesure où le montant des honoraires n'excède pas le plafond énoncé au point 3.3 de la politique 5.1 de la Bourse — Plafond des honoraires d'intermédiation. [Je souligne.]

[112] Section 3.1 entitles Sattva to be paid a finder's fee in shares based on the "Market Price". Section 2 of the Agreement states that Market Price for companies listed on the TSXV should be "calculated on close of business day before the issuance of the press release announcing the Acquisition". In this case, shares priced on the basis of the Market Price definition would be $0.15 per share. The words "provided the amount does not exceed the maximum amount as set out in the Exchange Policy 5.1, Section 3.3 Finder's Fee Limitations" in s. 3.1 of the Agreement constitute the "maximum amount" proviso. This proviso limits the amount of the finder's fee. The maximum finder's fee in this case is US$1.5 million (see s. 3.3 of the TSXV Policy 5.1 in Appendix II).

[113] While the "maximum amount" proviso limits the amount of the finder's fee, it does not affect the Market Price definition. As Justice Armstrong explained, the Market Price definition acts to fix the date at which one medium of payment (US$) is transferred into another (shares):

> The medium for payment of the finder's fee is clearly established by the fee agreement. The market value of those shares at the time that the parties entered into the fee agreement was unknown. The respondent analogizes between payment of the $1.5 million US finder's fee in shares and a hypothetical agreement permitting payment of $1.5 million US in Canadian dollars. Both agreements would contemplate a fee paid in different currencies. The exchange rate of the US and Canadian dollar would be fixed to a particulate date, as is the value of the shares by way of the Market Price in the fee agreement. That exchange rate would determine the number of Canadian dollars paid in order to satisfy the $1.5 million US fee, as the Market Price does for the number of shares paid in relation to the fee. The Canadian dollar is the form of the fee payment, as are the shares. Whether the Canadian dollar increased or decreased in value after the date on which the exchange rate is based is irrelevant. The amount of the fee paid remains $1.5 million US, payable in the number of Canadian dollars (or shares) equal to the

[112] L'article 3.1 de l'entente permet à Sattva de recevoir ses honoraires d'intermédiation en actions en fonction du « cours ». Aux termes de l'art. 2 de l'entente, le cours des titres des sociétés cotées à la Bourse de croissance TSX est égal au « cours de clôture des actions le dernier jour ouvrable avant la publication du communiqué de presse annonçant l'acquisition ». En l'espèce, compte tenu de la définition du cours, l'action vaudrait 0,15 $. Le passage « dans la mesure où le montant des honoraires n'excède pas le plafond énoncé au point 3.3 de la politique 5.1 de la Bourse — Plafond des honoraires d'intermédiation » tiré de l'art. 3.1 de l'entente constitue la stipulation relative au « plafond ». Cette stipulation limite le montant des honoraires d'intermédiation. Le plafond correspond dans le cas qui nous occupe à 1,5 million $US (voir le point 3.3 de la politique 5.1 de la Bourse à l'annexe II).

[113] La stipulation relative au « plafond » limite le montant des honoraires d'intermédiation, mais elle ne change rien à la définition du cours. Comme l'explique le juge Armstrong, la définition du cours fixe la date à laquelle un moyen de paiement (dollars américains) est converti en un autre (actions) :

> [TRADUCTION] Le moyen de paiement des honoraires d'intermédiation est clairement établi par l'entente conclue en ce sens. La valeur marchande de ces actions au moment où les parties ont conclu cette entente était inconnue. L'intimée établit une analogie entre le paiement en actions des honoraires d'intermédiation de 1,5 million $US et une entente hypothétique en vertu de laquelle la somme de 1,5 million $US serait convertie en dollars canadiens. Dans les deux cas, les honoraires seraient payés en devises différentes. Le taux de change d'une à l'autre serait fixé à une date précise, tout comme l'est le cours de l'action dans l'entente relative aux honoraires. Ce taux de change permettrait de calculer la somme à verser en dollars canadiens en règlement des honoraires de 1,5 million $US, tout comme le cours permet de déterminer le nombre d'actions cédées en règlement des honoraires. Le dollar canadien est une forme de paiement, au même titre que l'action. Il importe peu que la valeur du dollar canadien augmente ou diminue après la date fixée pour établir le taux de change. Le

amount of the fee based on the value of that currency on the date that the value is determined.

(SC Appeal Court decision, at para. 71)

[114] Justice Armstrong explained that Creston's position requires the Market Price definition to be ignored and for the shares to be priced based on the valuation done in anticipation of a private placement.

[115] However, nothing in the Agreement expresses or implies that compliance with the "maximum amount" proviso should be reassessed at a date closer to the payment of the finder's fee. Nor is the basis for the new valuation, in this case a private placement, mentioned or implied in the Agreement. To accept Creston's interpretation would be to ignore the words of the Agreement which provide that the "finder's fee is to be paid in shares of the Company based on Market Price".

[116] The arbitrator's decision that the shares should be priced according to the Market Price definition gives effect to both the Market Price definition and the "maximum amount" proviso. The arbitrator's interpretation of the Agreement, as explained by Justice Armstrong, achieves this goal by reconciling the Market Price definition and the "maximum amount" proviso in a manner that cannot be said to be unreasonable.

[117] As Justice Armstrong explained, setting the share price in advance creates a risk that makes selecting payment in shares qualitatively different from choosing payment in cash. There is an inherent risk in accepting a fee paid in shares that is not present when accepting a fee paid in cash. A fee paid in cash has a specific predetermined value. By contrast, when a fee is paid in shares, the price of the shares (or mechanism to determine the price of the shares) is set in advance. However, the price of those shares on the market will change over time. The recipient

montant des honoraires payé est toujours égal à 1,5 million $US. Il est converti en un certain nombre de dollars canadiens (ou d'actions) équivalant au montant des honoraires en fonction de la valeur de la devise à la date à laquelle cette valeur est déterminée.

(Décision de la CS sur l'appel, par. 71)

[114] Comme l'explique le juge Armstrong, accepter la position de Creston revient à ne pas tenir compte de la définition du cours et à fixer le cours de l'action en fonction de l'évaluation faite en prévision d'un placement privé.

[115] Cependant, rien dans l'entente n'indique, expressément ou implicitement, qu'il faille réévaluer avant la date du versement des honoraires d'intermédiation la conformité à la stipulation relative au « plafond ». L'entente ne précise pas non plus — ni expressément, ni implicitement — la base sur laquelle il faudrait procéder à une telle réévaluation — en l'occurrence un placement privé. Accepter l'interprétation de Creston reviendrait à faire fi du libellé de l'entente selon lequel les « honoraires d'intermédiation sont versés en actions de la société en fonction du cours ».

[116] La sentence arbitrale, selon laquelle l'action devrait être évaluée en fonction de la définition du cours, donne effet à cette dernière et à la stipulation relative au « plafond ». Comme l'explique le juge Armstrong, l'interprétation par l'arbitre de l'entente atteint cet objectif en conciliant la définition du cours et la stipulation relative au « plafond » d'une manière qui ne peut être considérée comme déraisonnable.

[117] Comme l'explique le juge Armstrong, fixer le cours de l'action en avance engendre un risque qui rend le paiement en actions qualitativement différent du paiement en argent. Le versement des honoraires sous forme d'actions présente un risque inhérent, qui ne se pose pas dans le cas du versement en argent. Les honoraires payés en argent ont une valeur prédéterminée. Par contre, quand les honoraires sont versés en actions, le cours de l'action (ou le mécanisme permettant de le déterminer) est fixé à l'avance. Cependant, le cours de l'action

of a fee paid in shares hopes the share price will rise resulting in shares with a market value greater than the value of the shares at the predetermined price. However, if the share price falls, the recipient will receive shares worth less than the value of the shares at the predetermined price. This risk is well known to those operating in the business sphere and both Creston and Sattva would have been aware of this as sophisticated business parties.

[118] By accepting payment in shares, Sattva was accepting that it was subject to the volatility of the market. If Creston's share price had fallen, Sattva would still have been bound by the share price determined according to the Market Price definition resulting in it receiving a fee paid in shares with a market value of less than the maximum amount of US$1.5 million. It would make little sense to accept the risk of the share price decreasing without the possibility of benefitting from the share price increasing. As Justice Armstrong stated:

> It would be inconsistent with sound commercial principles to insulate the appellant from a rise in share prices that benefitted the respondent at the date that the fee became payable, when such a rise was foreseeable and ought to have been addressed by the appellant, just as it would be inconsistent with sound commercial principles, and the terms of the fee agreement, to increase the number of shares allocated to the respondent had their value decreased relative to the Market Price by the date that the fee became payable. Both parties accepted the possibility of a change in the value of the shares after the Market Price was determined when entering into the fee agreement.

(SC Appeal Court decision, at para. 70)

[119] For these reasons, the arbitrator did not ignore the "maximum amount" proviso. The arbitrator's reasoning, as explained by Justice Armstrong, meets the reasonableness threshold of justifiability, transparency and intelligibility (*Dunsmuir*, at para. 47).

fluctue avec le temps. La personne qui reçoit des honoraires payés en actions espère une augmentation du cours, de sorte que ses actions auront une valeur marchande supérieure à celle qui est établie selon le cours prédéterminé. En revanche, si le cours chute, cette personne reçoit des actions dont la valeur est inférieure à celle des actions selon le cours prédéterminé. Ce risque est bien connu de ceux qui évoluent dans ce milieu, et Creston et Sattva, des parties avisées, en auraient eu connaissance.

[118] En acceptant un paiement en actions, Sattva acceptait de se soumettre à la volatilité du marché. Si l'action de Creston avait chuté, Sattva aurait tout de même été liée par la valeur déterminée en application de la définition du cours, de sorte qu'elle aurait reçu des actions d'une valeur marchande inférieure au plafond de 1,5 million $US. Il ne serait guère logique d'accepter le risque d'une baisse du cours de l'action sans avoir la possibilité de bénéficier d'une hausse. Pour reprendre les propos du juge Armstrong :

> [TRADUCTION] Il serait contraire aux principes commerciaux reconnus de protéger l'appelante de la hausse du cours de l'action dont bénéficiait l'intimée à la date de versement des honoraires, alors qu'une telle augmentation était prévisible et aurait dû être soulevée par l'appelante, tout comme il serait contraire aux principes commerciaux reconnus, et aux termes de l'entente relative aux honoraires, d'augmenter le nombre d'actions cédées à l'intimée dans le cas où leur valeur aurait baissé par rapport au cours en vigueur à la date du versement des honoraires. Les deux parties ont reconnu, quand elles ont conclu l'entente relative aux honoraires, la possibilité de fluctuation de la valeur de l'action après la définition du cours.

(Décision de la CS sur l'appel, par. 70)

[119] Pour ces raisons, on ne peut prétendre que l'arbitre n'a pas tenu compte de la stipulation de l'entente relative au « plafond ». Le raisonnement de l'arbitre, que le juge Armstrong explique, satisfait à la norme du caractère raisonnable dont les attributs sont la justification, la transparence et l'intelligibilité (*Dunsmuir*, par. 47).

E. *Appeal Courts Are Not Bound by Comments on the Merits of the Appeal Made by Leave Courts*

[120] The CA Appeal Court held that it and the SC Appeal Court were bound by the findings made by the CA Leave Court regarding not simply the decision to grant leave to appeal, but also the merits of the appeal. In other words, it found that the SC Appeal Court erred in law by ignoring the findings of the CA Leave Court regarding the merits of the appeal.

[121] The CA Appeal Court noted two specific findings regarding the merits of the appeal that it held were binding on it and the SC Appeal Court: (1) it would be anomalous if the Agreement allowed Sattva to receive US$1.5 million if it received its fee in cash, but allowed it to receive shares valued at approximately $8 million if Sattva received its fee in shares; and (2) that the arbitrator ignored this anomaly and did not address s. 3.1 of the Agreement:

> The [SC Appeal Court] judge found the arbitrator had expressly addressed the maximum amount payable under paragraph 3.1 of the Agreement and that he was correct.
>
> This finding is contrary to the remarks of Madam Justice Newbury in the earlier appeal that, if Sattva took its fee in shares valued at $0.15, it would receive a fee having a value at the time the fee became payable of over $8 million. If the fee were taken in cash, the amount payable would be $1.5 million US. Newbury J.A. specifically held that the arbitrator did not note this anomaly and did not address the meaning of paragraph 3.1 of the Agreement.
>
> The [SC Appeal Court] judge was bound to accept those findings. Similarly, absent a five-judge division in this appeal, we must also accept those findings. [paras. 42-44]

E. *La formation saisie de l'appel n'est pas liée par les observations formulées par la formation saisie de la demande d'autorisation sur le bien-fondé de l'appel*

[120] La Cour d'appel a conclu qu'elle-même et la formation de la CS saisie de l'appel étaient liées par les conclusions tirées par la formation de la CA saisie de la demande d'autorisation en ce qui a trait non seulement à la décision d'autoriser l'appel, mais aussi au bien-fondé de l'appel. Autrement dit, elle a conclu que la formation de la CS saisie de l'appel avait commis une erreur de droit en faisant fi des conclusions de la formation de la CA saisie de la demande d'autorisation quant au bien-fondé de l'appel.

[121] La formation de la CA saisie de l'appel a mis en relief deux conclusions précises quant au bien-fondé de l'appel qui, à son avis, la liaient elle, et aussi la formation de la CS saisie de l'appel : 1º il serait incongru que l'entente permette à Sattva, si elle opte pour le versement de ses honoraires en argent, de toucher 1,5 million $US alors que, si elle opte pour le versement sous forme d'actions, elle recevra un portefeuille valant environ 8 millions $ et 2º l'arbitre n'a pas tenu compte de cette anomalie et a fait fi de l'art. 3.1 de l'entente :

> [TRADUCTION] Le juge [de la CS saisi de l'appel] a conclu que l'arbitre avait expressément tenu compte du plafond des honoraires payables conformément au paragraphe 3.1 de l'entente et que sa sentence était correcte.
>
> Cette conclusion est contraire aux remarques formulées par la juge Newbury dans l'appel antérieur selon lesquelles, si ses honoraires étaient versés en actions, à raison de 0,15 $ l'unité, Sattva obtiendrait des honoraires d'une valeur, à la date du versement des honoraires, de plus de 8 millions $. Si elle optait pour le versement en argent, elle recevrait un montant de 1,5 million $US. La juge Newbury a statué expressément que l'arbitre n'avait pas soulevé cette anomalie et qu'il n'avait pas tenu compte du sens du paragraphe 3.1 de l'entente.
>
> Le juge [de la CS saisi de l'appel] était tenu d'accepter ces conclusions. De même, à défaut d'une décision d'une formation de cinq juges en l'espèce, nous devons aussi accepter ces conclusions. [par. 42-44]

[122] With respect, the CA Appeal Court erred in holding that the CA Leave Court's comments on the merits of the appeal were binding on it and on the SC Appeal Court. A court considering whether leave should be granted is not adjudicating the merits of the case (*Canadian Western Bank v. Alberta*, 2007 SCC 22, [2007] 2 S.C.R. 3, at para. 88). A leave court decides only whether the matter warrants granting leave, not whether the appeal will be successful (*Pacifica Mortgage Investment Corp. v. Laus Holdings Ltd.*, 2013 BCCA 95, 333 B.C.A.C. 310, at para. 27, leave to appeal refused, [2013] 3 S.C.R. viii). This is true even where the determination of whether to grant leave involves, as in this case, a preliminary consideration of the question of law at issue. A grant of leave cannot bind or limit the powers of the court hearing the actual appeal (*Tamil Co-operative Homes Inc. v. Arulappah* (2000), 49 O.R. (3d) 566 (C.A.), at para. 32).

[123] Creston concedes this point but argues that the CA Appeal Court's finding that it was bound by the CA Leave Court was inconsequential because the CA Appeal Court came to the same conclusion on the merits as the CA Leave Court based on separate and independent reasoning.

[124] The fact that the CA Appeal Court provided its own reasoning as to why it came to the same conclusion as the CA Leave Court does not vitiate the error. Once the CA Appeal Court treated the CA Leave Court's reasons on the merits as binding, it could hardly have come to any other decision. As counsel for Sattva pointed out, treating the leave decision as binding would render an appeal futile.

[122] Avec tout le respect que je lui dois, j'estime que la formation de la CA saisie de l'appel a commis une erreur en concluant que les commentaires sur le bien-fondé de l'appel formulés par la formation de la CA saisie de la demande d'autorisation la liaient elle, de même que la formation de la CS saisie de l'appel. Le tribunal chargé de statuer sur une demande d'autorisation ne tranche pas l'affaire sur le fond (*Banque canadienne de l'Ouest c. Alberta*, 2007 CSC 22, [2007] 2 R.C.S. 3, par. 88). Il détermine uniquement s'il est justifié d'accorder l'autorisation, et non si l'appel sera accueilli (*Pacifica Mortgage Investment Corp. c. Laus Holdings Ltd.*, 2013 BCCA 95, 333 B.C.A.C. 310, par. 27, autorisation d'appel refusée, [2013] 3 R.C.S. viii). Cela vaut même lorsque l'étude de la demande d'autorisation appelle un examen préliminaire de la question de droit en cause, comme c'est le cas en l'espèce. L'autorisation accordée ne saurait lier le tribunal chargé de statuer sur l'appel ni restreindre ses pouvoirs (*Tamil Co-operative Homes Inc. c. Arulappah* (2000), 49 O.R. (3d) 566 (C.A.), par. 32).

[123] Creston concède ce point, mais prétend que la conclusion tirée par la formation de la CA saisie de l'appel selon laquelle elle était liée par les conclusions de celle saisie de la demande d'autorisation était sans conséquence parce que la première est arrivée à la même conclusion que la seconde sur le bien-fondé, à l'issue d'un raisonnement distinct et indépendant.

[124] Le fait que la formation de la CA saisie de l'appel soit arrivée à la même conclusion que celle saisie de la demande d'autorisation pour des motifs différents n'annule pas l'erreur. Dès lors que la formation de la CA saisie de l'appel a accordé un caractère obligatoire aux motifs concernant le bien-fondé de l'appel énoncés par celle saisie de la demande d'autorisation, elle ne pouvait guère arriver à une autre décision. Comme le souligne l'avocat de Sattva, considérer comme impérative la décision relative à la demande d'autorisation rendrait l'appel futile.

VI. Conclusion

[125] The CA Leave Court erred in granting leave to appeal in this case. In any event, the arbitrator's decision was reasonable. The appeal from the judgments of the Court of Appeal for British Columbia dated May 14, 2010 and August 7, 2012 is allowed with costs throughout and the arbitrator's award is reinstated.

APPENDIX I

Relevant Provisions of the Sattva-Creston Finder's Fee Agreement

(a) "Market Price" definition:

2. DEFINITIONS

"Market Price" for companies listed on the TSX Venture Exchange shall have the meaning as set out in the Corporate Finance Manual of the TSX Venture Exchange as calculated on close of business day before the issuance of the press release announcing the Acquisition. For companies listed on the TSX, Market Price means the average closing price of the Company's stock on a recognized exchange five trading days immediately preceding the issuance of the press release announcing the Acquisition.

(b) Finder's fee provision (which contains the "maximum amount" proviso):

3. FINDER'S FEE

3.1 . . . the Company agrees that on the closing of an Acquisition introduced to Company by the Finder, the Company will pay the Finder a finder's fee (the "Finder's Fee") based on Consideration paid to the vendor equal to the maximum amount payable pursuant to the rules and policies of the TSX Venture Exchange. Such finder's fee

VI. Conclusion

[125] La formation de la CA saisie de la demande d'autorisation a commis une erreur en accordant l'autorisation d'interjeter appel en l'espèce. Quoi qu'il en soit, la sentence arbitrale était raisonnable. L'appel interjeté à l'encontre des décisions de la Cour d'appel de la Colombie-Britannique datées du 14 mai 2010 et du 7 août 2012 est accueilli avec dépens devant toutes les cours. La sentence arbitrale est rétablie.

ANNEXE I

Dispositions pertinentes de l'entente relative aux honoraires d'intermédiation conclue entre Sattva et Creston

a) Définition du « cours » :

[TRADUCTION]

2. DÉFINITIONS

« cours », pour les sociétés dont les titres sont inscrits à la cote de la Bourse de croissance TSX, a le sens qui lui est attribué dans le Guide du financement des sociétés de la Bourse de croissance TSX, c'est-à-dire qu'il s'entend du cours de clôture des actions le dernier jour ouvrable avant la publication du communiqué de presse annonçant l'acquisition. Pour les sociétés cotées à la Bourse TSX, le cours s'entend du cours de clôture moyen des actions de la société à une bourse reconnue cinq jours de bourse avant la publication du communiqué de presse annonçant l'acquisition.

b) Disposition relative aux honoraires d'intermédiation (laquelle contient la stipulation relative au « plafond ») :

[TRADUCTION]

3. HONORAIRES D'INTERMÉDIATION

3.1 . . . la société convient qu'à la conclusion d'une acquisition qui lui a été présentée par l'intermédiaire, elle verse à l'intermédiaire des honoraires (des « honoraires d'intermédiation »), calculés en fonction de la contrepartie versée au vendeur, dont le montant est égal au plafond payable conformément aux règles et politiques

is to be paid in shares of the Company based on Market Price or, at the option of the Finder, any combination of shares and cash, provided the amount does not exceed the maximum amount as set out in the Exchange Policy 5.1, Section 3.3 Finder's Fee Limitations.

APPENDIX II

Section 3.3 of TSX Venture Exchange Policy 5.1: Loans, Bonuses, Finder's Fees and Commissions

3.3 Finder's Fee Limitations

The finder's fee limitations apply if the benefit to the Issuer is an asset purchase or sale, joint venture agreement, or if the benefit to the Issuer is not a specific financing. The consideration should be stated both in dollars and as a percentage of the value of the benefit received. Unless there are unusual circumstances, the finder's fee should not exceed the following percentages:

Benefit	Finder's Fee
On the first $300,000	Up to 10%
From $300,000 to $1,000,000	Up to 7.5%
From $1,000,000 and over	Up to 5%

As the dollar value of the benefit increases, the fee or commission, as a percentage of that dollar value should generally decrease.

APPENDIX III

Commercial Arbitration Act, R.S.B.C. 1996, c. 55 (as it read on January 12, 2007) (now the *Arbitration Act*)

Appeal to the court

31 (1) A party to an arbitration may appeal to the court on any question of law arising out of the award if

de la Bourse de croissance TSX. Ces honoraires d'intermédiation sont versés en actions de la société en fonction du cours ou, au choix de l'intermédiaire, en actions et en argent, dans la mesure où le montant des honoraires n'excède pas le plafond énoncé au point 3.3 de la politique 5.1 de la Bourse — Plafond des honoraires d'intermédiation.

ANNEXE II

Point 3.3 de la politique 5.1 de la Bourse de croissance TSX : Emprunts, primes, honoraires d'intermédiation et commissions

3.3 Plafond des honoraires d'intermédiation

Les honoraires d'intermédiation sont assujettis à un plafond si l'avantage que retire l'émetteur prend la forme d'un achat ou d'une vente d'actifs ou d'une convention de coentreprise, ou si son avantage n'est pas lié à un financement précis. La contrepartie devrait être exprimée à la fois en valeur monétaire et en pourcentage de la valeur de l'avantage reçu. Sauf dans des circonstances exceptionnelles, les honoraires d'intermédiation ne doivent pas dépasser les pourcentages suivants :

Avantage	Honoraires d'intermédiation
300 000 $ et moins	Jusqu'à 10 %
Entre 300 000 $ et 1 000 000 $	Jusqu'à 7,5 %
1 000 000 $ et plus	Jusqu'à 5 %

De façon générale, les honoraires ou la commission, exprimés en pourcentage de la valeur monétaire de l'avantage, devraient être inversement proportionnels à cette valeur.

ANNEXE III

Commercial Arbitration Act, R.S.B.C. 1996, ch. 55 (dans sa version du 12 janvier 2007) (maintenant l'*Arbitration Act*)

[TRADUCTION]

Appel devant le tribunal

31 (1) Une partie à l'arbitrage peut interjeter appel au tribunal sur toute question de droit découlant de la sentence si, selon le cas :

(a) all of the parties to the arbitration consent, or

(b) the court grants leave to appeal.

(2) In an application for leave under subsection (1) (b), the court may grant leave if it determines that

(a) the importance of the result of the arbitration to the parties justifies the intervention of the court and the determination of the point of law may prevent a miscarriage of justice,

(b) the point of law is of importance to some class or body of persons of which the applicant is a member, or

(c) the point of law is of general or public importance.

(3) If the court grants leave to appeal under this section, it may attach conditions to the order granting leave that it considers just.

(4) On an appeal to the court, the court may

(a) confirm, amend or set aside the award, or

(b) remit the award to the arbitrator together with the court's opinion on the question of law that was the subject of the appeal.

Appeal allowed with costs throughout.

Solicitors for the appellant: McCarthy Tétrault, Vancouver.

Solicitors for the respondent: Miller Thomson, Vancouver.

Solicitor for the intervener the Attorney General of British Columbia: Attorney General of British Columbia, Victoria.

Solicitors for the intervener the BCICAC Foundation: Fasken Martineau DuMoulin, Vancouver.

(a) toutes les parties à l'arbitrage y consentent,

(b) le tribunal accorde l'autorisation.

(2) Relativement à une demande d'autorisation présentée en vertu de l'alinéa (1)(b), le tribunal peut accorder l'autorisation s'il estime que, selon le cas :

(a) l'importance de l'issue de l'arbitrage pour les parties justifie son intervention et que le règlement de la question de droit peut permettre d'éviter une erreur judiciaire,

(b) la question de droit revêt de l'importance pour une catégorie ou un groupe de personnes dont le demandeur fait partie,

(c) la question de droit est d'importance publique.

(3) Si le tribunal accorde l'autorisation en vertu du présent article, il peut assortir des conditions qu'il estime équitables l'ordonnance accordant l'autorisation.

(4) En appel, le tribunal peut, selon le cas :

(a) confirmer, modifier ou annuler la sentence,

(b) renvoyer la sentence à l'arbitre avec l'opinion du tribunal sur la question de droit qui a fait l'objet de l'appel.

Pourvoi accueilli avec dépens devant toutes les cours.

Procureurs de l'appelante : McCarthy Tétrault, Vancouver.

Procureurs de l'intimée : Miller Thomson, Vancouver.

Procureur de l'intervenant le procureur général de la Colombie-Britannique : Procureur général de la Colombie-Britannique, Victoria.

Procureurs de l'intervenante BCICAC Foundation : Fasken Martineau DuMoulin, Vancouver.

TAB 21

Tercon Contractors Ltd. *Appellant*

v.

Her Majesty The Queen in Right of the Province of British Columbia, by her Ministry of Transportation and Highways *Respondent*

and

Attorney General of Ontario *Intervener*

Indexed as: Tercon Contractors Ltd. *v.* British Columbia (Transportation and Highways)

2010 SCC 4

File No.: 32460.

2009: March 23; 2010: February 12.

Present: McLachlin C.J. and Binnie, LeBel, Deschamps, Fish, Abella, Charron, Rothstein and Cromwell JJ.

ON APPEAL FROM THE COURT OF APPEAL FOR BRITISH COLUMBIA

Contracts — Breach of terms — Tender — Ineligible bidder — Exclusion of liability clause — Doctrine of fundamental breach — Province issuing tender call for construction of highway — Request for proposals restricting qualified bidders to six proponents — Province accepting bid from ineligible bidder — Exclusion clause protecting Province from liability arising from participation in tendering process — Whether Province breached terms of tendering contract in entertaining bid from ineligible bidder — If so, whether Province's conduct fell within terms of exclusion clause — If so, whether court should nevertheless refuse to enforce the exclusion clause because of unconscionability or some other contravention of public policy.

The Province of British Columbia issued a request for expressions of interest ("RFEI") for the design and construction of a highway. Six teams responded with submissions including Tercon and Brentwood. A few months later, the Province informed the six proponents

Tercon Contractors Ltd. *Appelante*

c.

Sa Majesté la Reine du chef de la Colombie-Britannique, représentée par le ministère des Transports et de la Voirie *Intimée*

et

Procureur général de l'Ontario *Intervenant*

Répertorié : Tercon Contractors Ltd. *c.* Colombie-Britannique (Transports et Voirie)

2010 CSC 4

N° du greffe : 32460.

2009 : 23 mars; 2010 : 12 février.

Présents : La juge en chef McLachlin et les juges Binnie, LeBel, Deschamps, Fish, Abella, Charron, Rothstein et Cromwell.

EN APPEL DE LA COUR D'APPEL DE LA COLOMBIE-BRITANNIQUE

Contrats — Inexécution — Appel d'offres — Soumissionnaire inadmissible — Clause de non-responsabilité — Principe d'inexécution fondamentale — Appel d'offres lancé par la province pour la construction d'une route — Demande de propositions tenant seulement six entreprises pour admissibles — Acceptation par la province de la proposition d'un soumissionnaire inadmissible — Clause de non-recours protégeant la province contre toute responsabilité découlant de la participation à l'appel d'offres — La province s'est-elle rendue coupable d'inexécution du contrat issu de l'appel d'offres en considérant la proposition d'un soumissionnaire inadmissible? — Dans l'affirmative, son comportement tombait-il sous le coup de la clause de non-recours? — Dans l'affirmative, un tribunal devrait-il néanmoins refuser de faire respecter la clause en raison de son iniquité ou pour quelque autre atteinte à l'ordre public?

La province de la Colombie-Britannique a lancé une demande d'expression d'intérêt (« DEI ») pour la conception et la construction d'une route. Elle a reçu six soumissions, dont celles de Tercon et de Brentwood. Quelques mois plus tard, la province a fait savoir aux

that it now intended to design the highway itself and issued a request for proposals ("RFP") for its construction. The RFP set out a specifically defined project and contemplated that proposals would be evaluated according to specific criteria. Under its terms, only the six original proponents were eligible to submit a proposal; those received from any other party would not be considered. The RFP also included an exclusion of liability clause which provided: "Except as expressly and specifically permitted in these Instructions to Proponents, no Proponent shall have any claim for compensation of any kind whatsoever, as a result of participating in this RFP, and by submitting a Proposal each Proponent shall be deemed to have agreed that it has no claim." As it lacked expertise in drilling and blasting, Brentwood entered into a pre-bidding agreement with another construction company ("EAC"), which was not a qualified bidder, to undertake the work as a joint venture. This arrangement allowed Brentwood to prepare a more competitive proposal. Ultimately, Brentwood submitted a bid in its own name with EAC listed as a "major member" of the team. Brentwood and Tercon were the two short-listed proponents and the Province selected Brentwood for the project. Tercon successfully brought an action in damages against the Province. The trial judge found that the Brentwood bid was, in fact, submitted by a joint venture of Brentwood and EAC and that the Province, which was aware of the situation, breached the express provisions of the tendering contract with Tercon by considering a bid from an ineligible bidder and by awarding it the work. She also held that, as a matter of construction, the exclusion clause did not bar recovery for the breaches she had found. The clause was ambiguous and she resolved this ambiguity in Tercon's favour. She held that the Province's breach was fundamental and that it was not fair or reasonable to enforce the exclusion clause in light of the Province's breach. The Court of Appeal set aside the decision, holding that the exclusion clause was clear and unambiguous and barred compensation for all defaults.

Held (McLachlin C.J. and Binnie, Abella and Rothstein JJ. dissenting): The appeal should be allowed. The Court agreed on the appropriate framework of analysis but divided on the applicability of the exclusion clause to the facts.

The Court: With respect to the appropriate framework of analysis the doctrine of fundamental breach

six entreprises intéressées qu'elle entendait désormais concevoir elle-même la route et demander des propositions pour sa construction. La demande de propositions (« DP ») décrivait un projet précis et indiquait que les propositions seraient considérées au regard de certains critères. Elle stipulait que seules les six entreprises intéressées initialement étaient admises à soumissionner et que les propositions présentées par d'autres personnes ne seraient pas examinées. La DP renfermait également une clause de non-recours, dont le texte était le suivant : « Sauf ce que prévoient expressément les présentes instructions, un proposant ne peut exercer aucun recours en indemnisation pour sa participation à la DP, ce qu'il est réputé accepter lorsqu'il présente une soumission. » Comme elle n'avait pas d'expertise dans le forage et le dynamitage, Brentwood a conclu avec une autre entreprise de construction (« EAC ») — qui n'était pas admise à soumissionner — une entente préalable à la soumission prévoyant qu'elles réaliseraient les travaux en coentreprise. De la sorte, elle pouvait présenter une proposition plus concurrentielle. Elle a finalement soumissionné en son nom, présentant EAC comme un « membre important » de son équipe. La liste des adjudicataires possibles a été ramenée à deux entreprises — Brentwood et Tercon —, puis le ministère a finalement opté pour la première. Tercon a intenté une action en dommages-intérêts contre la province et elle a eu gain de cause. La juge de première instance a conclu que la soumission de Brentwood était en fait celle de la coentreprise formée avec EAC, et que la province, qui le savait, avait contrevenu aux stipulations expresses du contrat intervenu avec Tercon en acceptant la soumission d'une autre entreprise qui n'était pas admissible, puis en confiant les travaux à cette même entreprise. Elle a aussi statué que le libellé de la clause de non-recours ne faisait pas obstacle à l'indemnisation pour les inexécutions relevées. La clause était équivoque et elle l'a interprétée en faveur de Tercon. Elle a estimé que l'inexécution reprochée à la province était fondamentale et qu'il n'était ni juste ni raisonnable de faire respecter la clause de non-recours étant donné la nature de l'inexécution. La Cour d'appel a annulé sa décision, statuant que la clause de non-recours était claire et non équivoque et qu'elle faisait obstacle à l'indemnisation pour toute inexécution.

Arrêt (la juge en chef McLachlin et les juges Binnie, Abella et Rothstein sont dissidents) : Le pourvoi est accueilli. Les juges de la Cour conviennent du cadre de l'analyse qui s'impose, mais ils sont partagés sur l'applicabilité de la clause de non-recours aux faits de l'espèce.

La Cour : Pour ce qui concerne le cadre d'analyse approprié, il convient de donner le « coup de grâce » au

should be "laid to rest". The following analysis should be applied when a plaintiff seeks to escape the effect of an exclusion clause or other contractual terms to which it had previously agreed. The first issue is whether, as a matter of interpretation, the exclusion clause even applies to the circumstances established in evidence. This will depend on the court's interpretation of the intention of the parties as expressed in the contract. If the exclusion clause applies, the second issue is whether the exclusion clause was unconscionable and thus invalid at the time the contract was made. If the exclusion clause is held to be valid at the time of contract formation and applicable to the facts of the case, a third enquiry may be raised as to whether the court should nevertheless refuse to enforce the exclusion clause because of an overriding public policy. The burden of persuasion lies on the party seeking to avoid enforcement of the clause to demonstrate an abuse of the freedom of contract that outweighs the very strong public interest in their enforcement. Conduct approaching serious criminality or egregious fraud are but examples of well-accepted considerations of public policy that are substantially incontestable and may override the public policy of freedom to contract and disable the defendant from relying upon the exclusion clause. Despite agreement on the appropriate framework of analysis, the court divided on the applicability of the exclusion clause to the facts of this case as set out below.

Per LeBel, Deschamps, Fish, Charron and Cromwell JJ.: The Province breached the express provisions of the tendering contract with Tercon by accepting a bid from a party who should not even have been permitted to participate in the tender process and by ultimately awarding the work to that ineligible bidder. This egregious conduct by the Province also breached the implied duty of fairness to bidders. The exclusion clause, which barred claims for compensation "as a result of participating" in the tendering process, did not, when properly interpreted, exclude Tercon's claim for damages. By considering a bid from an ineligible bidder, the Province not only acted in a way that breached the express and implied terms of the contract, it did so in a manner that was an affront to the integrity and business efficacy of the tendering process.

Submitting a compliant bid in response to a tender call may give rise to "Contract A" between the bidder and the owner. Whether a Contract A arises and what its terms are depends on the express and implied terms and conditions of the tender call and the legal consequences of the parties' actual dealings in each case.

principe de l'inexécution fondamentale. L'analyse qui suit vaut lorsque le demandeur tente de se soustraire à l'application d'une clause d'exonération ou d'une autre stipulation contractuelle dont il a précédemment convenu. Il faut d'abord déterminer, par voie d'interprétation, si la clause de non-recours s'applique aux faits mis en preuve, ce qui dépend de l'intention des parties qui se dégage du contrat. Lorsque la clause s'applique, il faut en deuxième lieu se demander si elle était inique et de ce fait invalide au moment de la formation du contrat. Lorsqu'elle est jugée valide au moment de la formation du contrat et applicable aux faits de l'espèce, le tribunal peut se demander dans un troisième temps s'il devrait tout de même refuser de la faire respecter en raison d'une considération d'ordre public prépondérante. Il incombe à la partie qui tente de se soustraire à l'application de la clause de prouver un abus de la liberté contractuelle qui l'emporte sur le très grand intérêt public lié au respect des contrats. Le comportement qui se rapproche de l'acte criminel grave ou de la fraude monumentale n'est qu'un exemple de considération d'ordre public bien établie et « foncièrement incontestable » pouvant primer la liberté contractuelle, elle aussi d'ordre public, et empêcher le défendeur de se retrancher derrière la clause de non-recours. Même si les juges de la Cour conviennent du cadre de l'analyse qui s'impose, ils sont partagés sur l'applicabilité de la clause de non-recours aux faits de l'espèce, comme il appert ci-après.

Les juges LeBel, Deschamps, Fish, Charron et Cromwell : La province a contrevenu aux stipulations expresses du contrat issu de l'appel d'offres et intervenu avec Tercon en acceptant la proposition d'une entreprise qui n'était pas admise à prendre part au processus d'appel d'offres, puis en confiant les travaux à cette même entreprise inadmissible. Par ce comportement inacceptable, la province a également manqué à son obligation tacite d'équité envers les soumissionnaires. Correctement interprétée, la clause de non-recours, qui écartait toute demande d'indemnisation « pour [l]a participation » à l'appel d'offres, ne faisait pas obstacle au recours en dommages-intérêts de Tercon. En considérant l'offre d'un soumissionnaire inadmissible, la province a non seulement manqué à ses obligations contractuelles expresses et tacites, mais elle l'a fait d'une manière qui portait outrageusement atteinte à l'intégrité et à l'efficacité commerciale du processus d'appel d'offres.

Le dépôt d'une soumission conforme en réponse à un appel d'offres peut faire naître un « contrat A » entre le soumissionnaire et le propriétaire. L'existence d'un tel contrat et sa teneur dépendent des conditions expresses et tacites de l'appel d'offres ainsi que des conséquences juridiques des échanges intervenus entre les parties.

Here, there is no basis to interfere with the trial judge's findings that there was an intent to create contractual obligations upon submission of a compliant bid and that only the six original proponents that qualified through the RFEI process were eligible to submit a response to the RFP. The tender documents and the required ministerial approval of the process stated expressly that the Province was contractually bound to accept bids only from eligible bidders. Contract A therefore could not arise by the submission of a bid from any other party. The trial judge found that the joint venture of Brentwood and EAC was not eligible to bid as they had not simply changed the composition of their team but, in effect, had created a new bidder. The Province fully understood this and would not consider a bid from or award the work to that joint venture. The trial judge did not err in finding that in fact, if not in form, Brentwood's bid was on behalf of a joint venture between itself and EAC. The joint venture provided Brentwood with a competitive advantage in the bidding process and was a material consideration in favour of the Brentwood bid during the Province's evaluation process. Moreover, the Province took active steps to obfuscate the reality of the true nature of the Brentwood bid. The bid by the joint venture constituted "material non-compliance" with the tendering contract and breached both the express eligibility provisions of the tender documents, and the implied duty to act fairly towards all bidders.

En l'espèce, il n'y a pas lieu de modifier la conclusion de la juge de première instance selon laquelle la présentation d'une soumission conforme était censée faire naître des obligations contractuelles et seules les six entreprises intéressées initialement, devenues admissibles à l'issue de la DEI, pouvaient donner suite à la DP. L'obligation de la province de considérer seulement les propositions de soumissionnaires admissibles figurait expressément dans le dossier d'appel d'offres et dans l'approbation ministérielle requise du processus. Un contrat A ne pouvait donc pas naître de la présentation d'une soumission par une autre personne. La juge de première instance a conclu que la coentreprise formée de Brentwood et d'EAC n'était pas un soumissionnaire admissible, car la composition de l'équipe n'était pas simplement modifiée, mais un nouveau soumissionnaire voyait en fait le jour. La province le savait bien et elle estimait qu'elle ne pouvait ni considérer la proposition de cette coentreprise ni adjuger le contrat à celle-ci. La juge de première instance n'a pas eu tort de conclure qu'en dépit des apparences, la soumission de Brentwood était en fait présentée par la coentreprise formée avec EAC. L'existence de la coentreprise a fait bénéficier Brentwood d'un avantage concurrentiel dans le processus d'appel d'offres, et la province l'a considérée comme un élément favorable à Brentwood lors de son processus d'évaluation. De plus, la province a pris des mesures pour masquer la véritable nature de la soumission de Brentwood. La présentation d'une proposition par une coentreprise constituait une « inexécution importante » du contrat issu de l'appel d'offres ainsi qu'une inobservation des conditions expresses d'admissibilité et de l'obligation tacite d'agir équitablement vis-à-vis de tous les soumissionnaires.

When the exclusion clause is interpreted in harmony with the rest of the RFP and in light of the commercial context of the tendering process, it did not exclude a damages claim resulting from the Province unfairly permitting an ineligible bidder to participate in the tendering process. The closed list of bidders was the foundation of this RFP and the parties should, at the very least, be confident that their initial bids will not be skewed by some underlying advantage in the drafting of the call for tenders conferred only upon one potential bidder. The requirement that only compliant bids be considered and the implied obligation to treat bidders fairly are factors that contribute to the integrity and business efficacy of the tendering process. The parties did not intend, through the words found in this exclusion clause, to waive compensation for conduct, like that of the Province in this case, that strikes at the heart of the tendering process. Clear language would be necessary to exclude liability for breach of the implied obligation, particularly in the case of public procurement where

Interprétée en harmonie avec les autres conditions de la DP et eu égard au contexte commercial de l'appel d'offres, la clause de non-recours n'écartait pas le recours en dommages-intérêts intenté au motif que la province avait inéquitablement permis à une entreprise inadmissible de prendre part au processus. La limitation du nombre de soumissionnaires admissibles constituait l'assise de la DP, et un soumissionnaire devait à tout le moins être assuré que l'évaluation de sa soumission initiale ne serait pas biaisée par quelque avantage sous-entendu dans le dossier d'appel d'offres et dont ne bénéficiait qu'un seul soumissionnaire éventuel. L'exigence que seules soient examinées des soumissions conformes et l'obligation tacite de traiter tous les soumissionnaires équitablement sont généralement considérées comme des éléments contribuant à l'intégrité et à l'efficacité commerciale du processus d'appel d'offres. Les parties n'ont pas voulu, en employant le libellé de la clause de non-recours, écarter toute indemnisation pour un comportement comme celui reproché à la province

transparency is essential. Furthermore, the restriction on eligibility of bidders was a key element of the alternative process approved by the Minister. When the statutory provisions which governed the tendering process in this case are considered, it seems unlikely that the parties intended through this exclusion clause to effectively gut a key aspect of the approved process. The text of the exclusion clause in the RFP addresses claims that result from "participating in this RFP". Central to "participating in this RFP" was participating in a contest among those eligible to participate. A process involving other bidders — the process followed by the Province — is not the process called for by "this RFP" and being part of that other process is not in any meaningful sense "participating in this RFP".

Per McLachlin C.J. and Binnie, Abella and Rothstein JJ. (dissenting): The Ministry's conduct, while in breach of its contractual obligations, fell within the terms of the exclusion compensation clause. The clause is clear and unambiguous and no legal ground or rule of law permits a court to override the freedom of the parties to contract with respect to this particular term, or to relieve Tercon against its operation in this case. A court has no discretion to refuse to enforce a valid and applicable contractual term unless the plaintiff can point to some paramount consideration of public policy sufficient to override the public interest in freedom of contact and defeat what would otherwise be the contractual rights of the parties. The public interest in the transparency and integrity of the government tendering process, while important, did not render unenforceable the terms of the contract Tercon agreed to.

Brentwood was a legitimate competitor in the RFP process and all bidders knew that the road contract would not be performed by the proponent alone and required a large "team" of different trades and personnel to perform. The issue was whether EAC would be on the job as a major sub-contractor or identified with Brentwood as a joint venture "proponent" with EAC. Tercon has legitimate reason to complain about the Ministry's conduct, but its misconduct did not rise to the level where public policy would justify the court in depriving the Ministry of the protection of the exclusion of compensation clause freely agreed to by Tercon in the contract.

en l'espèce, un comportement qui porte directement atteinte à l'intégrité de l'appel d'offres. Seul un libellé clair peut écarter la responsabilité consécutive au non-respect de l'obligation tacite, spécialement dans le cas de la passation de marchés publics, où la transparence est de rigueur. Qui plus est, l'admissibilité restreinte constituait un élément essentiel de l'autre processus approuvé par le ministre. Au regard du cadre législatif régissant l'appel d'offres en l'espèce, il est peu probable que les parties aient vraiment voulu, en stipulant la clause de non-recours, supprimer un aspect essentiel de ce processus. Le texte de la clause de non-recours de la DP vise les demandes d'indemnisation d'un préjudice découlant de la « participation à la DP ». La participation à un concours ouvert aux seules personnes admises à y prendre part était donc au cœur de la « participation à la DP ». Un processus ouvert à d'autres entreprises — ce qui était le cas du processus suivi par la province — ne saurait s'entendre de « la DP », et le fait d'y prendre part ne saurait véritablement être considéré comme une « participation à la DP ».

La juge en chef McLachlin et les juges Binnie, Abella et Rothstein (dissidents) : Même s'il n'a pas respecté ses obligations contractuelles, le ministère bénéficie de la clause de non-recours en indemnisation. La clause est claire et non équivoque, et aucune règle de droit ou autre fondement juridique ne permet aux tribunaux de passer outre à la liberté des parties de convenir de cette condition ni de soustraire Tercon à son application en l'espèce. Le tribunal n'a pas le pouvoir discrétionnaire de refuser de faire respecter une clause contractuelle valide et applicable, sauf lorsque le demandeur fait valoir une considération d'ordre public prépondérante qui l'emporte sur l'intérêt public lié à la liberté de contracter et qui fait obstacle à ce qui, autrement, constitueraient les droits contractuels des parties. L'intérêt public lié à la transparence et à l'intégrité du processus gouvernemental d'appel d'offres, même s'il est important, n'a pas rendu inapplicables les clauses du contrat auxquelles Tercon avait consenti.

Brentwood était un concurrent légitime dans le processus de DP. Tous les soumissionnaires savaient que le contrat de construction routière ne serait pas exécuté seulement par le proposant retenu, mais bien par une grande « équipe » pluridisciplinaire. La question était celle de savoir si EAC serait sous-traitant principal ou « proposant » dans le cadre de la coentreprise avec Brentwood. Tercon a raison de dénoncer le comportement du ministère, mais celui-ci n'était pas répréhensible au point que l'ordre public justifie le tribunal de refuser au ministère la protection de la clause de non-recours en indemnisation à laquelle Tercon avait librement consenti.

Contract A is based not on some abstract externally imposed rule of law but on the presumed (and occasionally implied) intent of the parties. At issue is the intention of the actual parties not what the court may project in hindsight would have been the intention of reasonable parties. Only in rare circumstances will a court relieve a party from the bargain it has made.

The exclusion clause did not run afoul of the statutory requirements. While the *Ministry of Transportation and Highways Act* favours "the integrity of the tendering process", it nowhere prohibits the parties from negotiating a "no claims" clause as part of their commercial agreement and cannot plausibly be interpreted to have that effect. Tercon — a sophisticated and experienced contractor — chose to bid on the project, including the risk posed by an exclusion of compensation clause, on the terms proposed by the Ministry. That was its prerogative and nothing in the "policy of the Act" barred the parties' agreement on that point.

The trial judge found that Contract A was breached when the RFP process was not conducted by the Ministry with the degree of fairness and transparency that the terms of Contract A entitled Tercon to expect. The Ministry was at fault in its performance of the RFP, but the process did not thereby cease to be the RFP process in which Tercon had elected to participate.

The interpretation of the majority on this point is disagreed with. "[P]articipating in this RFP" began with "submitting a Proposal" for consideration. The RFP process consisted of more than the final selection of the winning bid and Tercon participated in it. Tercon's bid was considered. To deny that such participation occurred on the ground that in the end the Ministry chose a Brentwood joint venture (an ineligible bidder) instead of Brentwood itself (an eligible bidder) would be to give the clause a strained and artificial interpretation in order, indirectly and obliquely, to avoid the impact of what may seem to the majority *ex post facto* to have been an unfair and unreasonable clause.

Moreover, the exclusion clause was not unconscionable. While the Ministry and Tercon do not exercise the same level of power and authority, Tercon is a major contractor and is well able to look after itself in a commercial context so there is no relevant imbalance of bargaining power. Further, the clause is not as draconian as Tercon portrays it. Other remedies for breach of Contract A were available. The parties expected, even if they did not like it, that the "no claims" clause would

L'assise du contrat A demeure l'intention présumée (et parfois inférée) des parties, et non quelque règle de droit abstraite imposée par un tiers. C'est l'intention des parties elles-mêmes qui importe, et non ce qui, à l'issue d'une analyse rétrospective du tribunal, aurait été l'intention de parties raisonnables. Ce n'est qu'en de rares circonstances que le tribunal relève une partie de ses engagements.

La clause de non-recours ne dérogeait pas aux exigences légales. La *Ministry of Transportation and Highways Act* favorise « l'intégrité du processus d'appel d'offres », mais aucune de ses dispositions n'empêche les parties de faire figurer dans leur accord commercial une clause « écartant toute indemnisation » ni ne peut vraisemblablement être interprétée comme ayant cet effet. Tercon — une entreprise avertie et expérimentée — a décidé de participer au processus aux conditions proposées par le ministère malgré le risque posé par la clause de non-recours en indemnisation. C'était sa décision, et la « raison d'être de la Loi » ne faisait aucunement obstacle à la convention des parties sur ce point.

La juge du procès a conclu à l'inexécution du contrat A du fait que, dans sa DP, le ministère n'a pas agi avec l'équité et la transparence auxquelles Tercon était en droit de s'attendre vu le libellé du contrat A. Le ministère a été fautif dans sa mise en œuvre de la DP, mais le processus n'a pas cessé pour autant d'être la DP à laquelle Tercon avait décidé de prendre part.

Les juges dissidents ne souscrivent pas à l'interprétation des juges majoritaires à cet égard. La « participation à la DP » a commencé par la « présent[ation d']une soumission ». Le processus de DP ne se résumait pas au choix final de l'adjudicataire, et Tercon y a participé. La soumission de Tercon a été considérée. Nier cette participation au motif que le ministère a finalement choisi la coentreprise inadmissible dont faisait partie Brentwood, et non Brentwood elle-même (qui était admissible), équivaut à une interprétation forcée et artificielle visant à éviter, par des moyens indirects et détournés, les conséquences de ce qui peut sembler aux juges majoritaires, *ex post facto*, avoir été une clause injuste et déraisonnable.

En outre, la clause de non-recours n'était pas inique. Tercon n'a ni le pouvoir ni l'autorité du ministère, mais c'est une entreprise importante parfaitement en mesure de défendre ses intérêts commerciaux. Il n'y avait donc pas d'inégalité déterminante du pouvoir de négociation. Aussi, la clause de non-recours n'est pas aussi draconienne que le laisse entendre Tercon. L'inexécution du contrat A donnait ouverture à d'autres recours. Les parties s'attendaient, même si cette éventualité ne les

operate even where the eligibility criteria in respect of the bid (including the bidder) were not complied with.

Finally, the Ministry's misconduct did not rise to the level where public policy would justify the court in depriving the Ministry of the protection of the exclusion of compensation clause freely agreed to by Tercon in the contract.

Cases Cited

By Cromwell J.

Applied: *M.J.B. Enterprises Ltd. v. Defence Construction (1951) Ltd.*, [1999] 1 S.C.R. 619; *Martel Building Ltd. v. Canada*, 2000 SCC 60, [2000] 2 S.C.R. 860; **considered:** *Hunter Engineering Co. v. Syncrude Canada Ltd.*, [1989] 1 S.C.R. 426; *Cahill (G.J.) & Co. (1979) Ltd. v. Newfoundland and Labrador (Minister of Municipal and Provincial Affairs)*, 2005 NLTD 129, 250 Nfld. & P.E.I.R. 145; *Guarantee Co. of North America v. Gordon Capital Corp.*, [1999] 3 S.C.R. 423; *Fraser Jewellers (1982) Ltd. v. Dominion Electric Protection Co.* (1997), 34 O.R. (3d) 1; **referred to:** *Canadian Pacific Hotels Ltd. v. Bank of Montreal*, [1987] 1 S.C.R. 711; *Double N Earthmovers Ltd. v. Edmonton (City)*, 2007 SCC 3, [2007] 1 S.C.R. 116; *Hillis Oil and Sales Ltd. v. Wynn's Canada, Ltd.*, [1986] 1 S.C.R. 57.

By Binnie J. (dissenting)

Hunter Engineering Co. v. Syncrude Canada Ltd., [1989] 1 S.C.R. 426; *The Queen in right of Ontario v. Ron Engineering & Construction (Eastern) Ltd.*, [1981] 1 S.C.R. 111; *M.J.B. Enterprises Ltd. v. Defence Construction (1951) Ltd.*, [1999] 1 S.C.R. 619; *Naylor Group Inc. v. Ellis-Don Construction Ltd.*, 2001 SCC 58, [2001] 2 S.C.R. 943; *Martel Building Ltd. v. Canada*, 2000 SCC 60, [2000] 2 S.C.R. 860; *Double N Earthmovers Ltd. v. Edmonton (City)*, 2007 SCC 3, [2007] 1 S.C.R. 116; *Tercon Contractors Ltd. v. British Columbia* (1993), 9 C.L.R. (2d) 197, aff'd [1994] B.C.J. No. 2658 (QL); *Karsales (Harrow) Ltd. v. Wallis*, [1956] 1 W.L.R. 936; *Guarantee Co. of North America v. Gordon Capital Corp.*, [1999] 3 S.C.R. 423; *ABB Inc. v. Domtar Inc.*, 2007 SCC 50, [2007] 3 S.C.R. 461; *Re Millar Estate*, [1938] S.C.R. 1; *Plas-Tex Canada Ltd. v. Dow Chemical of Canada Ltd.*, 2004 ABCA 309, 245 D.L.R. (4th) 650.

Statutes and Regulations Cited

Ministry of Transportation and Highways Act, R.S.B.C. 1996, c. 311, ss. 4, 23.

enchantait guère, à ce que la clause « écartant toute indemnisation » s'applique advenant même le non-respect des critères d'admissibilité de la soumission (et de son auteur).

Enfin, l'inconduite n'était pas répréhensible au point que l'ordre public justifie le tribunal de refuser au ministère la protection de la clause de non-recours en indemnisation à laquelle Tercon a librement consenti.

Jurisprudence

Citée par le juge Cromwell

Arrêts appliqués : *M.J.B. Enterprises Ltd. c. Construction de Défense (1951) Ltée*, [1999] 1 R.C.S. 619; *Martel Building Ltd. c. Canada*, 2000 CSC 60, [2000] 2 R.C.S. 860; **arrêts examinés :** *Hunter Engineering Co. c. Syncrude Canada Ltée*, [1989] 1 R.C.S. 426; *Cahill (G.J.) & Co. (1979) Ltd. c. Newfoundland and Labrador (Minister of Municipal and Provincial Affairs)*, 2005 NLTD 129, 250 Nfld. & P.E.I.R. 145; *Guarantee Co. of North America c. Gordon Capital Corp.*, [1999] 3 R.C.S. 423; *Fraser Jewellers (1982) Ltd. c. Dominion Electric Protection Co.* (1997), 34 O.R. (3d) 1; **arrêts mentionnés :** *Société hôtelière Canadien Pacifique Ltée c. Banque de Montréal*, [1987] 1 R.C.S. 711; *Double N Earthmovers Ltd. c. Edmonton (Ville)*, 2007 CSC 3, [2007] 1 R.C.S. 116; *Hillis Oil and Sales Ltd. c. Wynn's Canada, Ltd.*, [1986] 1 R.C.S. 57.

Citée par le juge Binnie (dissident)

Hunter Engineering Co. c. Syncrude Canada Ltée, [1989] 1 R.C.S. 426; *La Reine du chef de l'Ontario c. Ron Engineering & Construction (Eastern) Ltd.*, [1981] 1 R.C.S. 111; *M.J.B. Enterprises Ltd. c. Construction de Défense (1951) Ltée*, [1999] 1 R.C.S. 619; *Naylor Group Inc. c. Ellis-Don Construction Ltd.*, 2001 CSC 58, [2001] 2 R.C.S. 943; *Martel Building Ltd. c. Canada*, 2000 CSC 60, [2000] 2 R.C.S. 860; *Double N Earthmovers Ltd. c. Edmonton (Ville)*, 2007 CSC 3, [2007] 1 R.C.S. 116; *Tercon Contractors Ltd. c. British Columbia* (1993), 9 C.L.R. (2d) 197, conf. par [1994] B.C.J. No. 2658 (QL); *Karsales (Harrow) Ltd. c. Wallis*, [1956] 1 W.L.R. 936; *Guarantee Co. of North America c. Gordon Capital Corp.*, [1999] 3 R.C.S. 423; *ABB Inc. c. Domtar Inc.*, 2007 CSC 50, [2007] 3 R.C.S. 461; *Re Millar Estate*, [1938] R.C.S. 1; *Plas-Tex Canada Ltd. c. Dow Chemical of Canada Ltd.*, 2004 ABCA 309, 245 D.L.R. (4th) 650.

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APPEAL from a judgment of the British Columbia Court of Appeal (Donald, Mackenzie and Lowry JJ.A.), 2007 BCCA 592, 73 B.C.L.R. (4th) 201, 40 B.L.R. (4th) 26, 289 D.L.R. (4th) 647, [2008] 2 W.W.R. 410, 249 B.C.A.C. 103, 414 W.A.C. 103, 66 C.L.R. (3d) 1, [2007] B.C.J. No. 2558 (QL), 2007 CarswellBC 2880, setting aside a decision of Dillon J., 2006 BCSC 499, 53 B.C.L.R. (4th) 138, [2006] 6 W.W.R. 275, 18 B.L.R. (4th) 88, 51 C.L.R. (3d) 227, [2006] B.C.J. No. 657 (QL), 2006 CarswellBC 730. Appeal allowed, McLachlin C.J. and Binnie, Abella and Rothstein JJ. dissenting.

Chris R. Armstrong, *Brian G. McLean*, *William S. McLean* and *Marie-France Major*, for the appellant.

J. Edward Gouge, *Q.C.*, *Jonathan Eades* and *Kate Hamm*, for the respondent.

Malliha Wilson and *Lucy McSweeney*, for the intervener.

The judgment of LeBel, Deschamps, Fish, Charron and Cromwell JJ. was delivered by

CROMWELL J. —

I. Introduction

[1] The Province accepted a bid from a bidder who was not eligible to participate in the tender and then took steps to ensure that this fact was not disclosed. The main question on appeal, as I see it, is whether the Province succeeded in excluding

Doctrine citée

Hall, Geoff R. *Canadian Contractual Interpretation Law*. Markham, Ont. : LexisNexis, 2007.

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Chris R. Armstrong, *Brian G. McLean*, *William S. McLean* et *Marie-France Major*, pour l'appelante.

J. Edward Gouge, *c.r.*, *Jonathan Eades* et *Kate Hamm*, pour l'intimée.

Malliha Wilson et *Lucy McSweeney*, pour l'intervenant.

Version française du jugement des juges LeBel, Deschamps, Fish, Charron et Cromwell rendu par

LE JUGE CROMWELL —

I. Introduction

[1] La province a accepté la soumission d'une entreprise non admise à participer à l'appel d'offres, puis elle a pris des mesures pour dissimuler ce fait. De mon point de vue, la principale question que soulève le pourvoi est celle de savoir si, grâce à

its liability for damages flowing from this conduct through an exclusion clause it inserted into the contract. I share the view of the trial judge that it did not.

[2] The appeal arises out of a tendering contract between the appellant, Tercon Contractors Ltd., who was the bidder, and the respondent, Her Majesty the Queen in Right of the Province of British Columbia, who issued the tender call. The case turns on the interpretation of provisions in the contract relating to eligibility to bid and exclusion of compensation resulting from participation in the tendering process.

[3] The trial judge found that the respondent (which I will refer to as the Province) breached the express provisions of the tendering contract with Tercon by accepting a bid from another party who was not eligible to bid and by ultimately awarding the work to that ineligible bidder. In short, a bid was accepted and the work awarded to a party who should not even have been permitted to participate in the tender process. The judge also found that this and related conduct by the Province breached the implied duty of fairness to bidders, holding that the Province had acted "egregiously" (2006 BCSC 499, 53 B.C.L.R. (4th) 138, at para. 150). The judge then turned to the Province's defence based on an exclusion clause that barred claims for compensation "as a result of participating" in the tendering process. She held that this clause, properly interpreted, did not exclude Tercon's claim for damages. In effect, she held that it was not within the contemplation of the parties that this clause would bar a remedy in damages arising from the Province's unfair dealings with a party who was not entitled to participate in the tender in the first place.

[4] The Province appealed and the Court of Appeal reversed (2007 BCCA 592, 73 B.C.L.R. (4th) 201). Dealing only with the exclusion clause issue, it held that the clause was clear and unambiguous and barred compensation for all defaults.

la clause de non-recours en indemnisation (« clause de non-recours ») qu'elle a insérée dans le contrat, la province parvient à échapper à la responsabilité civile découlant de ces actes. À l'instar de la juge de première instance, je conclus par la négative.

[2] Le pourvoi fait suite au contrat issu de l'appel d'offres et intervenu entre l'appelante Tercon Contractors Ltd., le soumissionnaire, et l'intimée Sa Majesté la Reine du chef de la Colombie-Britannique (la « province »), l'auteur de l'appel d'offres. Le dénouement de l'affaire tient à l'interprétation des clauses du contrat relatives à l'admissibilité à soumissionner et à l'exclusion de toute indemnité pour la participation à la demande de propositions.

[3] La juge de première instance conclut que la province a contrevenu aux stipulations expresses du contrat intervenu avec Tercon en acceptant la proposition d'un autre soumissionnaire qui n'était pas admissible, puis en confiant les travaux à ce même soumissionnaire. Pour faire court, une proposition a été acceptée et le marché a été accordé à une entreprise qui n'aurait même pas dû être admise à participer au processus. La juge de première instance conclut également que par ces actes et d'autres mesures connexes, la province a manqué à son obligation tacite d'équité envers les soumissionnaires et qu'elle a agi [TRADUCTION] « de manière inacceptable » (2006 BCSC 499, 53 B.C.L.R. (4th) 138, par. 150). Elle se penche ensuite sur la clause de non-recours qui, selon la province, ferait obstacle à toute demande d'indemnisation [TRADUCTION] « pour [l]a participation » à l'appel d'offres. Elle estime que, correctement interprétée, la clause ne faisait pas obstacle au recours en dommages-intérêts de Tercon. Elle statue en effet que les parties n'ont pas envisagé que la clause empêche un tel recours intenté pour l'iniquité dont a fait preuve la province en se mettant en rapport avec une entreprise qui n'était même pas admise à soumissionner.

[4] La province s'est adressée à la Cour d'appel, qui lui a donné raison, se prononçant uniquement sur la clause de non-recours et statuant qu'elle était claire et non équivoque et qu'elle faisait obstacle à l'indemnisation pour toute inexécution (2007 BCCA 592, 73 B.C.L.R. (4th) 201).

[5] On Tercon's appeal to this Court, the questions for us are whether the successful bidder was eligible to participate in the request for proposals ("RFP") and, if not, whether Tercon's claim for damages is barred by the exclusion clause.

[6] In my respectful view, the trial judge reached the right result on both issues. The Province's attempts to persuade us that it did not breach the tendering contract are, in my view, wholly unsuccessful. The foundation of the tendering contract was that only six, pre-selected bidders would be permitted to participate in the bidding. As the trial judge held, the Province not only acted in a way that breached the express and implied terms of the contract by considering a bid from an ineligible bidder, it did so in a manner that was an affront to the integrity and business efficacy of the tendering process. One must not lose sight of the fact that the trial judge found that the Province acted egregiously by "ensuring that [the true bidder] was not disclosed" (para. 150) and that its breach "attacke[d] the underlying premise of the [tendering] process" (para. 146), a process which was set out in detail in the contract and, in addition, had been given ministerial approval as required by statute.

[7] As for its reliance on the exclusion clause, the Province submits that the parties were free to agree to limitations of liability and did so. Consideration of this submission requires an interpretation of the words of the clause to which the parties agreed in the context of the contract as a whole. My view is that, properly interpreted, the exclusion clause does not protect the Province from Tercon's damage claim which arises from the Province's dealings with a party not even eligible to bid, let alone from its breach of the implied duty of fairness to bidders. In other words, the Province's liability did not arise from Tercon's participation in the process that the Province established, but from the Province's unfair dealings with a party who was not entitled to participate in that process.

[8] I would allow the appeal and restore the judgment of the trial judge.

[5] Dans le pourvoi formé par Tercon, la Cour est appelée à déterminer si l'adjudicataire était admis à participer à la demande de propositions (« DP ») et, dans la négative, si la clause de non-recours fait obstacle au recours en dommages-intérêts de Tercon.

[6] En toute déférence, j'estime que la juge de première instance tranche correctement les deux questions. La province n'est pas du tout parvenue, selon moi, à convaincre la Cour qu'elle n'avait pas manqué à ses obligations contractuelles. Suivant le contrat issu de l'appel d'offres, seules six entreprises présélectionnées pouvaient prendre part à l'appel d'offres. La juge statue qu'en considérant l'offre d'un soumissionnaire inadmissible, la province a manqué à ses obligations contractuelles expresses et tacites, et ce, d'une manière qui portait outrageusement atteinte à l'intégrité et à l'efficacité commerciale du processus d'appel d'offres. Sans oublier qu'à son avis, la province a agi de manière inacceptable en [TRADUCTION] « veillant à ce que [l'identité du véritable soumissionnaire] ne soit pas révélée » (par. 150). La juge ajoute que cette inexécution [TRADUCTION] « a sapé l'assise du processus [d'appel d'offres] » (par. 146), lequel était décrit en détail dans le contrat et, qui plus est, avait obtenu l'approbation ministérielle exigée par la loi.

[7] Pour ce qui concerne l'application de la clause de non-recours, la province soutient que les parties étaient libres de limiter leur responsabilité comme elles l'ont fait. Statuer sur cette prétention exige que l'on interprète le libellé de la clause dont les parties ont convenu, au vu du contrat dans son entier. J'estime que, correctement interprétée, la clause de non-recours ne protège pas la province contre l'action en dommages-intérêts intentée par Tercon pour la mise en rapport de la province avec une entreprise qui n'était même pas admise à soumissionner, sans compter le manquement à son obligation tacite d'équité envers les soumissionnaires. Autrement dit, la responsabilité de la province ne résulte pas de la participation de Tercon au processus, mais bien de l'iniquité dont la province s'est rendue coupable en se mettant en rapport avec une entreprise non admise à prendre part à ce processus.

[8] Je suis d'avis d'accueillir le pourvoi et de rétablir le jugement de première instance.

II. Brief Overview of the Facts

[9] I will have to set out more factual detail as part of my analysis. For now, a very brief summary will suffice. In 2000, the Ministry of Transportation and Highways (also referred to as the "Province") issued a request for expressions of interest ("RFEI") for designing and building a highway in northwestern British Columbia. Six teams made submissions, including Tercon and Brentwood Enterprises Ltd. Later that year, the Province informed the six proponents that it now intended to design the highway itself and would issue a RFP for its construction.

[10] The RFP was formally issued on January 15, 2001. Under its terms, only the six original proponents were eligible to submit a proposal. The RFP also included a clause excluding all claims for damages "as a result of participating in this RFP" (s. 2.10).

[11] Unable to submit a competitive bid on its own, Brentwood teamed up with Emil Anderson Construction Co. ("EAC"), which was not a qualified bidder, and together they submitted a bid in Brentwood's name. Brentwood and Tercon were the two short-listed proponents and the Ministry ultimately selected Brentwood as the preferred proponent.

[12] Tercon brought an action seeking damages, alleging that the Ministry had considered and accepted an ineligible bid and that, but for that breach, it would have been awarded the contract. The trial judge agreed and awarded roughly $3.5 million in damages and prejudgment interest. As noted, the Court of Appeal reversed and Tercon appeals by leave of the Court.

III. Issues

[13] The issues for decision are whether the trial judge erred in finding that:

1. the Province breached the tendering contract by entertaining a bid from an ineligible bidder.

II. Bref aperçu des faits

[9] Je reviendrai plus en détail sur les faits, mais pour l'heure, en voici un bref résumé. En 2000, le ministère des Transports et de la Voirie (également appelé la « province ») a lancé une demande d'expression d'intérêt (« DEI ») pour la conception et la construction d'une route dans le nord-ouest de la Colombie-Britannique. Elle a reçu six soumissions, dont celles de Tercon et de Brentwood Enterprises Ltd. Plus tard la même année, la province a fait savoir aux six entreprises intéressées qu'elle entendait désormais concevoir elle-même la route et demander des propositions pour sa construction.

[10] Lancée officiellement le 15 janvier 2001, la DP précisait que seules les six entreprises intéressées initialement étaient admises à soumissionner. Elle comportait aussi une clause écartant tout recours en indemnisation [TRADUCTION] « pour [l]a participation à la DP » (clause 2.10).

[11] Incapable de présenter seule une soumission concurrentielle, Brentwood s'est jointe à Emil Anderson Construction Co. (« EAC »), qui n'était pas un soumissionnaire admissible, et une proposition commune a été présentée au nom de Brentwood. La liste des adjudicataires possibles a été ramenée à deux entreprises — Brentwood et Tercon —, puis le ministère a finalement opté pour la première.

[12] Tercon a intenté une action en dommages-intérêts, alléguant que le ministère avait examiné puis accepté une soumission inadmissible et que, n'eût été ce manquement, elle aurait obtenu le contrat. Elle a eu gain de cause en première instance et obtenu une indemnité d'environ 3,5 millions de dollars plus l'intérêt avant jugement, mais elle a été déboutée en Cour d'appel. Tercon se pourvoit devant notre Cour sur autorisation.

III. Les questions en litige

[13] Notre Cour doit déterminer si la juge de première instance a eu tort ou non de tirer les conclusions suivantes :

1. la province a manqué à une obligation contractuelle en considérant la proposition d'un soumissionnaire inadmissible;

2. the exclusion clause does not bar the appellant's claim for damages for the breaches of the tendering contract found by the trial judge.

IV. Analysis

A. *Was the Brentwood Bid Ineligible?*

[14] The first issue is whether the Brentwood bid was from an eligible bidder. The judge found that the bid was in substance, although not in form, from a joint venture of Brentwood and EAC and that it was, therefore, an ineligible bid. The Province attacks this finding on three grounds:

(i) a joint venture is not a legal person and therefore the Province could not and did not contract with a joint venture;

(ii) it did not award the contract to EAC and EAC had no contractual responsibility to the Province for failure to perform the contract;

(iii) there was no term of the RFP that restricted the right of proponents to enter into joint venture agreements with others; this arrangement merely left Brentwood, the original proponent, in place and allowed it to enhance its ability to perform the work.

[15] While these were the Province's main points, its position became more wide-ranging during oral argument, at times suggesting that it had no contractual obligation to deal only with eligible bidders. It is therefore necessary to take a step back and look at that threshold point before turning to the Province's more focussed submissions.

1. The Province's Contractual Obligations in the Bidding Process

[16] The judge found, and it was uncontested at trial, that only the six original proponents that

2. la clause de non-recours ne faisait pas obstacle au recours en dommages-intérêts de l'appelante pour les inexécutions contractuelles relevées par le tribunal.

IV. Analyse

A. *La proposition de Brentwood était-elle admissible?*

[14] La première question est celle de savoir si la proposition de Brentwood était présentée par un soumissionnaire admissible. La juge de première instance conclut que, malgré sa forme, la proposition provenait essentiellement d'une coentreprise formée de Brentwood et d'EAC et qu'elle était donc inadmissible. La province invoque trois motifs à l'encontre de cette conclusion :

(i) une coentreprise étant dépourvue de la personnalité morale, elle ne pouvait contracter avec une telle entité et elle ne l'a pas fait;

(ii) elle n'a pas adjugé le marché à EAC, et EAC n'avait envers elle aucune responsabilité en cas d'inexécution contractuelle;

(iii) aucune disposition de la DP n'interdisait aux proposants de s'associer à des tiers en coentreprise : Brentwood, proposant initial, demeurait simplement en lice et accroissait sa capacité d'exécuter les travaux.

[15] Ce sont les principaux arguments invoqués par la province, mais celle-ci a défendu une thèse beaucoup plus large en plaidoirie orale, faisant valoir à certains moments qu'elle n'était pas contractuellement tenue de se mettre en rapport seulement avec des soumissionnaires admissibles. Il faut donc revenir sur cette question préliminaire avant d'analyser les points plus précis de son argumentation.

1. Les obligations contractuelles de la province dans le processus d'appel d'offres

[16] La juge de première instance conclut — ce qui n'a pas été contesté au procès — que seules les

qualified through the RFEI process were eligible to submit a response to the RFP. This finding is not challenged on appeal, although there was a passing suggestion during oral argument that there was no contractual obligation of this sort at all. The trial judge also held, noting that this point was uncontested, that a joint venture between Brentwood and EAC was ineligible to bid. This is also not contested on appeal. These two findings are critical to the case and provide important background for an issue that is in dispute, namely whether the Brentwood bid was ineligible. It is, therefore, worth reviewing the relevant background in detail. I first briefly set out the legal framework and then turn to the trial judge's findings.

2. Legal Principles

[17] Submitting a compliant bid in response to a tender call *may* give rise to a contract — called Contract A — between the bidder and the owner, the express terms of which are found in the tender documents. The contract may also have implied terms according to the principles set out in *Canadian Pacific Hotels Ltd. v. Bank of Montreal*, [1987] 1 S.C.R. 711; see also *M.J.B. Enterprises Ltd. v. Defence Construction (1951) Ltd.*, [1999] 1 S.C.R. 619, and *Martel Building Ltd. v. Canada*, 2000 SCC 60, [2000] 2 S.C.R. 860. The key word, however, is "may". The Contract A/Contract B framework is one that arises, if at all, from the dealings between the parties. It is not an artificial construct imposed by the courts, but a description of the legal consequences of the parties' actual dealings. The Court emphasized in *M.J.B.* that whether Contract A arises and if it does, what its terms are, depend on the express and implied terms and conditions of the tender call in each case. As Iacobucci J. put it, at para. 19:

> What is important . . . is that the submission of a tender in response to an invitation to tender may give

six entreprises intéressées initialement, devenues admissibles à l'issue de la DEI, pouvaient donner suite à la DP. Cette conclusion n'est pas contestée en appel même si, en plaidoirie orale, la province a laissé entendre qu'elle n'avait pas d'obligation contractuelle concomitante. La juge estime également — et relève l'absence de contestation sur ce point — que la coentreprise formée de Brentwood et d'EAC n'était pas un soumissionnaire admissible. Cette conclusion n'est pas non plus contestée en appel. Ces deux conclusions sont cruciales en l'espèce et elles offrent une toile de fond importante pour trancher une question en litige, à savoir l'admissibilité de la proposition de Brentwood. Il convient donc d'examiner ce contexte en détail. Je ferai brièvement état du cadre juridique applicable avant de me pencher sur les conclusions de la juge de première instance.

2. Les principes juridiques

[17] Le dépôt d'une soumission conforme en réponse à un appel d'offres *peut* faire naître entre le soumissionnaire et le propriétaire un contrat — le contrat A — dont les conditions sont celles figurant dans le dossier d'appel d'offres. Le contrat peut également comporter des clauses tacites, suivant les principes formulés dans l'arrêt *Société hôtelière Canadien Pacifique Ltée c. Banque de Montréal*, [1987] 1 R.C.S. 711; voir aussi les arrêts *M.J.B. Enterprises Ltd. c. Construction de Défense (1951) Ltée*, [1999] 1 R.C.S. 619, et *Martel Building Ltd. c. Canada*, 2000 CSC 60, [2000] 2 R.C.S. 860. L'élément clé réside toutefois dans l'emploi du mot « peut ». L'existence d'un contrat A et d'un contrat B dépend entièrement des échanges entre les parties. Il ne s'agit pas d'une conception artificielle imposée par les tribunaux, mais d'une description des conséquences juridiques des échanges intervenus entre les parties. Dans l'arrêt *M.J.B.*, la Cour souligne que ce sont les conditions expresses et tacites de l'appel d'offres qui déterminent chaque fois s'il y a ou non un contrat A et, le cas échéant, quelles en sont les conditions. Comme le dit le juge Iacobucci au par. 19 :

> L'important [. . .] c'est que la présentation d'une soumission en réponse à un appel d'offres peut donner

rise to contractual obligations, quite apart from the obligations associated with the construction contract to be entered into upon the acceptance of a tender, depending upon whether the parties intend to initiate contractual relations by the submission of a bid. If such a contract arises, its terms are governed by the terms and conditions of the tender call. [Emphasis added.]

3. The Trial Judge's Findings Concerning the Existence of Contract A

[18] The question of whether Tercon's submission of a compliant bid gave rise to contractual relations between it and the Province was contested by the Province at trial. The trial judge gave extensive reasons for finding against the Province on this issue. We are told that the Province did not pursue this point in the Court of Appeal but instead premised its submissions on the existence of Contract A. The Province took the same approach in its written submissions in this Court. However, during oral argument, there was some passing reference in response to questions that there was no Contract A. In light of the position taken by the Province on its appeal to the Court of Appeal and in its written submissions in this Court, it is now too late to revisit whether there were contractual duties between Tercon and the Province. Even if it were open to the Province to make this argument now, I can see no error in legal principle or any palpable and overriding error of fact in the trial judge's careful reasons on this point.

[19] The trial judge did not mechanically impose the Contract A/Contract B framework, but considered whether Contract A arose in light of her detailed analysis of the dealings between the parties. That was the right approach. She reviewed in detail the provisions of the RFP which supported her conclusion that there was an intent to create contractual relations upon submission of a compliant bid. She noted, for example, that bids were to be irrevocable for 60 days and that security of $50,000 had to be paid by all proponents and was to be increased to $200,000 by the successful proponent. Any revisions to proposals prior to the closing date had to be in writing, properly executed and received before the closing time. The RFP also set

naissance à des obligations contractuelles tout à fait distinctes des obligations découlant du contrat d'entreprise qui doit être conclu dès l'acceptation de la soumission, selon que les parties auront voulu établir des rapports contractuels par la présentation d'une soumission. Advenant la formation d'un tel contrat, ses modalités sont régies par les conditions de l'appel d'offres. [Je souligne.]

3. Les conclusions de la juge de première instance concernant l'existence du contrat A

[18] La province a nié au procès que la présentation d'une soumission conforme par Tercon a fait naître un lien contractuel entre elles. La juge du procès motive abondamment sa décision de donner tort à la province sur ce point. Il appert que la province n'aurait pas persisté dans cette voie devant la Cour d'appel, mais aurait plutôt invoqué l'existence d'un contrat A. La province défend la même thèse dans l'argumentation écrite présentée à notre Cour, mais en réponse à des questions posées lors de sa plaidoirie, elle a laissé entendre qu'il n'existait pas de contrat A. Vu la position de la province en Cour d'appel et l'argumentation écrite qu'elle nous a présentée, il est désormais trop tard pour revenir sur la question de l'existence d'obligations contractuelles entre Tercon et la province. Et même s'il était loisible à la province de faire valoir cet argument aujourd'hui, je ne relève pas d'erreur de droit ni d'erreur de fait manifeste et dominante dans les motifs soigneusement rédigés par la juge de première instance sur ce point.

[19] La juge de première instance n'a pas mécaniquement appliqué le modèle du contrat A et du contrat B. Elle s'est plutôt demandé si l'examen détaillé des échanges entre les parties révélait qu'un contrat A en avait résulté. C'est ce qu'il convenait de faire. Elle conclut à l'issue d'un examen minutieux des dispositions de la DP qu'il y avait intention que la présentation d'une soumission conforme crée un lien contractuel. Par exemple, elle relève que les soumissions devaient être irrévocables pendant 60 jours et que chaque soumissionnaire devait verser 50 000 $ à titre de garantie, montant qui passait à 200 000 $ si sa proposition était retenue. Toute modification de la proposition avant la date de clôture devait être faite par écrit, porter les

out detailed evaluation criteria and specified that they were to be the only criteria to be used to evaluate proposals. A specific form of alliance agreement was attached. There were detailed provisions about pricing that were fixed and non-negotiable. A proponent was required to accept this form of contract substantially, and security was lost if an agreement was not executed. The Ministry reserved a right to cancel the RFP under s. 2.9 but in such event was obliged to reimburse proponents for costs incurred in preparing their bids up to $15,000 each. Proponents had to submit a signed proposal form, which established that they offered to execute an agreement substantially in the form included in the RFP package. Further, they acknowledged that the security could be forfeited if they were selected as the preferred proponent and failed to enter into good faith discussions with the Ministry to reach an agreement and sign the alliance agreement.

[20] In summary, as the trial judge found, the RFP set out a specifically defined project, invited proposals from a closed and specific list of eligible proponents, and contemplated that proposals would be evaluated according to specific criteria. Negotiation of the alliance construction contract was required, but the negotiation was constrained and did not go to the fundamental details of either the procurement process or the ultimate contract.

[21] There is, therefore, no basis to interfere with the judge's finding that there was an intent to create contractual obligations upon submission of a compliant bid. I add, however, that the tender call in this case did not give rise to the classic Contract A/Contract B framework in which the bidder submits an irrevocable bid and undertakes to enter into Contract B on those terms if it is accepted. The alliance model process which was used here was more complicated than that and involved good faith negotiations for a Contract B in the form set out in the tender documents. But in my view, this should not distract us from the main question here. We do not have to spell out all of the terms of Contract A, let alone of Contract B, so as to define all of the duties and obligations of both

signatures requises et être reçue avant cette date. La DP donnait en outre le détail des critères d'évaluation, précisant qu'il s'agissait des seuls applicables. L'ébauche d'un accord de partenariat y était jointe. Des dispositions précises et non négociables sur les coûts y étaient prévues. Le soumissionnaire devait adhérer en substance à cette forme de contrat, sinon il perdait le montant de la garantie. À la clause 2.9, le ministère se réservait le droit d'annuler la DP, mais il devait alors rembourser les proposants des frais engagés pour la préparation des propositions, jusqu'à concurrence de 15 000 $ chacun. Le formulaire de proposition que devait signer le soumissionnaire portait qu'il s'engageait à signer un accord revêtant essentiellement la forme de celui compris dans les documents de la DP. Le proposant reconnaissait en outre que si son offre était retenue, l'omission de négocier de bonne foi avec le ministère en vue de la conclusion d'une entente et de signer l'accord de partenariat pouvait entraîner la perte du dépôt de garantie.

[20] En résumé, comme le conclut la juge, la DP décrivait un projet précis, invitait un certain nombre de proposants admissibles à soumissionner et indiquait que les propositions seraient considérées au regard de critères établis. Il devait y avoir négociation de l'accord de construction en partenariat, mais à l'intérieur de certaines limites et elle ne devait pas porter sur les éléments fondamentaux du processus d'appel d'offres ou du contrat final.

[21] Il n'y a donc pas lieu de modifier la conclusion de la juge selon laquelle il y avait intention de faire en sorte que la présentation d'une soumission conforme fasse naître des obligations contractuelles. J'ajoute cependant que l'appel d'offres considéré en l'espèce ne correspondait pas au modèle classique du contrat A et du contrat B où le soumissionnaire présente une offre irrévocable et s'engage à conclure le contrat B aux mêmes conditions s'il est choisi. Le modèle du partenariat adopté en l'espèce était plus complexe et supposait des négociations de bonne foi en vue de la conclusion du contrat B revêtant la forme indiquée dans les documents de l'appel d'offres. Toutefois, cette particularité ne doit pas nous faire perdre de vue la principale question en litige. Point n'est besoin d'exposer

the bidders and the Province. The question here is much narrower: did contractual obligations arise as a result of Tercon's compliant bid and, if so, was it a term of that contract that the Province would only entertain bids from eligible bidders? The trial judge found offer, acceptance and consideration in the invitation to tender and Tercon's bid. There is no basis, in my respectful view, to challenge that finding even if it were open to the Province to try to do so at this late stage of the litigation.

toutes les conditions du contrat A, encore moins celles du contrat B, pour circonscrire les obligations respectives du soumissionnaire et de la province. La question qu'il nous faut trancher est beaucoup plus étroite : la présentation d'une soumission conforme par Tercon a-t-elle fait naître des obligations contractuelles et, dans l'affirmative, l'obligation que la province n'examine que les propositions de soumissionnaires admissibles en faisait-elle partie? La juge de première instance estime qu'il y a eu offre, acceptation et contrepartie dans l'appel d'offres et dans la présentation d'une soumission par Tercon. Même si la province pouvait contester cette conclusion à ce stade avancé de l'instance, elle n'aurait à mon avis aucun motif valable de le faire.

4. The Trial Judge's Finding Concerning Eligibility

[22] It was not contested at trial that only the six original proponents that qualified through the RFEI process were eligible to bid. This point is not in issue on appeal; the question is what this eligibility requirement means. It will be helpful, therefore, to set out the background about this limited eligibility to bid in this tendering process.

[23] To begin, it is worth repeating that there is no doubt that the Province was contractually bound to accept bids only from eligible bidders. This duty may be implied even absent express stipulation. For example, in *M.J.B.*, the Court found that an implied obligation to accept only compliant bids was necessary to give business efficacy to the tendering process, noting, at para. 41, that a bidder must expend effort and incur expense in preparing its bid and must submit bid security and that it is "obvious" that it makes "little sense" for the bidder to comply with these requirements if the owner "is allowed, in effect, to circumscribe this process and accept a non-compliant bid". But again, whether such a duty should be implied in any given case will depend on the dealings between the parties. Here, however, there is no need to rely on implied terms. The obligation to consider only bids from eligible bidders

4. La conclusion de la juge de première instance sur l'admissibilité

[22] Nulle partie n'a contesté en première instance que seules les six entreprises intéressées initialement, qui s'étaient rendues admissibles en répondant à la DEI, étaient admises à soumissionner. Ce point échappe donc au présent pourvoi. La question est de savoir ce qu'il en est de cette condition d'admissibilité. Le contexte de cette limitation de l'admissibilité au processus d'appel d'offres est donc susceptible de nous éclairer.

[23] D'abord, il convient de répéter qu'il ne fait aucun doute que la province était contractuellement tenue de n'accepter que les propositions de soumissionnaires admissibles. Même en l'absence d'une stipulation expresse, cette obligation peut être inférée. Dans l'arrêt *M.J.B.*, par exemple, notre Cour a statué que l'obligation tacite de n'accepter que les soumissions conformes était nécessaire à l'efficacité commerciale du processus d'appel d'offres, signalant au par. 41 qu'un soumissionnaire doit consacrer efforts et sommes d'argent à la préparation de sa soumission et verser une garantie, de sorte qu'il est « évident » qu'il serait « déraisonnable » qu'il doive satisfaire à ces exigences si le propriétaire « peut, dans les faits, contourner ce processus et accepter une soumission non conforme ». Mais encore une fois, ce sont les échanges entre les parties qui déterminent s'il y a lieu d'inférer l'existence d'une telle

was stated expressly in the tender documents and in the required ministerial approval of the process which they described.

[24] As noted, in early 2000, the Province issued a RFEI based on a design-build model; the contractor would both design and build the highway. The RFEI contemplated that a short list of three qualified contractors, or teams composed of contractors and consultants, would be nominated as proponents. Each was to provide a description of the legal structure of the team and to describe the role of each team member along with the extent of involvement of each team member as a percentage of the total scope of the project and an organization chart showing each team member's role. Any change in team management or key positions required notice in writing to the Province which reserved the right to disqualify the proponent if the change materially and negatively affected the ability of the team to carry out the project.

[25] Expressions of interest ("EOI") were received from six teams including Tercon and Brentwood. The evaluation panel and independent review panel recommended a short list of three proponents with Tercon topping the evaluation. Brentwood was evaluated fifth and was not on the short list. Brentwood was known to lack expertise in drilling and blasting and so its EOI had included an outline of the key team members with that experience. EAC did not participate and had no role in the Brentwood submission. The results of this evaluation were not communicated and the process did not proceed because the Province decided to design the project itself and issue an RFP for an alliance model contract to construct the highway.

[26] It was clear from the outset that only those who had submitted proposals during the RFEI process would be eligible to submit proposals under the RFP. This was specified in the approval of the process by the Minister of Transportation and

obligation. Cependant, en l'espèce, toute inférence est inutile, car l'obligation de considérer seulement les propositions de soumissionnaires admissibles figurait expressément dans le dossier d'appel d'offres et dans l'approbation ministérielle requise du processus qui y était décrit.

[24] Rappelons qu'au début de l'année 2000, la province a lancé une DEI pour un projet où l'entrepreneur était appelé à concevoir une route puis à la construire. Suivant la DEI, le nombre de proposants devait être ramené à trois, qu'il s'agisse d'entrepreneurs ou d'équipes d'entrepreneurs et de consultants, tous qualifiés. Chaque proposant devait préciser la structure juridique de l'équipe, le rôle de chacun de ses membres ainsi que le pourcentage de sa contribution à l'ensemble du projet, et remettre un organigramme indiquant la tâche de chacun. Toute modification touchant la direction de l'équipe ou les postes clés devait être notifiée par écrit à la province, qui se réservait le droit d'écarter le proposant si la modification compromettait substantiellement l'aptitude à mener le projet à bien.

[25] Six équipes, dont Tercon et Brentwood, ont manifesté leur intérêt. Le comité d'évaluation et le comité de révision indépendant ont recommandé de retenir trois proposants, dont Tercon en tête de liste. Classée cinquième, Brentwood ne figurait pas sur cette liste. Comme elle n'avait pas d'expertise dans les domaines du forage et du dynamitage, Brentwood avait énuméré les membres clés de son équipe dotés de cette expertise. EAC n'a pas participé au processus ni joué de rôle dans la soumission de Brentwood. Les résultats de cette évaluation n'ont pas été communiqués, et la province a mis fin au processus après avoir décidé de se charger elle-même de la conception du projet et de demander des propositions en vue de la mise sur pied d'un partenariat pour la construction de la route.

[26] Il était clair dès le départ que seules les entreprises qui avaient manifesté leur intérêt pourraient présenter une proposition. C'est ce que prévoyait l'approbation du processus donnée par le ministre des Transports et de la Voirie (« ministre ») avant le

Highways ("Minister") before the RFP was issued. It is worth pausing here to briefly look at the Minister's role.

[27] Pursuant to s. 23 of the *Ministry of Transportation and Highways Act*, R.S.B.C. 1996, c. 311, the legislation in force at the relevant time, the Minister was required to invite public tenders for road construction unless he or she determined that another process would result in competitively established costs for the work. The section provided:

23 (1) The minister must invite tenders by public advertisement, or if that is impracticable, by public notice, for the construction and repair of all government buildings, highways and public works, except for the following:

. . .

(c) if the minister determines that an alternative contracting process will result in competitively established costs for the performance of the work.

(2) The minister must cause all tenders received to be opened in public, at a time and place stated in the advertisement or notice.

(3) The prices must be made known at the time the tenders are opened.

(4) In all cases where the minister believes it is not expedient to let the work to the lowest bidder, the minister must report to and obtain the approval of the Lieutenant Governor in Council before passing by the lowest tender, except if delay would be injurious to the public interest.

. . .

[28] These provisions make clear that the work in this case had to be awarded by public tender, absent the Minister's approval of an alternative process, and had to be awarded to the lowest bidder, absent approval of the Lieutenant Governor in Council. As noted, ministerial approval was given for an alternative process under s. 23(1)(c). The Minister issued

lancement de la DP. Il convient de se pencher brièvement sur le rôle du ministre.

[27] Suivant l'article 23 de la loi applicable à l'époque — la *Ministry of Transportation and Highways Act*, R.S.B.C. 1996, ch. 311 —, le ministre devait lancer un appel d'offres pour la construction d'une route, sauf s'il était d'avis qu'un autre moyen permettrait la réalisation des travaux à un coût concurrentiel. L'article prévoyait notamment ce qui suit :

[TRADUCTION]

23 (1) Le ministre procède à un appel d'offres par annonce publique ou, lorsque c'est impossible, par avis public, pour la construction et la réparation d'un immeuble gouvernemental, d'une route ou d'un ouvrage public, sauf dans les cas suivants :

. . .

c) il estime qu'un autre processus d'adjudication de marché permettra la réalisation des travaux à un coût concurrentiel.

(2) Le ministre veille à ce que toutes les soumissions reçues soient ouvertes en public à la date, à l'heure et à l'endroit indiqués dans l'annonce ou dans l'avis.

(3) Les prix doivent être communiqués lors de l'ouverture des soumissions.

(4) Lorsqu'il estime qu'il n'est pas opportun d'adjuger le marché au soumissionnaire le moins disant, le ministre en informe le lieutenant-gouverneur en conseil et obtient l'autorisation de ne pas retenir ce soumissionnaire, sauf s'il en résulte un retard préjudiciable à l'intérêt public.

. . .

[28] Il ressort de ces dispositions qu'à défaut de l'approbation d'un autre processus par le ministre, le marché devait en l'espèce être attribué par voie d'appel d'offres et que, sauf autorisation du lieutenant-gouverneur de choisir un autre adjudicataire, le marché devait être adjugé au soumissionnaire le moins disant. Un autre processus

a notice that, pursuant to that section, he approved the process set out in an attached document and had determined it to be an alternative contracting process that would result in competitively established costs for the performance of the work. The attached document outlined in seven numbered paragraphs the process that had been approved.

[29] The document described the background of the public RFEI (which I have set out earlier), noting that *only those firms identified through the EOI process would be eligible to submit proposals for the work* and that they would receive invitations to do so. The Minister's approval in fact referred to the firms who had been short-listed from the RFEI process as being eligible. If this were taken to refer only to the three proponents identified by the evaluation process of the RFEI, Tercon would be included but Brentwood would not. However, no one has suggested that anything turns on this and it seems clear that ultimately all six of the RFEI proponents — including both Tercon and Brentwood — were intended to be eligible. The ministerial approval then briefly set out the process. Proposals "by short-listed firms" were to be evaluated "using the considerations set out in the RFP".

[30] It is clear, therefore, that participation in the RFP process approved by the Minister was limited to those who had participated in the RFEI process.

[31] The Province's factum implies that the Minister approved inclusion of the exclusion clause in the RFP. However, there is no evidence of this in the record before the Court. The Minister's approval is before us. It is dated as having been prepared on August 23, 2000 and signed on October 19, 2000, and approves a process outlined in a two-page document attached to it. It says nothing about exclusion of the Province's liability. The RFP, containing the exclusion clause in issue here, is dated January 15, 2001 and was sent out to eligible bidders under cover of a letter of the

d'adjudication a fait l'objet d'une approbation ministérielle conformément à l'al. 23(1)*c*). Le ministre a donné avis de son approbation, en vertu de cette disposition, du processus décrit dans un document joint en annexe et de sa conclusion qu'il s'agissait d'un processus d'adjudication de marché permettant la réalisation des travaux à un coût concurrentiel. Le document joint en annexe décrivait en sept paragraphes numérotés le processus approuvé.

[29] Ce document faisait état du contexte (mentionné précédemment) de la DEI publique, précisant que *seules les entreprises retenues à l'issue du processus d'expression d'intérêt pourraient présenter une proposition* et seraient invitées à le faire. L'approbation ministérielle visait en fait les entreprises jugées admissibles par suite de la DEI. S'il s'agissait seulement des trois proposants sélectionnés dans le cadre de cette première évaluation, Tercon en faisait partie, mais non Brentwood. Or, nul ne laisse entendre que ce point est décisif à quelque égard, et il semble clair que, finalement, les six entreprises ayant donné suite à la DEI, dont Tercon et Brentwood, étaient tenues pour admissibles. L'approbation ministérielle décrit ensuite brièvement le processus. Les propositions des entreprises présélectionnées devaient être évaluées [TRADUCTION] « en fonction des critères énoncés dans la DP ».

[30] Il ne fait donc aucun doute que la participation au processus de DP approuvé par le ministre était réservée aux entreprises qui avaient répondu à la DEI.

[31] Dans son mémoire, la province laisse entendre que le ministre a approuvé la clause de non-recours figurant dans la DP. Or, selon le dossier de la Cour, aucun élément n'étaye sa prétention. Nous disposons du texte de l'approbation ministérielle. Suivant la date qui y est apposée, elle aurait été rédigée le 23 août 2000 et signée le 19 octobre de la même année. Elle vise le processus énoncé dans le document de deux pages qui y est joint. Aucune mention n'y est faite de la non-responsabilité de la province. La DP, qui renferme la clause de non-recours litigieuse, porte la date du 15 janvier 2001

same date, some three months after the Minister's approval.

[32] The RFP is a lengthy document, containing detailed instructions to proponents, required forms, a time schedule of the work, detailed provisions concerning contract pricing, a draft of the ultimate construction contract and many other things. Most relevant for our purposes are the terms of the instructions to proponents and in particular the eligibility requirements for bidders.

[33] The RFP reiterates in unequivocal terms that eligibility to bid was restricted as set out in the ministerial approval. It also underlines the significance of the identity of the proponent. In s. 1.1, the RFP specifies that only the six teams involved in the RFEI would be eligible. The term "proponent", which refers to a bidder, is defined in s. 8 as "a team that has become eligible to respond to the RFP as described in Section 1.1 of the Instructions to Proponents". Section 2.8(a) of the RFP stipulates that *only* the six proponents qualified through the RFEI process were eligible and that *proposals received from any other party would not be considered*. In short, there were potentially only six participants and "Contract A" could not arise by the submission of a bid from any other party.

[34] The RFP also addressed material changes to the proponent, including changes in the proponent's team members and its financial ability to undertake and complete the work. Section 2.8(b) of the RFP provided in part as follows:

If in the opinion of the Ministry a material change has occurred to the Proponent since its qualification under the RFEI, including if the composition of the Proponent's team members has changed . . . or if, for financial or other reasons, the Proponent's ability to undertake and complete the Work has changed, then the

et elle a été envoyée aux soumissionnaires admissibles avec lettre d'accompagnement datée du même jour quelque trois mois après l'approbation ministérielle.

[32] La DP est un document volumineux renfermant des instructions détaillées à l'intention des proposants, des formulaires à remplir, un calendrier des travaux, des dispositions précises sur la fixation du prix du contrat, une ébauche de l'accord final de construction en partenariat et bien d'autres éléments. Toutefois, ce qui importe le plus pour les besoins du présent pourvoi c'est le libellé des instructions aux proposants et, plus particulièrement, les conditions d'admissibilité des soumissionnaires.

[33] La DP rappelle de manière non équivoque que l'admissibilité à soumissionner est limitée comme le prévoit l'approbation ministérielle. Elle souligne aussi que l'identité du proposant importe. Le paragraphe 1.1 dispose que seules les six équipes ayant répondu à la DEI sont admissibles. L'article 8 prévoit que [TRADUCTION] « proposant » — l'équivalent de « soumissionnaire » — [TRADUCTION] « s'entend d'une équipe admise à répondre à la DP suivant le libellé du par. 1.1 des instructions aux proposants ». L'alinéa 2.8a) de la DP précise que *seuls* les six proposants devenus admissibles en répondant à la DEI peuvent soumissionner et qu'aucune *proposition d'une autre personne ne sera examinée*. En somme, il ne pouvait y avoir que six participants, et le « contrat A » ne pouvait naître de la présentation d'une proposition présentée par une autre personne.

[34] La DP aborde aussi la question de la modification substantielle visant un proposant, notamment en ce qui concerne la composition de son équipe et son aptitude financière à entreprendre les travaux et à les mener à bien. L'alinéa 2.8b) prévoit notamment ce qui suit :

[TRADUCTION] Lorsque de l'avis du ministère, depuis que le proposant est devenu admissible en répondant à la DEI, une modification substantielle le concernant s'est produite, notamment en ce qui a trait à la composition de son équipe [. . .] ou à son aptitude financière ou autre à entreprendre les travaux ou à les mener à bien, il peut

Ministry may request the Proponent to submit further supporting information as the Ministry may request in support of the Proponent's qualification to perform the Work. If in the sole discretion of the Ministry as a result of the changes the Proponent is not sufficiently qualified to perform the Work then the Ministry reserves the right to disqualify that Proponent, and reject its Proposal.

[35] The proponent was to provide an organization chart outlining the proponent's team members, structure and roles. If the team members were different from the RFEI process submission, an explanation was to be provided for the changes: s. 4.2(b)i). A list of subcontractors and suppliers was also to be provided and the Ministry had to be notified of any changes: s. 4.2(e).

[36] The RFP provided proponents with a mechanism to determine whether they remained qualified to submit a proposal. If a proponent was concerned about its eligibility as a result of a material change, it could make a preliminary submission to the Ministry describing the nature of the changes and the Ministry would give a written decision as to whether the proponent was still qualified: s. 2.8(b).

[37] Brentwood tried to take advantage of this process. The trial judge thoroughly outlined this, at paras. 17-23 of her reasons. In brief, Brentwood lacked expertise in drilling and blasting and by the time the RFP was issued, it faced limited local bonding capacity due to commitments to other projects, a shorter construction period, the potential unavailability of subcontractors and limited equipment to perform the work. It in fact considered not bidding at all. Instead, however, it entered into a pre-bidding agreement with EAC that the work would be undertaken by a joint venture of Brentwood and EAC and that upon being awarded the work, they would enter into a joint venture agreement and would share 50/50 the costs, expenses, losses and gains. The trial judge noted that it was common in the industry for contractors to agree to a joint venture on the basis of a pre-bid agreement with the specifics of the joint venture to be worked out once the contract was awarded and that Brentwood and EAC

exiger du proposant d'autres renseignements établissant qu'il est en mesure d'exécuter les travaux. Lorsque, à son seul gré, il estime que la modification fait en sorte que le proposant n'est pas suffisamment apte à exécuter les travaux, le ministère se réserve le droit de l'écarter et de rejeter sa proposition.

[35] Le proposant devait fournir un organigramme indiquant la composition et la structure de son équipe et le rôle de ses membres. Lorsque les membres de son équipe n'étaient pas les mêmes que ceux mentionnés dans sa réponse à la DEI, il devait s'en expliquer : sous-al. 4.2b)i). Une liste de sous-traitants et de fournisseurs devait également être remise, et tout changement qui y était apporté devait être notifié au ministère : al. 4.2e).

[36] La DP prévoyait un mécanisme permettant au proposant de s'assurer qu'il était toujours admissible. Le proposant désireux de savoir si un changement substantiel compromettait son admissibilité à soumissionner pouvait en communiquer la nature au ministère en vue d'obtenir une décision préalable confirmant ou non qu'il était toujours admissible : al. 2.8b).

[37] Brentwood a tenté de se prévaloir de ce mécanisme, et la juge de première instance relate sa démarche en détail aux par. 17 à 23 de ses motifs. Pour résumer, Brentwood n'avait pas d'expertise en matière de forage et de dynamitage et lorsque la DP a été lancée, le cautionnement qu'elle pouvait offrir était limité par d'autres engagements, la période de construction était écourtée, des sous-traitants pouvaient ne plus être disponibles et le matériel dont elle disposait pour exécuter les travaux était restreint. Elle a d'ailleurs envisagé de ne pas présenter de proposition du tout. Elle a cependant conclu avec EAC une entente préalable à la soumission prévoyant qu'elles réaliseraient les travaux en coentreprise et que, dès l'adjudication du marché, elles concluraient un accord de coentreprise et se répartiraient à parts égales les coûts, les dépenses, les pertes et les bénéfices. La juge signale qu'il est courant dans ce secteur d'activité qu'avant le dépôt d'une soumission, des entrepreneurs conviennent

acted consistently throughout in accordance with this industry standard.

[38] Brentwood sent the Province's project manager, Mr. Tasaka, a preliminary submission as provided for in s. 2.8(b) of the RFP, advising of a material change in its team's structure in that it wished to form a joint venture with EAC. This was done, the trial judge found, because Brentwood thought it would be disqualified if it submitted a proposal as a joint venture without the Ministry's prior approval under this section of the RFP. The Province never responded in writing as it ought to have according to s. 2.8(b).

[39] It seems to have been assumed by everyone that a joint venture of Brentwood and EAC was not eligible because this change would not simply be a change in the composition of the bidder's team, but in effect a new bidder. Without reviewing in detail all of the evidence referred to by the trial judge, it is fair to say that although Brentwood ultimately submitted a proposal in its own name, the proposal in substance was from the Brentwood/EAC joint venture and was evaluated as such. As the trial judge concluded:

> The substance of the proposal was as a joint venture and this must have been apparent to all. The [project evaluation panel] approved Brentwood/EAC as joint venturers as the preferred proponent. The [panel] was satisfied that Tercon had the capacity and commitment to do the job but preferred the joint venture submission of Brentwood/EAC. [para. 53]

[40] There was some suggestion by the Province during oral argument that the trial judge had wrongly imposed on it a duty to investigate Brentwood's bid, a duty rejected by the majority of the Court in *Double N Earthmovers Ltd. v. Edmonton (City)*, 2007 SCC 3, [2007] 1 S.C.R. 116. In my view, the trial judge did no such thing. As her detailed findings make clear, the Province: (1) fully understood that the Brentwood bid was in fact on behalf of a joint venture of Brentwood and EAC; (2) thought

de la création d'une coentreprise dont les modalités seront arrêtées dès l'adjudication du contrat. Elle ajoute que Brentwood et EAC ont toujours agi dans le respect de cette pratique établie.

[38] Conformément à l'al. 2.8b) de la DP, Brentwood a fait parvenir au gestionnaire du projet, M. Tasaka, une proposition préliminaire qui signalait la modification substantielle de la structure de son équipe résultant de son intention de former une coentreprise avec EAC. Selon la juge de première instance, Brentwood l'a fait parce qu'elle pensait que sa proposition serait rejetée si elle était présentée au nom d'une coentreprise sans que le ministère n'ait donné son approbation au préalable en application de cette disposition de la DP. La province n'a jamais répondu par écrit comme elle était censée le faire suivant l'al. 2.8b).

[39] Tous les intéressés semblent avoir tenu la coentreprise Brentwood/EAC pour inadmissible du fait que la composition de l'équipe n'était pas simplement modifiée, mais qu'un nouveau soumissionnaire voyait en fait le jour. Sans analyser en détail tous les éléments de preuve mentionnés par la juge de première instance, on peut à juste titre affirmer que même si la proposition de Brentwood a été présentée en son seul nom, elle provenait essentiellement de la coentreprise Brentwood/EAC et elle a été considérée en conséquence. Selon la juge,

> [TRADUCTION] [l]a proposition était essentiellement celle d'une coentreprise, ce qui a dû être évident pour tout le monde. Le [comité d'évaluation du projet] a arrêté son choix sur la coentreprise Brentwood/EAC. Il estimait que Tercon avait les moyens et la détermination nécessaires pour réaliser les travaux, mais il a préféré la proposition de Brentwood/EAC. [par. 53]

[40] Dans sa plaidoirie orale, la province a laissé entendre que la juge lui avait imputé à tort l'obligation de vérifier la soumission de Brentwood, ce qui allait à l'encontre de l'avis des juges majoritaires de notre Cour dans l'arrêt *Double N Earthmovers Ltd. c. Edmonton (Ville)*, 2007 CSC 3, [2007] 1 R.C.S. 116. Je ne crois pas que cela ait été le cas. Il ressort des conclusions détaillées de la juge que la province (1) savait pertinemment que la soumission de Brentwood était en fait celle d'une coentreprise

that a bid from that joint venture was not eligible; and (3) took active steps to obscure the reality of the situation. No investigation was required for the Province to know these things and the judge imposed no duty to engage in one.

5. The Province's Submissions

[41] I will address the Province's first two points together:

(i) a joint venture is not a legal person and therefore the Province could not and did not contract with a joint venture; and

(ii) it did not award the contract to EAC and EAC had no contractual responsibility to the Province for failure to perform the contract.

[42] I cannot accept these submissions. The issue is not, as these arguments assume, whether the Province contracted with a joint venture or whether EAC had contractual obligations to the Province. The issue is whether the Province considered an ineligible bid; the point of substance is whether the bid was from an eligible bidder.

[43] At trial there was no contest that a bid from a joint venture involving an ineligible bidder would be ineligible. The Province's position was that there was no need to look beyond the face of the bid to determine who was bidding: the proposal was in the name of Brentwood and therefore the bid was from a compliant bidder. Respectfully, I see no error in the trial judge's rejection of this position. There was a mountain of evidence to support the judge's conclusions that first, Brentwood's bid, in fact if not in form, was on behalf of a joint venture between itself and EAC; second, the Province knew this and took the position that it could not consider a bid from or award the work to that joint venture; third, the existence of the joint venture was a material consideration in favour of the Brentwood bid during the evaluation process; and finally, that steps were taken by revising and drafting documentation to obfuscate the reality of the situation.

formée avec EAC, (2) qu'elle estimait que la proposition de cette coentreprise était inadmissible et (3) qu'elle s'est activement employée à gommer ce fait. Nulle vérification ne s'imposait à cet égard, et la juge n'a pas imputé d'obligation de vérification à la province.

5. La thèse de la province

[41] Je me penche maintenant sur les deux premiers arguments de la province :

(i) une coentreprise étant dépourvue de la personnalité morale, la province ne pouvait contracter avec elle et elle ne l'a pas fait;

(ii) elle n'a pas adjugé le marché à EAC, et EAC n'avait envers elle aucune responsabilité en cas d'inexécution du contrat.

[42] Je ne peux faire droit à ces prétentions. Il ne s'agit pas de savoir si la province a contracté avec une coentreprise ou si EAC avait des obligations contractuelles envers elle, mais bien si la province a considéré une proposition inadmissible. Il faut déterminer si la proposition provenait d'un soumissionnaire admissible.

[43] Au procès, nul n'a contesté l'inadmissibilité d'une coentreprise comptant en son sein un soumissionnaire inadmissible. La province affirme qu'elle n'avait pas à se demander si la proposition provenait d'une autre entreprise que celle nommée : la proposition était présentée au nom de Brentwood, un soumissionnaire admissible. Je suis pourtant d'avis que la juge de première instance n'a pas eu tort d'écarter cet argument. Une preuve plus qu'abondante étayait ses conclusions selon lesquelles (1) la soumission de Brentwood, en dépit des apparences, était en fait présentée par la coentreprise avec EAC, (2) la province le savait et estimait qu'elle ne pouvait ni considérer la proposition de cette coentreprise ni adjuger le contrat à celle-ci, (3) l'existence de la coentreprise jouait en faveur de Brentwood dans le cadre du processus d'évaluation des propositions et, enfin, (4) la province s'est employée à masquer cette réalité en révisant et en rédigeant la documentation.

[44] Brentwood was one of the original RFEI proponents and was of course eligible to bid, subject to material changes in the composition of its team. EAC had not submitted a proposal during the RFEI process. It had been involved in advising the Ministry in relation to the project in 1998 and, in the fall of 2000, the Ministry had asked EAC to prepare an internal bid for comparison purposes (although EAC did not do so) as EAC was not entitled to bid on the Project.

[45] As noted earlier, after the RFP was issued, Brentwood and EAC entered into a pre-bidding agreement that provided that the work would be undertaken in the name of Brentwood/Anderson, a joint venture, that the work would be sponsored and managed by the joint venture and that upon being awarded the contract, the parties would enter into a joint venture agreement. Brentwood advised the Ministry in writing that it was forming a joint venture with EAC "to submit a more competitive price"; this fax was in effect a preliminary submission contemplated by s. 2.8(b) of the RFP and was written, as the trial judge found, because Brentwood assumed that it could be disqualified if it submitted a proposal as a joint venture unless prior arrangements had been made. The Province never responded in writing to this preliminary submission, as required by s. 2.8(b). There were, however, discussions with the Province's project manager, Mr. Tasaka who, the trial judge found, understood that a joint venture from Brentwood and EAC would not be eligible. As the judge put it, the Province's position appears to have been that the Brentwood/EAC proposal could proceed as long as the submission was in the name of Brentwood.

[46] In the result, EAC was listed in the ultimate submission as a "major member" of the team. The legal relationship with EAC was not specified and EAC was listed as a subcontractor even though, as the trial judge found, their relationship bore no resemblance to a standard subcontractor agreement. The trial judge found as facts — and these findings are not challenged — that Brentwood and EAC always intended between themselves to form a joint venture and to formalize that arrangement once the contract was secured, and further, that the

[44] Comme Brentwood faisait partie des entreprises ayant initialement répondu à la DEI, elle était bien sûr admise à soumissionner, sauf modification substantielle de la composition de son équipe. EAC n'avait pas donné suite à la DEI. En 1998, elle avait conseillé le ministère relativement au projet et, à l'automne 2000, ce dernier lui avait demandé de préparer une soumission interne aux fins de comparaison (ce qu'elle n'a cependant pas fait) puisqu'elle n'était pas admise à soumissionner.

[45] Rappelons qu'après le lancement de la DP, Brentwood et EAC ont conclu un accord préalable à la proposition prévoyant que les travaux seraient entrepris au nom de la coentreprise, que celle-ci les financerait et les gèrerait et qu'un accord de coentreprise interviendrait si le contrat leur était adjugé. Brentwood a informé le ministère par écrit qu'elle formait une coentreprise avec EAC [TRADUCTION] « afin de présenter une soumission plus concurrentielle ». Le document télécopié constituait en fait la proposition préliminaire visée à l'al. 2.8b) de la DP et, suivant la juge de première instance, Brentwood l'avait envoyé parce qu'elle pensait que faute de démarches préalables, la soumission présentée au nom de la coentreprise pouvait être rejetée. La province n'y a jamais donné suite par écrit comme l'exigeait l'al. 2.8b). Cependant, des discussions ont eu lieu avec le gestionnaire du projet, M. Tasaka, qui, selon la juge de première instance, était conscient de l'inadmissibilité d'une coentreprise formée de Brentwood et d'EAC. Comme le dit la juge, la province paraît avoir estimé que la soumission de Brentwood/EAC pouvait être considérée si elle était présentée au nom de Brentwood.

[46] Dans la proposition finale, EAC a donc été qualifiée de [TRADUCTION] « membre important » de l'équipe. Le lien juridique entre Brentwood et EAC n'était pas précisé, et EAC figurait dans la liste des sous-traitants, même si, comme l'indique la juge de première instance, la relation entre les deux parties ne s'apparentait en rien à celle créée par un contrat de sous-traitance. La juge conclut — et nul ne conteste — que Brentwood et EAC ont toujours eu l'intention commune de former une coentreprise et de rendre celle-ci officielle une fois le contrat

role of EAC was purposefully obfuscated in the bid to avoid an apparent conflict with s. 2.8(a) of the RFP.

[47] During the selection process, it became clear that the bid was in reality on behalf of a joint venture. The project evaluation panel ("PEP") requested better information than provided in the bid about the structure of the business arrangements between Brentwood and EAC. Brentwood responded by disclosing the pre-bid agreement between them to form a 50/50 joint venture if successful. The PEP understood from this that Brentwood and EAC had a similar interest in the risk and reward under the contract and that this helped satisfy them that the "risk/reward" aspect of the alliance contract could be negotiated with them flexibly. The PEP clearly did not consider EAC to be a subcontractor although shown as such in the bid. In its step 6 report, the PEP consistently referred to the proponent as being a joint venture of Brentwood and EAC or as "Brentwood/EAC" and the trial judge found that it was on the basis that they were indeed a joint venture that PEP approved Brentwood/EAC as the preferred proponent. This step 6 report was ultimately revised to refer only to the Brentwood team as the official proponent. The trial judge found as a fact that this revision was made because "it was apparent that a joint venture was not eligible to submit a proposal" (para. 56).

[48] The findings of the trial judge and the record make it clear that it was no mere question of form rather than a matter of substance whether the bidder was Brentwood with other team members or, as it in fact was, the Brentwood/EAC joint venture. As she noted, at para. 121 of her reasons, the whole purpose of the joint venture was to allow submission of a more competitive price than it would have been able to do as a proponent with a team as allowed under s. 2.8(b) of the RFP. The joint venture permitted a 50/50 sharing of risk and reward and co-management of the project while at the same time avoiding the restrictions on subcontracting in the tendering documents. As the judge put it, the bid by the joint venture constituted "material non-compliance" with the tendering contract: ". . .

obtenu et que le rôle d'EAC a été occulté à dessein dans la proposition afin d'éviter toute inobservation apparente de l'al. 2.8a) de la DP.

[47] Il est apparu clairement au cours du processus de sélection que la soumission était en fait présentée au nom d'une coentreprise. Le comité d'évaluation du projet (« CEP ») a demandé plus de précisions sur les liens d'affaires entre Brentwood et EAC. Brentwood a alors révélé l'existence de l'accord préalable prévoyant la formation d'une coentreprise à parts égales si sa soumission était retenue. Le CEP en a déduit que Brentwood et EAC avaient une même participation aux risques et aux bénéfices découlant du marché, ce qui a contribué à le convaincre qu'elles pourraient faire preuve de souplesse dans la négociation du volet « risques/bénéfices » de l'accord de partenariat. Manifestement, le CEP n'a pas considéré EAC comme un sous-traitant même si elle était présentée de la sorte dans la soumission. Dans son rapport de l'étape 6, le CEP renvoie systématiquement à la coentreprise formée de Brentwood et d'EAC ou à « Brentwood/EAC » pour parler du proposant. La juge de première instance conclut que c'est bien parce qu'elles formaient une coentreprise que le CEP a arrêté son choix sur elles. Le rapport a par la suite été modifié de façon que seule l'équipe Brentwood y figure comme proposant officiel. La juge de première instance y voit [TRADUCTION] « l'évidence qu'une coentreprise n'était pas admissible à soumissionner » (par. 56).

[48] Il ressort des conclusions de la juge de première instance et du dossier que la question de savoir si le soumissionnaire était Brentwood avec l'appui des autres membres de l'équipe ou — comme c'était effectivement le cas —, la coentreprise, ne tenait pas seulement à la forme, mais également au fond. La juge indique au par. 121 de ses motifs que la raison d'être de la coentreprise était essentiellement d'arriver à un prix plus concurrentiel que celui qu'aurait pu offrir un proposant appuyé d'une équipe comme le permettait l'al. 2.8b) de la DP. La coentreprise rendait possible le partage à parts égales des risques et des bénéfices ainsi que de la gestion du projet tout en soustrayant le soumissionnaire aux limitations de la sous-traitance prévues dans le dossier d'appel d'offres. Comme

the joint venture with EAC allowed Brentwood to put forward a more competitive price than contemplated under the RFEI proposal. This went to the essence of the tendering process" (para. 126).

[49] The Province suggests that the trial judge's reasons allow form to triumph over substance. In my view, it is the Province's position that better deserves that description. It had a bid which it knew to be on behalf of a joint venture, encouraged the bid to proceed and took steps to obfuscate the reality that it was on behalf of a joint venture. Permitting the bid to proceed in this way gave the joint venture a competitive advantage in the bidding process, and the record could not be clearer that the joint venture nature of the bid was one of its attractions during the selection process. The Province nonetheless submits that so long as only the name of Brentwood appears on the bid and ultimate Contract B, all is well. If ever a submission advocated placing form above substance, this is it.

[50] It is true that the Province had legal advice and did not proceed in defiance of it. However, the facts as found by the trial judge about this legal advice hardly advance the Province's position. The judge found that the Province's lawyer was not aware of the background relevant to the question of whether the Brentwood bid was eligible, never reviewed the proponent eligibility requirements in the RFP and was not asked to and did not direct his mind to the question of eligibility. As the trial judge put it, the lawyer "appears to have operated on the assumption that Brentwood had been irreversibly selected" (para. 70).

[51] The Brentwood/EAC joint venture having been selected as the preferred proponent, negotiations for the alliance contract ensued. The trial judge found that by this time, all agreed that a joint venture

l'explique la juge, la présentation d'une proposition par une coentreprise constituait une [TRADUCTION] « inexécution importante » du contrat issu de l'appel d'offres : [TRADUCTION] « . . . en formant une coentreprise avec EAC, Brentwood pouvait proposer un prix plus concurrentiel que celui offert en réponse à la DEI, ce qui touchait à l'essence même du processus d'appel d'offres » (par. 126).

[49] La province reproche à la juge de première instance de faire primer la forme sur le fond. À mon avis, c'est plutôt à sa thèse qu'on peut imputer pareille dérive. Elle avait en main une soumission qu'elle savait provenir d'une coentreprise, elle a encouragé sa présentation et elle a pris des mesures pour masquer le fait qu'elle était formulée par une coentreprise. Elle a ainsi conféré un avantage concurrentiel à celle-ci dans le processus d'appel d'offres, et il appert on ne peut plus clairement du dossier que l'existence de la coentreprise a été considérée comme un atout lors du processus de sélection. La province soutient néanmoins qu'il n'y a là rien d'irrégulier dans la mesure où le nom de Brentwood figurait sur la soumission, puis dans le contrat B. S'il est un argument qui fait primer la forme sur le fond, c'est bien celui-là.

[50] Certes, la province avait obtenu un avis juridique et elle n'a pas agi à l'encontre de celui-ci. Or, les faits établis selon la juge de première instance relativement à cet avis juridique n'appuient pas vraiment la prétention de la province. La juge relève que le conseiller juridique de la province ne disposait pas des éléments de contexte nécessaires pour déterminer si la soumission de Brentwood était admissible, il n'a jamais examiné les conditions d'admissibilité à soumissionner énoncées dans la DP et on ne lui a pas demandé de se pencher sur la question de l'admissibilité, ce qu'il n'a pas fait de son propre chef non plus. Comme le dit la juge, le conseiller juridique [TRADUCTION] « paraît avoir supposé au départ que Brentwood avait été irrévocablement retenue » (par. 70).

[51] La proposition de la coentreprise Brentwood/EAC ayant été retenue, les négociations en vue de la conclusion de l'accord de partenariat ont commencé. De l'avis de la juge de première instance,

was not an eligible proponent and the Ministry was taking the position that the contract could not be in the name of the joint venture. Brentwood and EAC executed a revised pre-contract agreement that provided, notwithstanding the letter of intent from the Ministry addressed to Brentwood indicating that the legal relationship between them would be contractor/subcontractor, the contract would be performed and the profits shared equally between them. The work was to be managed by a committee with equal representation, the bond required by the owner was to be provided by both parties and EAC indemnified Brentwood against half of any loss or cost incurred as a result of performance of the work. According to schedule B4 of the RFP, all subcontracts were to be attached to the RFP but no contract between Brentwood and EAC was ever provided or attached to the proposal.

[52] The Province has identified no palpable and overriding error in these many findings of fact by the trial judge. I conclude, therefore, that we must approach the case on the basis of the judge's finding that the bid was in fact, if not in form, submitted by a joint venture of Brentwood and EAC, that the Ministry was well aware of this, that the existence of the joint venture was a material consideration in favour of the bid during the evaluation process and that by bidding as a joint venture, Brentwood was given a competitive advantage in the bidding process.

[53] I reject the Ministry's submissions that all that matters is the form and not the substance of the arrangement. In my view, the trial judge's finding that this bid was in fact on behalf of a joint venture is unassailable.

[54] I turn to the Province's third point:

(iii) there was no term of the RFP that restricted the right of proponents to enter into joint venture agreements with others; this arrangement merely left Brentwood, the original

tous convenaient alors que la coentreprise n'était pas un soumissionnaire admissible, et le ministère estimait que le contrat ne pouvait être conclu avec elle. Brentwood et EAC ont signé un accord préalable modifié stipulant que, malgré la lettre d'intention du ministère adressée à Brentwood et selon laquelle la relation juridique entre les deux entreprises serait celle existant entre un entrepreneur et un sous-traitant, le contrat serait exécuté par les deux entreprises, et les bénéfices partagés entre elles à parts égales. L'accord prévoyait aussi que la gestion des travaux relèverait d'un comité constitué d'un nombre égal de représentants des deux entreprises, que le cautionnement exigé par le propriétaire serait fourni par les deux entreprises et qu'EAC dédommagerait Brentwood de la moitié des pertes ou des coûts découlant de l'exécution des travaux. Suivant l'annexe B4 de la DP, tous les sous-contrats devaient être joints à la proposition, mais nul contrat intervenu entre Brentwood et EAC ne l'avait été.

[52] La province ne relève aucune erreur manifeste et dominante dans ces nombreuses conclusions de fait tirées en première instance. J'estime donc qu'il nous faut trancher en tenant pour acquis, conformément à ces conclusions, que malgré les apparences, le soumissionnaire était en fait la coentreprise formée de Brentwood et d'EAC, le ministère le savait, l'existence de la coentreprise a été considérée comme un atout lors du processus d'évaluation et la présentation d'une proposition par une coentreprise a fait bénéficier Brentwood d'un avantage concurrentiel dans le processus d'appel d'offres.

[53] La prétention du ministère voulant que tout ce qui importe c'est la forme de l'accord, et non sa teneur, ne saurait tenir. Je conviens avec la juge de première instance que la proposition était en fait présentée par une coentreprise. Sa conclusion est inattaquable.

[54] Je passe maintenant au troisième argument de la province :

(iii) aucune disposition de la DP n'empêchait un proposant de conclure un accord de coentreprise; cette mesure permettait seulement à Brentwood, l'un des proposants initiaux, de

proponent in place and allowed it to enhance its ability to perform the work.

[55] This submission addresses the question of whether the joint venture was an eligible bidder. The Province submits that it is, arguing that s. 2.8(b) of the RFP shows that the RFP contemplated that each proponent would be supported by a team, that the composition of the team might change and that the Province under that section retained the right to approve or reject changes in the team of any proponent. I cannot accept these submissions.

[56] Section 2.8 must be read as a whole and in light of the ministerial approval which I have described earlier. Section 2.8(a), consistent with that approval, stipulates that only the six proponents qualified through the RFEI process were eligible to submit responses and that proposals from any other party "shall not be considered". The word "proponent" is defined in s. 8 as a team that has become eligible to respond to the RFP. The material change provisions in s. 2.8(b) should not be read as negating the express provisions of the RFP and the ministerial approval of the process. When read as a whole, the provisions about material change do not permit the addition of a new entity as occurred here. The process actually followed was not the one specified in the bidding contract and was not authorized by the statute because it was not the one approved by the Minister.

[57] Moreover, even if one were to conclude (and I would not) that this change from the Brentwood team that participated in the RFEI to the Brentwood/EAC joint venture by whom the bid was submitted could fall within the material change provisions of s. 2.8(b), the Province never gave a written decision to permit this change as required by that provision. As the trial judge noted, in fact the Province's position was that such a bid would not be eligible and its agents took steps to obfuscate the true proponent in the relevant documentation.

[58] The trial judge also found that there was an implied obligation of good faith in the contract and

demeurer en lice et d'accroître sa capacité d'exécuter les travaux.

[55] L'argument soulève la question de savoir si la coentreprise était un soumissionnaire admissible. La province prétend que c'était le cas, car selon elle, il appert de l'al. 2.8b) de la DP que chacun des soumissionnaires bénéficierait de l'appui d'une équipe, que la composition de cette équipe pouvait changer et que la province se réservait le droit d'approuver ou non la modification d'une équipe. Je ne puis adhérer à ce raisonnement.

[56] Il faut considérer l'art. 2.8 dans son ensemble et au vu de l'approbation ministérielle dont il est question précédemment. Conformément à cette approbation, l'al. 2.8a) prévoit que seuls les six proposants tenus pour admissibles à l'issue de la DEI peuvent présenter une proposition et que les propositions présentées par d'autres personnes [TRADUCTION] « ne seront pas examinées ». Suivant l'article 8, [TRADUCTION] « proposant » s'entend d'une équipe admise à répondre à la DP. L'alinéa 2.8b) — relatif aux changements substantiels — ne saurait être interprété de façon à contrecarrer les dispositions expresses de la DP et l'approbation ministérielle du processus. Considérées globalement, les dispositions relatives aux changements substantiels ne permettent pas l'adjonction d'une nouvelle entité comme celle qui a eu lieu en l'espèce. La procédure suivie dans les faits n'a pas été celle prévue dans le dossier d'appel d'offres et, n'ayant pas été approuvée par le ministre, elle n'était pas légalement autorisée.

[57] Qui plus est, à supposer même (et je ne suis pas disposé à le faire) que le passage de l'équipe Brentwood ayant répondu à la DEI à la coentreprise Brentwood/EAC qui a présenté la soumission constituait un changement substantiel pour les besoins de l'al. 2.8b), il reste que la province ne l'a jamais avalisé par écrit comme l'exigeait cette disposition. La juge du procès fait observer que la province jugeait la soumission inadmissible et que ses préposés ont occulté la véritable identité du proposant dans les documents en cause.

[58] La juge de première instance conclut également qu'il y avait une obligation contractuelle

that the Province breached this obligation by failing to treat all bidders equally by changing the terms of eligibility to Brentwood's competitive advantage. This conclusion strongly reinforces the trial judge's decision about eligibility. Rather than repeating her detailed findings, I will simply quote her summary at para. 138:

> The whole of [the Province's] conduct leaves me with no doubt that the [Province] breached the duty of fairness to [Tercon] by changing the terms of eligibility to Brentwood's competitive advantage. At best, [the Province] ignored significant information to its [i.e. Tercon's] detriment. At worst, the [Province] covered up its knowledge that the successful proponent was an ineligible joint venture. In the circumstances here, it is not open to the [Province] to say that a joint venture was only proposed. Nor can the [Province] say that it was unaware of the joint venture when it acted deliberately to structure contract B to include EAC as fully responsible within a separate contract with Brentwood, so minimizing the [Province's] risk that the contract would be unenforceable against EAC if arrangements did not work out. . . . The [Province] was . . . prepared to take the risk that unsuccessful bidders would sue: this risk did materialize.

[59] To conclude on this point, I find no fault with the trial judge's conclusion that the bid was in fact submitted on behalf of a joint venture of Brentwood and EAC which was an ineligible bidder under the terms of the RFP. This breached not only the express eligibility provisions of the tender documents, but also the implied duty to act fairly towards all bidders.

B. *The Exclusion Clause*

1. Introduction

[60] As noted, the RFP includes an exclusion clause which reads as follows:

> **2.10** . . .
>
> Except as expressly and specifically permitted in these Instructions to Proponents, no Proponent shall

tacite d'agir de bonne foi et que la province a manqué à cette obligation en ne traitant pas tous les soumissionnaires sur un pied d'égalité du fait de la modification des conditions d'admissibilité et de l'octroi d'un avantage concurrentiel à Brentwood. Cette conclusion de la juge affermit considérablement celle qu'elle tire au sujet de l'admissibilité. Je m'abstiens de reprendre ses conclusions détaillées, mais j'en cite le résumé (par. 138) :

> [TRADUCTION] Au vu de l'ensemble de la conduite [de la province], il ne fait pour moi aucun doute que celle-ci a manqué à son obligation d'équité à l'endroit de [Tercon] lorsqu'elle a modifié les conditions d'admissibilité à l'avantage de Brentwood du point de vue concurrentiel. Au mieux, elle a fait abstraction de renseignements importants au détriment de Tercon. Au pire, elle a dissimulé le fait que le soumissionnaire retenu était une coentreprise inadmissible. Dans ces circonstances, la province ne saurait faire valoir que la formation d'une coentreprise était seulement envisagée. Elle ne peut non plus prétendre avoir ignoré l'existence de la coentreprise alors qu'elle a délibérément conçu le contrat B de façon qu'EAC en accepte les modalités dans un contrat distinct conclu avec Brentwood, réduisant ainsi le risque [pour la province] que le contrat ne puisse être opposable à EAC si les accords projetés tournaient court. [. . .] [La province] était [. . .] prête à courir le risque que les soumissionnaires non retenus la poursuivent : ce risque s'est matérialisé.

[59] Pour clore sur ce point, sa conclusion selon laquelle la soumission était en fait celle d'une coentreprise formée de Brentwood et d'EAC qui n'était pas admise à soumissionner suivant la DP n'est à mon avis entachée d'aucune erreur. L'inobservation qui en découle touche non seulement les conditions d'admissibilité énoncées dans le dossier d'appel d'offres, mais aussi l'obligation tacite d'agir équitablement vis-à-vis de tous les soumissionnaires.

B. *La clause de non-recours*

1. Introduction

[60] Rappelons que la DP renferme une clause de non-recours, dont voici le texte :

> [TRADUCTION]
>
> **2.10** . . .
>
> Sauf ce que prévoient expressément les présentes instructions, un proposant ne peut exercer aucun

have any claim for compensation of any kind whatsoever, as a result of participating in this RFP, and by submitting a Proposal each Proponent shall be deemed to have agreed that it has no claim. [Emphasis added.]

[61] The trial judge held that as a matter of construction, the clause did not bar recovery for the breaches she had found. The clause, in her view, was ambiguous and, applying the *contra proferentem* principle, she resolved the ambiguity in Tercon's favour. She also found that the Province's breach was fundamental and that it was not fair or reasonable to enforce the exclusion clause in light of the nature of the Province's breach. The Province contends that the judge erred both with respect to the construction of the clause and her application of the doctrine of fundamental breach.

[62] On the issue of fundamental breach in relation to exclusion clauses, my view is that the time has come to lay this doctrine to rest, as Dickson C.J. was inclined to do more than 20 years ago: *Hunter Engineering Co. v. Syncrude Canada Ltd.*, [1989] 1 S.C.R. 426, at p. 462. I agree with the analytical approach that should be followed when tackling an issue relating to the applicability of an exclusion clause set out by my colleague Binnie J. However, I respectfully do not agree with him on the question of the proper interpretation of the clause in issue here. In my view, the clause does not exclude Tercon's claim for damages, and even if I am wrong about that, the clause is at best ambiguous and should be construed *contra proferentem* as the trial judge held. As a result of my conclusion on the interpretation issue, I do not have to go on to apply the rest of the analytical framework set out by Binnie J.

[63] In my view, the exclusion clause does not cover the Province's breaches in this case. The RFP process put in place by the Province was premised on a closed list of bidders; a contest with an ineligible bidder was not part of the RFP process and was in fact expressly precluded by its terms. A "Contract A" could not arise as a result of submission of a bid from any other party. However, as

recours en indemnisation pour sa participation à la DP, ce qu'il est réputé accepter lorsqu'il présente une soumission. [Je souligne.]

[61] La juge de première instance statue que le libellé de la clause ne fait pas obstacle à l'indemnisation pour les inexécutions relevées. À son avis, la clause est équivoque et, conformément à la règle *contra proferentem*, elle l'interprète en faveur de Tercon. Elle opine en outre que l'inexécution reprochée à la province est fondamentale et qu'il n'est ni juste ni raisonnable de faire respecter la clause de non-recours étant donné la nature de l'inexécution. La province fait valoir que la juge a interprété erronément la clause et qu'elle a eu tort de recourir au principe de l'inexécution fondamentale.

[62] En ce qui concerne son application aux clauses d'exonération, je crois que le temps est venu de donner le coup de grâce au principe de l'inexécution fondamentale comme le juge en chef Dickson y était enclin il y a plus de 20 ans : *Hunter Engineering Co. c. Syncrude Canada Ltée*, [1989] 1 R.C.S. 426, p. 462. Je souscris à la démarche analytique qui s'impose, selon mon collègue le juge Binnie, pour s'attaquer à une question touchant à l'applicabilité d'une clause d'exonération. Malheureusement, je ne puis faire mienne son interprétation de la clause litigieuse en l'espèce. À mon sens, la clause ne fait pas obstacle au recours en dommages-intérêts de Tercon et, même si j'ai tort sur ce point, la clause est au mieux équivoque et doit être interprétée *contra proferentem* comme le préconise la juge de première instance. Vu ma conclusion concernant l'interprétation, je n'ai pas à appliquer les autres volets de la démarche analytique du juge Binnie.

[63] J'estime que la clause de non-recours ne s'applique pas aux inexécutions imputées à la province. Le processus de DP mis en place par celle-ci supposait la participation d'un nombre limité d'entreprises. La mise en concurrence avec un soumissionnaire inadmissible n'en faisait pas partie et elle était même expressément exclue. La présentation d'une proposition par une autre entreprise ne

a result of how the Province proceeded, the very premise of its own RFP process was missing, and the work was awarded to a party who could not be a participant in the RFP process. That is what Tercon is complaining about. Tercon's claim is not barred by the exclusion clause because the clause only applies to claims arising "as a result of participating in [the] RFP", not to claims resulting from the participation of other, ineligible parties. Moreover, the words of this exclusion clause, in my view, are not effective to limit liability for breach of the Province's implied duty of fairness to bidders. I will explain my conclusion by turning first to a brief account of the key legal principles and then to the facts of the case.

2. Legal Principles

[64] The key principle of contractual interpretation here is that the words of one provision must not be read in isolation but should be considered in harmony with the rest of the contract and in light of its purposes and commercial context. The approach adopted by the Court in *M.J.B.* is instructive. The Court had to interpret a privilege clause, which is somewhat analogous to the exclusion clause in issue here. The privilege clause provided that the lowest or any tender would not necessarily be accepted, and the issue was whether this barred a claim based on breach of an implied term that the owner would accept only compliant bids. In interpreting the privilege clause, the Court looked at its text in light of the contract as a whole, its purposes and commercial context. As Iacobucci J. said, at para. 44, "the privilege clause is only one term of Contract A and must be read in harmony with the rest of the tender documents. To do otherwise would undermine the rest of the agreement between the parties."

[65] In a similar way, it is necessary in the present case to consider the exclusion clause in the RFP in light of its purposes and commercial context as well as of its overall terms. The question is whether the exclusion of compensation for claims resulting

pouvait faire naître un « contrat A ». La province a donc ignoré le fondement même de sa propre DP et elle a attribué le marché à une entreprise non admise à y prendre part. C'est ce dont Tercon lui fait grief. La clause de non-recours ne fait pas obstacle au recours de Tercon, car elle ne s'applique qu'à l'indemnisation demandée [TRADUCTION] « pour [l]a participation à la DP », et non au recours qui fait suite à la participation d'une autre entreprise, elle inadmissible. De plus, le texte de la clause ne limite pas selon moi la responsabilité de la province pour le manquement à son obligation tacite de faire preuve d'équité à l'égard des soumissionnaires. Je m'explique en exposant brièvement les principes juridiques essentiels, puis en les appliquant aux faits de l'espèce.

2. Les principes juridiques

[64] Le principe fondamental d'interprétation applicable en l'espèce veut qu'une clause contractuelle ne doive pas être considérée isolément mais en harmonie avec les autres et à la lumière de son objet et du contexte commercial dans lequel elle s'inscrit. La démarche suivie dans l'arrêt *M.J.B.* est éclairante. La Cour devait y interpréter une clause de réserve qui s'apparentait quelque peu à la clause de non-recours qui nous intéresse. La clause de réserve stipulait que le marché ne serait pas nécessairement attribué au soumissionnaire le moins disant ni même attribué du tout. La question était celle de savoir si elle faisait obstacle à une action en justice pour non-respect de la clause tacite voulant que le propriétaire n'accepte que les soumissions conformes. Pour l'interpréter, la Cour examine son libellé au vu du contrat dans son ensemble, de son objet et de son contexte commercial. Le juge Iacobucci conclut au par. 44 : « . . . la clause de réserve n'est qu'une condition du contrat A et elle doit être interprétée de façon à s'harmoniser avec le reste du dossier d'appel d'offres. Agir autrement, ce serait saper le reste de l'entente entre les parties. »

[65] De même, il faut en l'espèce examiner la clause de non-recours de la DP à la lumière de son objet et du contexte commercial dans lequel elle s'inscrit, ainsi que de l'ensemble de ses conditions. Il faut se demander si l'exclusion de toute

from "participating in this RFP", properly interpreted, excludes liability for the Province having unfairly considered a bid from a bidder who was not supposed to have been participating in the RFP process at all.

3. Application to This Case

[66] Having regard to both the text of the clause in its broader context and to the purposes and commercial context of the RFP, my view is that this claim does not fall within the terms of the exclusion clause.

[67] To begin, it is helpful to recall that in interpreting tendering contracts, the Court has been careful to consider the special commercial context of tendering. Effective tendering ultimately depends on the integrity and business efficacy of the tendering process: see, e.g., *Martel*, at para. 88; *M.J.B.*, at para. 41; *Double N Earthmovers*, at para. 106. As Iacobucci and Major JJ. put it in *Martel*, at para. 116, "it is imperative that all bidders be treated on an equal footing . . . . Parties should at the very least be confident that their initial bids will not be skewed by some underlying advantage in the drafting of the call for tenders conferred upon only one potential bidder."

[68] This factor is particularly weighty in the context of public procurement. In that context, in addition to the interests of the parties, there is the need for transparency for the public at large. This consideration is underlined by the statutory provisions which governed the tendering process in this case. Their purpose was to assure transparency and fairness in public tenders. As was said by Orsborn J. (as he then was) in *Cahill (G.J.) & Co. (1979) Ltd. v. Newfoundland and Labrador (Minister of Municipal and Provincial Affairs)*, 2005 NLTD 129, 250 Nfld. & P.E.I.R. 145, at para. 35:

The owner — in this case the government — is in control of the tendering process and may define the

indemnisation pour [TRADUCTION] « [l]a participation à la DP », correctement interprétée, soustrait la province à sa responsabilité lorsqu'elle se rend coupable d'iniquité en prenant en considération la proposition d'une entreprise qui n'était pas du tout censée participer à la DP.

3. Application à la présente espèce

[66] Compte tenu du libellé de la clause dans son contexte plus général ainsi que de l'objet et du contexte commercial de la DP, j'estime que le recours échappe à la clause de non-recours.

[67] D'abord, il convient de rappeler que pour interpréter le contrat issu de l'appel d'offres, la Cour tient dûment compte du contexte commercial particulier de la demande de propositions. Au final, le caractère fructueux du processus dépend de son intégrité et de son efficacité commerciale : voir, p. ex., les arrêts *Martel*, par. 88; *M.J.B.*, par. 41, et *Double N Earthmovers*, par. 106. Comme l'affirment les juges Iacobucci et Major dans l'arrêt *Martel*, au par. 116 : « Il est [. . .] impératif que tous les soumissionnaires soient traités sur un pied d'égalité [. . .] Un soumissionnaire devrait à tout le moins être assuré que l'évaluation de sa soumission initiale ne sera pas biaisée par quelque avantage sous-entendu dans le dossier d'appel d'offres et dont ne bénéficie qu'un seul soumissionnaire éventuel. »

[68] Ce facteur importe particulièrement dans le contexte de la passation de marchés publics. C'est pourquoi il faut non seulement protéger les intérêts des parties, mais également assurer la transparence du processus vis-à-vis des citoyens en général. Ce souci ressort des dispositions législatives qui régissaient le processus dans la présente affaire et dont l'objectif était d'assurer la transparence et l'équité des appels d'offres. Comme le dit le juge Orsborn (maintenant Juge en chef) dans l'arrêt *Cahill (G.J.) & Co. (1979) Ltd. c. Newfoundland and Labrador (Minister of Municipal and Provincial Affairs)*, 2005 NLTD 129, 250 Nfld. & P.E.I.R. 145, par. 35 :

[TRADUCTION] Le propriétaire — en l'occurrence l'État — est maître du processus d'appel d'offres. Il peut

parameters for a compliant bid and a compliant bidder. The corollary to this, of course, is that once the owner — here the government — sets the rules, it must itself play by those rules in assessing the bids and awarding the main contract.

[69] One aspect that is generally seen as contributing to the integrity and business efficacy of the tendering process is the requirement that only compliant bids be considered. As noted earlier, such a requirement has often been implied because, as the Court said in *M.J.B.*, it makes little sense to think that a bidder would comply with the bidding process if the owner could circumscribe it by accepting a non-compliant bid. Respectfully, it seems to me to make even less sense to think that eligible bidders would participate in the RFP if the Province could avoid liability for ignoring an express term concerning eligibility to bid on which the entire RFP was premised and which was mandated by the statutorily approved process.

[70] The closed list of bidders was the foundation of this RFP and there were important competitive advantages to a bidder who could side-step that limitation. Thus, it seems to me that both the integrity and the business efficacy of the tendering process support an interpretation that would allow the exclusion clause to operate compatibly with the eligibility limitations that were at the very root of the RFP.

[71] The same may be said with respect to the implied duty of fairness. As Iacobucci and Major JJ. wrote for the Court in *Martel*, at para. 88, "[i]mplying an obligation to treat all bidders fairly and equally is consistent with the goal of protecting and promoting the integrity of the bidding process." It seems to me that clear language is necessary to exclude liability for breach of such a basic requirement of the tendering process, particularly in the case of public procurement.

déterminer les paramètres de la conformité d'une soumission et de l'admissibilité d'un soumissionnaire. Il s'en suit évidemment que lorsque le propriétaire — en l'occurrence l'État — établit les règles, il doit les respecter au moment d'évaluer les offres et d'attribuer le contrat principal.

[69] L'exigence que seules soient examinées des soumissions conformes est généralement considérée comme un élément favorisant l'intégrité et l'efficacité commerciale du processus d'appel d'offres. J'ai déjà mentionné que cette exigence est souvent inférée parce que, pour reprendre les propos de la Cour dans l'arrêt *M.J.B.*, il est déraisonnable qu'un soumissionnaire doive se conformer au processus d'appel d'offres si le propriétaire peut le contourner en acceptant une soumission non conforme. J'ajoute qu'il est encore moins concevable qu'un soumissionnaire admissible prenne part à une DP si la province peut échapper à toute responsabilité malgré l'inobservation d'une condition expresse relative à l'admissibilité à soumissionner, une condition qui formait l'assise de la DP en entier et qui bénéficiait de l'approbation ministérielle requise par la loi.

[70] La limitation du nombre de soumissionnaires admissibles constituait l'assise de la DP, et l'entreprise admise à soumissionner malgré cette restriction se voyait conférer un avantage concurrentiel considérable. À mon sens, l'intégrité et l'efficacité commerciale du processus d'appel d'offres commandent donc une interprétation qui permet une application de la clause de non-recours compatible avec la limitation du nombre de soumissionnaires admissibles, laquelle formait l'assise même de la DP.

[71] Il en va de même de l'obligation tacite d'équité. Comme le disent les juges Iacobucci et Major au nom de la Cour dans l'arrêt *Martel*, « [l]'existence présumée d'une obligation de traiter tous les soumissionnaires équitablement et sur un pied d'égalité est compatible avec l'objectif de protéger et de promouvoir l'intégrité du mécanisme d'appel d'offres » (par. 88). J'estime que seul un libellé clair peut écarter la responsabilité consécutive au non-respect d'une exigence aussi fondamentale applicable au processus d'appel d'offres, spécialement lorsqu'il s'agit de passer un marché public.

[72] The proper interpretation of the exclusion clause should also take account of the statutory context which I have reviewed earlier. The restriction on eligibility of bidders was a key element of the alternative process approved by the Minister. It seems unlikely, therefore, that the parties intended through this exclusion clause to effectively gut a key aspect of the approved process. Of course, it is true that the exclusion clause does not bar all remedies, but only claims for compensation. However, the fact remains that as a practical matter, there are unlikely to be other, effective remedies for considering and accepting an ineligible bid and that barring compensation for a breach of that nature in practical terms renders the ministerial approval process virtually meaningless. Whatever administrative law remedies may be available, they are not likely to be effective remedies for awarding a contract to an ineligible bidder. The Province did not submit that injunctive relief would have been an option, and I can, in any event, foresee many practical problems that need not detain us here in seeking such relief in these circumstances.

[73] The Province stresses Tercon's commercial sophistication, in effect arguing that it agreed to the exclusion clause and must accept the consequences. This line of argument, however, has two weaknesses. It assumes the answer to the real question before us which is: what does the exclusion clause mean? The consequences of agreeing to the exclusion clause depend on its construction. In addition, the Province's submission overlooks its own commercial sophistication and the fact that sophisticated parties can draft very clear exclusion and limitation clauses when they are minded to do so. Such clauses contrast starkly with the curious clause which the Province inserted into this RFP. The limitation of liability clause in *Hunter*, for example, provided that "[n]otwithstanding any other provision in this contract or any applicable statutory provisions neither the Seller nor the Buyer shall be liable to the other for special or consequential damages or damages for loss of use arising directly or indirectly from any breach of this contract, fundamental or otherwise" (p. 450). The Court found this to be clear and unambiguous. The limitation clause in issue in *Guarantee Co. of North*

[72] La juste interprétation de la clause de non-recours doit aussi s'appuyer sur le cadre législatif examiné précédemment. L'admissibilité restreinte constituait un élément essentiel de l'autre processus approuvé par le ministre. Il est donc peu probable que les parties aient vraiment voulu, en stipulant la clause de non-recours, supprimer un aspect essentiel de ce processus. La clause ne fait évidemment obstacle qu'aux demandes d'indemnisation. Cependant, il demeure peu probable que l'examen et l'acceptation d'une soumission inadmissible confèrent un autre recours efficace, sans compter que l'exclusion de l'indemnisation du préjudice causé par un tel manquement supprime en fait toute la raison d'être du processus d'approbation ministérielle. Quel que soit le recours possible en droit administratif, il est peu probable qu'il permette d'obtenir réparation pour l'octroi d'un marché à un soumissionnaire inadmissible. La province ne plaide pas qu'une injonction aurait pu être obtenue et, de toute manière, je peux concevoir de nombreuses difficultés d'ordre pratique qui justifient de ne pas s'attarder davantage à cette avenue possible.

[73] La province insiste sur l'expérience commerciale de Tercon. Elle soutient en fait que l'entreprise a convenu de la clause de non-recours et qu'elle doit en accepter les conséquences. L'argument comporte toutefois deux failles. Il préjuge du règlement par la Cour de la véritable question en litige : quelle est la portée de la clause de non-recours? Les conséquences résultant de l'adhésion à cette clause dépendent de son interprétation. En outre, la province passe sous silence sa propre expérience commerciale et le fait que des parties rompues aux usages commerciaux peuvent rédiger des clauses très claires de non-recours ou de responsabilité limitée lorsqu'elles entendent le faire. Ce n'est manifestement pas le cas de la curieuse clause que la province a insérée dans sa DP. À titre d'exemple, la clause de responsabilité limitée visée dans l'arrêt *Hunter* disposait que « [n]onobstant toute autre disposition du présent contrat ou toute disposition législative applicable, ni le vendeur ni l'acheteur n'est tenu de verser à l'autre des dommages-intérêts spéciaux ni des dommages-intérêts pour un préjudice indirect ou encore pour la perte d'usage résultant directement ou indirectement d'une inexécution, fondamentale

America v. Gordon Capital Corp., [1999] 3 S.C.R. 423, provided that legal proceedings for the recovery of "any loss hereunder shall not be brought . . . after the expiration of 24 months from the discovery of such loss" (para. 5). Once again, the Court found this language clear. The Ontario Court of Appeal similarly found the language of a limitation of liability clause to be clear in *Fraser Jewellers (1982) Ltd. v. Dominion Electric Protection Co.* (1997), 34 O.R. (3d) 1. The clause provided in part that if the defendant "should be found liable for loss, damage or injury due to a failure of service or equipment in any respect, its liability shall be limited to a sum equal to 100% of the annual service charge or $10,000.00, whichever is less, as the agreed upon damages and not as a penalty, as the exclusive remedy" (p. 4). These, and many other cases which might be referred to, demonstrate that sophisticated parties are capable of drafting clear and comprehensive limitation and exclusion provisions.

[74] I turn to the text of the clause which the Province inserted in its RFP. It addresses claims that result from "participating in this RFP". As noted, the limitation on who could participate in this RFP was one of its premises. These words must, therefore, be read in light of the limit on who was eligible to participate in this RFP. As noted earlier, both the ministerial approval and the text of the RFP itself were unequivocal: only the six proponents qualified through the earlier RFEI process were eligible and *proposals received from any other party would not be considered*. Thus, central to "participating in this RFP" was participating in a contest among those eligible to participate. A process involving other bidders, as the trial judge found the process followed by the Province to be, is not the process called for by "this RFP" and being part of that other process is not in any meaningful sense "participating in this RFP".

ou autre, du présent contrat » (p. 450). La Cour a jugé ce texte clair et non équivoque. Dans l'affaire *Guarantee Co. of North America c. Gordon Capital Corp.*, [1999] 3 R.C.S. 423, la clause en litige prévoyait que des procédures judiciaires en vue de l'indemnisation de « tout sinistre visé aux présentes ne doivent pas être engagées [. . .] après l'expiration d'un délai de 24 mois suivant la découverte du sinistre » (par. 5). Là encore, la Cour conclut à la clarté du libellé. Dans l'arrêt *Fraser Jewellers (1982) Ltd. c. Dominion Electric Protection Co.* (1997), 34 O.R. (3d) 1, la Cour d'appel de l'Ontario conclut également au caractère non équivoque de la clause de responsabilité limitée, qui disposait notamment que si la défenderesse [TRADUCTION] « était tenue responsable d'un préjudice consécutif à une défaillance du service ou du matériel, quelle qu'elle soit, elle n'était tenue de verser que la totalité des frais de service annuels ou 10 000 $, selon le moindre des deux montants, à titre d'indemnité convenue, et non de pénalité, à l'exclusion de toute autre réparation » (p. 4). Ces exemples et bien d'autres que l'on pourrait citer montrent que des parties expérimentées sont en mesure de rédiger des clauses de responsabilité limitée ou de non-recours à la fois claires et exhaustives.

[74] Passons maintenant au texte de la clause insérée au contrat par la province. Il vise les demandes d'indemnisation d'un préjudice découlant de la [TRADUCTION] « participation à la DP ». Rappelons que l'une des assises de la DP était la limitation du nombre d'entreprises admises à y prendre part. Il faut donc interpréter ce texte au regard de cette limitation. Tant l'approbation ministérielle que le texte de la DP elle-même sont clairs : seuls les six proposants s'étant rendus admissibles en répondant à la DEI pouvaient soumissionner, et *aucune proposition d'une autre personne ne serait examinée*. La participation à un concours ouvert aux seules personnes admises à y prendre part était donc au cœur de la « participation à la DP ». Un processus ouvert à d'autres entreprises — ce qui était le cas du processus suivi dans les faits selon la juge de première instance — ne saurait s'entendre de « la DP », et le fait d'y prendre part ne saurait véritablement être considéré comme une « participation à la DP ».

[75] The Province would have us interpret the phrase excluding compensation "as a result of participating in this RFP" to mean that compensation is excluded that results from "submitting a Proposal". However, that interpretation is not consistent with the wording of the clause as a whole. The clause concludes with the phrase that "by submitting a Proposal each Proponent shall be deemed to have agreed that it has no claim". If the phrases "participating in this RFP" and "submitting a Proposal" were intended to mean the same thing, it is hard to understand why different words were used in the same short clause to express the same idea. The fact that the Minister had approved a closed list of participants strengthens the usual inference that the use of different words was deliberate so as not to exclude compensation for a departure from that basic eligibility requirement.

[75] La province nous exhorte à conclure que l'énoncé écartant toute indemnisation « pour [l]a participation à la DP » signifie qu'il ne saurait y avoir d'indemnisation d'un préjudice résultant de la [TRADUCTION] « présent[ation d']une soumission », ce qui pourtant serait incompatible avec le texte de la clause dans son ensemble. Il y est d'ailleurs stipulé à la toute fin que le proposant [TRADUCTION] « est réputé accepter [qu'il ne peut exercer aucun recours en indemnisation] lorsqu'il présente une soumission ». Si la « participation à la DP » et la « présent[ation d']une soumission » devaient s'entendre de la même chose, on s'expliquerait difficilement que des termes différents soient employés dans la même clause brève pour exprimer la même idée. L'aval donné par le ministre à la limitation du nombre de participants étaye l'interprétation habituelle voulant que l'emploi des termes différents visait délibérément à ne pas écarter l'indemnisation en cas d'inobservation de cette exigence fondamentale liée à l'admissibilité.

[76] This interpretation of the exclusion clause does not rob it of meaning, but makes it compatible with other provisions of the RFP. There is a parallel between this case and the Court's decision in *M.J.B.* There, the Court found that there was compatibility between the privilege clause and the implied term to accept only compliant bids. Similarly, in this case, there is compatibility between the eligibility requirements of the RFP and the exclusion clause. Not any and every claim based on any and every deviation from the RFP provisions would escape the preclusive effect of the exclusion clause. It is only when the defect in the Province's adherence to the RFP process is such that it is completely outside that process that the exclusion clause cannot have been intended to operate. What is important here, in my view, is that the RFP in its conception, in its express provisions and in the statutorily required approval it was given, was premised on limiting eligibility to the six proponents in the RFEI process. Competition among others was not at all contemplated and was not part of the RFP process; in fact, the RFP expressly excluded that possibility. In short, limiting eligibility of bidders to those who had responded to the RFEI was the foundation of the whole RFP. As the judge found, acceptance of

[76] Pareille interprétation de la clause de non-recours ne la prive pas de sens, mais assure sa compatibilité avec les autres clauses de la DP. Un parallèle peut être établi entre la présente espèce et l'affaire *M.J.B.*, où la Cour conclut à la compatibilité de la clause de réserve avec la condition tacite que seule une soumission conforme puisse être acceptée. Il y a également compatibilité en l'espèce entre les conditions d'admissibilité de la DP et la clause de non-recours. Toute action intentée pour quelque manquement aux dispositions de la DP n'échappe pas à l'application de la clause de non-recours. Ce n'est que lorsque le non-respect du processus de DP par la province est tel que la démarche suivie est totalement étrangère à ce processus qu'on ne peut conclure que les parties ont voulu l'application de la clause de non-recours. Ce qui importe en l'occurrence selon moi c'est que la DP, au vu de sa conception, de ses dispositions expresses et de son approbation légale, avait pour assise l'admissibilité des seuls six proposants ayant répondu à la DEI. La mise en concurrence avec des tiers n'était pas envisagée et elle ne faisait pas partie du processus; en fait, la DP l'excluait expressément. En bref, l'admissibilité des seuls proposants qui avaient répondu à la DEI était l'assise même la DP.

a bid from an ineligible bidder "attacks the underlying premise of the process" established by the RFP: para. 146. Liability for such an attack is not excluded by a clause limiting compensation resulting from participation in this RFP.

Comme le dit la juge de première instance, l'acceptation de la proposition d'un soumissionnaire inadmissible [TRADUCTION] « sape l'assise du processus » établi par la DP : par. 146. La clause écartant toute indemnisation pour la participation à la DP ne saurait soustraire une partie à la responsabilité découlant d'une telle atteinte.

[77] This interpretation is also supported by another provision of the RFP. Under s. 2.9, as mentioned earlier, the Province reserved to itself the right to unilaterally cancel the RFP and the right to propose a new RFP allowing additional bidders. If the exclusion clause were broad enough to exclude compensation for allowing ineligible bidders to participate, there seems to be little purpose in this reservation of the ability to cancel the RFP and issue a new one to a wider circle of bidders. It is also significant that the Province did not reserve to itself the right to accept a bid from an ineligible bidder or to unilaterally change the rules of eligibility. The RFP expressly did exactly the opposite. None of this, in my opinion, supports the view that the exclusion clause should be read as applying to the Province's conduct in this case.

[77] Une autre disposition de la DP valide cette interprétation. Comme je le signale précédemment, à la clause 2.9, la province se réserve le droit d'annuler unilatéralement la DP et celui de proposer la tenue d'un nouvel appel d'offres ouvert à d'autres soumissionnaires. Si la clause de non-recours avait une portée suffisamment large pour écarter la responsabilité résultant de l'acceptation de propositions présentées par des soumissionnaires non admissibles, point n'aurait été besoin de prévoir cette faculté de mettre fin à la DP et d'en lancer une nouvelle en élargissant le cercle des soumissionnaires éventuels. Il est aussi révélateur que la province ne se soit pas réservé le droit d'accepter la proposition d'un soumissionnaire inadmissible ou de modifier de son seul chef les règles d'admissibilité. La DP prévoit expressément l'exact contraire. À mon sens, rien de tout cela n'appuie la thèse que la clause de non-recours devrait être interprétée de façon à la rendre applicable au comportement de la province en l'espèce.

[78] To hold otherwise seems to me to be inconsistent with the text of the clause read in the context of the RFP as a whole and in light of its purposes and commercial context. In short, I cannot accept the contention that, by agreeing to exclude compensation for participating in this RFP process, the parties could have intended to exclude a damages claim resulting from the Province unfairly permitting a bidder to participate who was not eligible to do so. I cannot conclude that the provision was intended to gut the RFP's eligibility requirements as to who may participate in it, or to render meaningless the Minister's statutorily required approval of the alternative process where this was a key element. The provision, as well, was not intended to allow the Province to escape a damages claim for applying different eligibility criteria, to the competitive disadvantage of other bidders and for taking

[78] Selon moi, conclure le contraire va à l'encontre du texte de la clause interprété eu égard au contexte de la DP dans son ensemble et à la lumière de l'objet et du contexte commercial de celle-ci. En somme, je ne peux faire droit à la prétention selon laquelle, en écartant toute indemnité pour la participation à la DP, les parties ont pu vouloir faire obstacle à tout recours en dommages-intérêts intenté pour l'iniquité dont aurait pu faire preuve la province en permettant à une entreprise de participer à un processus auquel elle n'était pas admise à prendre part. Je ne peux conclure que la clause visait à supprimer les conditions d'admissibilité de la DP, à priver de sa raison d'être l'approbation ministérielle du nouveau processus exigée par la loi, dont les conditions d'admissibilité en question formaient un élément clé, non plus qu'à permettre à la province d'échapper à toute responsabilité après avoir

steps designed to disguise the true state of affairs. I cannot conclude that the parties, through the words found in this exclusion clause, intended to waive compensation for conduct like that of the Province in this case that strikes at the heart of the integrity and business efficacy of the tendering process which it undertook.

[79] If I am wrong about my interpretation of the clause, I would hold, as did the trial judge, that its language is at least ambiguous. If, as the Province contends, the phrase "participating in this RFP" could reasonably mean "submitting a Proposal", that phrase could also reasonably mean "competing against the other eligible participants". Any ambiguity in the context of this contract requires that the clause be interpreted against the Province and in favour of Tercon under the principle *contra proferentem*: see, e.g., *Hillis Oil and Sales Ltd. v. Wynn's Canada, Ltd.*, [1986] 1 S.C.R. 57, at pp. 68-69. Following this approach, the clause would not apply to bar Tercon's damages claim.

V. Disposition

[80] I conclude that the judge did not err in finding that the Province breached the tendering contract or in finding that Tercon's remedy in damages for that breach was not precluded by the exclusion clause in the contract. I would therefore allow the appeal, set aside the order of the Court of Appeal and restore the judgment of the trial judge. The parties advise that the question of costs has been resolved between them and that therefore no order in relation to costs is required.

The reasons of McLachlin C.J. and Binnie, Abella and Rothstein JJ. were delivered by

[81] BINNIE J. (dissenting) — The important legal issue raised by this appeal is whether, and in what

appliqué des critères d'admissibilité différents défavorisant des soumissionnaires sur le plan concurrentiel et pris des mesures pour dissimuler cette réalité. Je ne puis non plus arriver à la conclusion que les parties ont voulu, en employant le libellé de la clause de non-recours, exclure toute indemnité pour le préjudice infligé par un comportement comme celui reproché à la province en l'espèce, un comportement qui porte directement atteinte à l'intégrité de l'appel d'offres lancé et à son efficacité commerciale.

[79] Si toutefois j'avais tort d'interpréter la clause comme je le fais, je statuerais, à l'instar de la juge de première instance, que son texte est pour le moins équivoque. Si, comme le prétend la province, l'énoncé [TRADUCTION] « participation à la DP » pouvait raisonnablement s'entendre de la « présent[ation d']une proposition », il pourrait aussi bien équivaloir au fait de « se mesurer aux autres participants admissibles ». Toute ambiguïté dans le cadre du contrat commande que la clause soit interprétée au détriment de la province et en faveur de Tercon suivant la règle *contra proferentem* : voir, p. ex., *Hillis Oil and Sales Ltd. c. Wynn's Canada, Ltd.*, [1986] 1 R.C.S. 57, p. 68-69. Dès lors, la clause ne ferait pas obstacle au recours en dommages-intérêts de Tercon.

V. Dispositif

[80] Je conclus que la juge de première instance n'a pas commis d'erreur en statuant que la province n'avait pas respecté le contrat issu de l'appel d'offres et que la clause de non-recours figurant dans ce contrat ne faisait pas obstacle à l'action en dommages-intérêts intentée par Tercon pour cette inexécution. Je suis donc d'avis d'accueillir le pourvoi, d'annuler l'ordonnance de la Cour d'appel et de rétablir le jugement de première instance. Les parties ayant réglé entre elles la question des dépens, il n'est donc pas nécessaire de rendre d'ordonnance à ce sujet.

Version française des motifs de la juge en chef McLachlin et des juges Binnie, Abella et Rothstein rendus par

[81] LE JUGE BINNIE (dissident) — Le présent pourvoi soulève une question de droit importante,

circumstances, a court will deny a defendant contract breaker the benefit of an exclusion of liability clause to which the innocent party, not being under any sort of disability, has agreed. Traditionally, this has involved consideration of what is known as the doctrine of fundamental breach, a doctrine which Dickson C.J. in *Hunter Engineering Co. v. Syncrude Canada Ltd.*, [1989] 1 S.C.R. 426, suggested should be laid to rest 21 years ago (p. 462).

[82] On this occasion we should again attempt to shut the coffin on the jargon associated with "fundamental breach". Categorizing a contract breach as "fundamental" or "immense" or "colossal" is not particularly helpful. Rather, the principle is that a court has no discretion to refuse to enforce a valid and applicable contractual exclusion clause unless the plaintiff (here the appellant Tercon) can point to some paramount consideration of public policy sufficient to override the public interest in freedom of contact and defeat what would otherwise be the contractual rights of the parties. Tercon points to the public interest in the transparency and integrity of the government tendering process (in this case, for a highway construction contract) but in my view such a concern, while important, did not render unenforceable the terms of the contract Tercon agreed to. There is nothing inherently unreasonable about exclusion clauses. Tercon is a large and sophisticated corporation. Unlike my colleague Justice Cromwell, I would hold that the respondent Ministry's conduct, while in breach of its contractual obligations, fell within the terms of the exclusion clause. In turn, there is no reason why the clause should not be enforced. I would dismiss the appeal.

I. Overview

[83] This appeal concerns a contract to build a $35 million road in the remote Nass Valley of British Columbia (the "Kincolith project"). The respondent Ministry accepted a bid from Brentwood

celle de savoir si le tribunal peut refuser à la partie coupable d'inexécution — et dans l'affirmative, à quelles conditions — le bénéfice d'une clause d'exonération de la responsabilité à laquelle a consenti l'autre partie alors qu'elle n'était frappée d'aucune inaptitude. Les tribunaux appelés à se prononcer en la matière s'en sont traditionnellement remis au principe de l'inexécution fondamentale, un principe auquel le juge en chef Dickson proposait d'asséner le coup de grâce il y a 21 ans dans l'arrêt *Hunter Engineering Co. c. Syncrude Canada Ltée*, [1989] 1 R.C.S. 426, p. 462.

[82] Nous devrions saisir l'occasion qui nous est à nouveau donnée d'éliminer le jargon associé à l'« inexécution fondamentale ». Qualifier l'inexécution contractuelle de « fondamentale », « monumentale » ou « phénoménale » n'est pas spécialement utile. En fait, le tribunal n'a pas le pouvoir discrétionnaire de refuser de faire respecter une clause de non-recours valide et applicable, sauf lorsque le demandeur (en l'espèce, l'appelante Tercon) fait valoir une considération d'ordre public prépondérante qui l'emporte sur l'intérêt public lié à la liberté de contracter et qui fait obstacle à ce qui, autrement, constitueraient les droits contractuels des parties. Tercon invoque l'intérêt public lié à la transparence et à l'intégrité du processus gouvernemental d'appel d'offres (visant en l'occurrence la construction d'une route), mais à mon sens, même s'il s'agit d'une condition importante, son inobservation n'a pas rendu inapplicable les clauses du contrat auxquelles Tercon avait consenti. La clause de non-recours n'a rien d'intrinsèquement déraisonnable. Tercon est une grande entreprise dotée d'une vaste expérience. Contrairement à mon collègue le juge Cromwell, j'estime que même s'il n'a pas respecté ses obligations contractuelles, le ministère intimé bénéficie de la clause de non-recours. Il n'y a donc pas de raison de ne pas faire respecter celle-ci. Je suis d'avis de rejeter le pourvoi.

I. Survol

[83] Le contrat avait pour objet la construction d'une route au coût de 35 millions de dollars dans la vallée isolée de la Nass, en Colombie-Britannique (le « projet Kincolith »). Le ministère intimé a

Enterprises Ltd. that did not comply with the terms of tender. Tercon, as the disappointed finalist in the bidding battle, seeks compensation equivalent to the profit it expected to earn had it been awarded the contract.

[84] Tercon alleged, and the trial judge found, that although the winning bid was submitted in the name of Brentwood (an eligible bidder), Brentwood in fact intended, with the Ministry's knowledge and encouragement, to do the work in a co-venture with an ineligible bidder, Emil Anderson Construction Co. ("EAC"). The respondent Ministry raised a number of defences including the fact that the formal contract was signed in the name of Brentwood alone. This defence was rejected in the courts below. The Ministry's substantial defence in this Court is that even if it failed to abide by the bidding rules, it is nonetheless protected by an exclusion of compensation clause set out clearly in the request for proposals ("RFP"). The clause provided that "no Proponent shall have any claim for compensation of any kind whatsoever, as a result of participating in this RFP" and that "by submitting a Proposal each Proponent shall be deemed to have agreed that it has no claim" (s. 2.10 of the RFP).

[85] The appeal thus brings into conflict the public policy that favours a fair, open and transparent bid process, and the freedom of contract of sophisticated and experienced parties in a commercial environment to craft their own contractual relations. I agree with Tercon that the public interest favours an orderly and fair scheme for tendering in the construction industry, but there is also a public interest in leaving knowledgeable parties free to order their own commercial affairs. In my view, on the facts of this case, the Court should not rewrite — nor should the Court refuse to give effect to — the terms agreed to by the parties.

[86] I accept, as did the courts below, that the respondent Ministry breached the terms of its own RFP when it contracted with Brentwood, knowing the work would be carried out by a co-venture with Brentwood and EAC. The addition of EAC, a

accepté de Brentwood Enterprises Ltd. une soumission qui n'était pas conforme aux conditions de son appel d'offres. Écartée à l'étape ultime du processus, Tercon a réclamé une indemnité équivalant au profit escompté advenant l'obtention du contrat.

[84] Tercon a allégué que même si la soumission retenue avait été présentée au nom de Brentwood, ce soumissionnaire admissible entendait en fait exécuter les travaux en coentreprise avec un soumissionnaire inadmissible, Emil Anderson Construction Co. (« EAC »), au su et avec l'appui du ministère. La juge de première instance lui a donné raison. Le ministère intimé a invoqué divers moyens de défense, dont le fait que Brentwood seule était signataire du contrat intervenu. Ce moyen a été rejeté par les juridictions inférieures. Devant notre Cour, le ministère fait valoir comme moyen de fond qu'en dépit de l'inobservation des règles de l'appel d'offres, il peut se prévaloir de la clause de non-recours en indemnisation que prévoit clairement la demande de propositions (« DP »). Une clause stipule en effet qu'[TRADUCTION] « un proposant ne peut exercer aucun recours en indemnisation pour sa participation à la DP, ce qu'il est réputé accepter lorsqu'il présente une soumission » (clause 2.10 de la DP).

[85] S'opposent donc en l'espèce des considérations d'ordre public privilégiant un appel d'offres équitable, ouvert et transparent et la liberté de personnes compétentes et expérimentées de définir leurs liens contractuels dans un contexte commercial. Je conviens avec Tercon que, dans le secteur de la construction, il est dans l'intérêt public que les appels d'offres se déroulent de manière ordonnée et équitable. Mais il est également dans l'intérêt public que des personnes rompues aux usages d'un domaine conservent la faculté d'organiser leurs propres affaires. Vu les faits de la présente espèce, la Cour ne devrait pas reformuler les conditions arrêtées par les parties ni refuser de leur donner effet.

[86] Je conviens avec les juridictions inférieures que le ministère intimé n'a pas respecté les conditions de sa propre DP en accordant le marché à Brentwood alors qu'il savait que les travaux seraient exécutés en coentreprise avec EAC. L'adjonction

bigger contractor with greater financial resources than Brentwood, created a stronger competitor for Tercon than Brentwood alone. However, I also agree with the B.C. Court of Appeal that the exclusion of compensation clause is clear and unambiguous and that no legal ground or rule of law permits us to override the freedom of the parties to contract (or to decline to contract) with respect to this particular term, or to relieve Tercon against its operation in this case.

II. The Tendering Process

[87] For almost three decades, the law governing a structured bidding process has been dominated by the concept of Contract A/Contract B initially formulated in *The Queen in right of Ontario v. Ron Engineering & Construction (Eastern) Ltd.*, [1981] 1 S.C.R. 111. The analysis advanced by Estey J. in that case was that the bidding process, as defined by the terms of the tender call, may create contractual relations ("Contract A") prior in time and quite independently of the contract that is the actual subject matter of the bid ("Contract B"). Breach of Contract A may, depending on its terms, give rise to contractual remedies for non-performance even if Contract B is never entered into or, as in the present case, it is awarded to a competitor. The result of this legal construct is to provide unsuccessful bidders with a *contractual* remedy against an owner who departs from its own bidding rules. Contract A, however, arises (if at all) as a matter of interpretation. It is not imposed as a rule of law.

[88] In *Ron Engineering*, the result of Estey J.'s analysis was that as a matter of contractual interpretation, the Ontario government was allowed to retain a $150,000 bid bond put up by Ron Engineering even though the government was told, a little over an hour after the bids were opened, that Ron Engineering had made a $750,058 error in the calculation of its bid and wished to withdraw it. Estey J. held:

> The contractor was not asked to sign a contract which diverged in any way from its tender but simply to sign a

de cet autre entrepreneur à la taille et aux moyens financiers plus grands que ceux de Brentwood a opposé à Tercon un concurrent plus puissant que Brentwood seule. Toutefois, je conviens aussi avec la Cour d'appel de la Colombie-Britannique que la clause de non-recours en indemnisation est claire et non équivoque et qu'aucune règle de droit ou autre fondement juridique ne nous permet de passer outre à la liberté des parties de convenir (ou non) de cette condition ni de soustraire Tercon à son application en l'espèce.

II. Le processus d'appel d'offres

[87] Depuis près de trois décennies, le modèle du contrat A et du contrat B appliqué pour la première fois dans l'arrêt *La Reine du chef de l'Ontario c. Ron Engineering & Construction (Eastern) Ltd.*, [1981] 1 R.C.S. 111, prédomine dans le droit applicable en matière d'appel d'offres. Suivant l'analyse du juge Estey dans cet arrêt, le processus défini par les conditions de l'appel d'offres peut faire naître des relations contractuelles (« contrat A ») antérieures au marché projeté (« contrat B ») et tout à fait indépendantes de celui-ci. Le non-respect du contrat A, dépendant de sa teneur, peut donner ouverture à un recours contractuel pour inexécution même si le contrat B ne voit pas le jour et même si, comme en l'espèce, il est octroyé à un concurrent. Cette construction juridique permet au soumissionnaire non retenu d'exercer un recours *contractuel* contre le propriétaire qui ne respecte pas les règles de l'appel d'offres qu'il a lui-même établies. Cependant, l'existence du contrat A relève de l'interprétation, elle n'est pas dictée par une règle de droit.

[88] Dans l'arrêt *Ron Engineering*, le juge Estey conclut que suivant son interprétation du contrat, le gouvernement de l'Ontario pouvait conserver le cautionnement de soumission de 150 000 $ même s'il avait appris un peu plus d'une heure après l'ouverture des soumissions que Ron Engineering avait commis une erreur de 750 058 $ dans le calcul du montant offert et qu'elle souhaitait retirer sa soumission. Le juge Estey dit :

> On n'a pas demandé à l'entrepreneur de signer un contrat qui différait en quoi que ce soit de sa soumission, mais

contract in accordance with the instructions to tenderers and in conformity with its own tender. [p. 127]

In other words, harsh as it may have seemed to Ron Engineering, the parties were held to their bargain. The Court was not prepared to substitute "fair and reasonable" terms for what the parties had actually agreed to.

[89] In *M.J.B. Enterprises Ltd. v. Defence Construction (1951) Ltd.*, [1999] 1 S.C.R. 619, Contract A included a "privilege" clause which stated that the owner was not obliged to accept the lowest or *any* tender. The Court implied a term, based on the presumed intention of the parties, that notwithstanding the privilege clause, only compliant bids were open to acceptance. While the owner was not obliged to accept the lowest compliant bid, the privilege clause did not, as a matter of contractual interpretation, give the owner "the privilege" of accepting a non-compliant bid. *M.J.B.* stops short of the issue in the present appeal because in that case, there was a breach of Contract A but no clause purporting to exclude liability on the part of the owner to pay compensation in the event of a Contract A violation.

[90] In *Naylor Group Inc. v. Ellis-Don Construction Ltd.*, 2001 SCC 58, [2001] 2 S.C.R. 943, the Court enforced the rules of the bid depository system against a contractor whose bid was based on what turned out to be a mistaken view of its collective bargaining status with the International Brotherhood of Electrical Workers. The Court again affirmed that "[t]he existence and content of Contract A will depend on the facts of the particular case" (para. 36). Ellis-Don sought relief from its bid on the basis of a labour board decision rendered subsequent to its bid that upheld, to its surprise, the bargaining rights of the union. This Court held that no relief was contemplated in the circumstances under Contract A and none was afforded, even though this was a costly result when viewed from the perspective of Ellis-Don.

simplement de signer un contrat conforme aux instructions adressées aux soumissionnaires et à sa propre soumission. [p. 127]

Autrement dit, les parties ne pouvaient revenir sur le marché conclu, aussi draconien que cela ait pu paraître à Ron Engineering. La Cour n'était pas disposée à substituer des conditions « justes et raisonnables » à celles dont les parties avaient convenu.

[89] Dans l'arrêt *M.J.B. Enterprises Ltd. c. Construction de Défense (1951) Ltée*, [1999] 1 R.C.S. 619, le contrat A renfermait une clause « de réserve » portant que le propriétaire n'était tenu d'accepter ni la soumission la plus basse ni *aucune* soumission. Invoquant l'intention présumée des parties, la Cour infère du contrat, malgré la clause de réserve, l'obligation tacite du propriétaire de n'accepter qu'une soumission conforme. Le propriétaire n'était pas tenu d'accepter la soumission conforme la plus basse, mais suivant son interprétation, la clause de réserve ne « réservait » pas au propriétaire le droit d'accepter une soumission non conforme. L'arrêt *M.J.B.* ne tranche pas la question soulevée dans le présent pourvoi, car même s'il y avait eu inexécution du contrat A, aucune clause n'avait pour objet d'écarter l'obligation du propriétaire de verser une indemnité en cas de non-respect du contrat A.

[90] Dans l'arrêt *Naylor Group Inc. c. Ellis-Don Construction Ltd.*, 2001 CSC 58, [2001] 2 R.C.S. 943, la Cour donne effet aux règles régissant le système de soumissions au détriment d'un entrepreneur dont la soumission se fondait sur ce qui s'est révélé être une mauvaise interprétation de l'obligation de négocier collectivement avec la Fraternité internationale des ouvriers en électricité. La Cour y confirme que « [l]'existence et le contenu du contrat A dépendent des faits de chaque affaire » (par. 36). Ellis-Don tentait d'échapper à ses obligations contractuelles en invoquant une décision de la Commission des relations de travail — rendue après le dépôt de sa soumission — qui reconnaissait contre toutes attentes les droits de négociation collective du syndicat. La Cour statue que le contrat A ne prévoyait aucune mesure réparatrice en pareil cas et elle n'en accorde aucune, même si le résultat se révèle coûteux pour Ellis-Don.

[91] In *Martel Building Ltd. v. Canada*, 2000 SCC 60, [2000] 2 S.C.R. 860, citing *M.J.B.*, the Court implied a term in Contract A obligating the owner to be fair and consistent in the assessment of tender bids. On the facts, the disappointed bidder's claim of unfair treatment was rejected.

[92] Finally, in *Double N Earthmovers Ltd. v. Edmonton (City)*, 2007 SCC 3, [2007] 1 S.C.R. 116, the unsuccessful bidder claimed that Edmonton had accepted, in breach of Contract A, a competitor's non-compliant bid to provide heavy equipment of a certain age to move refuse at a waste disposal site. The Court refused to imply a term "requiring an owner to investigate to see if bidders will really do what they promised in their tender" (para. 50). Accepting the existence of a duty of "fairness and equality", the majority nevertheless held that "[t]he best way to make sure that all bids receive the same treatment is for an owner to weigh bids on the basis of what is actually in the bid, not to weigh them on the basis of subsequently discovered information" (para. 52). In other words, the majority's interpretation of the express terms of Contract A was enforced despite Double N Earthmovers' complaint of double dealing by the owner.

[93] On the whole, therefore, while *Ron Engineering* and its progeny have encouraged the establishment of a fair and transparent bidding process, Contract A continues to be based not on some abstract externally imposed rule of law but on the presumed (and occasionally implied) intent of the parties. Only in rare circumstances will the Court relieve a party from the bargain it has made.

[94] As to implied terms, *M.J.B.* emphasized (at para. 29) that the focus is "the intentions of the actual parties". A court, when dealing with a claim to an implied term, "must be careful not to slide

[91] Dans l'arrêt *Martel Building Ltd. c. Canada*, 2000 CSC 60, [2000] 2 R.C.S. 860, s'appuyant sur l'arrêt *M.J.B.*, la Cour conclut que le contrat A obligeait tacitement le propriétaire à évaluer les soumissions de façon équitable et uniforme. Mais au vu des faits, elle rejette la prétention du soumissionnaire éconduit selon laquelle il n'avait pas été traité avec équité.

[92] Enfin, dans l'affaire *Double N Earthmovers Ltd. c. Edmonton (Ville)*, 2007 CSC 3, [2007] 1 R.C.S. 116, à l'issue d'un appel d'offres pour la fourniture de machinerie lourde devant servir au déplacement des déchets dans une décharge, un soumissionnaire non retenu prétendait que la ville d'Edmonton avait contrevenu au contrat A en acceptant une soumission non conforme pour ce qui était de l'année de fabrication des machines. La Cour refuse de conclure à l'obligation tacite du propriétaire « de vérifier si les soumissionnaires respecteront vraiment les engagements qu'ils ont pris dans leur soumission » (par. 50). Les juges majoritaires reconnaissent que le propriétaire est tenu de traiter tous les soumissionnaires « équitablement et sur un pied d'égalité », mais ils estiment néanmoins que « [l]e meilleur moyen pour le propriétaire de s'assurer que toutes les soumissions sont traitées de façon équitable est de les évaluer d'après leur contenu réel et non en fonction des renseignements révélés ultérieurement » (par. 52). Ainsi, il est donné effet à leur interprétation des conditions expresses du contrat A malgré l'allégation de duplicité formulée par Double N Earthmovers contre le propriétaire.

[93] Dans l'ensemble, bien que l'arrêt *Ron Engineering* et ceux rendus dans sa foulée préconisent un processus d'appel d'offres équitable et transparent, l'assise du contrat A demeure l'intention présumée (et parfois inférée) des parties, et non quelque règle de droit abstraite imposée par un tiers. Ce n'est qu'en de rares circonstances que le tribunal relèvera une partie de ses engagements.

[94] Dans l'arrêt *M.J.B.*, la Cour souligne que, pour les conditions implicites, l'accent est mis sur « l'intention des parties elles-mêmes » (par. 29). Le tribunal appelé à statuer sur l'existence alléguée

into determining the intentions of reasonable parties" (emphasis in original). Thus, "if there is evidence of a contrary intention, on the part of either party, an implied term may not be found on this basis".

[95] Tercon is a large and experienced contractor. As noted by Donald J.A. in the B.C. Court of Appeal, it had earlier "successfully recovered damages from the [Ministry] on a bidding default in a previous case" (2007 BCCA 592, 73 B.C.L.R. (4th) 201, at para. 15). See *Tercon Contractors Ltd. v. British Columbia* (1993), 9 C.L.R. (2d) 197 (B.C.S.C.), aff'd [1994] B.C.J. No. 2658 (QL) (C.A.). Thus Tercon would have been more sensitive than most contractors to the risks posed by an exclusion of compensation clause. It nevertheless chose to bid on the project on the terms proposed by the Ministry.

III. Tercon's Claim for Relief From the Exclusionary Clause It Agreed to

[96] In these circumstances, the first question is whether there is either a statutory legal obstacle to, or a principled legal argument against, the freedom of these parties to contract out of the obligation that would otherwise exist for the Ministry to pay compensation for a breach of Contract A. If not, the second question is whether there is any other barrier to the court's enforcement of the exclusionary clause in the circumstances that occurred. On the first branch, Tercon relies on the *Ministry of Transportation and Highways Act*, R.S.B.C. 1996, c. 311 ("*Transportation Act*" or the "Act"). On the second branch, Tercon relies on the doctrine of fundamental breach.

A. *The Statutory Argument*

[97] Section 4 of the *Transportation Act* provides that before awarding a highway contract, "the minister must invite tenders in any manner that will make the invitation for tenders reasonably available

d'une condition implicite « doit se garder de chercher à déterminer l'intention de parties raisonnables » (souligné dans l'original). Ainsi, « en présence d'une preuve d'intention contraire de la part de l'une ou l'autre des parties, l'on ne peut conclure à l'existence d'une condition implicite sur ce fondement ».

[95] Tercon est une grande entreprise expérimentée et, comme le fait observer le juge Donald de la Cour d'appel, elle [TRADUCTION] « a déjà obtenu des dommages-intérêts du [ministère] dans une autre affaire d'irrégularité du processus d'appel d'offres » (2007 BCCA 592, 73 B.C.L.R. (4th) 201, par. 15). Voir *Tercon Contractors Ltd. c. British Columbia* (1993), 9 C.L.R. (2d) 197 (C.S.C.-B.), conf. par [1994] B.C.J. No. 2658 (QL) (C.A.). Tercon aurait donc été plus consciente que la plupart des autres entreprises du risque que posait la clause de non-recours en indemnisation. Elle a néanmoins décidé de participer au processus aux conditions proposées par le ministère.

III. Demande de Tercon visant à la soustraire à l'application de la clause de non-recours à laquelle elle a consenti

[96] Dans ces circonstances, il faut premièrement se demander si un élément législatif ou un argument juridique valable s'oppose à la liberté des parties d'exclure dans leur contrat l'obligation qu'aurait le ministère de verser une indemnité en cas d'inexécution du contrat A. S'il n'y en a pas, il convient deuxièmement de déterminer si, au vu des faits de l'espèce, il existe un autre obstacle à l'application de la clause de non-recours. Pour le premier volet, Tercon invoque la *Ministry of Transportation and Highways Act*, R.S.B.C. 1996, ch. 311 (« *Loi sur les transports* » ou « Loi »), pour le second, le principe de l'inexécution fondamentale.

A. *L'argument de nature législative*

[97] L'article 4 de la *Loi sur les transports* dispose qu'avant d'accorder un contrat de voirie, [TRADUCTION] « le ministre lance l'appel d'offres de manière à informer raisonnablement le public de

to the public", but then provides for several exceptions: "The minister need not invite tenders for a project . . . if . . . (c) the minister believes that an alternative contracting process will result in a competitively established cost for the project". Here the required ministerial authorization was obtained for an "alternative process". The reason is as follows. As noted by Cromwell J., the Ministry's original idea was to use a "design-build" model where a single contractor would design and build the highway for a fixed price. The Ministry issued a request for expressions of interest ("RFEI") which attracted six responses. One was from Tercon. Another was from Brentwood. EAC declined to bid because it did not think the "design-build" concept was appropriate for the job.

[98] On further reflection, the Ministry decided not to pursue the design-build approach. It decided to design the highway itself. The contract would be limited to construction, as EAC had earlier advocated. EAC was not allowed to bid despite the Ministry coming around to its point of view on the proper way to tender the project. The Ministry limited bidding on the new contest to the six respondents to the original RFEI, all of whom had been found capable of performing the contract. But to do so, it needed, and did obtain, the Minister's s. 4 approval.

[99] A question arose during the hearing of the appeal as to whether the Minister actually approved an "alternative process" that not only restricted eligibility to the six participants in the RFEI process (an advantage to Tercon and the other five participants), but also contained the "no claims" clause excluding compensation for non-observance of its terms (no doubt considered a disadvantage). In its factum, the Ministry states:

In this case, the Minister approved an alternate process under [s. 4(2) of the B.C. *Transportation Act*]. That process was set out in the Instructions to Proponents, which included the No Claim Clause. Having been approved by the Minister, the package (including the No Claim

sa tenue », sauf dans certains cas, notamment lorsque [TRADUCTION] « c) le ministre estime qu'un autre processus d'adjudication de marché permettra la réalisation des travaux à un coût concurrentiel ». En l'espèce, le ministre a approuvé un « autre processus ». La raison en est — comme le signale le juge Cromwell — que le ministère prévoyait initialement qu'un seul entrepreneur se chargerait de la conception et de la construction de la route moyennant un prix fixe. Il a lancé une demande d'expression d'intérêt (« DEI ») et reçu six réponses, dont celles de Tercon et de Brentwood. Estimant que les travaux ne se prêtaient pas au modèle « conception-construction », EAC n'a pas manifesté son intérêt.

[98] Après réflexion, le ministère a renoncé à ce modèle. Il a décidé de concevoir lui-même la route et de ne passer un marché que pour sa construction, comme l'avait préconisé EAC. Cette dernière ne pouvait cependant pas soumissionner même si le ministère s'était rangé à son avis sur les modalités qu'il convenait d'établir pour l'appel d'offres. Le ministère a réservé la participation au nouveau processus aux six entrepreneurs ayant initialement répondu à la DEI, qu'il avait tous jugés aptes à exécuter les travaux. Il devait toutefois obtenir du ministre l'approbation visée à l'art. 4, et il l'a obtenue.

[99] Lors de l'audition du pourvoi, la question s'est posée de savoir si le ministre avait effectivement approuvé un « autre processus » qui non seulement tenait pour admissibles les six participants à la DEI (conférant ainsi un avantage à Tercon et aux cinq autres entreprises), mais renfermait également une clause « écartant tout recours » en indemnisation d'un préjudice découlant du non-respect de ses conditions (assurément perçue comme un élément défavorable). Dans son mémoire, le ministère soutient ce qui suit :

[TRADUCTION] Dans la présente affaire, le ministre a approuvé un autre processus [en application du par. 4(2) de la *Transportation Act* de la Colombie-Britannique]. Ce processus était énoncé dans les instructions aux proposants, qui comprenaient la clause « écartant tout

Clause) complied with section 4 of the *Transportation Act*. [para. 70]

[100] Tercon argued at the hearing of this appeal that as a matter of *law*, Contract A could not have included the exclusion clause because

> [t]he policy of the [*Transportation Act*] is to ensure that the Ministry is accountable; to preserve confidence in the integrity of the tendering process. To ensure that is so and that the Minister is accountable, the Ministry must be held liable for its breach of Contract A in considering and accepting a proposal from the joint venture . . . .
>
> . . .
>
> **MADAM JUSTICE ABELLA:** Can I just ask you one question. Is it your position, sir, that you can never have -- that a government can never have a no claims clause?
>
> **MR. McLEAN:** Yes. Under this statute because of the policy of the statute. [Transcript, at p. 27]

[101] While it is true that the Act favours "the integrity of the tendering process", it nowhere prohibits the parties from negotiating a "no claims" clause as part of their commercial agreement, and cannot plausibly be interpreted to have that effect.

[102] In the ordinary world of commerce, as Dickson C.J. commented in *Hunter*, "clauses limiting or excluding liability are negotiated as part of the general contract. As they do with all other contractual terms, the parties bargain for the consequences of deficient performance" (p. 461). Moreover, as Mr. Hall points out, "[t]here are many valid reasons for contracting parties to use exemption clauses, most notably to allocate risks" (G. R. Hall, *Canadian Contractual Interpretation Law* (2007), at p. 243). Tercon, for example, is a sophisticated and experienced contractor and if it decided that it was in its commercial interest to proceed with the bid despite the exclusion of compensation clause, that was its prerogative and nothing in the "policy of the Act" barred the parties' agreement on that point.

recours ». Avalisé par le ministre, l'ensemble des conditions (dont la clause « écartant tout recours ») était conforme à l'article 4 de la *Transportation Act*. [par. 70]

[100] Tercon a soutenu à l'audience que le contrat A ne pouvait *légalement* comprendre la clause de non-recours, car

> [TRADUCTION] [l]a raison d'être de la [*Transportation Act*] est de rendre le ministre responsable de ses actes, de protéger la foi dans l'intégrité du processus d'appel d'offres. C'est pourquoi le ministre doit engager sa responsabilité en cas d'inexécution du contrat A lorsqu'il considère puis accepte la proposition d'une coentreprise . . .
>
> . . .
>
> **MADAME LA JUGE ABELLA :** Puis-je seulement vous poser une question? Allez-vous jusqu'à prétendre, Maître, qu'il ne peut jamais y avoir de clause « écartant tout recours », qu'un gouvernement ne peut jamais stipuler une telle clause?
>
> **MAÎTRE McLEAN :** Oui. Sous le régime de cette loi, à cause de sa raison d'être. [Transcription, p. 27]

[101] Certes la Loi favorise « l'intégrité du processus d'appel d'offres », mais aucune de ses dispositions n'empêche les parties de faire figurer dans leur accord commercial une clause écartant toute indemnisation ni ne peut vraisemblablement être interprétée comme ayant cet effet.

[102] Dans l'arrêt *Hunter*, le juge en chef Dickson fait observer que dans le contexte ordinaire du commerce, « les clauses de limitation ou d'exclusion de responsabilité sont négociées dans le cadre de l'ensemble du contrat. Comme elles le font pour les autres conditions du contrat, les parties négocient les conséquences de l'exécution insuffisante » (p. 461). De plus, Hall fait remarquer que [TRADUCTION] « [b]on nombre de raisons valables justifient les parties contractantes de recourir à une clause exonératrice, le plus souvent pour répartir le risque » (G. R. Hall, *Canadian Contractual Interpretation Law* (2007), p. 243). Tercon est une entreprise avertie et expérimentée, et si elle a jugé commercialement opportun de présenter une soumission malgré la clause de non-recours en indemnisation, c'était sa décision. La « raison d'être de la Loi » ne faisait aucunement obstacle à la convention des parties sur ce point.

[103] To the extent Tercon is now saying that as a matter of *fact* the Minister, in approving the RFP, did not specifically approve the exclusion clause, and that the contract was thus somehow *ultra vires* the Ministry, this is not an issue that was either pleaded or dealt with in the courts below. The details of the ministerial approval process were not developed in the evidence. It is not at all evident that s. 4 *required* the Minister to approve the actual terms of the RFP. It is an administrative law point that Tercon, if so advised, ought to have pursued at pre-trial discovery and in the trial evidence. We have not been directed to any exploration of the matter in the testimony and it is too late in the proceeding for Tercon to explore it now. Accordingly, I proceed on the basis that the exclusion clause did not run afoul of the statutory requirements.

B. *The Doctrine of the Fundamental Breach*

[104] The trial judge considered the applicability of the doctrine of fundamental breach. Tercon argued that the Ministry, by reason of its fundamental breach, had forfeited the protection of the exclusion of compensation clause.

[105] The leading case is *Hunter* which also dealt with an exclusion of liability clause. The appellants Hunter Engineering and Allis-Chalmers Canada Ltd. supplied gearboxes used to drive conveyor belts at Syncrude's tar sands operations in Northern Alberta. The gearboxes proved to be defective. At issue was a broad exclusion of warranty clause that limited time for suit and the level of recovery available against Allis-Chalmers (i.e. no recovery beyond the unit price of the defective products). Dickson C.J. observed: "In the face of the contractual provisions, Allis-Chalmers can only be found liable under the doctrine of fundamental breach" (p. 451).

[106] This doctrine was largely the creation of Lord Denning in the 1950s (see, e.g., *Karsales*

[103] Tercon prétend aujourd'hui devant nous que, dans les *faits*, lorsqu'il a approuvé la DP, le ministre n'a pas approuvé la clause de non-recours comme telle, si bien que le contrat était en quelque sorte *ultra vires* du pouvoir du ministère. Or, cette thèse n'a été ni formulée devant les tribunaux inférieurs ni examinée par eux. Le détail du processus d'approbation ministérielle n'a pas été mis en preuve. Il n'est pas du tout évident que l'art. 4 *exigeait* du ministre qu'il approuve les conditions précises de la DP. Il s'agit d'un point de droit administratif que Tercon aurait dû soulever, si elle le souhaitait, à l'interrogatoire préalable ou lors de la présentation de la preuve au procès. La preuve ne nous a pas incités à explorer la question, et il est désormais trop tard pour que Tercon s'engage dans cette voie. Je poursuis donc l'analyse en tenant pour acquis que la clause de non-recours ne dérogeait pas aux exigences légales.

B. *La notion d'inexécution fondamentale*

[104] La juge de première instance s'est penchée sur l'applicabilité de cette notion. Tercon soutenait qu'en raison de l'inexécution fondamentale dont il s'était rendu coupable, le ministère n'avait plus droit à la protection découlant de la clause de non-recours en indemnisation.

[105] *Hunter* est l'arrêt de principe en la matière. Une clause d'exonération de la responsabilité y était également en cause. Les appelantes Hunter Engineering et Allis-Chalmers Canada Ltd. fournissaient des boîtes d'engrenage pour les convoyeurs à courroie utilisés par Syncrude pour l'exploitation de sables bitumineux dans le nord de l'Alberta. Le matériel s'est révélé défectueux. L'objet du litige était une clause générale d'exclusion de la garantie limitant le délai de poursuite et plafonnant au prix unitaire du produit défectueux le montant de l'indemnité qu'Allis-Chalmers pouvait être tenue de verser. Le juge en chef Dickson conclut que « [c]ompte tenu des dispositions du contrat, Allis-Chalmers ne peut être tenue responsable qu'aux termes du principe de l'inexécution fondamentale » (p. 451).

[106] Ce principe de droit datant des années 1950 était en grande partie attribuable à lord Denning

(Harrow) Ltd. v. Wallis, [1956] 1 W.L.R. 936 (C.A.)). It was said to be a rule of law that operated independently of the intention of the parties in circumstances where the defendant had so egregiously breached the contract as to deny the plaintiff substantially the whole of its benefit. In such a case, according to the doctrine, the innocent party was excused from further performance but the defendant could still be held liable for the consequences of its "fundamental" breach even if the parties had excluded liability by clear and express language. See generally S. M. Waddams, *The Law of Contracts* (5th ed. 2005), at para. 478; J. D. McCamus, *The Law of Contracts* (2005), at pp. 765 *et seq.*

[107] The five-judge *Hunter* Court was unanimous in the result and gave effect to the exclusion clause at issue. Dickson C.J. and Wilson J. both emphasized that there is nothing inherently unreasonable about exclusion clauses and that they should be applied unless there is a compelling reason not to give effect to the words selected by the parties. At that point, there was some divergence of opinion.

[108] Dickson C.J. (La Forest J. concurring) observed that the doctrine of fundamental breach had "spawned a host of difficulties" (p. 460), the most obvious being the difficulty in determining whether a particular breach is fundamental. The doctrine obliged the parties to engage in "games of characterization" (p. 460) which distracted from the real question of what agreement the parties themselves intended. Accordingly, in his view, the doctrine should be "laid to rest". The situations in which the doctrine is invoked could be addressed more directly and effectively through the doctrine of "unconscionability", as assessed at the time the contract was made:

> It is preferable to interpret the terms of the contract, in an attempt to determine exactly what the parties agreed. If on its true construction the contract excludes liability for the kind of breach that occurred, the party in breach will generally be saved from liability. Only where the contract is unconscionable, as might arise from situations of unequal bargaining power between the parties,

(voir, p. ex., *Karsales (Harrow) Ltd. c. Wallis*, [1956] 1 W.L.R. 936 (C.A.)). Il devait s'appliquer indépendamment de l'intention des parties lorsque le défendeur avait à ce point manqué à ses obligations contractuelles qu'il avait privé le demandeur de la quasi-totalité du bénéfice censé découler du contrat. Ainsi, le cocontractant innocent était dès lors relevé de ses obligations, et le défendeur pouvait en outre être tenu responsable des conséquences de son inexécution « fondamentale » même si les parties avaient clairement et expressément écarté toute responsabilité. Voir de façon générale S. M. Waddams, *The Law of Contracts* (5e éd. 2005), par. 478; J. D. McCamus, *The Law of Contracts* (2005), p. 765 et suiv.

[107] Dans l'arrêt *Hunter*, les cinq juges de la Cour s'entendent sur l'issue du pourvoi et donnent effet à la clause d'exclusion. Le juge en chef Dickson et la juge Wilson font tous deux ressortir qu'une telle clause n'est pas intrinsèquement déraisonnable et qu'il faut la faire respecter sauf motif impérieux de ne pas donner effet au libellé employé par les parties. Certaines divergences d'opinions apparaissent ensuite.

[108] Le juge en chef Dickson (avec l'accord du juge La Forest) fait remarquer que le principe de l'inexécution fondamentale a « engendré un grand nombre de difficultés » (p. 460), la plus évidente tenant à la détermination du caractère fondamental de l'inexécution. Les parties devaient en effet se livrer à des « jeux de caractérisation » (p. 460) qui détournaient leur attention de la question véritable, celle de savoir ce dont elles avaient elles-mêmes voulu convenir. Il est donc d'avis de « donner le coup de grâce » au principe, les situations où il est invoqué pouvant être réglées plus directement et plus efficacement sous l'angle de l'« iniquité » considérée au moment de la formation du contrat :

> Il est préférable d'interpréter les conditions du contrat dans le but de déterminer exactement ce que les parties ont convenu. Si d'après son interprétation juste, le contrat écarte la responsabilité pour le genre d'inexécution qui s'est produit, la partie fautive sera généralement soustraite à la responsabilité. Ce n'est que lorsque le contrat est inique, comme cela pourrait se produire

should the courts interfere with agreements the parties have freely concluded. [p. 462]

Dickson C.J. explained that "[t]he courts do not blindly enforce harsh or unconscionable bargains" (p. 462), but "there is much to be gained by addressing directly the protection of the weak from overreaching by the strong, rather than relying on the artificial legal doctrine of 'fundamental breach'" (p. 462). To enforce an exclusion clause in such circumstances could tarnish the institutional integrity of the court. In that respect, it would be contrary to public policy. However, a *valid* exclusion clause would be enforced according to its terms.

[109] Wilson J. (L'Heureux-Dubé J. concurring) disagreed. In her view, the courts retain some residual discretion to refuse to enforce exclusion clauses in cases of fundamental breach where the doctrine of *pre*-breach unconscionability (favoured by Dickson C.J.) did not apply. Importantly, she rejected the imposition of a general standard of reasonableness in the judicial scrutiny of exclusion clauses, affirming that "the courts . . . are quite unsuited to assess the fairness or reasonableness of contractual provisions as the parties negotiated them" (p. 508). Wilson J. considered it more desirable to develop through the common law a *post*-breach analysis seeking a "balance between the obvious desirability of allowing the parties to make their own bargains . . . and the obvious undesirability of having the courts used to enforce bargains in favour of parties who are totally repudiating such bargains themselves" (p. 510).

[110] Wilson J. contemplated a two-stage test, in which the threshold step is the identification of a fundamental breach where "the foundation of the contract has been undermined, where the very thing bargained for has not been provided" (p. 500). Having found a fundamental breach to exist, the exclusion clause would *not* automatically be set

dans le cas où il y a inégalité de pouvoir de négociation entre les parties, que les tribunaux devraient modifier les conventions que les parties ont formées librement. [p. 462]

Le juge en chef Dickson explique que « [l]es tribunaux n'appliquent pas aveuglément les conventions draconiennes ou iniques » (p. 462), mais qu'« il y a beaucoup à gagner à aborder directement la question de la protection des plus faibles contre l'exploitation des plus forts, plutôt que de s'en remettre au principe juridique artificiel de l'"inexécution fondamentale" » (p. 462). Faire respecter une clause de non-recours en pareil cas pourrait porter atteinte à l'intégrité de l'appareil judiciaire. Sous ce rapport, ce serait contraire à l'ordre public. Toutefois, une clause de non-recours *valide* sera appliquée conformément à son libellé.

[109] La juge Wilson (avec l'appui de la juge L'Heureux-Dubé) exprime son désaccord, opinant que les tribunaux doivent continuer d'exercer un certain pouvoir discrétionnaire et refuser d'appliquer une clause d'exclusion en cas d'inexécution fondamentale lorsque le principe de l'iniquité *préalable* à l'inexécution (privilégié par le juge en chef Dickson) ne s'applique pas. Elle s'oppose surtout à ce que l'examen judiciaire d'une clause d'exonération se fasse au regard d'une norme générale de raisonnabilité : « . . . les tribunaux [. . .] sont fort mal placés pour déterminer le caractère juste ou raisonnable de dispositions contractuelles négociées par les parties » (p. 508). Elle préconise plutôt une démarche *a posteriori* fondée sur la common law visant à établir « un équilibre entre ce qui est manifestement souhaitable, c'est-à-dire permettre aux parties de conclure leurs propres contrats [. . .] et ce qui est manifestement peu souhaitable, c'est-à-dire recourir aux tribunaux pour faire respecter des contrats en faveur de parties qui elles-mêmes refusent catégoriquement de les exécuter » (p. 510).

[110] La juge Wilson propose un double critère dont le premier volet consiste à déterminer l'existence d'une inexécution fondamentale, à savoir une situation « où le fondement même du contrat a été miné, c'est-à-dire lorsque l'objet même du contrat n'a pas été réalisé » (p. 500). Le tribunal qui conclut à l'existence d'une inexécution fondamentale

aside, but the court should go on to assess whether, having regard to the circumstances of the breach, the party in fundamental breach should escape liability:

> Exclusion clauses do not automatically lose their validity in the event of a fundamental breach by virtue of some hard and fast rule of law. They should be given their natural and true construction so that the meaning and effect of the exclusion clause the parties agreed to at the time the contract was entered into is fully understood and appreciated. But, in my view, the court must still decide, having ascertained the parties' intention at the time the contract was made, whether or not to give effect to it in the context of subsequent events such as a fundamental breach committed by the party seeking its enforcement through the courts. . . . [T]he question essentially is: in the circumstances that have happened should the court lend its aid to A to hold B to this clause? [Emphasis added; pp. 510-11.]

[111] Wilson J. reiterated that "as a general rule" courts should give effect to exclusion clauses *even in the case of fundamental breach* (p. 515). Nevertheless, a residual discretion to withhold enforcement exists:

> Lord Wilberforce [in *Photo Production Ltd. v. Securicor Transport Ltd.*, [1980] A.C. 827 (H.L.)] may be right that parties of equal bargaining power should be left to live with their bargains regardless of subsequent events. I believe, however, that there is some virtue in a residual power residing in the court to withhold its assistance on policy grounds in appropriate circumstances. [Emphasis added; p. 517.]

Wilson J. made it clear that such circumstances of disentitlement would be rare. She acknowledged that an exclusion clause might well be accepted with open eyes by a party "very anxious to get" the contract (p. 509). However, Wilson J. did not elaborate further on what such circumstances might be because she found in *Hunter* itself that no reason existed to refuse the defendant Allis-Chalmers the benefit of the exclusion clause.

[112] The fifth judge, McIntyre J., in a crisp two-paragraph judgment, agreed with the conclusion of

*n'*écarte *pas* automatiquement la clause d'exclusion, mais il poursuit son examen pour déterminer si l'auteur de l'inexécution fondamentale devrait, compte tenu des circonstances de celle-ci, échapper à sa responsabilité :

> Il n'y a aucune règle de droit absolue qui dit que les clauses d'exclusion sont automatiquement frappées d'invalidité en cas d'inexécution fondamentale. Il faut leur donner une interprétation naturelle et juste afin de pouvoir saisir et apprécier parfaitement le sens et l'effet de la clause d'exclusion sur laquelle les parties se sont accordées au moment de la passation du contrat. J'estime toutefois qu'après avoir déterminé l'intention qu'avaient les parties au moment où elles ont conclu le contrat, la cour doit encore décider si elle appliquera ce contrat dans le contexte d'événements subséquents tels qu'une inexécution fondamentale de la part de la partie qui s'adresse aux tribunaux pour le faire respecter. [. . .] [L]a question qui se pose est essentiellement celle de savoir si, suite aux faits survenus, la cour devrait prêter son concours à A pour obliger B à respecter cette clause. [Je souligne; p. 510-511.]

[111] La juge Wilson rappelle qu'« en règle générale », les tribunaux doivent faire respecter la clause d'exclusion *même en cas d'inexécution fondamentale* (p. 515), sous réserve de leur pouvoir résiduel d'écarter son application :

> Il se peut que [dans *Photo Production Ltd. c. Securicor Transport Ltd.*, [1980] A.C. 827 (H.L.)] lord Wilberforce ait raison d'affirmer qu'on devrait laisser des parties ayant négocié à armes égales vivre avec leurs contrats, quels que soient les événements subséquents. Je crois cependant qu'il y a un certain intérêt à ce que les tribunaux soient revêtus d'un pouvoir résiduel de refuser pour des motifs de principe de prêter leur concours à une partie, lorsque cela est indiqué. [Je souligne; p. 517.]

La juge Wilson précise qu'il sera rarement indiqué d'écarter une clause d'exclusion. Elle ajoute qu'une telle clause peut très bien avoir été acceptée en pleine connaissance de cause par une partie qui « tenait beaucoup à [. . .] avoir » le contrat (p. 509). Elle ne précise toutefois pas les circonstances dans lesquelles il conviendrait de l'écarter, car dans *Hunter*, elle ne voit pas de raisons d'empêcher la défenderesse Allis-Chalmers de bénéficier de son application.

[112] Dans un jugement incisif de deux paragraphes, le juge McIntyre, le cinquième à se prononcer,

Wilson J. in respect of the exclusion clause issue but found it "unnecessary to deal further with the concept of fundamental breach in this case" (p. 481).

[113] The law was left in this seemingly bifurcated state until *Guarantee Co. of North America v. Gordon Capital Corp.*, [1999] 3 S.C.R. 423. In that case, the Court breathed some life into the dying doctrine of fundamental breach while nevertheless affirming (once again) that whether or not a "fundamental breach prevents the breaching party from continuing to rely on an exclusion clause is a matter of construction rather than a rule of law" (para. 52). In other words, the question was whether the parties *intended* at the time of contract formation that the exclusion or limitation clause would apply "in circumstances of contractual breach, whether fundamental or otherwise" (para. 63). The Court thus emphasized that what was important was not the label ("fundamental or otherwise") but the intent of the contracting parties when they made their bargain. "The only limitation placed upon enforcing the contract as written in the event of a fundamental breach", the Court in *Guarantee Co.* continued,

> would be to refuse to enforce an exclusion of liability in circumstances where to do so would be unconscionable, according to Dickson C.J., or [note the disjunctive "or"] unfair, unreasonable or otherwise contrary to public policy, according to Wilson J. [Emphasis added; para. 52.]

(See also para. 64.)

What has given rise to some concern is not the reference to "public policy", whose role in the enforcement of contracts has never been doubted, but to the more general ideas of "unfair" and "unreasonable", which seemingly confer on courts a very broad after-the-fact discretion.

[114] The Court's subsequent observations in *ABB Inc. v. Domtar Inc.*, 2007 SCC 50, [2007] 3 S.C.R. 461, should be seen in that light. *Domtar* was a products liability case arising under the civil

souscrit à la conclusion de la juge Wilson en ce qui concerne la clause d'exclusion, mais il trouve « inutile de s'arrêter davantage à la notion d'inexécution fondamentale en l'espèce » (p. 481).

[113] Cette orientation apparemment bicéphale du droit a valu jusqu'à ce que, dans l'arrêt *Guarantee Co. of North America c. Gordon Capital Corp.*, [1999] 3 R.C.S. 423, la Cour ravive la notion moribonde d'inexécution fondamentale tout en (ré)affirmant que « la question de savoir si l'inexécution fondamentale empêche la partie qui en est l'auteur de continuer d'invoquer une clause d'exclusion est une question d'interprétation plutôt que de règle de droit » (par. 52). En d'autres termes, la question est celle de savoir si les parties ont *voulu*, lors de la formation du contrat, que la clause d'exclusion (prévoyant le délai de prescription) s'applique « à la suite d'une inexécution de contrat, qu'elle soit fondamentale ou autre » (par. 63). La Cour souligne donc que ce n'est pas la qualification qui compte (« fondamentale ou autre »), mais bien l'intention des parties au moment de contracter. Elle ajoute :

> En cas d'inexécution fondamentale, la seule restriction à l'exécution du contrat tel que rédigé consisterait à refuser d'appliquer une exonération de responsabilité dans le cas où il serait inique de le faire, selon le juge en chef Dickson, ou [notez l'emploi du *ou* disjonctif] injuste, déraisonnable ou par ailleurs contraire à l'ordre public, selon l[a] juge Wilson. [Je souligne; par. 52.]

(Voir aussi le par. 64.)

La difficulté n'a pas résulté du renvoi à l'« ordre public », une notion dont la pertinence en matière d'exécution des contrats n'a jamais été mise en doute, mais bien des considérations plus générales évoquées par les mots « injuste » et « déraisonnable », qui paraissent ouvrir la voie à l'exercice a posteriori d'un très grand pouvoir judiciaire discrétionnaire.

[114] Les observations subséquentes de la Cour dans l'arrêt *ABB Inc. c. Domtar Inc.*, 2007 CSC 50, [2007] 3 R.C.S. 461, doivent être considérées dans ce contexte. L'arrêt porte sur la responsabilité du

law of Quebec, but the Court observed with respect to the common law:

> Once the existence of a fundamental breach has been established, the court must still analyse the limitation of liability clause in light of the general rules of contract interpretation. If the words can reasonably be interpreted in only one way, it will not be open to the court, even on grounds of equity or reasonableness, to declare the clause to be unenforceable since this would amount to rewriting the contract negotiated by the parties. [Emphasis added; para. 84.]

While the *Domtar* Court continued to refer to "fundamental breach", it notably repudiated any judicial discretion to depart from the terms of a valid contact upon vague notions of "equity or reasonableness". It did not, however, express any doubt about the residual category mentioned in *Guarantee Co.*, namely a refusal to enforce an exclusion clause on the grounds of public policy.

[115] I agree with Professor Waddams when he writes:

> [I]t is surely inevitable that a court must reserve the ultimate power to decide when the values favouring enforceability are outweighed by values that society holds to be more important. [para. 557]

[116] While memorably described as an unruly horse, public policy is nevertheless fundamental to contract law, both to contractual formation and enforcement and (occasionally) to the court's relief *against* enforcement. As Duff C.J. observed:

> It is the duty of the courts to give effect to contracts and testamentary dispositions according to the settled rules and principles of law, since we are under a reign of law; but there are cases in which rules of law cannot have their normal operation because the law itself recognizes some paramount consideration of public policy which over-rides the interest and what otherwise would be the rights and powers of the individual.
>
> (*Re Millar Estate*, [1938] S.C.R. 1, at p. 4)

See generally B. Kain and D. T. Yoshida, "The Doctrine of Public Policy in Canadian Contract

fabricant en droit civil québécois, mais la Cour y signale ce qui suit au sujet de la common law :

> Une fois l'inexécution fondamentale constatée, le tribunal doit encore analyser la clause limitative selon les règles générales d'interprétation des contrats. Dans la mesure où les termes sont raisonnablement susceptibles d'une seule interprétation, le tribunal ne pourra déclarer la clause limitative de responsabilité inapplicable, même pour des motifs d'équité ou de raisonnabilité, puisque cela reviendrait à réécrire le contrat négocié entre les parties. [Je souligne; par. 84.]

Même si elle renvoie encore à la notion d'« inexécution fondamentale », la Cour exclut nettement tout pouvoir discrétionnaire de passer outre aux conditions d'un contrat valide pour de vagues considérations « d'équité ou de raisonnabilité ». Elle ne remet cependant pas en cause le pouvoir résiduel — mentionné dans l'arrêt *Guarantee Co.* — de refuser de donner effet à une clause de non-recours pour des motifs liés à l'ordre public.

[115] Je conviens avec le professeur Waddams de ce qui suit :

> [TRADUCTION] [I]l est certes incontournable que les tribunaux se réservent le pouvoir suprême de déterminer si des valeurs privilégiées par la société l'emportent sur celles favorables à l'applicabilité. [par. 557]

[116] L'ordre public, qu'on a pourtant mémorablement comparé à un « cheval rétif », joue un rôle fondamental en droit contractuel pour ce qui est de la formation et de l'exécution du contrat, mais aussi (parfois) lorsqu'un tribunal est appelé à déclarer un contrat *non* applicable. Comme l'a signalé le juge en chef Duff :

> [TRADUCTION] Dans un système soumis à la règle de droit, il incombe aux tribunaux de donner effet aux stipulations contractuelles et testamentaires suivant les règles et les principes de droit établis. Or, il arrive parfois que l'on ne puisse appliquer ceux-ci normalement parce que le droit lui-même reconnaît une considération d'ordre public prépondérante qui prime les intérêts de l'intéressé et ce qui, autrement, constituerait ses droits.
>
> (*Re Millar Estate*, [1938] R.C.S. 1, p. 4)

Se reporter généralement à B. Kain et D. T. Yoshida, « The Doctrine of Public Policy in Canadian

Law", in T. L. Archibald and R. S. Echlin, eds., *Annual Review of Civil Litigation, 2007* (2007), 1.

[117] As Duff C.J. recognized, freedom of contract will often, but not always, trump other societal values. The residual power of a court to decline enforcement exists but, in the interest of certainty and stability of contractual relations, it will rarely be exercised. Duff C.J. adopted the view that public policy "should be invoked only in clear cases, in which the harm to the public is substantially incontestable, and does not depend upon the idiosyncratic inferences of a few judicial minds" (p. 7). While he was referring to public policy considerations pertaining to the nature of the *entire contract*, I accept that there may be well-accepted public policy considerations that relate directly to the nature of the *breach*, and thus trigger the court's narrow jurisdiction to give relief against an exclusion clause.

[118] There are cases where the exercise of what Professor Waddams calls the "ultimate power" to refuse to enforce a contract may be justified, even in the commercial context. Freedom of contract, like any freedom, may be abused. Take the case of the milk supplier who adulterates its baby formula with a toxic compound to increase its profitability at the cost of sick or dead babies. In China, such people were shot. In Canada, should the courts give effect to a contractual clause excluding civil liability in such a situation? I do not think so. Then there are the people, also fortunately resident elsewhere, who recklessly sold toxic cooking oil to unsuspecting consumers, creating a public health crisis of enormous magnitude. Should the courts enforce an exclusion clause to eliminate contractual liability for the resulting losses in such circumstances? The answer is no, but the contract breaker's conduct need not rise to the level of criminality or fraud to justify a finding of abuse.

Contract Law », dans T. L. Archibald et R. S. Echlin, dir., *Annual Review of Civil Litigation, 2007* (2007), 1.

[117] Le juge en chef Duff reconnaît donc que la liberté contractuelle prime souvent les autres valeurs sociétales, mais pas toujours. Le pouvoir résiduel du tribunal d'écarter l'application existe bien, mais la certitude et la stabilité des rapports contractuels commandent de l'exercer rarement. Le juge en chef Duff adopte le point de vue selon lequel l'ordre public [TRADUCTION] « ne doit être invoqué que lorsqu'il est manifeste que le préjudice infligé au public est foncièrement incontestable et ne tient pas seulement aux conclusions bien personnelles de quelques magistrats » (p. 7). Même s'il renvoie à des considérations d'ordre public liées à la nature du *contrat en entier*, je reconnais qu'il peut y avoir des considérations d'ordre public bien établies se rapportant directement à la nature de l'*inexécution* et conférant alors au tribunal le pouvoir limité d'écarter la clause de non-recours.

[118] Il arrive que l'exercice de ce que le professeur Waddams appelle le [TRADUCTION] « pouvoir suprême » de refuser de faire respecter un contrat puisse se justifier, même en contexte commercial. On peut abuser de la liberté contractuelle comme de toute autre liberté. Considérons le cas de fournisseurs de lait qui, pour accroître leur profit, altèrent une formule pour nourrissons en y ajoutant une substance toxique, causant ainsi maladies et décès. En Chine, de tels fournisseurs sont fusillés. Au Canada, les tribunaux devraient-ils en pareil cas faire respecter une clause contractuelle écartant la responsabilité civile? Je ne crois pas. Considérons également le cas de ces gens sans scrupules — résidant heureusement dans un autre pays — qui ont vendu de l'huile de cuisson toxique à des consommateurs qui ne se doutaient de rien, créant ainsi une crise sanitaire publique d'une ampleur considérable. Dans de telles circonstances, nos tribunaux devraient-ils faire respecter une clause de non-recours de façon à écarter la responsabilité contractuelle pour le préjudice ainsi causé? Je ne le crois pas non plus. Cependant, point n'est besoin que l'inexécution contractuelle équivaille à un acte criminel ou à une fraude pour qu'il y ait véritablement abus.

[119] A less extreme example in the commercial context is *Plas-Tex Canada Ltd. v. Dow Chemical of Canada Ltd.*, 2004 ABCA 309, 245 D.L.R. (4th) 650. The Alberta Court of Appeal refused to enforce an exclusion clause where the defendant Dow knowingly supplied defective plastic resin to a customer who used it to fabricate natural gas pipelines. Instead of disclosing its prior knowledge of the defect to the buyer, Dow chose to try to protect itself by relying upon limitation of liability clauses in its sales contracts. After some years, the pipelines began to degrade, with considerable damage to property and risk to human health from leaks and explosions. The court concluded that "a party to a contract will not be permitted to engage in unconscionable conduct secure in the knowledge that no liability can be imposed upon it because of an exclusionary clause" (para. 53). (See also McCamus, at p. 774, and Hall, at p. 243.) What was demonstrated in *Plas-Tex* was that the defendant Dow was so contemptuous of its contractual obligation and reckless as to the consequences of the breach as to forfeit the assistance of the court. The public policy that favours freedom of contract was outweighed by the public policy that seeks to curb its abuse.

[119] L'affaire *Plas-Tex Canada Ltd. c. Dow Chemical of Canada Ltd.*, 2004 ABCA 309, 245 D.L.R. (4th) 650, constitue un cas d'inexécution contractuelle moins extrême. La Cour d'appel de l'Alberta a refusé d'appliquer une clause de responsabilité limitée au bénéfice de la défenderesse, Dow, qui avait sciemment fourni de la résine plastique défectueuse à un client qui s'en était servi pour la fabrication de conduites de gazoducs. Au lieu de signaler à l'acheteur la défectuosité dont elle connaissait l'existence, Dow avait tenté de se protéger en limitant sa responsabilité dans les contrats de vente. Après quelques années, les gazoducs ont commencé à se fissurer, causant d'importants dommages matériels et compromettant la santé de la population ainsi exposée à un risque grave de fuites et d'explosions. La Cour d'appel a conclu qu'un [TRADUCTION] « contractant ne saurait agir de façon inique avec la certitude qu'il pourra échapper à toute responsabilité grâce à une clause d'exonération » (par. 53). (Voir également McCamus, p. 774, et Hall, p. 243.) Ainsi, dans cette affaire, la défenderesse Dow a manifesté un tel mépris pour ses obligations contractuelles et fait preuve d'une telle insouciance pour les conséquences du non-respect de celles-ci qu'il était exclu que les tribunaux lui prêtent leur concours. Les considérations d'ordre public visant à réprimer l'abus de la liberté contractuelle l'emportaient sur celles qui privilégient celle-ci.

[120] Conduct approaching serious criminality or egregious fraud are but examples of well-accepted and "substantially incontestable" considerations of public policy that may override the countervailing public policy that favours freedom of contract. Where this type of misconduct is reflected in the breach of contract, all of the circumstances should be examined very carefully by the court. Such misconduct may disable the defendant from hiding behind the exclusion clause. But a plaintiff who seeks to avoid the effect of an exclusion clause must identify the overriding public policy that it says outweighs the public interest in the enforcement of the contract. In the present case, for the reasons discussed below, I do not believe Tercon has identified a relevant public policy that fulfills this requirement.

[120] Le comportement qui se rapproche de l'acte criminel grave ou de la fraude monumentale n'est qu'un exemple de considération d'ordre public bien établie et « foncièrement incontestable » pouvant primer la liberté de contracter, elle aussi d'ordre public. Lorsque l'inexécution du contrat se traduit par des actes répréhensibles de cette nature, le tribunal doit examiner très attentivement les circonstances. De tels actes peuvent empêcher le défendeur de se retrancher derrière la clause de non-recours. Mais le demandeur désireux de se soustraire à l'application d'une telle clause doit faire valoir la considération d'ordre public prépondérante qui, à son avis, l'emporte sur l'intérêt public lié à l'application des contrats. Pour les motifs qui suivent, je ne crois pas que Tercon invoque une considération d'ordre public applicable qui satisfait à cette exigence.

[121] The present state of the law, in summary, requires a series of enquiries to be addressed when a plaintiff seeks to escape the effect of an exclusion clause or other contractual terms to which it had previously agreed.

[122] The first issue, of course, is whether as a matter of interpretation the exclusion clause even *applies* to the circumstances established in evidence. This will depend on the Court's assessment of the intention of the parties as expressed in the contract. If the exclusion clause does not apply, there is obviously no need to proceed further with this analysis. If the exclusion clause applies, the second issue is whether the exclusion clause was unconscionable at the time the contract was made, "as might arise from situations of unequal bargaining power between the parties" (*Hunter*, at p. 462). This second issue has to do with contract formation, not breach.

[123] If the exclusion clause is held to be valid and applicable, the Court may undertake a third enquiry, namely whether the Court should nevertheless refuse to enforce the valid exclusion clause because of the existence of an overriding public policy, proof of which lies on the party seeking to avoid enforcement of the clause, that outweighs the very strong public interest in the enforcement of contracts.

IV. Application to the Facts of This Case

[124] I proceed to deal with the issues in the sequence mentioned above.

A. *Did the Ministry Breach Contract A?*

[125] The trial judge found that the parties intended to create contractual relations at the bidding stage (i.e. Contract A): 2006 BCSC 499, 53 B.C.L.R. (4th) 138, at para. 88. I agree with that conclusion. If there were no intent to form Contract A, there would be no need to exclude liability for compensation in the event of its breach.

[126] The Ministry argued that Contract A was not breached. It was entitled to enter into Contract B

[121] En résumé, dans l'état actuel du droit, le tribunal doit répondre à plusieurs questions lorsqu'une partie lui demande de la soustraire à l'application d'une clause de non-recours ou d'une autre stipulation contractuelle à laquelle elle a précédemment consenti.

[122] Évidemment, il lui faut d'abord déterminer, par voie d'interprétation, si même la clause de non-recours *s'applique* aux faits mis en preuve, ce qui dépend de l'intention des parties qu'il dégage du contrat. De toute évidence, lorsque la clause ne s'applique pas, point n'est besoin de poursuivre l'examen. Lorsqu'elle s'applique, il doit en deuxième lieu se demander si la clause était inique au moment de la formation du contrat, « comme cela pourrait se produire dans le cas où il y a inégalité de pouvoir de négociation entre les parties » (*Hunter*, p. 462). Cette deuxième considération touche à la formation du contrat, non à l'inexécution.

[123] Lorsque la clause de non-recours est jugée valide et applicable, le tribunal peut se demander dans un troisième temps s'il convient tout de même de refuser de la faire respecter en raison d'une considération d'ordre public prépondérante, dont la preuve incombe à la partie qui veut se soustraire à l'application de la clause, qui l'emporte sur le très grand intérêt public lié à l'application des contrats.

IV. Application aux faits de l'espèce

[124] J'examine maintenant les questions en litige dans l'ordre susmentionné.

A. *Le ministère a-t-il respecté le contrat A?*

[125] La juge de première instance conclut que les parties ont voulu faire naître un lien contractuel dès le dépôt de la soumission (le contrat A) : 2006 BCSC 499, 53 B.C.L.R. (4th) 138, par. 88. Je suis d'accord. Si les parties n'avaient pas eu l'intention de conclure le contrat A, il n'aurait pas été nécessaire d'écarter toute obligation d'indemnisation en cas d'inexécution.

[126] Le ministère soutient qu'il n'y a pas eu inexécution du contrat A. Il lui était loisible de

with Brentwood and it did so. There was no privity between the Ministry and EAC. The Ministry would have had no direct claim against EAC in the event of deficient performance. I accept as correct that Brentwood, having obtained Contract B, was in a position of considerable flexibility as to how and with whom it carried out the work. Nevertheless, it was open to the trial judge to conclude, as she did, that the RFP process was not conducted by the Ministry with the degree of fairness and transparency that the terms of Contract A entitled Tercon to expect. At the end of an unfair process, she found, Contract B was not awarded to Brentwood (the eligible bidder) but to what amounted to a joint venture consisting of Brentwood and EAC. I therefore proceed with the rest of the analysis on the basis that Contract A was breached.

B. *What Is the Proper Interpretation of the Exclusion of Compensation Clause and Did the Ministry's Conduct Fall Within Its Terms?*

[127] It is at this stage that I part company with my colleague Cromwell J. The exclusion clause is contained in the RFP and provides as follows:

2.10 . . .

> Except as expressly and specifically permitted in these Instructions to Proponents, no Proponent shall have any claim for compensation of any kind whatsoever, as a result of participating in this RFP, and by submitting a Proposal each Proponent shall be deemed to have agreed that it has no claim.

In my view, "participating in this RFP" began with "submitting a Proposal" for consideration. The RFP process consisted of more than the final selection of the winning bid and Tercon participated in it. Tercon's bid *was* considered. To deny that such participation occurred on the ground that in the end the Ministry chose a Brentwood joint venture (ineligible) instead of Brentwood itself (eligible) would, I believe, take the Court up the dead end identified by Wilson J. in *Hunter*:

. . . exclusion clauses, like all contractual provisions, should be given their natural and true construction.

conclure le contrat B avec Brentwood, et il l'a fait. Il n'avait pas de lien contractuel avec EAC. Il n'aurait eu aucun recours direct contre EAC en cas d'exécution insuffisante. J'estime qu'après avoir obtenu le contrat B, Brentwood jouissait effectivement d'une grande latitude pour arrêter les modalités d'exécution des travaux et choisir ses partenaires. La juge du procès pouvait néanmoins conclure comme elle le fait que, dans sa DP, le ministère n'a pas agi avec l'équité et la transparence auxquelles Tercon était en droit de s'attendre au vu du libellé du contrat A. Elle conclut qu'au terme d'un processus inéquitable, le contrat B n'a pas été adjugé à Brentwood (le soumissionnaire admissible), mais bien à une coentreprise formée de Brentwood et d'EAC. Je conclus donc qu'il y a eu inexécution du contrat A et je poursuis l'analyse en conséquence.

B. *Quelle est la juste interprétation de la clause de non-recours en indemnisation, et les actes du ministère tombent-ils sous le coup de celle-ci*?

[127] C'est à cette étape que je me dissocie de mon collègue le juge Cromwell. La clause de non-recours figurant dans la DP est libellée comme suit :

[TRADUCTION]

2.10 . . .

> Sauf ce que prévoient expressément les présentes instructions, un proposant ne peut exercer aucun recours en indemnisation pour sa participation à la DP, ce qu'il est réputé accepter lorsqu'il présente une soumission.

À mon avis, la « participation à la DP » a débuté par la « [présentation d']une soumission ». Le processus ne se résumait pas au choix final de l'adjudicataire, et Tercon y a participé. La soumission de Tercon *a été* considérée. Selon moi, nier la participation de Tercon au motif que le ministère a finalement choisi la coentreprise inadmissible dont faisait partie Brentwood, et non Brentwood elle-même (qui était admissible), mène la Cour dans l'impasse relevée par la juge Wilson dans l'arrêt *Hunter* :

. . . les clauses d'exclusion, comme toutes les stipulations d'un contrat, doivent recevoir une interprétation

Great uncertainty and needless complications in the drafting of contracts will obviously result if courts give exclusion clauses strained and artificial interpretations in order, indirectly and obliquely, to avoid the impact of what seems to them *ex post facto* to have been an unfair and unreasonable clause. [p. 509]

Professor McCamus expresses a similar thought:

. . . the law concerning exculpatory clauses is likely to be more rather than less predictable if the underlying concern is openly recognized, as it is in *Hunter*, rather than suppressed and achieved indirectly through the subterfuge of strained interpretation of such terms. [p. 778]

[128] I accept the trial judge's view that the Ministry was at fault in its performance of the RFP, but the conclusion that the process thereby ceased to be the RFP process appears to me, with due respect to colleagues of a different view, to be a "strained and artificial interpretatio[n] in order, indirectly and obliquely, to avoid the impact of what seems to them *ex post facto* to have been an unfair and unreasonable clause".

[129] As a matter of interpretation, I agree with Donald J.A. speaking for the unanimous court below:

The [trial] judge said the word "participating" was ambiguous. With deference, I do not find it so. The sense it conveys is the contractor's involvement in the RFP/contract A stage of the process. I fail to see how "participating" could bear any other meaning. [Emphasis added; para. 16.]

Accordingly, I conclude that on the face of it, the exclusion clause applies to the facts described in the evidence before us.

C. *Was the Claim Excluding Compensation Unconscionable at the Time Contract A Was Made?*

[130] At this point, the focus turns to contract formation. Tercon advances two arguments: firstly, that it suffered from an inequality of bargaining power and secondly, (as mentioned) that the

juste et naturelle. Il est évident que, si les tribunaux donnent aux clauses d'exclusion des interprétations forcées et artificielles afin d'éviter, par des moyens indirects et détournés, les conséquences de ce qui leur semble *ex post facto* avoir été une clause injuste et déraisonnable, il en résultera une grande incertitude et des complications inutiles dans la rédaction de contrats. [p. 509]

Le professeur McCamus va dans le même sens :

[TRADUCTION] . . . le droit régissant les clauses d'exonération sera assurément plus prévisible, et non moins, si la considération sous-jacente est ouvertement reconnue, comme elle l'est dans *Hunter*, au lieu d'être occultée et prise en compte indirectement par le moyen détourné de l'interprétation forcée du libellé en cause. [p. 778]

[128] Je conviens avec la juge de première instance que le ministère a été fautif dans la mise en œuvre de la DP. Cependant, en toute déférence pour les tenants de l'avis contraire, sa conclusion selon laquelle le processus a cessé dès lors d'être la DP me parait être le fruit d'« interprétations forcées et artificielles afin d'éviter, par des moyens indirects et détournés, les conséquences de ce qui leur semble *ex post facto* avoir été une clause injuste et déraisonnable ».

[129] Sur le plan de l'interprétation, je suis d'accord avec le juge Donald qui exprime l'avis unanime de la Cour d'appel :

[TRADUCTION] La juge de première instance dit que le mot « participation » est ambigu. Avec déférence, je ne suis pas d'accord. Il renvoie à la part que prend l'entrepreneur à l'étape du contrat A du processus de DP. Je ne vois pas quel autre sens pourrait avoir ce mot. [Je souligne; par. 16.]

Par conséquent, je conclus qu'à première vue, la clause de non-recours s'applique aux faits établis selon le dossier de la Cour.

C. *La clause de non-recours était-elle inique au moment de la formation du contrat A?*

[130] Pour ce volet, l'accent est mis sur la formation du contrat. Tercon avance deux arguments : premièrement, son pouvoir de négociation était moins grand que celui du ministère et, deuxièmement (je

exclusion clause violates public policy as reflected in the *Transportation Act*.

(1) Unequal Bargaining Power

[131] In *Hunter*, Dickson C.J. stated, at p. 462: "Only where the contract is unconscionable, as might arise from situations of unequal bargaining power between the parties, should the courts interfere with agreements the parties have freely concluded." Applying that test to the case before him, he concluded:

> I have no doubt that unconscionability is not an issue in this case. Both Allis-Chalmers and Syncrude are large and commercially sophisticated companies. Both parties knew or should have known what they were doing and what they had bargained for when they entered into the contract. [p. 464]

While Tercon is not on the same level of power and authority as the Ministry, Tercon is a major contractor and is well able to look after itself in a commercial context. It need not bid if it doesn't like what is proposed. There was no relevant imbalance in bargaining power.

(2) Policy of the *Transportation Act*

[132] As mentioned earlier, Tercon cites and relies upon the policy of the Act which undoubtedly favours the transparency and integrity of the bidding process. I have already discussed my reasons for rejecting Tercon's argument that this "policy" operates as a bar to the ability of the parties to agree on such commonplace commercial terms as in the circumstances they think appropriate. In addition, the exclusion clause is not as draconian as Tercon portrays it. Other remedies for breach of Contract A (specific performance or injunctive relief, for example) were available.

[133] In this case, injunction relief *was* in fact a live possibility. Although Tercon was not briefed on the negotiations with other bidders, the trial judge found that Glenn Walsh, the owner of Tercon, "had seen representatives of EAC with Brentwood following [the Brentwood/EAC interviews with the

le rappelle), la clause de non-recours va à l'encontre de la raison d'être de la *Loi sur les transports*.

(1) Inégalité du pouvoir de négociation

[131] Dans l'arrêt *Hunter*, le juge en chef Dickson affirme à la p. 462 : « Ce n'est que lorsque le contrat est inique, comme cela pourrait se produire dans le cas où il y a inégalité de pouvoir de négociation entre les parties, que les tribunaux devraient modifier les conventions que les parties ont formées librement. » Appliquant ce critère à l'espèce dont la Cour était saisie, il conclut :

> Je n'ai aucun doute que l'iniquité n'est pas en cause en l'espèce. Allis-Chalmers et Syncrude sont d'importantes sociétés commerciales ayant une grande expérience des affaires. Les deux parties savaient ou auraient dû savoir ce qu'elles faisaient et ce qu'elles avaient négocié au moment de conclure le contrat. [p. 464]

Tercon n'a ni le pouvoir ni l'autorité du ministère, mais c'est une entreprise importante parfaitement en mesure de défendre ses intérêts commerciaux. Elle n'a pas à donner suite à un appel d'offres dont les conditions ne lui conviennent pas. Il n'y avait pas d'inégalité déterminante du pouvoir de négociation.

(2) Raison d'être de la *Loi sur les transports*

[132] J'ai déjà signalé que Tercon s'en remet à la raison d'être de la Loi, qui favorise indubitablement la transparence et l'intégrité du processus d'appel d'offres. J'ai également fait état des motifs pour lesquels je rejette la thèse de Tercon selon laquelle cette « raison d'être » fait obstacle à la faculté des parties de convenir des conditions commerciales courantes qu'elles jugent indiquées dans les circonstances. En outre, la clause de non-recours n'est pas aussi draconienne que le laisse entendre Tercon. L'inexécution du contrat A donnait ouverture à d'autres recours (dont l'exécution en nature et l'injonction).

[133] En l'espèce, l'injonction *était* effectivement une avenue possible. Bien que Tercon n'ait pas été informée des négociations avec les autres soumissionnaires, la juge de première instance relève que son propriétaire, Glenn Walsh, [TRADUCTION] « avait rencontré des représentants d'EAC et de

Ministry and Bill Swain of Brentwood]", and when asked whether Tercon was going to sue, Walsh had said "no" without further comment. Had Tercon pushed for more information and sought an injunction (as a matter of private law, not public law), at that stage the exclusion clause would have had no application, but Tercon did not do so. This is not to say that estoppel or waiver applies. Nor is it to say that injunctive relief would be readily available in many bidding situations (although if an injunction had been sought here, the unavailability of the alternative remedy of monetary damages might have assisted Tercon). It is merely to say that the exclusion clause is partial, not exhaustive.

[134] The Kincolith road project presented a serious construction challenge on a tight time frame and within a tight budget. Contract A did not involve a bid for a fixed price contract but for the right to negotiate the bid details once the winning proponent was selected. In such a fluid situation, *all* participants could expect difficulties in the contracting process. Members of the construction bar are nothing if not litigious. In the circumstances, the bidders might reasonably have accepted (however reluctantly) the Ministry's need for a bidding process that excluded compensation, and adjusted their bids accordingly. The taxpayers of British Columbia were not prepared to pay the contractor's profit twice over — once to Brentwood/EAC for actually building the road, and now to Tercon, even though in Tercon's case the "profit" would be gained without Tercon running the risks associated with the performance of Contract B. The Court should not be quick to declare such a clause, negotiated between savvy participants in the construction business, to be "contrary to the Act".

D. *Assuming the Validity of the Exclusion Clause at the Time the Contract Was Made, Is There Any Overriding Public Policy That Would Justify the Court's Refusal to Enforce It?*

[135] If the exclusion clause is not invalid from the outset, I do not believe the Ministry's performance

Brentwood après [les rencontres de Brentwood et d'EAC avec le ministère et Bill Swain, de Brentwood] »; interrogé quant à savoir si Tercon allait poursuivre, M. Walsh avait répondu « non » sans autre commentaire. Si Tercon avait alors tenté d'en savoir plus et sollicité une injonction (en droit privé, et non en droit public), la clause de non-recours ne se serait pas appliquée, mais Tercon ne l'a pas fait. Il n'y a pas pour autant préclusion ou renonciation. Certes, il n'est pas facile d'obtenir une injonction dans bon nombre de processus d'appel d'offres (quoique, en l'espèce, l'impossibilité d'obtenir des dommages-intérêts aurait sans doute joué en faveur de Tercon). Simplement, l'absence de recours est partielle, et non totale.

[134] Le projet de Kincolith, dont le calendrier et le budget étaient serrés, présentait un défi de taille. En décrochant le contrat A, le soumissionnaire n'obtenait pas un marché à prix fixe, mais bien le droit de négocier le détail du contrat de construction. Dans un cadre aussi mouvant, *tous* les participants pouvaient s'attendre à des difficultés lors du processus d'adjudication. Le droit de la construction n'existerait pas sans les litiges. Dans les circonstances, il est raisonnable de penser que les soumissionnaires ont accepté (même avec réticence) que l'appel d'offres du ministère exclue toute indemnisation et qu'ils ont rajusté leurs soumissions en conséquence. Les contribuables de la Colombie-Britannique n'étaient pas disposés à payer deux fois le profit de l'entrepreneur — d'abord à la coentreprise Brentwood/EAC pour la construction effective de la route, puis à Tercon, qui réalisait le « profit » sans avoir couru le risque associé à l'exécution du contrat B. La Cour ne doit pas s'empresser de déclarer « contraire à la Loi » une clause de non-recours négociée par des entreprises rompues aux usages du domaine de la construction.

D. *À supposer que la clause de non-recours était valable au moment de la formation du contrat, une considération d'ordre public prépondérante justifie-t-elle le tribunal de refuser de la faire respecter?*

[135] Si la clause de non-recours n'était pas invalide au départ, je ne crois pas que l'exécution du

can be characterized as so aberrant as to forfeit the protection of the contractual exclusion clause on the basis of some overriding public policy. While there is a public interest in a fair and transparent tendering process, it cannot be ratcheted up to defeat the enforcement of Contract A in this case. There *was* an RFP process and Tercon participated in it.

[136] Assertions of ineligible bidders and ineligible bids are the bread and butter of construction litigation. If a claim to defeat the exclusion clause succeeds here on the basis that the owner selected a joint venture consisting of an eligible bidder with an ineligible bidder, so also by a parity of reasoning should an exclusion clause be set aside if the owner accepted a bid ineligible on other grounds. There would be little room left for the exclusion clause to operate. A more sensible and realistic view is that the parties here expected, even if they did not like it, that the exclusion of compensation clause would operate even where the eligibility criteria in respect of the bid (including the bidder) were not complied with.

[137] While the Ministry's conduct was in breach of Contract A, that conduct was not so extreme as to engage some overriding and paramount public interest in curbing contractual abuse as in the *Plas-Tex* case. Brentwood was not an outsider to the RFP process. It was a legitimate competitor. All bidders knew that the road contract (i.e. Contract B) would not be performed by the proponent alone. The work required a large "team" of different trades and personnel to perform. The issue was whether EAC would be on the job as a major sub-contractor (to which Tercon could not have objected) or identified with Brentwood as a joint venture "proponent" with EAC. All bidders were made aware of a certain flexibility with respect to the composition of any proponent's "team". Section 2.8(b) of the RFP provided that if "a material change has occurred to the Proponent since its qualification under the RFEI, including if the composition of the Proponent's team members has changed, . . . the Ministry may

contrat par le ministère s'éloigne à ce point de la norme qu'une considération d'ordre public prépondérante justifie le tribunal d'écarter la protection découlant de la clause contractuelle de non-recours. Il est certes dans l'intérêt public que le processus d'appel d'offres soit équitable et transparent, mais cette considération ne suffit pas à justifier le refus de faire respecter le contrat A en l'espèce. Un processus de DP *s'est* déroulé et Tercon y a participé.

[136] En droit de la construction, les litiges naissent souvent à la suite d'allégations d'inadmissibilité de soumissionnaires et de soumissions. Si, dans la présente affaire, on faisait droit à la demande parce que le propriétaire a choisi une coentreprise formée de deux soumissionnaires dont un était admissible et l'autre non, par souci de cohérence, faudrait-il également écarter la clause de non-recours lorsque le propriétaire accepte une soumission inadmissible sous quelque autre rapport, laissant ainsi peu de place à l'application d'une telle clause? D'un point de vue plus réaliste et rationnel, les parties s'attendaient en l'espèce, même si cette éventualité ne les enchantait guère, à ce que la clause excluant toute indemnisation s'applique advenant même le non-respect des critères d'admissibilité de la soumission (et de son auteur).

[137] Les actes du ministère ont certes contrevenu au contrat A, mais j'estime qu'ils n'étaient pas répréhensibles au point de faire en sorte qu'une considération d'ordre public prépondérante justifie la répression d'un abus contractuel comme dans l'affaire *Plas-Tex*. Brentwood n'était pas étrangère au processus de DP. Il s'agissait d'un concurrent légitime. Tous les soumissionnaires savaient que le proposant retenu n'exécuterait pas seul le contrat de construction routière (le contrat B). Il fallait pouvoir compter sur une « équipe » pluridisciplinaire pour mener le projet à bien. La question était celle de savoir si EAC serait sous-traitant principal (ce à quoi Tercon n'aurait pu s'opposer) ou « proposant » dans le cadre de la coentreprise avec Brentwood. Une certaine latitude était accordée à tous les soumissionnaires pour la constitution de leur « équipe ». L'alinéa 2.8b) de la DP prévoyait en effet que lorsque [TRADUCTION] « depuis que le proposant est devenu admissible en répondant à la

request [further information and] . . . reserves the right to disqualify that Proponent, and reject its Proposal". Equally, "[i]f a qualified Proponent is concerned that it has undergone a material change, the Proponent can, at its election, make a preliminary submission to the Ministry, in advance of the Closing Date, and before submitting a Proposal. . . . The Ministry will, within three working days of receipt of the preliminary submission give a written decision as to whether the Proponent is still qualified to submit a Proposal."

[138] The RFP issued on January 15, 2001. The Ministry was informed by Brentwood of a "proposed material change to our team's structure" in respect of a joint venture with EAC by fax dated January 24, 2001. From the Ministry's perspective, the change was desirable. EAC was a bigger company, had greater expertise in rock drilling and blasting (a major part of the contract) and a stronger balance sheet. EAC was identified in Brentwood's amended proposal as a sub-contractor. In the end, the Ministry did not approve the January 14, 2001 request, presumably because it doubted that a change in the "composition of the Proponent's team's members" could , according to the terms of the RFP, include a change in the Proponent itself.

[139] The Ministry did obtain legal advice and did not proceed in defiance of it. On March 29, 2001, the Ministry noted in an internal e-mail that a Ministry lawyer (identified in the e-mail) had come to the conclusion that the joint venture was not an eligible proponent but advised that Contract B could lawfully be structured in a way so as to satisfy both Brentwood/EAC's concerns and avoid litigation from disappointed proponents.

[140] I do not wish to understate the difference between EAC as a sub-contractor and EAC as a joint-venturer. Nor do I discount the trial judge's condemnation of the Ministry's lack of fairness

DEI, une modification substantielle le concernant s'est produite, notamment en ce a trait à la composition de son équipe [. . .], [le ministère] peut exiger du proposant d'autres renseignements [. . .] et [il] se réserve le droit de l'écarter et de rejeter sa soumission ». Puis, « le proposant admissible qui estime qu'une modification substantielle le concernant a pu se produire peut à son gré présenter au ministère une soumission préliminaire avant la date de clôture et avant de formuler une proposition. [. . .] Dans les trois jours ouvrables qui suivent la réception de la soumission préliminaire, le ministère lui fait savoir par écrit s'il est toujours admissible. »

[138] La DP a été lancée le 15 janvier 2001. Dans une télécopie datée du 24 janvier 2001, Brentwood a informé le ministère de la [TRADUCTION] « modification substantielle qu'elle se proposait d'apporter à la composition de son équipe » en vue de la formation d'une coentreprise avec EAC. Le ministère voyait le changement d'un bon œil. EAC était une société de plus grande taille, dotée d'une plus grande expertise dans le forage de roches et le dynamitage (ce qui comptait pour une grande partie des travaux) et elle affichait une meilleure santé financière. Elle figurait à titre de sous-traitant dans la proposition modifiée de Brentwood. Finalement, le ministère n'a pas approuvé la modification signalée le 14 janvier 2001, vraisemblablement parce qu'il craignait que la modification de la « composition de [l']équipe [du proposant] » ne puisse, suivant la DP, englober la modification du proposant lui-même.

[139] Le ministère a obtenu un avis juridique, et il n'a pas agi à l'encontre de celui-ci. Le 29 mars 2001, le ministère signalait dans un courriel interne qu'un avocat du ministère (nommé dans le courriel) avait conclu que la coentreprise n'était pas un proposant admissible, mais que le contrat B pouvait en toute légalité être rédigé de façon à tenir compte des préoccupations de Brentwood et d'EAC et à éviter toute contestation des proposants non retenus.

[140] Je ne veux pas minimiser la différence entre le fait, pour EAC, d'être un sous-traitant ou un coentrepreneur. Je ne mésestime pas non plus les conclusions de la juge de première instance

and transparency in making a Contract B which on its face was at odds with what the trial judge found to be the true state of affairs. Tercon has legitimate reason to complain about the Ministry's conduct. I say only that based on the jurisprudence, the Ministry's misconduct did not rise to the level where public policy would justify the court in depriving the Ministry of the protection of the exclusion of compensation clause freely agreed to by Tercon in the contract.

[141] The construction industry in British Columbia is run by knowledgeable and sophisticated people who bid upon and enter government contracts with eyes wide open. No statute in British Columbia and no principle of the common law override their ability in this case to agree on a tendering process including a limitation or exclusion of remedies for breach of its rules. A contractor who does not think it is in its business interest to bid on the terms offered is free to decline to participate. As Donald J.A. pointed out, if enough contractors refuse to participate, the Ministry would be forced to change its approach. So long as contractors are willing to bid on such terms, I do not think it is the court's job to rescue them from the consequences of their decision to do so. Tercon's loss of anticipated profit is a paper loss. In my view, its claim is barred by the terms of the contract it agreed to.

V. Disposition

[142] I would dismiss the appeal without costs.

Appeal allowed, McLachlin C.J. *and* Binnie, Abella *and* Rothstein JJ. *dissenting.*

Solicitors for the appellant: McLean & Armstrong, West Vancouver.

Solicitor for the respondent: Attorney General of British Columbia, Victoria.

selon lesquelles le ministère a fait preuve d'un manque d'équité et de transparence en établissant un contrat B qui ne correspondait manifestement pas à la réalité. Tercon a raison de dénoncer le comportement du ministère. Seulement, au vu de la jurisprudence, l'inconduite n'était pas répréhensible au point que l'ordre public justifie le tribunal de refuser au ministère la protection de la clause de non-recours en indemnisation à laquelle Tercon a librement consenti.

[141] Dans le secteur de la construction de la Colombie-Britannique, des gens compétents dotés d'une grande expérience répondent à des appels d'offres et concluent des contrats avec l'État en toute connaissance de cause. Aucune loi de cette province et aucun principe de common law ne l'emporte en l'espèce sur leur faculté de convenir d'un processus d'appel d'offres, y compris d'une responsabilité limitée ou d'une absence de recours advenant le non-respect des conditions applicables. L'entrepreneur qui estime qu'il n'est pas dans son intérêt commercial de répondre à un appel d'offres aux conditions proposées est libre de s'en abstenir. Comme le fait observer le juge Donald, si un nombre suffisant d'entrepreneurs refusent de soumissionner, le ministère sera bien obligé de modifier sa façon de faire. Tant que des entrepreneurs seront disposés à soumissionner à de telles conditions, je ne crois pas qu'il revienne aux tribunaux de les soustraire aux conséquences de leurs actes. La perte du profit escompté par Tercon est théorique. Selon moi, les conditions du contrat auxquelles elle a consenti font obstacle à sa demande.

V. Dispositif

[142] Je suis d'avis de rejeter le pourvoi sans dépens.

Pourvoi accueilli, la juge en chef McLachlin *et les juges* Binnie, Abella *et* Rothstein *sont dissidents.*

Procureurs de l'appelante : McLean & Armstrong, West Vancouver.

Procureur de l'intimée : Procureur général de la Colombie-Britannique, Victoria.

Solicitor for the intervener: Attorney General of Ontario, Toronto.

Procureur de l'intervenant : Procureur général de l'Ontario, Toronto.

TAB 22

Canadian Contractual Interpretation Law

THIRD EDITION

Geoff R. Hall

LexisNexis

Chapter 2

FUNDAMENTAL PRECEPTS OF CONTRACTUAL INTERPRETATION

2.1 WORDS AND THEIR CONTEXT

2.1.1 The principle

Contractual interpretation is, for the most part, an exercise in giving effect to the intentions of the parties. In doing so, it is of paramount importance to achieve accuracy in interpretation. There is little point in giving effect to the intentions of the parties if the court has not accurately discerned what those intentions are. Accuracy in interpretation requires consideration of two things, namely the words selected by the parties to set out their agreement, and the context in which those words have been used.[1] Words and their context, therefore, are the primary theme of the law of interpretation of contracts, and set the parameters for the interpretive exercise. An interpretation which strays too far from the words selected by the parties is not legitimate because it fails to give effect to the very means the parties invoked to define their legal obligations. An interpretation which strays too far from the context in which the parties used those words risks inaccuracy; even if an interpretation is literally correct, if the words are taken out of context, the meaning does not accurately correspond to what the parties were attempting to achieve. Interpretation therefore involves a search for meaning within the constraints of the words and their context. An ideal interpretation is one which accords with both.

The reconciliation of words and context is a practical, not a technical one. At one point in history, the law of contractual interpretation was dominated by a laundry list of "cannons of construction" which set out a somewhat inflexible set of rules. That approach no longer prevails. The courts recognize that language and its usage are flexible, and that an infinite variety of commercial and business arrangements requires a holistic approach. As recently expressed by the Supreme Court of Canada in *Sattva Capital Corp. v. Creston Moly Corp.*, "the interpretation of contracts has evolved towards a practical, common-sense approach not dominated by technical rules of construction."[2]

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1 *Golden Capital Securities Ltd. v. Investment Industry Regulatory Organization of Canada*, [2010] B.C.J. No. 1458, 8 B.C.L.R. (5th) 227 at para. 44 (B.C.C.A.).

2 [2014] S.C.J. No. 53, [2014] 2 S.C.R. 633 at para. 47 (S.C.C.).

The interpretation of a contract always begins with the words it uses. All of the various aspects of contractual interpretation are rooted in the actual language used by the parties.[3] "[E]ffect must first be given to the intention of the parties, to be gathered from the words they have used."[4] A court "should give effect to the intentions of the parties as expressed in their written document".[5] It is a "cardinal presumption" that the parties have intended what they have said in a contract.[6] As expressed by the New Brunswick Court of Appeal: "It is beyond dispute that the goal of any contractual interpretation is the determination of the parties' intent at the time of entry into the contract. That state of mind is ascertained by reference to the meaning of the words as used by the parties."[7] While some rules of contractual interpretation may take meaning beyond the words used by the parties — sometimes because context is paramount,[8] other times because some other policy goal or substantive principle of law is paramount[9] — the words are always the starting point for the exercise and provide an anchor for the endeavour.

Indeed, some cases go so far as to suggest that an examination of the language of a contract can be the beginning and the end of the interpretive exercise. The Ontario Court of Appeal has expressed the sentiment in the following manner:

> The cardinal interpretive rule of contracts ... is that the court should give effect to the intention of the parties as expressed in their written agreement. Where that intention is plainly expressed in the language of the agreement, the court should not stray beyond the four corners of the agreement.[10]

The Supreme Court of Canada has expressed the same sentiment in the following manner:

> Were I convinced that a different interpretation would advance the true intent of the parties, I would gladly subscribe to it. However, when the wording of a contract is unambiguous, as in my view it is in this case, courts should not give it a meaning different from that which is expressed by its clear terms,

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3 *Leggett & Platt Canada Co. v. Brink Forest Products Ltd.*, [2010] B.C.J. No. 52, 69 B.C.L.R. (4th) 1 at para. 20 (B.C.C.A.).

4 *Consolidated-Bathurst Export Ltd. v. Mutual Boiler and Machinery Insurance Co.*, [1979] S.C.J. No. 133, [1980] 1 S.C.R. 888 at 889 (headnote) (S.C.C.).

5 *Manulife Bank of Canada v. Conlin*, [1996] S.C.J. No. 101, [1996] 3 S.C.R. 415 at para. 79 (S.C.C.), *per* Iacobucci J., dissenting.

6 *Ventas, Inc. v. Sunrise Senior Living Real Estate Investment Trust*, [2007] O.J. No. 1083, 85 O.R. (3d) 254 at para. 24 (Ont. C.A.) and *Venture Capital USA Inc. v. Yorkton Securities Inc.*, [2005] O.J. No. 1885, 75 O.R. (3d) 325 at para. 26 (Ont. C.A.).

7 *Stenstrom v. McCain Foods Ltd.*, [2000] N.B.J. No. 379, 230 N.B.R. (2d) 234 at para. 16 (N.B.C.A.).

8 See, for example, the discussion of consumer contracts in section 8.2.

9 See, for example, the discussion of arbitration clauses in section 9.1 and the discussion of choice of forum clauses in section 9.4.

10 *KPMG Inc. v. Canadian Imperial Bank of Commerce*, [1998] O.J. No. 4746 at para. 5 (Ont. C.A.), leave to appeal refused [1999] S.C.C.A. No. 36, [1999] 2 S.C.R. vi (S.C.C.).

> unless the contract is unreasonable or has an effect contrary to the intention of the parties.[11]

While it is true that the words of a contract must always be the starting point for interpretation and that any legitimate interpretation of a contract must be consistent with the language that it uses, it is an overstatement to say that the interpretive exercise can ever end with them because context is always important to discerning meaning accurately.[12] "[R]arely is it truly possible to interpret a document without any knowledge of the context."[13] As noted in *Dumbrell v. Regional Group of Companies Inc.*, a leading statement by the Ontario Court of Appeal of the proper approach to interpretation of contracts:

> No doubt, the dictionary and grammatical meaning of the words (sometimes called the "plain meaning") used by the parties will be important and often decisive in determining the meaning of the document. However, the former cannot be equated with the latter. The meaning of a document is derived not just from the words used, but from the context or the circumstances in which the words were used.[14]

As a result, examination of context is an integral part of the process of contractual interpretation and cannot be limited to cases where the language of the contract viewed in isolation suggests ambiguity.[15] While it may once have been the case that courts would consider the contractual language first and only turn to context or other extrinsic evidence if the text contained a linguistic ambiguity, that approach is no longer accepted. Context is always part of the process of contractual interpretation.

Context has two separate aspects, each of which is discussed in greater detail elsewhere in this book. The first is the context of the document. The second is the surrounding circumstances which give rise to the contract.

The first aspect, the context of the document, is important because words are never used in isolation. As a result, interpretation of a word or group of words must have regard for the way language is used in the document as a whole. This element of context is given effect by the rule that contracts must be read as a whole with meaning given to all provisions.[16] Employing this aspect of context has several purposes. One is to avoid inconsistency within a contract:

> It is unquestionable that the object of interpretations of all written instruments is to ascertain the intention of the parties thereto as expressed in the instrument itself. To ascertain the true intention of the parties, however, one must look at each provision in the context in which it is found and, in construing it, regard

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11 *Scott v. Wawanesa Mutual Insurance Co.*, [1989] S.C.J. No. 55, [1989] 1 S.C.R. 1445 at para. 51 (S.C.C.).

12 *Leggett & Platt Canada Co. v. Brink Forest Products Ltd.*, [2010] B.C.J. No. 52, 69 B.C.L.R. (4th) 1 at para. 21 (B.C.C.A.).

13 *Eco-Zone Engineering Ltd. v. Grand Falls — Windsor (Town)*, [2000] N.J. No. 377, 5 C.L.R. (3d) 55 at para. 7 (Nfld. C.A.).

14 *Dumbrell v. Regional Group of Companies Inc.*, [2007] O.J. No. 298, 220 O.A.C. 64 at para. 52 (Ont. C.A.).

15 *Ibid.*, at para. 54 (Ont. C.A.).

16 See section 2.2.

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TAB 23

Canadian Contractual Interpretation Law

FOURTH EDITION

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FOURTH EDITION

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Chapter 2

Fundamental Precepts of Contractual Interpretation

2.1. WORDS AND THEIR CONTEXT

2.1.1 The principle

Contractual interpretation is, for the most part, an exercise in giving effect to the intentions of the parties. In doing so, it is of paramount importance to achieve accuracy in interpretation. There is little point in giving effect to the intentions of the parties if the court has not accurately discerned what those intentions are. Accuracy in interpretation requires consideration of two things, namely the words selected by the parties to set out their agreement, and the context in which those words have been used.[1] Words and their context, therefore, are the primary theme of the law of interpretation of contracts, and set the parameters for the interpretive exercise. An interpretation which strays too far from the words selected by the parties is not legitimate because it fails to give effect to the very means the parties invoked to define their legal obligations. An interpretation which strays too far from the context in which the parties used those words risks inaccuracy; even if an interpretation is literally correct, if the words are taken out of context, the meaning does not accurately correspond to what the parties were attempting to achieve. Interpretation therefore involves a search for meaning within the constraints of the words and their context. An ideal interpretation is one which accords with both.

The reconciliation of words and context is a practical, not a technical one. At one point in history, the law of contractual interpretation was dominated by a laundry list of "cannons of construction" which set out a somewhat inflexible set of rules. That approach no longer prevails. The courts recognize that language and its usage are flexible, and that an infinite variety of commercial and business arrangements requires a holistic approach. As expressed by the Supreme Court of Canada in *Sattva Capital Corp. v. Creston Moly Corp.*, "the interpretation of contracts has evolved towards a practical, common-sense approach not dominated by technical rules of construction."[2]

The interpretation of a contract always begins with the words it uses. All of the various aspects of contractual interpretation are rooted in the actual language used by the parties.[3] A court "should give effect to the intentions of the parties as expressed in their written document".[4] It is a "cardinal presumption" that the parties have intended what they have said in a contract.[5] As expressed by the New Brunswick Court of Appeal: "It is beyond dispute that the goal of any contractual interpretation is the determination of the parties' intent at the time of entry into the contract. That state of mind is ascertained by reference to the meaning of the words as used by the parties."[6] While some rules of contractual interpretation may take meaning beyond the words used by the parties — sometimes because context is paramount,[7] other times because some other policy goal or substantive principle of law is paramount[8] — the words are always the starting point for the exercise and provide an anchor for the endeavour.

Yet words alone are not enough. Context is always important to discerning meaning accurately.[9] "[R]arely is it truly possible to interpret a document without any knowledge of the context."[10] As noted in *Dumbrell v. Regional Group of Companies Inc.*, a leading statement by the Ontario Court of Appeal of the proper approach to interpretation of contracts:

No doubt, the dictionary and grammatical meaning of the words (sometimes called the "plain meaning") used by the parties will be important and often decisive in determining the meaning of the document. However, the former cannot be equated with the latter. The meaning of a document is derived not just from the words used, but from the context or the circumstances in which the words were used.[11]

As a result, examination of context is an integral part of the process of contractual interpretation and cannot be limited to cases where the language of the contract viewed in isolation suggests ambiguity.[12] While it may once have been the case that courts would consider the contractual language first and only turn to context or other

extrinsic evidence if the text contained a linguistic ambiguity, that approach is no longer accepted. Context is always part of the process of contractual interpretation.

Context has two separate aspects, each of which is discussed in greater detail elsewhere in this book. The first is the context of the document. The second is the surrounding circumstances which give rise to the contract.

The first aspect, the context of the document, is important because words are never used in isolation. As a result, interpretation of a word or group of words must have regard for the way language is used in the document as a whole. This element of context is given effect by the rule that contracts must be read as a whole with meaning given to all provisions.[13] Employing this aspect of context has several purposes. One is to avoid inconsistency within a contract:

It is unquestionable that the object of interpretations of all written instruments is to ascertain the intention of the parties thereto as expressed in the instrument itself. To ascertain the true intention of the parties, however, one must look at each provision in the context in which it is found and, in construing it, regard must be had to the language used in that and other parts of the document to avoid inconsistency.[14]

However, the primary purpose of considering this aspect of context is to achieve interpretive accuracy. The Nova Scotia Court of Appeal has commented twice on this purpose, noting that "[i]t is also fundamental to the task of interpretation that the words must be understood in the context in which they are used",[15] such that "particular words and phrases should not be lifted from the contract and considered in isolation. They must be interpreted within the context, scheme and objectives of the entire [contract]".[16] Thus even where terms with strict legal meanings are used, it is not enough to look at the strict legal meanings because such terms might be used in an "ordinary and popular sense" to describe different things: "Their intended meaning may only be understood in light of the legal context from which the terms are adopted and the particular context in which they are used."[17]

The second aspect is the context of the surrounding circumstances which give rise to the contract. There is always a background to a contract. Whether simple or complex, the background is essential to discerning its correct meaning. In contractual interpretation, this aspect of context is given effect by the rule that the factual matrix must be considered when interpreting a contract.[18]

Evidence of the factual matrix is always admissible, even where the words of a contract are unambiguous: "Indeed, because words always take their meaning from their context, evidence of the circumstances surrounding the making of a contract has been regarded as admissible in every case."[19] Again, the primary purpose of looking to this element of context is to achieve interpretive accuracy:

[I]n determining what was contemplated by the parties, the words used in a document need not be looked at in a vacuum. The specific context in which a document was executed may well assist in understanding the words used. It is perfectly proper, and indeed may be necessary, to look at the surrounding circumstances *in order to ascertain what the parties were really contracting about*.[20]

Contractual interpretation is all about giving meaning to words in their context. The balance of this book is an elaboration of this process.

2.1.2 The precept in Québec

The foregoing demonstrates that the common law precept conceives of contractual interpretation as a one-stage exercise, with words and context considered together. Québec law takes a different approach to the interaction between words and context.

As the Supreme Court of Canada recognized in *Uniprix inc. v. Gestion Gosselin et Bérubé inc.*,[21] in Québec there is a two-stage process. The first step is to determine whether the contractual language is clear or ambiguous. If the language is clear and unambiguous, the court must *apply* the contract, not *interpret* it. The purpose of the first step, which can be referred to as the règle de l'acte clair (the clear act rule), is to prevent judges from departing (either deliberately or inadvertently) from the clearly expressed intention of the parties, and to ensure that a judge defers to a clear contract.[22] It is only if an ambiguity is identified at the first step that the analysis proceeds to a second step, at which the contract is interpreted to determine the parties' common intention. An ambiguity exists where the wording of the contract would raise a doubt as to its meaning in the mind of a reasonable person.[23]

2.6. COMMERCIAL EFFICACY

2.6.1 The principle

It is a fundamental precept of the law of contractual interpretation that commercial contracts must be interpreted in accordance with sound commercial principles and good business sense.[254] Thus, "where one possible interpretation will allow the contract to function and meet the commercial objective in view, and the other scarcely will, the former is to be chosen".[255]

The commercial efficacy principle is closely linked to other fundamental precepts of the law of contractual interpretation. It is grounded in the intentions of the parties, pursued not as its own policy goal but rather in furtherance of the goal of accurately giving effect to the parties' intentions. Like all aspects of contractual interpretation, it is assessed objectively and requires a contextual analysis with the court undertaking a close examination of both the contract as a whole and the factual matrix.

The commercial efficacy principle has an important corollary: an interpretation which is commercially absurd is to be avoided. This corollary leads to some difficulties when a literal reading of the text of a contract would result in a commercial absurdity, and the courts have struggled with the question of how far a contextual analysis can depart from the words of an agreement in order to avoid a commercially absurd outcome.

2.6.2 The commercial efficacy principle is grounded in the intentions of the parties

Courts seek a commercially sensible interpretation of a contract to give effect to the intentions of the contracting parties. Since those who enter into commercial contracts generally have sensible goals, a commercially sensible interpretation is more likely to be consistent with their intentions than is one that does not make commercial sense. This point was made by the Manitoba Court of Appeal in the following way:

In determining the meaning of the language of a commercial contract, and unilateral contractual notices, the law therefore generally favours a commercially sensible construction. *The reason for this approach is that a commercial construction is more likely to give effect to the intention of the parties.*[256]

The House of Lords, in a passage which has been applied in Canada, put the point the following way: "The more unreasonable the result the more unlikely it is that the parties can have intended it, and if they do intend it the more necessary it is that they shall make that intention abundantly clear."[257] The Alberta Court of Appeal has made the same point in somewhat more colourful terms:

A contract must be interpreted in a positive and purposive manner, trying to make it work. The parties' purpose here was to make a workable commercial deal between oilfield servicing companies. The court must presume that these business people intended that the contract work in substance and frankly, beyond the nominal or technical. The court must not be too quick to find gaps or flaws in a commercial contract's wiring which prevent power from reaching all its operative parts. The parties are presumed not to have been wasting ink on an academic exercise.[258]

Thus seeking a commercially sensible interpretation is not a policy goal in and of itself. The purpose of the commercial efficacy principle is not to protect business people from absurd results of their own contracts.[259] Instead, the commercial efficacy principle relates to the overall goal of contractual interpretation, which is to give an accurate meaning to the parties' intentions.

2.6.3 Commercial reasonableness is not to be determined from the perspective of only one contracting party

Since contractual interpretation is an objective exercise, commercial reasonableness cannot be judged solely from the perspective of one of the contracting parties but rather must be assessed objectively:

[T]he document should be construed in accordance with sound commercial principles and good business sense. Care must be taken, however, to do so objectively rather than from the perspective of one contracting party or the other, since what might make good business sense to one party would not necessarily do so for the other.[260]

Thus even interpretations which lead to draconian results for one contracting party can be found to be commercially reasonable. *Shahinian v. Precinda Inc.*[261] involved a claim by a holder of preference shares for the redemption of his shares. Redemption was required only in three specified circumstances, the relevant one being "the failure of Precision [the corporation] to remedy a default in payment of dividends on the Class X Preference Shares as prescribed in the Articles, within 60 days of such default".[262] The corporation had refused to pay dividends, despite having available funds, because it believed that the shareholder had breached confidentiality and non-compete obligations to the company. The corporation argued that the redemption provision should only apply when the corporation, though still solvent, lacked the necessary funds to pay the dividends, and pointed to the other two circumstances in which redemption was required in support of that interpretation. The Ontario Court of Appeal rejected the corporation's interpretation. In doing so, it acknowledged that while the remedy of redemption might seem draconian from the perspective of the corporation, it was commercially reasonable from the shareholder's point of view, especially since the refusal to pay his dividends had been based on suspicions for which there had been no evidence.[263]

2.6.4 The commercial efficacy principle is applied with reference to the entire context, including the language of the contract as a whole and the factual matrix

Since contractual interpretation is always a contextual exercise, when ascertaining whether an interpretation is commercially reasonable, a court will look at the entire context. Thus in assessing commercial reasonableness the court will consider both the language of the contract as a whole (such that individual provisions are not assessed in isolation for commercial reasonableness) and the factual matrix (as the surrounding circumstances are essential to understanding whether a particular interpretation makes good business sense). Thus in *Tercon Contractors Ltd. v. British Columbia (Transportation and Highways)*,[264] the interpretation of an exclusion clause in a request for proposals in a tender process was undertaken with a view to the business efficacy of the tendering process, and was considered within the entire context of that process.

As part of the contextual analysis, language is not closely parsed and read in the fashion that a lawyer would read it, but rather it is understood in the manner that a reasonable business person would understand it: "Words are therefore interpreted in the way in which a reasonable commercial person would construe them. And the standard of the reasonable commercial person is hostile to technical interpretations and undue emphasis on niceties of language."[265]

A court's assessment of commercial reasonableness must be grounded in the evidence. Speculative conclusions about commercial reasonableness in the absence of evidence should be rejected.[266] This is important to bear in mind because creative counsel can often dream up circumstances in which a proposed interpretation might have unreasonable commercial results. The mere possibility of unreasonableness based on counsel's submissions is not enough to reject a proposed interpretation.

Lack of precision in contractual language provides greater scope for the application of the commercial efficacy precept, a point that was candidly made in *Bell Mobility Inc. v. Anderson*:

> Parties can contract on almost any terms that they wish. They can contract for sinecures or other payments for nothing. But where the wording of the contract is ambiguous, a court should be slow to adopt an interpretation which gives one party pay for nothing, or for what is virtually nothing. That is because ambiguous words give the court a choice; those words should not be given the unfair or non-commercial or non-sensible alternate reading….[267]

Thus where a contract for the provision of cellular telephone services did not clearly provide that customers would pay a fee for 911 service, even in areas where such service was not available, the commercial efficacy principle was invoked to reinforce a conclusion that the contract should not be interpreted to obligate customers to pay the 911 fee even if they did not receive 911 service. Clearer contractual language could have limited recourse to the commercial efficacy principle, and could have led to the opposite result.

Conversely, the greater the precision in contractual language, the less scope there is to rely on commercial efficacy to depart from the text. The point was well expressed by the Ontario Court of Appeal in *Atos IT Solutions and Services GmbH v. Sapient Canada Inc.*:

The interpretive principle of commercial efficacy – and its corollary, avoiding interpretations that result in a commercial absurdity – is merely one of several tools used by courts to give an accurate meaning to the parties' intentions as stated in a contract….

The trial judge's reasons disclose that he was attentive to the plain language of s. 17.4, the provisions of the Subcontract as a whole, and the factual matrix from which the Subcontract emerged. Given those circumstances, little ground remains on which Sapient can erect an argument based on commercial absurdity.[268]

A helpful example of how the commercial efficacy principle mandates a highly contextualized approach both to the language of a contract and to the surrounding circumstances is found in *Mississauga Teachers' Retirement Village Limited Partnership v. L.M.C. (1993) Ltd.*[269] After a period of time, one partner of a limited partnership formed for a real estate investment wanted to sell the property and dissolve the partnership, while the other wished to retain the property and continue the partnership. The partners agreed to resolve their differences by listing the property for sale for six months at a specified price and on specified terms. If the specified price and terms were achieved, the property would be sold and the partnership would be dissolved. If not, there would be a standstill and they would continue to hold the property for five years. This agreement was incorporated into the following provision: "In the event the Property is not sold prior to the expiry of the Listing Agreement in accordance with the terms and provisions hereof, neither LMC nor MTRV LP without the written consent of the other, shall take any action with respect to the sale or proposed sale of the Property until the earlier of December 31, 2008 or the date of a material continuing breach by either LMC or MTRV LP … ." On the last day of the listing agreement, an offer to purchase was received, but it was conditional for approximately six more weeks. The disputed issue was whether "sold" meant an unconditional sale or whether the property was "sold" by virtue of the conditional offer to purchase. Looking to the entire context (language and surrounding circumstances), the court held that the commercial efficacy principle led to the conclusion that "sold" meant an unconditional agreement of purchase and sale:

Where, as here, words of a contract can bear two constructions, the preferred meaning is the one that best promotes a sensible commercial result and advances the objective of the parties in entering the commercial transaction in the first place. … As the application judge said: "Preference is to be given to an interpretation which yields a fair or commercially reasonable result which could reasonably have been anticipated in the atmosphere in which the agreement was made."

The purposes of the Sale and Dissolution Agreement was to resolve the longstanding dispute between the parties whether the property should be sold. LMC did not want to sell, but agreed to list the property for sale for a limited period. MTVR LP wanted to sell, but made the commitment that if the property did not sell during the limited period, it would standstill for five years. Exactly when the listing agreement expired, and MTVR LP's standstill obligation commenced was a matter of enormous importance to the parties. In this commercial context, the parties required a clear and certain event to determine this question. Given the function of Article 1.06 to mark the end of the listing period and the beginning of the standstill agreement, we find that the word "sold" meant an unconditional sale.[270]

The factors which will be included in an examination of the entire context cannot be listed exhaustively and depend on each individual case. The authorities suggest a number of matters which can be taken into account depending upon the circumstances, including both general commercial practices and an assessment of economic returns. Some examples serve to illustrate the point.

In *Buildevco Ltd. v. Monarch Construction Ltd.*,[271] the court considered general commercial practices and rejected a contention that a provision in a joint venture agreement requiring a party to "provide" funds meant that the party could only use its own funds. Looking to general business practices, the court found that interpreting the word "provide" as permitting the sourcing of funds through borrowing would yield a more commercially sensible interpretation:

It seems to me to be contrary to business common sense *and practice* to limit the source and the means by which the corporate parties are to obtain the funds necessary for the defaulted amount, especially when large sums of money are involved. Commercial loans and other corporate financing arrangements, including financing through an agent company, are *common business practices*.[272]

Two Ontario cases which arose from long-term ground leases illustrate the phenomenon of favouring an interpretation which results in a reasonable rate of return on an investment over one which results in an

inadequate return. *Corporate Properties Ltd. v. Manufacturers Life Insurance Co.*[273] involved a long-term ground lease which provided for a base rent of $49,000 per year plus participating rent in "a sum equal to ten per cent (10%) of the amount by which the gross annual income from all sources derived from the lands and premises in each year exceeds the amount of Six Hundred Thousand Dollars ($600,000)". At issue was whether the participating rent was to be based upon the gross income of the party to the lease or the gross income of the entire building. The court found the latter interpretation to be the correct one because the alternative would render nothing payable on account of participating rent, creating an illusory right to participating rent, which would be a commercial absurdity. *Revenue Properties Co. v. Victoria University*[274] involved an appeal from an arbitration which had set the rate of rent under a long-term (100-year) ground lease. The tenant at one of two properties argued that its interpretation, which would take into account legislation enacted subsequent to the lease that restricted the amount of rent it could derive from the building it had erected on the land, should be accepted because otherwise there would be insufficient revenue for it to pay the rent to the landlord. The tenant argued that the parties could not have contemplated such a financial impossibility. The court rejected the tenant's argument, finding that the lease provided a certain return for the landlord and imposed risks on the tenant to be able to earn sufficient revenue to pay that rent. A provision in the lease that no partnership was created was found to reinforce this conclusion.

One contextual factor which may be underappreciated in the courts' application of the commercial efficacy precept is the presence of a government entity. Government lawyers sometimes perceive that when applying the commercial efficacy precept, the courts wrongly assume that commercial efficacy is always to be determined solely from the perspective of a private profit-oriented entity. They perceive that the courts sometimes adopt interpretations which misapprehend the commercial goals of governmental contracting parties, which may involve policy considerations beyond the maximization of profit.[275] The point is well taken. A purely private paradigm is inapt unless all of the contracting parties share the perspective of private contracting parties. A contextual analysis requires recognition that government entities may have different motivations and goals than private entities. Commercial efficacy should not be assessed from a purely private perspective if all of the contracting parties do not share that perspective.

1 Canadian Contractual Interpretation Law 2.62.6.5 (2020)

2.6.5 The corollary: interpretations which result in commercial absurdity are to be avoided

The corollary of the commercial efficacy principle is the precept that commercially absurd interpretations are to be avoided. "In a commercial contract the words must be construed in a business fashion and in accordance with business common sense so as to avoid any interpretation that would result in commercial absurdity."[276] As expressed by the Supreme Court of Canada in the oft-quoted case *Toronto (City) v. W.H. Hotel Ltd.*:[277] "[T]his transaction being an ordinary commercial transaction it is the duty of the Court in interpreting that document to avoid such an interpretation as would result in commercial absurdity."[278]

Like the myriad of factors which can be taken into account as relevant context, it is impossible to provide an exhaustive list of what constitutes commercial absurdity because such a finding requires an overall assessment of the facts of a particular case. However, reviewing some examples from the authorities does help to illustrate the types of circumstances that courts have found to be commercially absurd.

In one case, an interpretation of a right of first refusal in a commercial lease which would require the tenant to vacate the premises and then return at some later point in time to exercise the right was found to be commercially absurd.[279] In another case, an interpretation of a separation agreement between an employer and an employee which would have obligated the employer to provide the employee with office space and secretarial assistance for 16 years without regard to whether such an arrangement would assist in the sales of the employer's own products was found to be "quite unrealistic, almost absurd".[280] In another case, an interpretation of an agreement of purchase and sale for an individual condominium unit which would have held the individual unit holder responsible for the total value of all units if something went wrong in dealings to which the individual unit holder was not privy was found to "make no commercial sense at all".[281]

However, the mere fact that a business arrangement is unusual does not make it commercially absurd. Indeed, the business world is full of unusual arrangements that suit the parties to them quite well. Thus the court takes into account the entire context, since an arrangement which superficially appears absurd may in fact have a

9.18. PENALTY CLAUSES (STIPULATED REMEDY CLAUSES SPECIFYING DAMAGES)

9.18.1 The principle

Parties to a contract may, at the time of contracting, turn their minds to the appropriate remedy in the event of breach, and specify that remedy in their contract. Where the stipulated remedy is an injunction, the courts are reluctant to enforce the parties' intentions and instead often insist on making their own assessment of the appropriateness of the remedy.[356] Where the stipulated remedy is a specific quantum of damages, the courts have historically been reluctant to enforce the parties' intentions. A "venerable common law rule" classifies such provisions as penalty clauses which are unenforceable unless they were a genuine pre-estimate, made at the time of contracting, of the damages likely to be incurred by the innocent party in the event of breach.

The law respecting penalty clauses is an interesting special case in contractual interpretation. The entire process is an interpretive one, as the court has to construe the stipulated remedy clause by reference to the words selected by the parties and the relevant context to determine whether it was a penalty or a genuine pre-estimate of damages. Yet once the clause in question is found to be a penalty, the court will strike it down and consciously enforce a contract which does not reflect the parties' intentions. Thus penalty clauses represent one of several instances in which the principle of interpretive accuracy gives way to another policy goal, in this case the goal of protecting contracting parties from provisions deemed to be unfair and unreasonable.

However, since the mid-1990s a second approach to stipulated remedy clauses specifying damages has emerged in the case law. Under this approach, stipulated remedy clauses specifying damages are enforced unless the result would be unconscionability at the time of enforcement. Put somewhat more technically, the alternative approach employs the perspective of relief from forfeiture, with the stipulated remedy being considered a forfeiture and with relief being granted if the forfeiture would be unconscionable. Adoption of the new rule has been driven by a recognition that a categorical rule is a significant intrusion on the parties' freedom of contract, which is not justifiable in the absence of oppression.

The new approach to stipulated remedy clauses has not been universally adopted, but is much easier to reconcile with the courts' usual approach to the interpretation of contracts. The primary issue is interpretive accuracy, which is driven by giving meaning to the words selected by the parties in the context in which those words would have been reasonably understood at the time of contracting. Divergence from the result dictated by interpretive accuracy is the exception, occurring only in circumstances of unconscionability. Interpretation and enforcement of penalty clauses has therefore been aligned with the law of contract generally, such that the intention of the parties as expressed in the words they have selected is enforced unless, as with any other contractual provision, unconscionability mandates the opposite result.

9.18.2 Requirement for both a breach and a stipulated remedy for the issue to arise

The issue of the enforceability of a penalty clause only arises if there is a penalty clause in the first place. The cases have recognized that two elements must both be present for a clause to raise penalty clause concerns: the provision must be triggered by a breach of contract, and the provision must provide for a stipulated remedy. These two requirements impose some limits on the circumstances in which the penalty clause rule can be applied, thereby somewhat limiting the scope of interference with freedom of contract occasioned by the rule.

The requirement for a breach of contract was at issue in *Do v. Nichols*.[357] An agreement of purchase and sale for a development property provided that a property was to be subdivided but contemplated that the subdivision might not occur. In that case, the vendor was obliged to pay $500,000. The argument that this provision was an unenforceable penalty clause was rejected because the provision was not triggered by a breach of contract:

It was not a breach of contract to fail to subdivide, but rather a term specifically contemplated by the parties. There was, accordingly, no breach of contract. Accordingly and with respect, the question of whether the

$500,000 obligation was a penalty, or a genuine pre-estimate of liquidated damages, does not arise in the circumstances of this case.

Similarly a provision requiring the forfeiture of a deposit if the purchase did not close by a specified date was found not to be a penalty clause because the forfeiture did not depend on a breach of contract.[358]

The requirement for a payment of a stipulated sum was at issue in *Ottawa Community Housing Corp. v. Foustanellos*.[359] A construction contract included a "stop payment" provision that permitted the owner to halt payments to the contractor pending determination of the owner's losses arising from a breach of contract by the contractor. The provision was found to be neither a penalty clause nor a liquidated damages clause because it did not require payment of a stipulated sum upon breach: "the critical common element is that both penalty and liquidated damages clauses specify a stipulated sum agreed on by the parties at the time of contract formation."

1 Canadian Contractual Interpretation Law 9.189.18.3 (2020)

9.18.3 The venerable rule

"There is a venerable common law rule to the effect that the courts will not require a party to pay a genuine or true penalty on grounds of public policy."[360] The venerable rule distinguishes between a penalty clause, which is unenforceable, and a liquidated damages clause, which is enforceable. The distinction is whether the clause represents a genuine pre-estimate, made at the time of contracting, of the damages to be suffered in the event of breach: "A penalty is the payment of a stipulated sum on breach of the contract, irrespective of the damage sustained. The essence of liquidated damages is a genuine covenanted pre-estimate of damage."[361] Non-enforcement is based on notions of fairness and reasonableness, with a concern that a penalty clause acts "*in terrorem* of the offending party"[362] and coerces that party to perform for fear of being exposed to damages in excess of what is reasonable to compensate the innocent party for its loss of bargain.

The venerable rule is intimately bound up with contractual interpretation. The exercise begins with an interpretation of the stipulated remedy provision within the relevant context. If that examination leads to a conclusion that the parties were attempting to stipulate for a penalty, the courts refuse to enforce the bargain as agreed by the parties in order to achieve a policy goal, namely protection from unfairness and unreasonableness. The relationship between penalty clauses and the interpretive exercise was candidly discussed by Laskin C.J.C. in *H.F. Clarke Ltd. v. Thermidaire Corp.*:[363]

> *[T]he Court will begin by construing the contract in which the parties have objectively manifested their intentions, and will consider the surrounding circumstances so far as they can illuminate the contract and thus aid in its construction*. It seems to me, however, that if, in the face of the parties' assertion in their contract that they were fixing liquidated damages, the Court concludes that a penalty was provided, it would be patently absurd to say that the Court was giving effect to the real intention of the parties when the Court's conclusion was in disregard of that intention as expressed by the parties.
>
> *What the Court does in this class of case, as it does in other contract situations, is to refuse to enforce a promise in strict conformity with its terms*. The Court exercises a dispensing power (which is unknown to the civil law of Québec) because *the parties' intentions, directed at the time to the performance of their contract, will not alone be allowed to determine how the prescribed sum or the loss formula will be characterized*. The primary concern in breach of contract cases (as it is in tort cases, albeit in a different context) is compensation, and *judicial interference with the enforcement of what the Courts regard as penalty clauses is simply a manifestation of a concern for fairness and reasonableness, rising above contractual stipulation, whenever the parties seek to remove from the Courts their ordinary authority to determine not only whether there has been a breach but what damages may be recovered as a result thereof*.[364]

Thus while it is always open to contracting parties to make a predetermination of the damages to be suffered in the event of breach, such a determination "must yield to judicial appraisal of its reasonableness in the circumstances".[365]

The interpretive exercise results in a contextualized assessment: "The question whether a sum stipulated is penalty or liquidated damages is a question of construction to be decided upon the terms and inherent circumstances of each particular contract, judged of as at the time of the making of the contract, not as at the time of the breach."[366] In undertaking this interpretive exercise, the parties' use of the words "penalty" or

"liquidated damages" is not conclusive. Instead, the court has to determine substantively whether the provision in question matched the label placed on it by the parties.[367]

In determining whether a provision is a penalty, the court considers whether the recovery under the stipulated remedy clause would be "extravagant" as compared with the actual probable loss in the event of breach.[368] Where recovery would be "grossly excessive", "punitive" or "disproportionate and unreasonable when compared with the damages sustained or which would be recoverable through an action in the Courts for breach of the covenant in question", the clause is labelled a penalty and held to be unenforceable.[369]

Applying the venerable rule, there have been numerous instances in which contractual provisions have been struck down as penalties. Often it has been a simple matter of arithmetic, with stipulated remedy provisions resulting in damages many times what would be awarded as expectation damages being held to be penalty clauses.[370] Acceleration clauses have often been struck down as penalty clauses, although this has been done on a case-by-case basis and there has never been a blanket rule that acceleration clauses were unenforceable as penalty clauses.[371]

1 Canadian Contractual Interpretation Law 9.189.18.4 (2020)

9.18.4 The modified approach: stipulated remedy clauses specifying damages are enforceable unless they are unconscionable

Despite being "venerable", as a result of a series of decisions rendered by provincial appellate courts since the mid-1990s, there is a strong tendency away from the historical approach to penalty clauses. The approach that is now generally favoured is to enforce a stipulated remedy clause specifying damages unless the provision is unconscionable. However, some vestiges of the venerable rule remain. Not all courts that have looked at the issue have been willing to eschew the venerable rule. Moreover, while the framework for the analysis is completely different (focused on unconscionability and whether it is appropriate to grant relief from forfeiture, rather than on the question of whether the clause constituted a genuine pre-estimate of damages at the time of contracting), much of the former law of penalty clauses survives, as unconscionability is often assessed by reference to what formerly would have been considered to be a penalty clause.

The venerable common law rule began to crumble with a simple observation by the Supreme Court of Canada that striking down penalty clauses is an interference with freedom of contract, which is difficult to justify unless there is oppression. The observation came in *J.G. Collins Insurance Agencies Ltd. v. Elsley Estate*:[372]

> It is now evident that the power to strike down a penalty clause is a blatant interference with freedom of contract and is designed for the sole purpose of providing relief against oppression for the party having to pay the stipulated sum. It has no place where there is no oppression.[373]

This observation was then picked up in subsequent cases,[374] and "[j]udicial enthusiasm for the refusal to enforce penalty clauses … waned in the face of a rising recognition of the advantages of allowing parties to define for themselves the consequences of breach".[375]

As a result of the concern about interference with freedom of contract, a number of cases have adopted a modified rule that stipulated remedy clauses are to be enforced unless doing so would be unconscionable. The Alberta and British Columbia Courts of Appeal were first to adopt the new rule, doing so in 1994. The Alberta case, *Fern Investments Ltd. v. Golden Nugget Restaurant (1987) Ltd.*,[376] relied on *obiter dicta* in a 1960s decision of the Supreme Court of Canada[377] and the comment in *Elsley* that striking down a penalty clause is a blatant interference with freedom of contract to conclude that a penalty clause should be enforced unless it would be unconscionable or oppressive to give effect to it, having regard for the circumstances of the case at the time when enforcement is sought.[378] The British Columbia case, *Prudential Insurance Co. of America v. Cedar Hills Properties Ltd.*,[379] came to the same conclusion, remarking that a penalty clause is part of the parties' bargain and that it is an unwarranted interference with freedom of contract to strike down such a provision in the absence of oppression. The New Brunswick Court of Appeal adopted the new rule two years later, in 1996.[380]

The Ontario Court of Appeal appeared to adopt the new approach in 2005 in *Peachtree II Associates — Dallas L.P. v. 857486 Ontario Ltd.*,[381] although as noted below a subsequent decision from that court has cast some doubt on whether the venerable common law rule is really gone.

Peachtree II noted that parallel to the common law rule that a penalty clause is unenforceable is a distinctive equitable rule, namely that penal forfeitures will be relieved against where enforcement would be inequitable

and unconscionable. It stated that the common law rule is not an iron-clad rule precluding enforcement of all penalty clauses, instead applying the equitable rule such that penalty clauses are enforced as forfeitures where enforcement would not be unconscionable. It cited a number of reasons for adopting the equitable rule over the common law one, including the policy of upholding freedom of contract.[382] Thus "courts should, whenever possible, favour analysis on the basis of equitable principles and unconscionability over the strict common law rule pertaining to penalty clauses".[383]

Peachtree II ended with a statement that the court's conclusion on the relief from forfeiture analysis rendered it unnecessary to consider "whether there is a residual discretion to enforce a payment that would be a penalty under the common law rule", deciding to "leave that question to another day".[384] In *Birch v. Union of Taxation Employees, Local 70030*,[385] another panel of the Ontario Court of Appeal latched onto that statement to cast doubt on whether the common law "venerable rule" has really been abolished. *Birch* characterized *Peachtree II*'s comments about the common law rule as *obiter dicta*, and declared that there should be no "sweeping pronouncement that the rule is no longer applicable to the law of contract generally".[386] *Birch* nonetheless went on to apply an unconscionability analysis. As a result, the precise state of the law was left somewhat unclear. To muddy the waters further, a 2008 decision of the Saskatchewan Court of Appeal also appears to follow the old common law rule.[387]

Despite the doubts expressed in *Birch* and reflected in the Saskatchewan case, the equitable analysis based on unconscionability should be regarded as the prevailing one. The conclusion in *Birch* that *Peachtree II*'s comments as to the preferability of the unconscionability approach were mere *obiter* seems to be a very narrow reading of *Peachtree II*. Moreover, there is not much to commend the common law rule, aside perhaps from its status as "venerable". In an era in which restrictions on limitation of liability provisions are generally considered too much of an interference with freedom of contract such that parties are generally permitted to stipulate their own remedies for breach even if the result is less liability than would otherwise prevail,[388] it is difficult to see why contracting parties should not also be permitted to stipulate a remedy that might result in more liability than would otherwise prevail. The new rule based on equity and unconscionability eliminates one of the relatively rare instances in the law of contractual interpretation in which interpretive accuracy is subordinated to some other policy goal, and aligns the interpretation of penalty clauses with contract law generally: such clauses are enforced according to the parties' intentions as expressed by the words they have used as understood in their proper context, unless there is a reason drawn from the substantive law of contract (*i.e.*, unconscionability) not to enforce the parties' bargain.

Even if the new approach is applied, the old law regarding penalty clauses remains relevant because it may be used to ascertain whether relief from forfeiture is warranted. Thus it has been held that a forfeiture provision becomes a penalty when it goes beyond a genuine pre-estimate of the damages, that where a stipulated remedy clause can be characterized in law as being a penalty it may be subject to relief from forfeiture, and that the requirements for relief from forfeiture are "generally, that the sum is out of all proportion to the damage suffered i.e. a penalty; and second, that it would be unconscionable for the vendor to retain the money".[389]

Footnotes — 9.18:

356 See section 9.14.

357 [2016] B.C.J. No. 535, 2016 BCCA 128 at para. 23 (B.C.C.A.), leave to appeal refused [2016] S.C.C.A. No. 206 (S.C.C.).

358 *Peterson v. 446690 BC Ltd. (c.o.b. Seymour Arm Hotel & Restaurant)*, [2017] B.C.J. No. 2301, 2017 BCCA 394 at para. 25 (B.C.C.A.).

359 [2015] O.J. No. 2015, 2015 ONCA 276 at para. 34 (Ont. C.A.), leave to appeal refused [2015] S.C.C.A. No. 270 (S.C.C.).

360 *Peachtree II Associates — Dallas L.P. v. 857486 Ontario Ltd.*, [2005] O.J. No. 2749, 76 O.R. (3d) 362 at para. 23 (Ont. C.A.), leave to appeal refused [2005] S.C.C.A. No. 420 (S.C.C.). However, for a compelling argument that the common law rule is not as simple and as blunt as stated in *Peachtree II*, see *Mortgage Makers Inc. v. McKeen*, [2009] N.B.J. No. 306, 349 N.B.R. (2d) 115 at paras. 17-39 (N.B.C.A.).

361 *Canadian General Electric Co. v. Canadian Rubber Co. of Montréal*, [1915] S.C.J. No. 58, 52 S.C.R. 349 at 351 (S.C.C.).

362 *Prudential Insurance Co. of America v. Cedar Hills Properties Ltd.*, [1994] B.C.J. No. 3055, 100 B.C.L.R. (2d) 312 at para. 16 (B.C.C.A.), citing *Dunlop Pneumatic Tyre Co. v. New Garage and Motor Co.*, [1915] A.C. 79 (H.L.).

363 [1974] S.C.J. No. 151, [1976] 1 S.C.R. 319 (S.C.C.).

364 *Ibid.*, at 330. [Emphasis added.]

365 *Ibid.*, at 331.

366 *Prudential Insurance Co. of America v. Cedar Hills Properties Ltd.*, [1994] B.C.J. No. 3005, 100 B.C.L.R. (2d) 312 at para. 16 (B.C.C.A.).

367 *Dezcam Industries Ltd. v. Kwak*, [1983] B.C.J. No. 2349, 44 B.C.L.R. 105 at para. 14 (B.C.C.A.) and *Federal Business Development Bank v. Eldridge*, [1986] N.B.J. No. 140, 76 N.B.R. (2d) 399 (N.B.C.A.).

TAB 24

PENALTY CLAUSES IN CANADIAN CONTRACT LAW*

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Abstract

This article critically examines the current state of the law of penalty clauses in Canada. First, while many commentators regard the law of penalty clauses as being relatively settled, this article tracks the development of two competing lines of authority. This article contends that lower courts' decisions across Canada have been split between (1) the traditional standard regarding the non-enforceability of true penalty clauses, which stems from the House of Lords' decision in Dunlop Pneumatic Tyre Co. Ltd. v. New Garage and Motor Co. Ltd., *and (2) a more recent oppression-based standard under which courts have been increasingly reluctant to strike down supra-compensatory penalty clauses, which has emerged from the Supreme Court of Canada's decision in* J.G. Collins Insurance Agencies Ltd. v. Elsley Estate. *Second, this article examines whether the recent authority in favour of greater enforceability of penalty clauses is a positive change in the law of penalty clauses. While many authors have argued in favour of greater enforceability of penalty clauses, this article argues that there are policy reasons in favour of the traditional position of stricter scrutiny of penalty clauses. Taking these policy considerations into account, this article proposes a reformulated test of the enforceability of such clauses based on* Dunlop.

Résumé

Cet article examine d'une manière critique l'état présent de la loi sur les clauses de pénalité au Canada. Premièrement, bien que plusieurs commentateurs considèrent la loi sur les clauses de pénalité comme étant relativement établie, cet article trace le développement de deux types d'autorités qui sont en compétition. Cet article suggère que les décisions des tribunaux inférieurs à travers le Canada sont divisées entre (1) le standard traditionnel de non validité des clauses de pénalités véritables, qui dérive de la décision de la Chambre des Lords dans l'arrêt Dunlop Pneumatic Tyre Co. Ltd. v. New Garage and Motor Co. Ltd., *et (2) un plus récent standard d'oppression sous lequel les tribunaux ont été de plus en plus réticents à invalider des clauses de pénalités supra compensatoires, standard qui émergea de la décision de la Court Suprême du Canada dans l'arrêt* J.G. Collins Insurance Agencies Ltd. v. Elsley Estate. *Deuxièmement, cet article ce penche sur les autorités récentes en faveur d'une plus grande applicabilité des clauses de pénalité et se demande si elles constituent un développement positif à la loi sur les clauses de pénalité. Bien que plusieurs auteurs se prononcent en faveur d'une plus grande applicabilité des clauses de pénalité, cet article suggère qu'il existe des raisons politiques en faveur de la position traditionnelle d'examen plus minutieux des clauses de pénalité. Prenant en compte ces considérations politiques, cet article propose un test reformulé, basé sur l'arrêt* Dunlop, *sur l'applicabilité de ces clauses.*

I INTRODUCTION

Canadian contract law and the British contract law from which it developed have generally tended to support the ability of individuals to enter into contracts on their own terms. One notable exception to this general principle of freedom of contract has been the scrutiny with which courts have treated certain contractual arrangements specifying in advance the damages which will flow from a breach of contract. More specifically, courts have often been quite willing to strike down stipulated damages clauses which require the breaching party to a contract to pay a specified sum of money to the non-breaching party. In this respect, courts have traditionally made a distinction between liquidated damages clauses, which are enforceable, and penalty clauses, which are not enforceable. Judicial scrutiny in this area has struck many as anomalous, and it seems *prima facie* that the courts' willingness to strike down penalty clauses is an unreasonable and unprincipled interference with freedom of contract.

Despite a rather substantial volume of case law relating to the enforceability of such clauses in Canadian courts in recent years, substantial legal commentary on this area of contract law has been limited. Texts on Canadian contract law have devoted only a few pages to examining select historically important cases and briefly articulating a few policy arguments in favour of upholding penalty clauses, and no academic articles have appeared on the topic of penalty clauses in Canadian law in the last three decades. A few brief comments on the topic have appeared in more specialized reviews, but these have tended to focus on some very specific aspect of penalty clauses or on their application in a particular industry.[1] Perhaps this is because of a general perception that, as claimed by Hunt J.A. of the Alberta Court of Appeal, the principles governing this area of law are "long standing and relatively free of controversy".[2] This article will demonstrate the incorrectness of this view and will seek to contribute to the scholarly debate on a topic which has been undeservedly lacking in attention, at least from a strictly legal perspective.

Following this introduction, part two of this article will review in some detail the Canadian case law on penalty clauses, primarily focusing on the developments which have occurred since the Supreme Court's decision in *J.G. Collins Insurance Agencies Ltd. v. Elsley Estate* in 1978.[3] This article will argue that rather than being settled, the law on the enforceability of such clauses is actually in a state of flux, as two distinct yet muddled strands of case law have emerged. Moreover, this article will posit that the trend in the Canadian law on penalty clauses has been a gradual movement away from the traditional position articulated in *Dunlop Pneumatic Tyre Co. Ltd. v. New Garage and Motor Co. Ltd.* and will

1 Barry Tarshis, "Loan Exit Fees: *Pike v. Bel-Tronics Co.*" (2001) 17 B.F.L.R. 259; Warren Mueller, "Liquidated Damages" (2006) 49 C.L.R. (3d) 10; Paul Dollak, "Commentary: The Law of Penalty Clauses is 'unsettled and developing'" (14 October 2005) 25:22 *The Lawyers Weekly* 10.

2 *32262 B.C. Ltd. v. See-Rite Optical Ltd.*, 1998 ABCA 89, [1998] A.J. No. 312 at para. 11. [*See-Rite Optical*].

3 *J.G. Collins Insurance Agencies Ltd. v. Elsley Estate*, [1978] 2 S.C.R. 916 [*Elsley*].

conclude that courts are increasingly reluctant to strike down stipulated damages clauses, even if they could be characterized as penalty clauses according to the traditional test.[4]

Following the arguments relating to the development of the law presented in part two, part three of this article will critically assess the policy arguments related to the enforceability of stipulated damages clauses. While there has been significant academic commentary, particularly from the law and economics movement, on the policy considerations related to the enforceability of stipulated damages clauses, such analysis has often been undertaken in the abstract without application to the more pertinent issue of deciding between competing legal principles governing the enforceability of such clauses. This section will fill this lacuna by situating the policy discussion in the context of the two competing principles discussed in the previous section, and it will argue that many of the policy considerations underlying the enforceability of stipulated damages clauses suggest that the traditional *Dunlop* approach is superior to the *Elsley* approach.

The fourth part of this article will synthesize the conclusions of the discussion in the previous section with the aim of articulating the appropriate legal framework that courts should be employing in their analysis of the enforceability of stipulated damages clauses. This part will posit that courts should apply a test of enforceability similar to the test articulated in *Dunlop* under which courts refuse to enforce supra-compensatory penalty clauses. Rather than providing wholesale support for the framework outlined in *Dunlop*, however, this article will propose a modified framework which remains based on the *Dunlop* approach but also incorporates some of the policy considerations outlined in the third part. Specifically, this section will argue that stipulated damages clauses should generally be enforced where it would be difficult to determine exactly what truly compensatory damages would be, that is, where damages cannot be easily quantified at the time of breach or there is evidence that the non-breaching party has a particularly high subjective valuation of performance of the contract. A fifth part will then serve as a brief conclusion.

A few points of clarification must be made from the outset about the scope of this article. This article deals with stipulated damages clauses which require a party to pay a certain amount of money upon a breach of contract. More specifically, this article is primarily concerned with the enforceability of supra-compensatory stipulated damages clauses, commonly referred to as penalty clauses; such clauses are frequently litigated and are the most contentious in academic work on the topic. By contrast, this article does not deal with forfeitures and deposits, which are clauses requiring a party to forfeit any claim to certain money already paid upon a breach of contract. Historically, and arguably irrationally, Anglo-Canadian law has made a distinction between penalty clauses and forfeitures; even more problematic is the fact that in many instances courts have used the term "penalty" to describe both. This article, however, will only deal

4 *Dunlop Pneumatic Tyre Co. Ltd v. New Garage and Motor Co. Ltd.*, [1915] A.C. 79 (H.L.) [*Dunlop*].

with penalty clauses, as the law on this point is already sufficiently muddled without introducing the further complication of forfeitures.

II THE EVOLUTION OF THE LAW OF STIPULATED DAMAGES CLAUSES IN CANADA

This section provides a comprehensive overview of significant developments in the law of stipulated damages in Canada. In doing so, this section attempts to highlight two points. First, in contrast to the view of Hunt J.A. noted above, this part will demonstrate that the law on penalty clauses is not settled and that there are currently two very different lines of case law being applied by Canadian courts in testing the enforceability of such clauses. It will be posited that although there is no judicial consensus, the general trend has been towards the greater enforceability of penalty clauses. Second, by analyzing a number of cases underlying each of the doctrines, this section will demonstrate that, even within each of the lines of case law, there is significant doctrinal confusion about the proper test to be applied in determining the enforceability of stipulated damages clauses. Thus, this section will highlight the significant uncertainty which currently plagues the Canadian law of stipulated damages.

Dunlop and the Traditional Doctrine

The House of Lords' decision in *Dunlop Pneumatic Tyre Co. Ltd. v. New Garage and Motor Co. Ltd.* represents the traditional starting point for Canadian courts' analyses of penalty clauses.[5] The facts of *Dunlop* are relatively straight-forward and well-known. Dunlop and New Garage entered into an agreement whereby Dunlop would provide New Garage with a variety of its products. That agreement contained clauses prohibiting New Garage from reselling those products to certain parties or at certain prices, and it contained a clause wherein New Garage agreed to pay £5 for each item sold in breach of the contract. At trial, it was concluded that the clause in question was a liquidated damages clause, but this was reversed at the Court of Appeal, which concluded that it was a penalty clause. On further appeal to the House of Lords, the Court concluded that it was a liquidated damages clause rather than a penalty clause.

The facts of the case and the courts' proper characterization of the clause are less important than the framework of analysis outlined by Lord Dunedin in his judgment in this case. As will be seen below, this framework has been cited extensively by Canadian courts, and at least until 1978, this decision provided the dominant paradigm for determining the enforceability of penalty clauses. Because of its importance in this respect, the relevant portions of that decision deserve reproduction here, as these passages have been integral to Canadian courts' reasoning in numerous cases dealing with penalty clauses. Lord Dunedin's delineation in *Dunlop* of the rules relating to penalty clauses, edited for clarity, is as follows:

---

5 *Ibid.*

> (i) Though the parties to a contract who use the words "penalty" or "liquidated damages" may prima facie be supposed to mean what they say, yet the expression used is not conclusive. The court must find out whether the payment stipulated is in truth a penalty or liquidated damages.
>
> (ii) The essence of a penalty is a payment of money stipulated as in terrorem of the offending party; the essence of liquidated damages is a genuine covenanted pre-estimate of damage.
>
> (iii) The question whether a sum stipulated is penalty or liquidated damages is a question of construction to be decided upon the terms and inherent circumstances of each particular contract, judged of as at the time of the making of the contract, not as at the time of the breach.
>
> (iv) To assist this task of construction various tests have been suggested, which, if applicable to the case under consideration, may prove helpful or even conclusive. Such are:
>
> > It will be held to be a penalty if the sum stipulated for is extravagant and unconscionable in amount in comparison with the greatest loss which could conceivably be proved to have followed from the breach;
> >
> > It will be held to be a penalty if the breach consists only in not paying a sum of money, and the sum stipulated is a sum greater than the sum which ought to have been paid. This, though one of the most ancient instances, is truly a corollary to the last test.
> >
> > There is a presumption (but no more) that it is a penalty when "a single lump sum is made payable by way of compensation, on the occurrence of one or more or all of several events, some of which may occasion serious and others but trifling damages". On the other hand:
> >
> > It is no obstacle to the sum stipulated being a genuine pre-estimate of damage that the consequences of the breach are such as to make precise pre-estimation almost an impossibility. On the contrary, that is just the situation when it is probable that pre-estimated damage was the true bargain between the parties.[6]

While this framework is relatively extensive and provides a number of alternative and somewhat disconnected tests, the bulk of this reasoning was distilled in Canadian law to the proposition, expressed by the Supreme Court of Canada in *Canadian General Electric Co. v. Canadian Rubber Co. of Montreal*, that "a penalty is the payment of a stipulated sum on breach of the contract, irrespective of the damage sustained. The essence of liquidated damages is a genuine covenanted pre-estimate of damage".[7] Thus, between 1915 and 1978, the test that courts purported to employ for determining whether a stipulated damages clause was

6 *Ibid.* at 87-88.

7 *Canadian General Electric Co. v. Canadian Rubber Co. of Montreal* (1915), 52 S.C.R. 349, [1915] S.C.J. No. 58 [*Canadian General Electric*].

enforceable was whether it was a genuine pre-estimate of damages.[8] In employing this test, the primary concern of the courts seemed to be one of ensuring fair compensation to the non-breaching party: clauses intended to be compensatory were enforced under this test, while clauses intended to provide punitive or supra-compensatory damages were struck down.

Even following the 1978 decision of the Supreme Court in *Elsley*, a significant body of case law has continued to scrutinize stipulated damages clauses primarily on the basis of the "genuine pre-estimate" test articulated in *Dunlop*. A brief overview of some of the more recent case law is necessary to highlight the continued relevance of the *Dunlop* approach. Typical of this reasoning is the decision in *Newman, Hill, Duncan & Lacoursiere v. Murray*, wherein the British Columbia Court of Appeal struck down as an unenforceable penalty a clause in a non-compete contract which specified that for every customer of the firm for which an accountant undertook work in violation of the non-compete clause, the accountant would have to pay damages equal to 150 percent of the fees charged by that firm to that client in the past twelve months.[9] The Court concluded that this was not a genuine pre-estimate of damages.[10]

A similar type of clause was considered by Weiler J.A. of the Ontario Court of Appeal in *Infinite Maintenance Systems Ltd. v. ORC Management Ltd.* In that case, the plaintiff provided maintenance and janitorial services, and in its contract with the defendant, it specified that if the defendant hired any of the plaintiff's employees within twelve months of the termination of the contract, the defendant would be liable for the gross value of one year of the maintenance contract. While noting that both parties entering the contract were represented by "sophisticated business persons", the Court nevertheless found the contract not to be a genuine pre-estimate of damages but rather an unenforceable penalty clause.[11]

Justice Panet of the Ontario Superior Court of Justice also struck down a penalty clause in *1259121 Ontario Inc. v. Canada Trust Co.*, where he found that a clause in a mortgage, which imposed on the borrowers a fee of $15,000 whenever the lender had to begin collection or legal proceedings, was not a genuine pre-estimate of damages and was thus unenforceable.[12] Similarly, using these

8 For examples of Canadian courts applying this approach, see *Janse-Mitchell Construction Co. v. Calgary (City)*, [1919] 3 W.W.R. 150; *Reimer v. Rosen* (1919), 29 Man. R. 241, [1919] 1 W.W.R. 429, 45 D.L.R. 1; *Shatilla v. Feinstein* (1923), 16 Sask. L.R. 454, [1923] 1 W.W.R. 1474, [1923] 3 D.L.R. 1035; *Inch v. Farmers' Co-operative Dairy Co.*, 15 M.P.R. 315, [1941] 2 D.L.R. 27; *Waugh v. Pioneer Logging Co.*, [1949] S.C.R. 299, [1949] 2 D.L.R. 577; *Pitman v. Pletzke*, [1949] 1 W.W.R. 808, [1949] 2 D.L.R. 219; *Neonette Sign Co. v. Stankovic*, 66 B.C.L.R. 269; *Canadian Acceptance Corp. v. Regent Park Butcher Shop Ltd.* (1969), 13 C.B.R. (N.S.) 8, 67 W.W.R. 297, 3 D.L.R. (3d) 304.

9 *Newman, Hill, Duncan & Lacoursiere v. Murray*, [1988] B.C.W.L.D. 75, [1987] B.C.J. No. 2326.

10 For additional cases where stipulated damages clauses were struck down in the context of non-compete agreements, see *Fox Estate v. Stelmaszyk*, [2002] O.J. No. 5083, 119 A.C.W.S. (3d) 751 (Sup. Ct.); *Community Credit Union Ltd. v. Ast.*, 2007 ABQB 46, 72 Alta. L.R. (4th) 160, [2007] A.W.L.D. 1181, [2007] 5 W.W.R. 300, 28 B.L.R. (4th) 26.

11 *Infinite Maintenance Systems Ltd. v. ORC Management Ltd.*, 139 O.A.C. 331, 2001 C.L.L.C. 210-021, 5 C.P.C. (5th) 241 at para. 7 [*Infinite Maintenance Systems*].

12 *1259121 Ontario Inc. v. Canada Trust Co.*, 30 B.L.R. (4th) 193 (Ont. S.C.J.).

principles, the New Brunswick Court of Appeal in *F.B.D.B. v. Eldridge* struck down as a penalty a commitment fee on a mortgage equal to roughly 3 percent of the value of the loan.[13] A clause wherein a contractor was to pay $200 per day for late completion of a home was also found to be an unenforceable penalty under these principles.[14]

While most of the cases of this period applying the *Dunlop* doctrine ultimately struck down the stipulated damages clause in question as an unenforceable penalty, there are some cases of courts upholding such clauses as valid liquidated damages clauses. For example, in *Nystoruk v. Precision Diversified Services Ltd.*, a clause in an employment contract which provided for six months' salary upon termination was found to be a genuine pre-estimate of damages and thus enforceable.[15] Similarly, in *Tkachuk Farms Ltd. v. LeBlanc Auction Service Ltd.*, Wilkinson J. applied the *Dunlop* test and upheld a liquidated damages provision, primarily because of the significant difficulty assessing damages and because the clause in question was not unreasonable.[16] Taking these cases as a whole, however, it is quite clear that the courts applying the test formulated in *Dunlop* have been quite willing to exercise their power to strike down such stipulated damages clauses.

In summarizing the case law above, four points are worth noting about the application of the *Dunlop* test in Canadian law. First, while Canadian courts have consistently used the language of "genuine" pre-estimate in determining the enforceability of a stipulated damages clause, the focus of the enforceability analysis has instead primarily been on the magnitude of the stipulated damages rather than on the intention of the parties at the time of contract formation. This was explicitly recognized by the Supreme Court of Canada in *H.F. Clarke Ltd. v. Thermidaire Corp.*, where Laskin C.J. noted that it was the reasonableness of the clause rather than the intention of the parties which was paramount.[17] Thus, the

13 *F.B.D.B. v. Eldridge* (1986), 76 N.B.R. (2d) 399, 192 A.P.R. 399 (C.A.) [*Eldridge*].

14 *Homes By Wallace Ltd. v. Werklund* (1992), 130 A.R. 87, 1 C.L.R. (2d) 53 (Alta. Q.B.).

15 *Nystoruk v. Precision Diversified Services Ltd.*, 2003 ABQB 222, 13 Alta. L.R. (4th) 284, [2003] 6 W.W.R. 583.

16 *Tkachuk Farms Ltd. v. LeBlanc Auction Service Ltd.*, 2006 SKQB 536, [2007] 2 W.W.R. 662, 26 B.L.R. (4th) 69, 290 Sask. R. 203 [*Tkachuk*]. An appeal from this decision was dismissed though. There was no consideration of the stipulated damages provision, as the appellant did not appeal the conclusion that the stipulated damages clause was a liquidated damages clause rather than a penalty clause. See *Tkachuk Farms Ltd. v. LeBlanc Auction Service Ltd.*, 2008 SKCA 31, 41 B.L.R. (4th) 29, [2008] 6 W.W.R. 132, 307 Sask. R. 188, 417 W.A.C. 188.

17 *H.F. Clarke Ltd. v. Thermidaire Corp.*, [1976] 1 S.C.R. 319 at 330-31 [*Thermidaire*]: "If all that was involved in determining whether the parties had agreed on a measure of liquidated damages or on a penalty was the intention of those parties, there could be no quarrel with the result reached at trial and on appeal. Indeed, if that was the case it is difficult to conceive how any penalty conclusion could ever be reached when business men or business corporations, with relatively equal bargaining power, entered into a contract which provided for payment of a fixed sum or for payment pursuant to a formula for determining damages, in case of a breach of specified covenants, including a covenant not to compete.... What the court does in this class of case, as it does in other contract situations, is to refuse to enforce a promise in strict conformity with its terms. The court exercises a dispensing power...

mere fact that parties genuinely intended a stipulated damages clause to be an enforceable liquidated damages clause is not determinative. Rather, the primary criterion of enforceability is whether the stipulated damages clause is roughly in line with the pre-estimated damages. The underlying concern of courts, therefore, has been to enforce clauses which appeared to be compensatory while refusing to enforce clauses which were not compensatory.

Second, there has been some ambiguity in the case law as to whether the test of enforceability should compare the stipulated damages clause with (1) the anticipated damages resulting from a breach at the time of the contract formation, or (2) the actual damage suffered at the time of the breach. The decision in *Dunlop* explicitly favours the former assessment, and most Canadian decisions have engaged in that type of analysis. Nevertheless, several more recent decisions based on the *Dunlop* framework, including *Thermidaire*, have held that it is appropriate to compare the stipulated damages clause with the damages actually sustained as a result of the breach.[18] In practice, the two approaches will frequently yield similar conclusions, though they may yield different conclusions where circumstances change drastically and unexpectedly between the time of contract formation and the time of breach.

Third, and perhaps obviously from the above discussion, courts employing the *Dunlop* framework have subjected such stipulated damages clauses to significant scrutiny. While some cases have held that "the onus of establishing that the clause is a penalty is on...the person seeking to set it aside",[19] other cases have seemed to at least implicitly switch the burden to the party seeking to uphold the clause.[20] While many decisions have not actually discussed on which party the burden lies, even where the burden is not explicitly placed on the party seeking to uphold the stipulated damages clause, the reasoning and outcomes in the above cases demonstrate significant reluctance on the part of courts to uphold stipulated damages clauses.

Finally, the above applications of the *Dunlop* test demonstrate that it is a relatively rigid test under which the enforceability of a stipulated damages clause rests entirely upon a comparison between the amount of the stipulated damages

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because the parties' intentions, directed at the time to the performance of their contract, will not alone be allowed to determine how the prescribed sum or the loss formula will be characterized. The primary concern in breach of contract cases... is compensation, and judicial interference with the enforcement of what the courts regard as penalty clauses is simply a manifestation of a concern for fairness and reasonableness, rising above contractual stipulation, whenever the parties seek to remove from the courts their ordinary authority to determine not only whether there has been a breach but what damages may be recovered as a result thereof."

18 *Ibid.* See also *Ashland Scurlock Permian Canada Ltd. v. NESI Energy Marketing Canada Ltd. (Trustee of)* (1998), 61 Alta. L.R. (3d) 218, (sub nom. Ashland Scurlock Permian Canada Ltd. v. NESI Energy Marketing Canada Ltd. (Bankrupt)) 226 A.R. 242, [1999] 1 W.W.R. 364 at paras. 7-9 [*Ashland*].

19 *Infinite Maintenance Systems*, *supra* note 11 at para. 13.

20 *Eldridge*, *supra* note 13 at para. 7. See also *Coco Paving (1990) Inc. v. 882885 Ontario Ltd.*, [2006] O.J. No. 4904 at para. 15. For an overview of similar confusion in American law over which party bears the burden, see Larry DiMatteo, "A Theory of Efficient Penalty: Eliminating the Law of Liquidated Damages" (2001) 38 Am. Bus. L.J. 633 at 664-68.

and the amount of anticipated (and in some cases actual) damages. Thus, it does not take into account the relationship between the parties, the sophistication of the parties agreeing to the contract, or other contextual factors relating to the inclusion of the stipulated damages clause.

Elsley and the Emergence of an Oppression-Based Doctrine

The decision of the Supreme Court of Canada in *J.G. Collins Insurance Agencies Ltd. v. Elsley Estate* represented a major development in the law of penalty clauses in Canada. As will be seen below, the Court's decision in *Elsley* in 1978 spawned a new line of cases with substantially different reasoning and conclusions from the dominant line of reasoning prior to it.

The facts of *Elsley* are straightforward, but they gave rise to a rather unusual legal problem in the context of penalty clauses.[21] In 1956, J.G. Collins Insurance purchased a rival insurance firm, D.C. Elsley Limited, which was prior to that time owned by Elsley. The purchase agreement contained a covenant by Elsley that he would not for ten years engage in the practice of insurance in the relevant geographic area. Liquidated damages were set at $1,000 for each and every breach. By a second agreement, Elsley became employed as a manager of the new insurance firm; this second contract contained another restraint of trade clause whereby Elsley covenanted not to engage in the business of an insurance agent in the area in question while employed at the firm or for five years afterwards. In this contract, liquidated damages were simply set at $1,000. A number of years later, Elsley left the firm and began work as an insurance agent, in breach of the second contract. The interesting fact in this case was that, unlike in many cases, it was the party who had breached the contract who sought to take advantage of it as a liquidated damages clause. Since actual damages exceeded the $1,000 stipulated in the contract, it was beneficial for Elsley to try to invoke the benefit of the liquidated damages clause.

The Supreme Court found that the clause was valid, and it thereby ruled that Elsley's damages were limited to $1,000. Interestingly, contrary to certain earlier jurisprudence, the Court ruled that "[i]n the context of the present discussion of the measure of damages, the result is that an agreed sum payable on breach represents the maximum amount recoverable *whether the sum is a penalty or a valid liquidated damages clause*".[22] A narrow reading of *Elsley* thus stands for the interesting yet by no means revolutionary proposition that clauses which stipulate damages may serve to limit liability, whether they are characterized as penalty clauses or liquidated damages clauses.[23]

While this ratio may seem to have rather limited impact upon penalty clauses in general, the importance of *Elsley* has stemmed not from this ratio, but rather from the following more general dictum in Dickson J.'s judgment:

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21 *Elsley*, *supra* note 3.

22 *Ibid.* at 937 [emphasis added].

23 McCamus suggests that the decision in *Elsley* is indeed limited in this respect and makes no suggestion of a general rule of oppression-based analysis stemming from *Elsley*. John McCamus, *The Law of Contracts* (Toronto: Irwin Law, 2005) at 903-04.

> It is now evident that the power to strike down a penalty clause is a blatant interference with freedom of contract and is designed for the sole purpose of providing relief against oppression for the party having to pay the stipulated sum. It has no place where there is no oppression.[24]

These words, taken at their most general, suggest a much less stringent test for non-enforceability of penalty clauses than was developed in *Dunlop* and *Canadian General Electric*. They suggest that even if a damages clause is not a liquidated damages clause in the *Dunlop* sense of being a genuine pre-estimate of damages, it will be enforceable if there is no oppression. Thus, formally, the dictum in *Elsley* seems to have added on a second layer of analysis, as it suggested that even if the clause was found to be a penalty clause within the definition articulated by *Dunlop*, it should be enforced unless there is oppression.[25]

Following the Supreme Court's decision in *Elsley*, the law on penalty clauses entered a period of uncertainty, as courts grappled with the impact of the oppression-based doctrine articulated in *Elsley* on the traditional legal framework exemplified by *Dunlop*. Many court decisions—as well as some of the most highly-esteemed academic commentators on contract law[26]—have continued to treat the law of penalty clauses as being largely that articulated by *Dunlop*. Yet, as will be demonstrated below, this view is less tenable than it once was, as courts have over time increasingly refocused their analysis on an examination of whether a penalty clause is oppressive or unconscionable rather than whether it is a genuine pre-estimate of damages. While this has by no means been a uniform trend and decisions continue to be divided between the two doctrinal bases, it is

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24 *Elsley*, *supra* note 3 at 937.

25 However, as shown in the cases discussed below, many courts applying this standard have seemed to largely bypass the first step and approached the question of enforceability primarily from the twin issues of oppression and unconscionability.

26 See Stephen Waddams, *The Law of Contracts*, 5th ed. (Aurora, ON: Canada Law Book, 2005) at 321 (arguing that while the underlying approach to these decisions must be recognized to be the fairness of the provision, courts have instead primarily used test of enforceability of whether the clause is a genuine pre-estimate of damages); G.H.L. Friedman, *The Law of Contract*, 5th ed. (Toronto: Thomson Canada, 2006) at 771 ("In *Dunlop Pneumatic Tyre Co. v. New Garage & Motor Co.*, Lord Dunedin laid down some general rules for the guidance of courts. These were culled from earlier decisions, and have been accepted by courts in Canada, which, indeed operated on those principles before 1915 and still do so."); McCamus, *supra* note 23 at 898-900. The opposite view has been suggested by Swan, who argues that *Dunlop* could be interpreted as holding that only "extravagant and unconscionable" penalty clauses will be struck down. See John Swan, *Canadian Contract Law*, 1st ed. (Canada: LexisNexis Canada, 2006) at 715-20. While it is true that the House of Lords did use the words "extravagant and unconscionable", its focus was not on whether the sum was extravagant and unconscionable, but rather whether "the sum stipulated for is extravagant and unconscionable in amount in comparison with the greatest loss which could conceivably be proved to have followed from the breach". While similar, the House of Lords' formulation places the analysis of unconscionability within the question of whether the agreed sum was a genuine pre-estimate of damages. Indeed, Canadian courts prior to *Elsley* typically employed the test of whether it was a genuine pre-estimate rather than simply using the analysis of unconscionability per se. Thus, Swan's view of the pre-1978 case law seems to be largely incorrect. See the cases cited above, *supra* note 8.

evident that there has been at least a general trend towards an oppression-based analysis of penalty clauses, as a number of decisions have seized on Dickson J.'s dictum in *Elsley* and have developed a line of case law wherein the enforceability of penalty clauses depends on an analysis of oppression and unconscionability. Employing this analysis, courts have on a number of occasions enforced clauses that would have been struck down under the *Dunlop* test. Indeed, the reasoning in the following cases shows not only how the framework of analysis of enforceability of such clauses is substantially different from the *Dunlop* approach, but also how courts applying such reasoning have been much more reluctant to strike down such clauses.

In *Nortel Networks Corp. v. Jervis*, Rivard J. of the Ontario Superior Court of Justice considered a case where an employee of Nortel had a contract for stock options which specified that, upon taking employment with a competitor within a specific time frame, the employee would be required to disgorge the profit made from those stock options.[27] Justice Rivard accepted that it was a penalty clause, but applying the test in *Elsley*, he found that there was no oppression in this case, and thus he declined to give relief from the penalty. This finding of a lack of oppression was partially based on the fact that Jervis was "sophisticated" with respect to these matters as well as the fact that the amount disgorged was merely equal to Jervis's profit.[28] This situation clearly demonstrates the difference between the *Elsley* approach and the *Dunlop* test, as under the *Dunlop* test, the stipulated damages clause would not have been enforced, due to Rivard J.'s acceptance that the clause was a penalty clause.

In *Redfearn v. Elkford (District)*, Melnick J. of the British Columbia Supreme Court examined the situation of an individual whose employment contract specified that if he was terminated, he was entitled to full salary and benefits until the end of his term.[29] While Melnick J. cited the above quoted portions of both *Dunlop* and *Elsley*, he did not actually consider whether the liquidated damages constituted a genuine pre-estimate of the damages, but rather the primary consideration seems to have been that the amount was not unconscionable or oppressive.

In *Global Entertainment v. Yeo*, the Alberta Provincial Court considered another restraint of trade contract.[30] In that case, the defendant hired a disc jockey provided by the plaintiff, and a condition in that contract was that the defendants would be liable to a service fee of $5,000 if they hired the disc jockey directly within 12 months after the agreement between the plaintiff and the defendant ended. The defendants breached the contract and hired the disc jockey

27 *Nortel Networks Corp. v. Jervis* (2002), 33 C.C.P.B. 71, 18 C.C.E.L. (3d) 100 (Ont. S.C.J.).

28 *Ibid.* at 47-50; for an earlier Ontario decision applying the *Elsley* standard to a stipulated damages clause in another non-compete arrangement, see *Meunier v. Cloutier* (1984), 46 O.R. (2d) 188, 9 D.L.R. (4th) 486, 1 C.P.R. (3d) 60 at para. 21 ("the test is that of unconscionability").

29 *Redfearn v. Elkford (District)* (1998), 34 C.C.E.L. (2d) 161, 49 B.C.L.R. (3d) 172 (S.C.).

30 *Global Entertainment v. Yeo*, 2005 ABPC 117, [2005] A.W.L.D. 2080, [2005] A.W.L.D. 2081, 7 B.L.R. (4th) 213.

directly. Justice Ingram resolved the case on the grounds that this was not a true penalty clause—since there was no clause specifying in the contract that the defendants would not hire the disc jockey directly, the damages were contingent on the happening of some other event rather than on a breach of contract. While this approach is somewhat dubious given the facts of the case, even more important is Ingram J.'s dictum that "if it were [a penalty] it would be valid unless it is unconscionable".[31] This case entirely avoids the *Dunlop* line of reasoning in favour of Dickson J.'s test in *Elsley*.

Similar reasoning prevailed in *Wolfe Chevrolet Oldsmobile Ltd. v. 552234 B.C. Ltd.*, where Barnett J. of the British Columbia Provincial Court observed, on the basis of *Elsley*, that "not every penalty clause must necessarily be struck down".[32] In that case, a clause which imposed a penalty of $5,000 for a breach of an agreement not to export cars to the United States was upheld because there was no unconscionability. It was upheld despite Barnett J.'s acceptance that this was a true penalty, thereby implicitly acknowledging that it would not be enforceable under the *Dunlop* approach. Material to Barnett J.'s judgment was the fact that the defendant was a sophisticated individual who understood that the clause in question was an integral term of the contract. A similar liquidated damages clause considered by the British Columbia Supreme Court in *MTK Auto West Ltd. v. Allen* was found to be an unenforceable penalty clause.[33] The Court's reasoning in this case, however, is similar to that in *Wolfe*, as even though it had determined that the clause in question constituted a penalty within the framework established by *Dunlop*, the Court found it necessary to determine whether it was unconscionable in order to strike it down.[34]

In *Prudential Insurance Co. of America v. Cedar Hills Properties Ltd.*, the British Columbia Court of Appeal considered the case of a loan agreement for $6,400,000 where the agreement provided for an interest standby fee of $100,000.[35] The agreement was executed, but shortly thereafter the borrower repudiated the contract and returned the money. The borrower was required to provide the $100,000 as security prior to signing the loan agreement, but this had not been done, and it was argued at trial that the lender's claim for $100,000 represented an unenforceable penalty clause. While the trial judge accepted this reasoning, the Court of Appeal overturned the decision and enforced the damages

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31 *Ibid.* at para. 21.

32 *Wolfe Chevrolet Oldsmobile Ltd. v. 552234 B.C. Ltd.*, 2004 BCPC 154, 49 B.L.R. (3d) 247, [2004] B.C.W.L.D. 792 [*Wolfe*].

33 *MTK Auto West Ltd. v. Allen*, 2003 BCSC 1613, [2003] B.C.J. No. 2430.

34 *Ibid.* As the Court wrote at para. 22, "A court should not strike down a penalty clause as being unconscionable lightly because it is a significant intrusion on freedom of contract." Importantly, however, the Court's conclusion that the penalty clause was unconscionable seemed to be largely based on the fact that the damages provided by the clause were more than three times the actual damages. Thus, despite the fact that the Court found that the breaching party was sophisticated and quite aware of the consequences of breach, it concluded that the clause was oppressive.

35 *Prudential Insurance Co. of America v. Cedar Hills Properties Ltd.*, [1994] B.C.J. No. 3055 (B.C.C.A.).

clause. In reaching its conclusion, it relied on the analysis of oppression articulated in *Elsley* and found no evidence of such oppression in this case.

In *869163 Ontario Ltd. v. Torrey Springs II Associates Limited Partnership*, Sutherland J. of the Ontario Superior Court considered an appeal from an arbitration award in which the arbitrator concluded that although a clause in a contract was a penalty clause, it should not be struck down.[36] The appellant contended that once the arbitrator found that the clause was a penalty clause, it should have been struck down. Justice Sutherland dismissed the appeal and endorsed a two-step approach to penalty clauses wherein even if a clause can be characterized as a penalty clause, it will only be struck down if it is found to be unconscionable.[37] On further appeal, the Ontario Court of Appeal reached the same result but resolved the case on different grounds. It found that because the clause was properly characterized as a forfeiture clause rather than a penalty clause, the more flexible rules dealing with forfeiture applied, and it was thus within the arbitrator's discretion not to strike down the clause in question.[38] Indeed, the Court of Appeal explicitly refused to rule on whether the arbitrator would have discretionary power to refuse to strike down a genuine penalty clause.[39]

Despite the Court of Appeal's reluctance to endorse conclusively the proposition that penalty clauses are enforceable absent oppression or unconscionability, there are strong reasons in the decision for supposing that the Court nonetheless would have supported this type of analysis. First, in obiter, the Court cited from *Elsley* and clearly favoured an analysis based on unconscionability rather than on the strict common law rule relating to penalty clauses, despite its refusal to decide the case on those grounds.[40] Second, it approved of the argument that courts ought to generally uphold the policy of freedom of contract as a reason why courts should tread lightly in striking down such clauses.[41] Third, and perhaps most importantly, while the Court refused to rule on whether arbitrators had a residual discretion to choose not to enforce penalty clauses, the Court

36 *869163 Ontario Ltd. v. Torrey Springs II Associates Limited Partnership* (2004), 243 D.L.R. (4th) 502, 48 B.L.R. (3d) 184 (Ont. S.C.J.).

37 *Ibid.*

38 *Peachtree II Associates - Dallas, L.P. v. 857486 Ontario Ltd.* (2005), 76 O.R. (3d) 362, 256 D.L.R. (4th) 490, 10 B.L.R. (4th) 44, 200 O.A.C. 159 [*Peachtree*]. For a brief but insightful comment on this decision, see Jan Weir, "Logic may not be the best guide for reforms to the law of penalty clauses" (12 May 2006) 26:2 *The Lawyers Weekly* 9.

39 For a lower court decision holding that *Peachtree* did not modify the *Dunlop* rule, see *Birch v. Union of Taxation Employees, Local 70030*, [2007] O.J. No. 3980 [*Birch*]. However, it is important to note that, despite this holding, Smith J. proceeded to consider at length whether the penalty clauses were unconscionable (At para. 25, he states, "However in view of the comments of Justice Sharpe in the *Peachtree II* decision, I will also consider if the penalties imposed would be enforced if the equitable principle of unconscionability was applied in the circumstances of this case"). He ultimately concluded that the penalty was unconscionable because of the unfairness of bargain and the inequality in bargaining power between the parties.

40 *Peachtree*, *supra* note 38, at para. 32.

41 *Ibid.* at para. 34.

implicitly expanded the scope of analysis based on unconscionability by holding that "courts should, if at all possible, avoid classifying contractual clauses as penalties and, when faced with a choice between considering stipulated remedies as penalties or forfeitures, favour the latter".[42] Thus, although the Court did not explicitly relax the rule on penalty clauses, it attempted to reduce the range of clauses which would be captured by the strict rule.

Cases dealing with acceleration clauses—that is, clauses in ongoing contracts requiring a party to pay the entire future value of the contract immediately upon breach—have also demonstrated the importance of *Elsley*. While historically most courts have tended to enforce such clauses, the law dealing with these clauses was not entirely settled, as some courts have found them to be penalty clauses.[43] Recent case law citing *Elsley*, however, has confirmed the enforceability of these clauses and, more importantly, has articulated more generally the need for oppression or unconscionability in striking down such clauses.[44]

The difference between the *Elsley* test and the *Dunlop* test can be most clearly seen when comparing the application of the two tests in similar factual situations. One set of cases where the divergence between these two competing doctrines has been evident are those cases dealing with contracts where one party has been obligated to pay a certain sum of money and upon breach of contract is obligated to pay a greater sum of money. Under the traditional doctrine, clauses requiring parties to pay a greater amount of money on breach of contract must almost necessarily be penalty clauses, since a genuine pre-estimate of damages in such a case would be the amount of the money which the breaching party was obligated to pay in the first place. Indeed, this is specifically discussed in section (iv)(b) of the test articulated in *Dunlop*, with the Court noting that, "[I]t will be held to be a penalty if the breach consists only in not paying a sum of money, and the sum stipulated is a sum greater than the sum which ought to have been paid."[45]

In *Dezcam Industries Ltd. v. Kwak*, applying the test formulated in *Dunlop*, the British Columbia Court of Appeal found that a clause which required an individual to pay an additional sum of $85,000 upon a contractual failure to pay a sum of $70,000 was void as a penalty.[46] By contrast, other cases have used an unconscionability-based standard in these circumstances and have found such clauses to be valid. In *Hall v. Cooper*, while not directly applying the reasoning in *Elsley*, the trial judge nevertheless used an unconscionability-based standard

42 *Ibid.* at para. 32.

43 Waddams, *supra* note 26 at 326.

44 For example, see *32262 B.C. Ltd. v. Mohawk Oil Co.*, [1995] B.C.J. No. 2892, [1996] B.C.W.L.D. 706 (B.C.S.C.); *Wallace Sign-Crafters West Ltd. v. Delta Hotels Ltd.*, [1994] B.C.J. No. 896, [1994] B.C.W.L.D. 1441; *See-Rite Optical*, *supra* note 2 ("an emphasis on the need to show oppression is apparent" at para. 13); *Carnoustie Holdings Ltd. v. Brennan Educational Supply Ltd.*, 2008 SKQB 257 at paras. 17-35.

45 *Dunlop*, *supra* note 4 at 87.

46 *Dezcam Industries Ltd. v. Kwak*, [1983] B.C.J. No. 2349, 44 B.C.L.R. 105 (C.A.).

to enforce a clause which granted $2,000 in damages for each week a father failed to pay $625 in child support.[47]

A particular manifestation of this line of case law has been that where the contract has specified a particular rate of interest on a loan and has also specified a higher rate to be applied upon default. Decisions in these cases have been similarly diverse from a doctrinal standpoint. The traditional viewpoint articulated in *Dunlop* was followed by the Ontario Court of Appeal in *Place Concorde East Ltd. Partnership v. Shelter Corp. of Canada Ltd.*[48] There, the Court considered a case where the interest payable on promissory notes increased by 4.25 percent upon default, and it concluded that this was an unenforceable penalty for not being a genuine pre-estimate of damages. By contrast, in *Volvo Truck Finance Canada Ltd. v. Premier Pacific Holdings Inc.*, the British Columbia Supreme Court considered a loan agreement which specified an interest rate of 9 to 10 percent which increased to 18 percent upon default.[49] While the Court concluded that the higher interest rate was indeed a penalty clause, it declined to give relief, as it found no evidence of oppression or unconscionability.

Similar factual situations have been those where a contract has specified the interest rate that will apply to late payments or defaults. In *Deer Valley Shopping Centre Ltd. v. Sniderman Radio Sales & Services Ltd.*, the Alberta Court of Queen's Bench concluded that an interest rate of prime plus 5 percent on late payments on a lease was not a genuine pre-estimate of damages and was therefore an unenforceable penalty clause.[50] In a later case decided by the Alberta Court of Queen's Bench, *Markdale Ltd. v. Ducharme*, a 30 percent rate of interest specified in a lease contract was found to be void.[51] While this latter case relied on *Sniderman*, it based its reasoning equally on the fact that a 30 percent rate of interest was oppressive within the framework of *Elsley*, thereby indicating increased judicial sensitivity to the need to show oppression when dealing with penalty clause cases.[52]

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47 *Hall v. Cooper* (1994), 3 R.F.L. (4th) 29 (Ont. Gen. Div.). This case was reversed on appeal on different grounds: *Hall v. Cooper* (1998), 36 R.F.L. (4th) 19 (Ont. C.A.).

48 *Place Concorde East Ltd. Partnership v. Shelter Corp. of Canada Ltd.* (2006), 18 B.L.R. (4th) 230, 46 R.P.R. (4th) 1, 211 O.A.C. 141, 270 D.L.R. (4th) 181.

49 *Volvo Truck Finance Canada Ltd. v. Premier Pacific Holdings Inc.*, 2002 BCSC 1137, 29 B.L.R. (3d) 213.

50 *Deer Valley Shopping Centre Ltd. v. Sniderman Radio Sales & Services Ltd.* (1989), 67 Alta. L.R. (2d) 203, 96 A.R. 321 (Q.B.) [*Sniderman*].

51 *Markdale Ltd. v. Ducharme* (1998), 235 A.R. 283 at paras. 63-68 (Alta. Q.B.) [*Markdale*].

52 Interestingly, while in *Markdale* the judge took judicial notice of the fact that a 30% interest rate was sufficiently high to constitute a penalty, in *Metropolitan Toronto Condominium Corp. No. 1250 v. Mastercraft Group Inc.*, Pitt J. of the Ontario Superior Court of Justice was unwilling to take judicial notice of a 24% interest rate being exorbitant, and he refused to find that such an interest rate constituted a penalty clause absent direct evidence. While Pitt J.'s comments were rather limited on this point, no reference is made to whether the interest rate is a genuine pre-estimate, with the only question being whether it is "exorbitant". See *Metropolitan Toronto Condominium Corp. No. 1250 v. Mastercraft Group Inc.* (2007), 54 R.P.R. (4th) 260 at paras. 145-54 (Ont. S.C.J.). Elsewhere, in two linked cases, the Alberta Court of Appeal allowed contracts which specified interest rates upon default of 26.4%. See *See-Rite Optical*, *supra* note 2 and *32262 B.C. Ltd. v. G. Pataki Enterprises Ltd.* (1998), 216 A.R. 78, 175 W.A.C. 78.

Having outlined a number of decisions in which courts have employed the *Elsley* framework, it must be asked what unconscionability and oppression mean in the context of stipulated damages clauses and how courts have actually gone about determining whether a given clause is oppressive. While the exact reasoning courts have employed in determining enforceability has been somewhat vague, two broad factors relevant to this inquiry can be identified. The first and most important factor has been the reasonableness or extravagance of the sum specified in the clause. While courts applying the *Dunlop* test also examined the extravagance of the sum, this consideration was anchored to the concept of extravagance in comparison with a genuine pre-estimate of damages; indeed, the above discussion of the application of the *Dunlop* standard suggests that under that framework, any stipulated sum which was not a genuine pre-estimate of damages was extravagant. Conversely, the idea of a genuine pre-estimate has been largely irrelevant under the *Elsley* line of cases, and such clauses have not been found to be unreasonable merely because they were greater than expected or than the actual damages suffered by the non-breaching party. Under the *Elsley* standard, there is a presumption of enforceability of stipulated damages clauses, and such a clause will only be held to be unenforceable if the stipulated sum is perceived by the judge to be exceptionally unfair or unreasonable. Indeed, judges' perceptions of fairness have played a determinative role in this process, since the principled basis of what constitutes fairness or oppression in the context of penalty clauses has not been adequately articulated by any court to date.

In line with the move towards a quasi-unconscionability-based standard, a second factor which some courts undertaking this analysis have investigated and emphasized is the relative sophistication of the parties in reaching their decisions. While such considerations logically had no place in the *Dunlop* analysis, they have in some cases played an important role in the courts' decisions to strike down or uphold stipulated clauses under the *Elsley* standard. The fact that these considerations are starting to be given weight by the courts suggests a possible legal avenue which courts may further employ to refuse to strike down penalty clauses. Indeed, if the analysis of penalty clauses were fully subsumed into the principles governing unconscionability, it would seem that a necessary requirement for courts to strike down a penalty clause would be evidence of something similar to undue influence, incapacity, or some other inequality of bargaining power.[53] While this has been an important factor in some decisions, the above discussion of the case law shows that it has not been required in all cases by courts applying the doctrine in *Elsley* to strike down a stipulated damages clause, indicating that at least some courts which favour greater enforceability of penalty clauses have nevertheless thus far been reluctant to fully subsume the analysis of penalty clauses into principles of unconscionability. Finally, it is important to note that the *Elsley* standard can theoretically take into account a variety of factors beyond merely the extravagance of the sum and the relative sophistication of the parties. Anchored in the vague context of oppression, the *Elsley* approach can theoretically include any contextual factors related to the fairness of enforcing the stipulated damages clause, though, as mentioned above, it is unclear what the principled basis of fairness is in this context.

Having examined much of the case law on penalty clauses in Canadian courts since the Supreme Court's decision in *Elsley*, it can be concluded that there are effectively two different and equally muddled tests which courts have applied in recent years to determine whether to enforce a contractual provision which specifies the damages that will flow from a breach. Some courts have continued to rely on the strict test articulated in *Dunlop*, under which the primary test of enforceability was whether the clause constituted a genuine pre-estimate of damages. Under this standard, where stipulated damages are in excess of estimated damages courts are unwilling to enforce the stipulated damages clause. By contrast, other courts have placed greater emphasis on the dictum of Dickson J. in *Elsley* and have held that a stipulated clause will be enforced unless there is oppression or unconscionability.[54] Thus, in stark contrast to those courts applying the *Dunlop* test, courts applying the *Elsley* standard are now willing, absent oppression or unconscionability, to enforce stipulated damages clauses where the stipulated damages significantly exceed expected damages—that is, supra-compensatory stipulated damages. As these two approaches represent markedly different judicial attitudes towards the enforceability of stipulated damages clauses, it remains to be determined which approach is normatively preferable.

III COMPARING DUNLOP AND ELSLEY: A NORMATIVE ANALYSIS OF COMPETING APPROACHES

While the previous section examined the changes which have occurred in the law relating to the enforceability of penalty clauses since the Supreme Court of Canada's decision in *Elsley*, this section takes a normative approach and asks whether the current developmental trajectory of the law has been a good thing. As discussed above, a line of cases following *Elsley* has evinced more reluctance to strike down penalty clauses, choosing to do so only when the penalty clause was found to be oppressive or unconscionable. This is essentially the position favoured by Stephen Waddams in his treatise on contract law, wherein he argues that there are strong reasons why courts should generally enforce penalty clauses, subject only to review on the grounds of unconscionability.[55]

While arguments supporting a more permissive judicial attitude towards penalty clauses have attracted significant support from many judges and academic commentators, this section challenges this position. By examining many of the policy arguments surrounding stipulated damages clauses in the particular context of the two competing principles outlined above, this section will argue

53 Waddams, *supra* note 26 at 385-86; McCamus, *supra* note 23 at 404-07.

54 To complicate matters further, some courts in reaching their decision have declined to conclusively endorse either approach, thereby providing no additional authority on which approach is to be preferred. The clearest example of this is *Peachtree*, *supra* note 38. See also *Ashland*, *supra* note 18. In the view of at least one commentator, *Peachtree* has significantly muddled the law of penalty clauses; see Dollak, *supra* note 1 and Weir, *supra* note 38.

55 Waddams, *supra* note 26 at 327. For another Canadian contract scholar arguing for greater enforcement of penalty clauses, see Swan, *supra* note 26 at 719.

that (1) the benefits of a more relaxed standard based on oppression or unconscionability are not as clear as posited by commentators and courts, and (2) that there are strong arguments in favour of the stricter test for the enforceability of penalty clauses as elaborated in *Dunlop*.

Stipulated Damages as a Mechanism for Increasing Contractual Certainty

One argument often presented in favour of greater judicial enforcement of penalty clauses is the notion that when parties are able to negotiate their damages in advance, it allows parties and society more generally to avoid a number of the inefficiencies associated with uncertainty as to damages.[56] There are three mechanisms through which this operates. First, where parties have specified in advance the damages that will flow from breach, it reduces the need for parties to litigate to ascertain damages. This both reduces the costs on parties of enforcing contracts and also reduces the general cost on society which stems from the provision of a court system. Second, where damages are ascertainable in advance by a party considering a breach of contract, that party is in a better position to determine whether to breach or not, thereby encouraging efficient decision-making with respect to performance or breach.[57] Third, additional certainty over the quantum of damages might lower the risks of contracting in the first place, thereby making parties who are averse to uncertainty more likely to engage in contractual relations.[58]

Without denying that there can be benefits from the certainty of having damages stipulated in advance, some objections must be made in the application of these principles to the law on penalty clauses as it stands. First, it should be noted where damages are easily ascertainable by both courts and parties *ex post* even without a stipulated damages clause, the increased certainty provided by stipulated damages clauses is marginal or non-existent. Thus, while these benefits may be significant where the quantum of damages is difficult to assess *ex post*, they will be relatively unimportant where damages can be easily assessed.

Second, the above arguments support a legal rule under which parties are absolutely certain that courts will enforce all clauses in which parties specify damages. This is not, however, the direction in which the courts are moving nor is it the position articulated by Waddams, all of whom have simply preferred a rule based on unconscionability or oppression rather than the traditional rule in *Dunlop*.[59] Because this judicial check on the enforceability of penalty clauses remains, the arguments suggesting that their enforcement will ensure greater certainty are lessened somewhat, as, under either approach, parties may still be uncertain *ex ante* about whether the courts will choose to enforce the penalty clause in question.

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56 Waddams, *ibid.* at 327; E. Allan Farnsworth, *Contracts* (New York: Aspen Publishers, 2004) at 811.

57 Aristides Hatzis, "Having the cake and eating it too: efficient penalty clauses in Common and Civil contract law" (2003) 22 Int'l. Rev. L. & Econ. 381 at 391.

58 DiMatteo, *supra* note 20 at 682.

59 Waddams, *supra* note 26 at 324.

Moreover, it is quite plausible that in some circumstances there might be *more* rather than less uncertainty under the *Elsley* standard than under the approach in *Dunlop*. This stems from the fact that, although under the *Elsley* standard there might be more certainty over damages as more stipulated damages clauses in general are enforced, there might be less certainty *ex ante* as to whether any given stipulated damages clause is enforceable. Because the *Dunlop* rule is a relatively simple one that only includes a limited number of factors, it is relatively easy to predict whether a court will choose to uphold a given stipulated damages clause. In contrast, because the *Elsley* standard can incorporate additional considerations and is much more context-specific, the parties might be more uncertain as to whether the court applying that standard would uphold a given clause.[60] With significant uncertainty *ex ante* about whether the courts will enforce a given stipulated damages clause, even where more clauses are ultimately enforceable *ex post*, the benefits outlined above are significantly lessened.

Furthermore, even beyond the uncertainty occasioned by a more fact-specific approach, it is important to note that the degree of certainty provided by a particular stipulated damages clause decreases as the measure of damages specified by that clause deviates from the measure of damages which would flow from the probable measure of expectation damages. This is because, under any approach where the court retains the discretion to not enforce a stipulated damages clause, the further the measure of damages specified by the penalty clause deviates from the measure of damages which would flow from the probable measure of expectation damages, the greater are the incentives for the parties to litigate to try to strike down or uphold the penalty clause. Under the *Dunlop* approach, supra-compensatory penalty clauses would seldom be litigated, as they would almost certainly be found to be unenforceable, while parties would have relatively little incentive to litigate over the enforceability of a liquidated damages clause, as the measure of damages provided under that approach would be rather similar to expectation damages. Conversely, under the *Elsley* approach, because a supra-compensatory stipulated damages clause would be presumptively enforceable, the non-breaching party would have a significant incentive to litigate to enforce the clause, while the breaching party would have an equal and opposing incentive to try to get the clause struck down as being oppressive. Thus, the foregoing considerations suggest that there might actually be more litigation and uncertainty under a more liberal *Elsley*-like approach to

60 Applying some of the literature regarding rules and standards to this point is illustrative. Although neither approach is a perfect archetype of a rule or a standard, the *Dunlop* approach can be characterized as relatively rule-like while the *Elsley* approach can be characterized as relatively standard-like. Kaplow suggests that the primary consideration regarding the desirability of a rule versus a standard is the frequency of the behaviour subject to the rule or standard, with a rule being relatively more desirable as the frequency of the behaviour increases. Because the inclusion of stipulated damages clauses in contracts is by no means a rare occurrence, this suggests that a relatively rule-like approach to the enforceability of stipulated damages clauses will be preferable. See Louis Kaplow, "Rules versus Standards: An Economic Analysis" (1992) 42 Duke L.J. 557.

stipulated damages clauses—provided that courts retain the discretion to not enforce the clause—than there would be under the *Dunlop* rule.

Stipulated Damages as a Mechanism for Avoiding Under-Compensation

A second argument sometimes advanced in favour of the enforceability of parties' stipulated damages provisions rests on the notion that individuals may not be fully-compensated under the standard rules of contract law. As Waddams writes, it allows a non-breaching party to "avoid the risk of under-compensation that may be caused by the legal restrictions on damages, such as remoteness, certainty of proof, mitigation, and the failure to recognize intangible losses".[61] More generally, under-compensation may arise in any circumstance where one party has a subjective valuation of performance which is higher than an objective valuation by courts. Such under-compensation may be problematic both from a perspective of injustice as well as under considerations of efficiency.[62] Stipulated damages clauses avoid this risk, it is argued, as parties can negotiate clauses which will ensure that they are fully compensated in the event of a breach. Under this reasoning, an oppression-based standard which strikes down fewer clauses as penalty clauses can lead to fewer cases of under-compensation.

While such worries about under-compensation are well-founded, it is not clear that the best way to address these concerns is through changes to the law of penalty clauses. Indeed, insofar as there are problems in the law of damages which result in systematic under-compensation for certain types of wrongs, it is preferable for courts or legislatures to directly address those problems rather than relying on individuals to recognize the existence of such problems in the law and contract around them. Reforming the law on penalty clauses is a second-best response to a failure in another area of law. Moreover, reforms in the law of damages present a better solution to these problems than simply allowing parties to determine *ex ante* the quantum of damages in the event of a breach. This is for two reasons. First, the negotiation of detailed stipulated damages clauses increases the transaction costs of forming a contract in the first place, and reforms in the law of damages can remove these transaction costs. Second, since it cannot be presumed that parties will always contractually specify damages in advance, reforms in the law of damages would provide adequate compensation to all those entering contracts, not simply the subset of contracting parties for whom there is a sufficient incentive to negotiate such clauses in advance. Thus, insofar as the law of damages is perceived as under-compensating non-breaching parties, a more efficient and just solution would be for courts to rectify these problems

61 Waddams, *supra* note 26 at 327.

62 Under-compensation may be inefficient as it may deter an individual from entering a welfare-enhancing contract if (1) the individual is sufficiently risk-averse and (2) the individual perceives a significant enough possibility of the other party breaching the contract. For more on under-compensation and the efficiency implications of stipulated damages clauses, see Charles Goetz & Robert Scott, "Liquidated Damages, Penalties and the Just Compensation Principle: Some Notes on an Enforcement Model and a Theory of Efficient Breach" (1977) 77 Colum. L. Rev. 554.

directly. Indeed, courts have recently shown interest in some of the potential sources of under-compensation which Waddams identifies; for example, in *Fidler v. Sun Life Assurance Co. of Canada*, the Supreme Court of Canada opened the door slightly wider for damages for intangible losses.[63]

It is readily conceded that there are certain cases where such reforms are for other reasons problematic, implausible or insufficient. For example, as Goetz and Scott argue, it may be that "the proof problems inherent in fully recovering idiosyncratic values within the context of operationally practical damage sanctions...prevent the non-breaching party from recovering his subjective expectations if recovery is limited to legally determined remedies".[64] For example, in complex agreements between two sophisticated commercial parties, it may be exceptionally difficult for courts to accurately quantify damages in the event of a breach. Where this is the case, stipulated damages clauses can play a useful role, as parties may be able to determine the idiosyncratic value of performance *ex ante* more accurately and more efficiently than could a court *ex post*.[65] Nonetheless, the admittedly desirable enforcement of stipulated damages clauses in these circumstances does not support the *Elsley* approach over the *Dunlop* rule. Rather, the under-compensation which results from extraordinary subjective valuations of performance or the difficulty of assigning a value to performance can be accommodated within the *Dunlop* framework of stipulated damages analysis and would not require a more deferential attitude towards penalty clauses generally.

The main situations under which expectation damages are likely to fail to fully compensate the non-breaching party are (1) where the contract in question was for an individualized good or service which cannot easily be acquired in the market and which is therefore difficult to value, and (2) where the complexity of a transaction makes it difficult for a court to ascertain the true quantum of the damage flowing from a breach. Yet, in section (iv)(d) of the *Dunlop* test itself as well as in subsequent cases, courts have recognized that it is precisely where damages are difficult to quantify that liquidated damages clauses will tend to be enforced as being a genuine pre-estimate of damages.[66] Thus, the concerns that expectation damages may lead to under-compensation in certain cases can be accommodated within the *Dunlop* approach, thereby lessening the need for a general change in the law towards an oppression-based standard of enforceability.

63 *Fidler v. Sun Life Assurance Co. of Canada*, 2006 SCC 30, [2006] 2 S.C.R. 3, 271 D.L.R. (4th) 1, 57 B.C.L.R. (4th) 1. Alternatively, some of the rules within the law of damages which might seem to limit compensation unfairly might actually be sound principles of damages that ought to be enforced. In these circumstances it might be desirable for the law not to sanction parties' attempts to avoid these principles.

64 Goetz & Scott, *supra* note 62 at 577. While the availability of specific performance will sometimes overcome the concerns about under-compensation, it is by no means generally available, and it is often impractical, inefficient, or overly oppressive to the breaching party.

65 On this, see generally Robert E. Scott and George G. Triantis, "Anticipating Litigation in Contract Design" (2005) 115 Yale L.J. 814.

66 *Dunlop*, *supra* note 4. See also *Tkachuk*, *supra* note 16.

The Signaling Function of Supra-Compensatory Stipulated Damages

Supra-compensatory stipulated damages may also play a signaling function by conveying information about a party's reputation to other contracting parties. If A is unsure about B's reputation regarding the likelihood or quality of B's performance of the contractual provisions, B can offer to include a supra-compensatory stipulated damages provision in the contract.[67] By offering to pay a supra-compensatory premium in case of default, B is signaling his intention to perform to A, thereby providing A with information about B's reputation and thereby leading A to be more likely to sign a contract with B. While such signaling is possible under the *Elsley* approach which allows supra-compensatory stipulated damages, such signaling would not be possible under the *Dunlop* approach, as the appropriate signal would only be conveyed by a clause which is necessarily not a genuine pre-estimate of damages. Of course, even under the *Dunlop* approach, B could still include a supra-compensatory penalty clause in a contract with A; on the other hand, if A knows that the courts will not enforce that penalty clause, then B has simply made an unenforceable promise which does not provide any information about B's actual reputation. Thus, to the extent that this type of signaling is socially useful, it is a consideration which speaks in favour of the *Elsley* approach to stipulated damages.

There are three reasons, however, to think that the social utility of the signaling function of supra-compensatory stipulated damages is limited. First, as an empirical matter, it is rather unclear how frequently parties actually do use supra-compensatory stipulated damages as a signal. Although there is limited research on this point, in a recent paper in which he experimentally assessed various claims relating to behavioural decision theory and stipulated damages clauses, DiMatteo found no statistically significant evidence of a signaling effect stemming from a voluntary offer by one party to include a penalty clause in a contract.[68] Although additional empirical work is required on this point, the potential positive welfare effects of the signaling function of supra-compensatory stipulated damages should not be overstated in the presence of such limited empirical support.

Second, the signaling function of supra-compensatory stipulated damages clauses will only be socially useful where A is unsure about B's reputation for performance. Where A already has knowledge about B's reputation, the signal is unnecessary. Given the mass of information available about most firms and their products as well as the steps that many firms take to establish positive reputations, the signaling function is largely irrelevant with respect to most firms. In contrast, to the extent that it occurs, the signaling function of such clauses could be important to new entrants seeking to establish themselves in the marketplace. Nevertheless, the benefits of signaling will likely not extend much beyond new entrants.

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67 See Anthony Kronman and Richard Posner, *The Economics of Contract Law* (Boston: Little, Brown and Company Law Book Division, 1979) at 224.

68 Larry DiMatteo, "Penalties as Rational Response to Bargaining Irrationality" (2006) Mich. St. L. Rev. 883 at 897.

Finally, at least some of the benefit of signaling which comes from a promise to pay supra-compensatory damages in case of a breach may still arise even if the promise to pay those damages is not legally enforceable. For the signaling function to operate, A must believe that B's promise to pay supra-compensatory damages in case of a breach is credible. Given that many commercial relationships and transactions are much more dependent on the establishment of a strong reputation than on strict legal entitlements,[69] once B has promised to pay supra-compensatory damages, B will often be compelled to pay even if not strictly required to do so by law, as B's reputation would be significantly injured if B reneged on the promise.[70] Thus, even if B's promise to pay supra-compensatory damages is not legally enforceable, the mere making of the promise can itself in many circumstances play a signaling function. Taken together, these considerations suggest that while there may be *some* social utility in the legal enforcement of supra-compensatory stipulated damages clauses in terms of their signaling function, this benefit is likely relatively minor.

Freedom of Contract and Bargaining Failures in Stipulated Damages

Perhaps the most compelling argument often made for enforcing penalty clauses generally is one which underlies the principle of freedom of contract more generally. Indeed, it was specifically because of the general principle of freedom of contract that Dickson J. initially wrote in *Elsley* that penalty clauses ought not to be struck down except where there is oppression.[71] In a system which upholds freedom of contract generally, it would seem to be an aberration that it is not supported in this particular instance. As Waddams has pointed out, it seems especially anomalous that the law will allow parties to craft clauses which require one party to pay a certain amount upon the happening of a certain event, but it will not enforce such clauses specifically when that event is the breach of the contract in question.[72]

From a welfare perspective, such inroads upon freedom of contract seem unjustified at first glance. One major reason for supporting the principle of freedom of contract more generally is the idea that it is the parties themselves who

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69 On this point, see *e.g.* Stewart Macaulay, "Non-Contractual Relations in Business: A Preliminary Study" (1963) 28 American Sociological Review 55; Lisa Bernstein, "Opting out of the Legal System: Extralegal Contractual Relations in the Diamond Industry" (1992) 21 J. Legal Stud. 115.

70 From a game-theoretic perspective, provided that B is trying to establish itself in the market rather than trying to make a quick profit and exit, B's decision about whether to pay the supra-compensatory stipulated damages is characterized as one decision in the context of a repeated prisoner's dilemma. Despite not being in B's immediate interest to pay supra-compensatory damages, B may decide to do so because it is more profitable to cooperate with its contractual partners in the long-term. For a brief overview of some of this literature, see Robert Axelrod, *The Evolution of Cooperation* (New York: Basic Books, 1984); Robert Axelrod, "The Emergence of Cooperation Among Egoists" (1981) 75 American Political Science Review 306.

71 As Dickson J. wrote in that case, "[T]he power to strike down a penalty clause is a blatant interference with freedom of contract." *Elsley*, *supra* note 3 at 937.

72 Waddams, *supra* note 26 at 324-25.

are best positioned to negotiate the terms of contracts which will maximize their joint welfare or surplus from the exchange.[73] If both parties agree to a penalty clause in a contract, then it must in some sense be welfare-enhancing; if it were otherwise, absent unconscionability or undue pressure, a party would simply have chosen not to agree to that contract. Thus, even if a penalty clause appears to be detrimental to one party in the contract, the fact that it remains in the contract means that it must be jointly more valuable to the parties to include it in the contract than to not include it in the contract. This type of reasoning includes the specific considerations listed earlier in this section, but it is also significantly broader—it is based on the foundational premise that individuals are best positioned to order their own affairs and that external regulation of voluntary transactions can only operate to make parties worse off.

While such reasoning forms the core of one of the strongest arguments in favour of a more permissive standard towards the enforcement of penalty clauses, a deconstruction of this argument also exposes one of the strongest arguments in favour of striking down penalty clauses. The above argument in favour of enforcing penalty clauses assumes that individuals are perfectly able to rationally evaluate the costs and benefits of doing so. The decision of whether or not to agree to a penalty clause, as well as the more foundational question of what value or cost to assign subjectively to a given penalty clause in a contract, depends upon both an exceptional range of information being available to the decision-maker as well as the capacity on the part of that decision-maker to properly process and evaluate that information. Most importantly for this exposition, it requires the decision-maker to be able to properly evaluate the likelihood that they will need to breach the contract, either because the cost of performance becomes too high or performance is otherwise effectively impossible. Given, however, that individuals possess neither limitless computational capacity nor the ability to process information without any biases—and because individuals are typically particularly poor at assessing probabilities—individuals may be prone to reasoning errors in determining the value or cost of a penalty clause.[74]

Even if the above is correct, it might be countered that the same consideration applies to all contractual arrangements and that contract law does not and should not generally prevent people from making bad bargains. Along these lines, Goetz

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73 Generally on this point, see Michael Trebilcock, *The Limits of Freedom of Contract* (Cambridge, Mass.: Harvard University Press, 1993) at 7-8. In the context of stipulated damages, see generally DiMatteo, *supra* note 20 at 683.

74 For papers dealing more generally with human limitations on the evaluation of probabilities as well as different policy applications, see Roger G. Noll & James Krier, "Some Implications of Cognitive Psychology for Risk Regulation" in Cass Sunstein, ed. *Behavioral Law & Economics* (Cambridge: Cambridge University Press, 2000) at 325; Colin Camerer & Howard Kunreuther, "Decision Processes for Low Probability Events: Policy Implications" (1989) 8 Journal of Policy Analysis and Management 565. For an interesting paper arguing more generally that cognitive limitations justify some degree of paternalism, see Colin Camerer *et. al.*, "Regulation for Conservatives: Behavioral Economics and the Case for 'Asymmetric Paternalism'" (2003) 151 U. Pa. L. Rev. 1211; see also Cass Sunstein & Richard Thaler, "Libertarian Paternalism is not an Oxymoron" (2003) 70 U. Chicago L. Rev. 1159. For an application of these principles to an analysis of unconscionability in contracts in the

and Scott assert that "there is no reason to presume that liquidated damages provisions are more susceptible to duress or other bargaining aberrations than other contractual allocations of risk".[75] Nevertheless, while it is true that all contractual arrangements might be subject to such errors in reasoning, there are reasons to believe that penalty clauses as a class of arrangements are more particularly prone to errors of reasoning than most other contractual arrangements or clauses. As Eisenberg has argued:

> [T]he justification for the special scrutiny is not that liquidated damages provisions are especially amenable to advantage taking and oppression, but that such provisions are systematically more likely to be the products of the limits of cognition than performance terms, that is, terms that specify the performance each party is to render.[76]

More specifically, Eisenberg argues that certain cognitive limitations result in people systematically underestimating the potential negative impact of a penalty clause and thereby agreeing to them far too readily or at too low a price. In other words, this might be a class of provisions where individuals systematically make poor or even welfare-decreasing arrangements.

Drawing from behavioural economics literature, Eisenberg identifies three potential sources of imperfect cognitive reasoning which leads to such systematic errors with respect to penalty clauses. First, recognizing that people are not perfect computational machines, but rather exhibit a form of bounded rationality, Eisenberg argues that while individuals are typically quite able to process information relating to the evaluation of performance terms, "at the time the contract is made it is often impracticable, if not impossible, to imagine all the scenarios of breach".[77] Moreover, even if individuals were capable of imagining all the potential scenarios and computing all the requisite information, because of the existence of costs occasioned when searching for and processing information, individuals may choose *ex ante* to be "rationally ignorant", as the perceived marginal cost of searching and processing may outweigh the perceived marginal benefit at a very early stage in the evaluative process.[78] Both of these problems mean that individuals will typically not understand the full implications of penalty clauses when negotiating them.

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emergency response industry, see Paul Bennett Marrow, "The Unconscionability of a Liquidated Damage Clause: A Practical Application of Behavioral Decision Theory" (2001) 22 Pace L. Rev. 27. For a general overview of behavioural law and economics, see Christine Jolls, Cass Sunstein, & Richard Thaler, "A Behavioral Approach to Law and Economics" in Cass Sunstein, ed. *Behavioral Law & Economics* (Cambridge: Cambridge University Press, 2000) at 13.

75 Goetz & Scott, *supra* note 62 at 592.

76 Melvin Aron Eisenberg, "The Limits of Cognition and the Limits of Contract" (1995) Stan. L. Rev. 211 at 227.

77 *Ibid.* For a discussion of Eisenberg's reasoning and conclusion on this point, see Russell Korobkin & Thomas Ulen, "Law and Behavioral Science: Removing the Rationality Assumption from Law and Economics" (2000) 88 Cal. L. Rev. 1051 at 1083-84.

78 *Ibid.*

Second, as has been documented in a variety of settings, individuals are "unrealistically optimistic", especially with respect to their own affairs.[79] In the case of penalty clauses, such optimism may be reflected in overly optimistic assessments of the probability that the contract will actually be performed. If individuals systematically overestimate the probability of contractual performance and consequently underestimate the probability of contractual breach, they may agree to be bound by rather stringent penalty clauses because they underestimate the probability of the penalty being imposed on them.

Third, individuals often assess probabilities or expectations on the basis of heuristics rather than objective reasoning, and this can lead to faulty decision-making. Eisenberg notes two commonly-employed heuristics which can have detrimental consequences in the context of penalty clauses: the availability heuristic and the representativeness heuristic.[80] The availability heuristic refers to the fact that in assessing the probability of an event, individuals often estimate "that probability on the basis of comparable data and scenarios that are readily available to his memory or imagination".[81] In the context of penalty clauses, Eisenberg posits that because individuals enter into a contract with the intention to perform that contract, they may overweigh that intention as an indicator of the likelihood of performance.[82] Similarly, the representativeness heuristic refers to the fact that individuals "usually make decisions on the basis of some subset of the data that they judge to be representative".[83] By similar reasoning to that above, if individuals take as their sample present evidence relating to the intention to perform, they may underestimate the likelihood of breach. Both of these factors suggest that individuals might systematically underestimate the likelihood of breach and therefore also systematically underestimate the cost of agreeing to a penalty clause. Thus, these factors taken together suggest that individuals may generally tend to make poor decisions regarding penalty clauses, and, from a perspective of Pareto-superiority, this suggests the case of penalty clauses demonstrates a situation where courts should not be overly reluctant to infringe on freedom of contract, as freedom of contract in these situations might not actually lead to mutually welfare-enhancing agreements.[84]

While the analyses of Eisenberg and others suggest that individuals tend to make poor decisions with respect to the inclusion of penalty clauses, it might be countered that the law of contract cannot be geared toward the protection of individuals from their own cognitive imperfections. Indeed, it might be posited

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79 *Ibid.* See also Neil Weinstein, "Unrealistic Optimism About Future Life Events" (1980) 39 Journal of Personality and Social Psychology 806; Lyle Brenner *et. al.*,"Overconfidence in Probability and Frequency Judgments: A Critical Examination" (1996) 65 Organizational Behavior & Human Decision Processes 212.

80 Amos Tversky & Daniel Kahneman, "Judgment under Uncertainty: Heuristics and Biases" (1974) 185 Science 1124.

81 Eisenberg, *supra* note 76 at 220.

82 *Ibid.* at 228.

83 *Ibid.* at 222.

84 For some empirical support for this position, see Eisenberg's analysis of a number of leading American cases on penalty clauses, *ibid.* at 228-30.

that these same considerations might apply to contracts more generally and it is not the place of the law to protect people from making bad bargains. Nonetheless, it is important to note the unique position which penalty clauses occupy in this analysis. First, while all contractual arrangements may be affected by cognitive limitations, the reasons presented above suggest that the nature of penalty clauses is such that they lead to decision-making which is systematically poorer than that regarding other contractual provisions. Second, even if the previous contention is incorrect and the same cognitive limitations apply equally to all contractual arrangements, the social cost of protecting individuals from their own decision-making is much lower with penalty clauses specifically than with contractual arrangements in general. In order to protect individuals generally from entering into poor contracts because of their limited cognitive capacities, the law would have to refuse to enforce all contracts which turn out *ex post* to have been bad arrangements for one party. Clearly this would undermine contract law generally and result in the disruption of the vast social benefits flowing from allowing parties to contract freely. Conversely, as discussed throughout this section, the social benefits flowing from greater enforcement of genuine penalty clauses are limited, and the relative social cost of protecting individuals from themselves in this specific circumstance is thus relatively low. Therefore, the claim made here is that contract law should be attentive and take a restrictive attitude towards those specific types of clauses and contracts which are particularly prone to errors in human reasoning, particularly where the social benefits of enforcing such clauses are marginal.[85]

Despite the seeming aberrance of such a principle within contract law more generally, a contractual rule which strikes down penalty clauses based on the fact that individuals tend to make poor bargains involving penalty clauses is not actually anomalous compared to other contractual doctrines which prevent individuals from making bad bargains due to a variety of circumstances.[86] The doctrine of unconscionability is the most obvious example of this, as it explicitly prevents unscrupulous individuals from taking advantage of the impairments or incapacities of others. A strict doctrine relating to penalty clauses merely serves as another instantiation of this principle.[87]

Despite the similar bases of the two doctrines, however, this does not suggest that the law on penalty clauses should be subsumed into the doctrine of

85 More generally, the above reasoning suggests that individuals will generally be much better at assessing and rationally deciding on the terms of contractual performance than they will on the terms regarding contractual breach and that courts should thus subject the latter to more scrutiny than the former. This assessment seems to coincide with the common law's scrutiny of many clauses relating contractual breach, including penalty clauses, forfeitures, positive and negative covenants, and limitations of liability.

86 For a principled overview of some of these doctrines, see Trebilcock, *supra* note 73, especially chapters 4-7. For a list of some of the legal doctrines which serve this end, see Stephen Waddams, "Unconscionable Contracts: Competing Perspectives" (1999) 62 Sask. L. Rev. 1 at n. 1.

87 Indeed, Marrow argues that strict judicial scrutiny over penalty clauses can, from a behavioural decision theory perspective, be viewed as an extension of principles of substantive unconscionability. See Marrow, *supra* note 74.

unconscionability. This is because a strict rule with respect to penalty clauses would operate to protect those individuals even when the elements of unconscionability would be insufficient. The doctrine of unconscionability protects those individuals who can demonstrate either their own impairment or that they suffered from undue pressure. This doctrine has limited use in the context of many penalty clauses, since the faulty decision-making does not stem from either the general impairment of cognitive capacities or from undue pressure, both of which are relatively amenable to being proven where they exist. Rather, the faulty decision-making simply stems from systematic flaws in individuals' decision-making, which in contrast, are not easily directly observable or easy to prove. While it would be relatively easy to prove general impairment or undue pressure where it exists, it would be virtually impossible to prove that an individual exhibited flawed decision-making with respect to a given penalty clause, as would be required if the law of penalty clauses were swallowed into general principles of unconscionability. Thus, a strict rule on penalty clauses stems from the same conceptual basis as the doctrine of unconscionability, but rather than requiring proof of poor cognitive capacities in each case—which would be nearly impossible to demonstrate—it recognizes that penalty clauses are as a class typically the subject of poor decision-making.[88] From this perspective, a relatively strict rule on penalty clauses that is independent of the doctrine of unconscionability seems justified.

Returning specifically to the issue of comparing the *Dunlop* test and the *Elsley* test for the enforceability of penalty clauses, the above argument suggests the superiority of the *Dunlop* test over the *Elsley* test. On the one hand, the *Elsley* test is able to deal with the most obvious situations of bargaining failures, such as general mental incapacity, harsh terms in standard form contracts,[89] undue pressure, or other forms of overt bargaining inequality. Where a stipulated damages clause is punitive or oppressive for any of these reasons, both the *Elsley* approach and the *Dunlop* test will lead to the non-enforcement of the clause. On the other hand, the *Elsley* approach is unable to provide relief from unfair or welfare-reducing clauses in the class of cases where the bargaining failure is due to systematic failures in human cognition and reasoning. Because it is impossible for courts to determine the extent of a contracting party's cognitive failures in a given case, it may instead be better to use the *Dunlop* approach and take a more restrictive attitude with respect to the enforceability of clauses, which as a class tend to be the product of errors in individuals' reasoning.

88 For a related point on the blurring between procedural and substantive unconscionability, see P.S. Atiyah, "Contract and Fair Exchange" (1985) 35 U.T.L.J. 1 at 6: "Suppose a contract in which the outcome favours one party vastly more than the other; our natural reaction today is to believe that something must have gone wrong with the bargaining process....We may be so sceptical that such a contract could have been the result of the ordinary and proper bargaining processes that we examine the case with a strong, almost conclusive presumption that a sufficiently unfair contract must have been the result of improper procedures."

89 For a behavioural analysis of the inefficiencies that can arise in standard form contracts, see Russell Korobkin, "Bounded Rationality, Standard Form Contracts, and Unconscionability" (2003) 70 U. Chicago L. Rev. 1203.

It is important to note that such rationales based on behavourial theories do not conclusively justify strict judicial scrutiny of penalty clauses. Indeed, some scholars in the field argue that the evidence is more mixed. Generally, while there is relatively little controversy that individuals' decision-making is often flawed in the manner discussed above, there is still debate over the exact implications of these cognitive limitations on judicial oversight of penalty clauses. For example, Hillman argues that while some heuristics may imply increased judicial scrutiny, others justify a more lenient judicial attitude.[90] While this article does not contend that behavioral analyses necessarily justify striking down penalty clauses, it does suggest that because (1) the potential detrimental welfare effects which could arise from enforcing penalty clauses negotiated under significant cognitive limitations are quite significant, and (2) the benefits of less judicial scrutiny of penalty clauses are not as clear as suggested by some authors, absent further research on the topic, decreased judicial scrutiny of penalty clauses is not necessarily desirable.

Inefficient Behaviour and Supra-Compensatory Stipulated Damages

Another set of considerations surrounding the enforceability of stipulated damages clauses relate to the inefficient incentives that such clauses can potentially generate after the execution of the contract. Where a stipulated damages clause provides the non-breaching party with damages equal to that party's expectation interest, no inefficient incentives arise, as the expectation measure of damages generally provides incentives for parties to act efficiently with respect to performance and breach.[91] However, where a stipulated damages clause provides for damages which are greater than the damages that would arise under the ordinary contractual measure of expectation damages, the enforcement of that provision can lead to a variety of inefficient behaviours. In general, supra-compensatory stipulated damages clauses can lead to two types of inefficient behaviour.

The first type of inefficiency which can arise under a supra-compensatory stipulated damages clause is that it deters parties from breaching contracts when

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90 Robert Hillman, "The Limits of Behavioral Decision Theory in Legal Analysis: The Case of Liquidated Damages" (1999) 85 Cornell L. Rev. 717. See also Stephen Walt, "Liquidated Damages After Behavioral Law and Economics" (2002) Univ. of Virginia Law & Econ. Paper No. 02-18, online: SSRN <http://papers.ssrn.com/sol3/papers.cfm?abstract_id=353260> (arguing that the empirical results of behavioural law and economics do not justify substantial judicial scrutiny).

91 For example, see Steven Shavell, "Damage Measures for Breach of Contract" (1980) 11 Bell Journal of Economics 466. As Farber has pointed out, supra-compensatory damages can be efficient if breaches are not always detected or enforced. Daniel A. Farber, "Reassessing the Economic Efficiency of Compensatory Damages for Breach of Contract" (1980) 66 Va. L. Rev. 1443. Farber's critique of compensatory damages, however, can be answered if courts award punitive damages selectively to deter bad faith breaches. His analysis does not require the enforcement generally of supra-compensatory penalty clauses. Indeed, the selective awarding of punitive damages in cases of bad faith may be a more efficient way to deal with the issues he identifies, especially in light of the inefficiencies associated with supra-compensatory stipulated damages discussed in this section.

it would be efficient for them to do so. The notion underlying the efficient breach theory is that there are situations where the value of contractual breach is so great to one party that even after fully compensating the non-breaching party for the breach, the breaching party is still in a better position than he would have been had he kept the contract.[92] In other words, there may be situations where breach of contract is Pareto superior—in other words, both parties are at least as well off under the breach as they would have been if the contract had been kept. Because such breaches can be welfare-enhancing for both parties, it has been argued that courts should not deter efficient breaches.

Where a stipulated damages clause provides for supra-compensatory damages—either intentionally or because the value of contractual performance to the non-breaching party was overestimated at the time of contract formation—the stipulated damages clause will deter efficient breach and thereby make both parties worse off.[93] More specifically, where (1) the damages stipulated by a penalty clause are greater than the value of performance to the non-breaching party, (2) the damages stipulated by a penalty clause are greater than the value of non-performance to the party desiring to breach the contract, and (3) the value of non-performance to the party desiring to breach the contract is greater than the value of performance to the non-breaching party, enforcing a penalty clause will deter an efficient breach and thereby be welfare-reducing. While these three conditions indicate that not every penalty clause will deter efficient breach, it is apparent that the probability of deterring an efficient breach increases in line with the willingness of courts to enforce supra-compensatory stipulated damages clauses.[94]

While such notions of efficient breach have historically been much more common to American legal thinking than to Canadian legal thinking, there are some signs that the idea of efficient breach is beginning to gain acceptance in

92 For a classic paper regarding the idea of efficient breach, see Robert Birmingham, "Breach of Contract, Damage Measures, and Economic Efficiency" (1970) 24 Rutgers L. Rev 273. See also the Restatement (Second) of Contracts (1981) at chapter 16. For a critique of the efficient breach hypothesis based on the existence of transaction costs, see Ian Macneil, "Efficient Breach of Contract: Circles in the Sky" (1982) 68 Va. L. Rev 947.

93 Richard Posner, *Economic Analysis of Law*, 6th ed. (New York: Aspen Publishers, 2003) at 128. Where they deter efficient breach, excessive penalty clauses can also generate broader social inefficiencies. Aghion & Bolton argue that stipulated damages clauses can act as an entry fee that keeps more efficient firms out of a market. See Philippe Aghion & Patrick Bolton, "Contracts as a Barrier to Entry" (1987) 77 American Economic Review 388. As a corollary to the idea that super-compensatory stipulated damages can deter efficient breach, sub-compensatory stipulated damages can result in inefficient breach, as the low cost of breach may lead contracting parties to breach even where it is not jointly profitable for them to do so.

94 DiMatteo counters the efficient breach hypothesis by noting that even in the presence of a penalty clause, parties may still choose to breach where it is sufficiently profitable to do so. In these circumstances, the supra-compensatory aspect of the penalty clause merely represents "a sharing of the promisor's surplus". See DiMatteo, *supra* note 20 at 677. While it is undoubtedly true that not *all* efficient breaches will be deterred, the principle remains that the likelihood of deterring efficient breach increases as does the degree of supra-compensatory stipulated damages clauses that courts are willing to enforce.

Canada. For example, in 2002, Major J. wrote on behalf of the Supreme Court of Canada that "[e]fficient breach should not be discouraged by the courts", thereby indicating that efficient breach is a principle which Canadian courts should at least consider in issuing judgments.[95] Thus, if not deterring efficient breach is something which Canadian courts should consider, they should not become too permissive in allowing supra-compensatory stipulated damages clauses.

A second source of inefficiency caused by supra-compensatory penalty clauses, originally identified by Clarkson, Miller, and Muris, is that supra-compensatory penalty clauses can induce parties to spend resources on "activities that may induce breach and from activities to prevent breach inducement".[96] Where the value to A of B breaching the contract is greater than B performing the contract, A may take steps to try to induce B to breach the contract. As Clarkson Miller, and Muris concede, this will only be an issue where A has both the incentive and the opportunity to induce B to breach. As they further highlight, however, in many situations, it will be difficult or costly to determine whether A is inducing breach, "particularly where [B's] performance depends at least in part upon [A's] cooperation and assistance".[97] Moreover, where there exists the possibility for A to take steps to induce B to breach, B must take corresponding steps to detect and prevent this breach. Both the inducement to breach and the steps taken to prevent the inducement to breach are inefficient, as parties may take costly measures to these ends without actually producing anything.[98]

Applying these considerations to the two legal approaches to stipulated damages discussed above, it is clear that these inefficiencies are unlikely to arise under the *Dunlop* rule, as courts employing that rule will generally strike down supra-compensatory stipulated damages. In contrast, under the *Elsley* standard, whereby courts will much more readily enforce supra-compensatory stipulated damages clauses, such inefficiencies are much more likely to arise. Indeed, the set of stipulated damages clauses that would likely be enforced under the *Elsley* standard but would not be enforced under the *Dunlop* rule are precisely those which are potentially subject to the inefficiencies discussed above.

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95 *Bank of America Canada v. Mutual Trust Co.*, 2002 SCC 43, [2002] 2 S.C.R. 601 at para. 31.

96 Kenneth Clarkson, Roger Leroy Miller & Timothy Muris, "Liquidate Damages v. Penalties: Sense or Nonsense?" (1978) Wis. L. Rev. 351 at 368.

97 *Ibid.* at 371. DiMatteo suggests that there will actually be relatively few situations in which parties will have opportunities to induce inefficient breach, as in most circumstances such inducement can identified be *ex ante* by the parties or *ex post* by the courts. See DiMatteo, *supra* note 20 at 677-78. While it is unclear whether DiMatteo's assertion on this point is correct, even accepting for the moment that such inducement typically can be detected, this still necessitates that parties or courts must spend resources on monitoring the party with an incentive to induce the breach in order to ensure that such an opportunity does not exist.

98 Rubin notes that a particular manifestation of this inefficiency, which arises out of the same incentives, is the increased litigation which penalty clauses can occasion. In Rubin's view, this is especially problematic, as the fact that society subsidizes litigation means that contracting parties externalize at least a portion of the cost of their dispute to society in the form of increased socially-useless litigation. See Paul H. Rubin, "Unenforceable Contracts: Penalty Clauses and Specific Performance" (1981) 10 J. Legal Stud. 237.

IV A REFORMULATED TEST FOR THE ENFORCEABILITY OF STIPULATED DAMAGES CLAUSES

The previous section outlined the various policy considerations that relate to the enforceability of stipulated damages clauses. It is still necessary to articulate the appropriate legal test for the enforceability of stipulated damages clauses. In general, the considerations in the previous section suggest that on balance the *Dunlop* approach is preferable to the *Elsley* approach. Nonetheless, as noted above in the discussion of the evolution of the *Dunlop* test, there remains some ambiguity even within that approach regarding its proper application. Moreover, not all the factors discussed in the previous section necessarily support all aspects of the approach originally outlined in *Dunlop*. Thus, this section will build on the policy discussion in the previous section to briefly sketch an outline of a more satisfactory rule on the enforceability of stipulated damages clauses. This section will posit that a modified version of the *Dunlop* test is the appropriate approach for courts to use in determining the enforceability of a stipulated damages clause.

As the discussion in the previous section suggests, there are a wide variety of considerations that affect whether a stipulated damages clause is welfare-enhancing or welfare-reducing in a given case. Far from suggesting that all penalty clauses are welfare-reducing, the above discussion suggests that many penalty clauses are indeed welfare-enhancing. Nevertheless, the benefits of having a clear rule of enforceability of stipulated damages clauses suggests that it may be preferable to have a clear rule that fails to enforce some welfare-enhancing penalty clauses rather than to have an ambiguous standard of enforceability.[99] Indeed, as noted above in the section "Stipulated Damages as a Mechanism for Increasing Contractual Certainty", if one of the primary benefits of stipulated damages clauses is that they increase certainty, an exceptionally uncertain standard of enforceability entirely undermines one of the primary benefits of such clauses. Thus, the rules governing stipulated damages clauses should be sufficiently clear that parties can reasonably understand the circumstances in which such clauses will be enforced.

Since stipulated damages clauses can be both welfare-enhancing and welfare-reducing, it is necessary to establish a rule which will tend to enforce welfare-enhancing clauses and to refuse to enforce welfare-reducing clauses. In the discussion above of "Stipulated Damages as a Mechanism for Avoiding Under-Compensation", the analysis suggests that the primary benefit of stipulated damages clauses is that they can ensure that parties are fully compensated in situations where courts' assessments of damages for breach are unlikely to fully compensate parties for their actual loss. Yet, the following discussions of

99 Indeed, DiMatteo is incorrect when he states that "[t]he current law of liquidated damages is premised on the belief that penalty clauses are per se unfair. If it can be shown that some penalty clauses are indeed fair, then the rationale for the current law is severely flawed." DiMatteo, *supra* note 20 at 706. Even if some penalty clauses are welfare-enhancing, if penalty clauses are generally welfare-reducing and it is difficult to accurately separate the fair ones from the unfair ones, then the law may be justified in having a general policy of refusing to enforce such clauses. See also the considerations noted in Kaplow, *supra* note 60.

"Freedom of Contract and Bargaining Failures in Stipulated Damages" and "Inefficient Behaviour and Supra-Compensatory Stipulated Damages" both suggest that supra-compensatory penalty clauses are likely to be welfare-reducing. In line with the framework of the *Dunlop* approach, the overarching principle should be that courts should enforce stipulated damages clauses when they are compensatory and not enforce them when they are not compensatory.

In contrast with the original *Dunlop* approach, however, the criterion of enforceability should not be whether the stipulated sum represents a genuine pre-estimate of damage, but instead *whether the stipulated sum is reasonably compensatory in light of the damages actually sustained.* There are two reasons why the analysis of enforceability should be undertaken at the time of breach rather than at the time of contract formation. First, the incentives to undertake the inefficient behaviour described earlier in "Inefficient Behaviour and Supra-Compensatory Stipulated Damages" arise when the measures of stipulated damages diverge from the actual damages which the non-breaching party would sustain in the event of a breach. These incentives have no direct relationship to the anticipated damage at the time of contract formation but only to the actual damage at the time of breach. This suggests that a rule which seeks to prevent these inefficiencies would compare the stipulated damages measure with the actual damages sustained. Second, it is easier and clearer for the courts to compare the stipulated damages measure with the actual damages sustained rather than estimated damages at the time of contract formation. Asking courts to determine the latter requires them to engage in the imprecise and often distorted exercise of hindsight speculation, and this would significantly reduce clarity as to the enforceability of a particular clause.[100]

A distinction should be drawn between those situations where damages cannot be easily ascertained at the time of breach and those where they can be. Following the discussion above in "Stipulated Damages as a Mechanism for Avoiding Under-Compensation", stipulated damages clauses should generally be enforced where damages cannot be easily quantified at the time of breach or there is evidence that the non-breaching party has a particularly high subjective valuation of performance of the contract. This would include situations where the non-breaching party loses a good, service, or intangible benefit which cannot be easily valued in the market or where the sheer complexity of a commercial transaction makes it such that the value of performance is difficult to ascertain or quantify. Nonetheless, in line with the reasoning in the previous paragraph, it is not sufficient that damages cannot be easily quantified merely at the time of contract formation. Rather, the operative question should be whether the damages cannot be easily quantified at the time of breach of contract. Where this question is answered in the affirmative, courts should only refuse to enforce a stipulated damages clause if it is clearly unreasonable and wholly disproportionate to the

100 See Jeffrey Rachlinski, "A Positive Psychological Theory of Judging in Hindsight" (1998) 65 U.Chicago L. Rev. 571. See also Walt, *supra* note 90 at 16-17.

damages plausibly sustained in light of the breach.[101] There should thus be a strong presumption in favour of the enforceability of stipulated damages clauses in these circumstances. This ensures that courts will not strike down lightly those stipulated damages clauses which are most welfare-enhancing both in terms of increased certainty and ensuring full compensation.

In contrast, where courts can easily quantify damages at the time of the breach, as in simple commercial transactions, contracts for non-unique goods, or in loan agreements, courts should subject stipulated damages to significantly more scrutiny. In these cases, the ordinary measure of expectation damages is likely to be sufficient to fully compensate the non-breaching party, and supra- compensatory stipulated damages are likely to create inefficient incentives. Thus, in these circumstances, courts should only enforce a stipulated damages clause if it is reasonable and comparable to the damages actually suffered in light of the breach. The enforcement of reasonable clauses gives contracting parties some additional certainty by providing them with a means of avoiding trivial disputes about the quantum of damages, while also ensuring that distortionary supra-compensatory penalty clauses will not be enforced.

To summarize, the following test should be used in ascertaining the enforceability of a stipulated damages clause:

The general principle is that a stipulated damages clause should be enforced where the stipulated sum is reasonably compensatory in light of the damages suffered.

- Where damages cannot be easily quantified at the time of breach or there is other evidence that the non-breaching party has a particularly high subjective valuation of performance of the contract, a court should only refuse to enforce a stipulated damages clause if it is clearly unreasonable and wholly disproportionate to the damages plausibly suffered in light of the breach.
- Where damages can be easily quantified at the time of breach and there is no evidence that the non-breaching party has a particularly high subjective valuation of performance of the contract, a court should only enforce a stipulated damages clause if it is reasonable and comparable to the damages actually suffered in light of the breach.

Although this test is in some respects different from the test originally articulated in *Dunlop*, it is relatively consonant with the basic framework and intention of the *Dunlop* test as well as with the subsequent case law applying the *Dunlop* test. Moreover, insofar as it does deviate from the *Dunlop* test, it

101 It is important to note here that the comparison is with the damages plausibly suffered rather than with the damages actually suffered. Because, by assumption, it is difficult to quantify precisely the damages in these circumstances, courts should not undermine the very benefit of the clause by comparing the stipulated damages with their estimate of the actual damages, as the very problem here is that courts are likely to underestimate the damages. Rather, courts should be much more deferential and compare the stipulated damages with the damages plausibly suffered by the non-breaching party.

by no means represents a radical change in the law of stipulated damages. Indeed, the test outlined above is in many respects a reformulation and elaboration of the approach employed by Laskin C.J. in *Thermidaire*, indicating that there is some authority for this approach in Canadian law.[102] Moreover, this test is also in many respects similar to the approach outlined in American law in § 2-718 of the Uniform Commercial Code.[103] Therefore, the above test represents a reformulation of the *Dunlop* test which is both (1) more in line with the policy considerations underlying the enforceability of stipulated damages clauses than was the original *Dunlop* test, and (2) an incremental change from the original *Dunlop* test which is supported by some authority in both Canadian and American law.

V CONCLUSION

This article has presented two contentions. First, it has argued that far from being settled, the law on penalty clauses entered a period of uncertainty with the Supreme Court's decision in *Elsley*, with two distinct tests relating to the enforceability of penalty clauses now being employed by courts throughout Canada. Second, it has argued that, contrary to some of the judicial and academic commentary in Canada, the move towards greater judicial enforceability of stipulated damages clauses is not a positive development in Canadian contract law. Rather, this article has argued that various policy considerations suggest that the appropriate test of enforceability of such clauses is a modified version of the *Dunlop* test which focuses on whether a stipulated damages clause is reasonably compensatory.

With respect to the first of these contentions, this article has argued that courts have been divided as to which doctrine they have chosen to apply to a given case, with the oppression-based standard gaining increasing sway with courts as time goes on. Because of the existence of two lines of case law, there is significant confusion in the law of penalty clauses as it currently stands. The Supreme Court has not rendered a decision clarifying the law of penalty clauses since its judgment in *Elsley*, and the court should seek an early opportunity to clarify the law on this point. As it stands, the enforceability of a penalty clause in a given case will largely depend on which of the two competing standards a judge chooses to apply in that case. Such uncertainty is by no means desirable, as parties ought to understand at the very least the general standard the law will apply in choosing whether or not to enforce a penalty clause.

Turning to this article's second claim, it was argued that the greater reluctance that some courts have shown with respect to striking out penalty clauses may not be a positive development from a policy perspective. It was argued that many of

102 *Thermidaire*, *supra* note 17.

103 § 2-718 (1) of the Uniform Commercial Code states: "Damages for breach by either party may be liquidated in the agreement but only at an amount which is reasonable in the light of the anticipated or actual harm caused by the breach, the difficulties of proof of loss, and the inconvenience or nonfeasibility of otherwise obtaining an adequate remedy." U.C.C. § 2-718 (1995). For an overview and critique of American decisions applying this approach, see DiMatteo, *supra* note 20 at 659-62.

the standard policy rationales supporting greater enforcement of penalty clauses are much weaker and more tenuous than typically assumed. Conversely, it was posited that there are strong policy reasons not to enforce penalty clauses, both in terms of fairness to contracting parties as well as economic efficiency. Thus, courts and commentators should not simply rely on the mantra of freedom of contract as an axiomatic truth which leads inexorably to the conclusion that courts ought to only very rarely strike down penalty clauses. Instead, unless further research suggests substantial efficiency benefits in the enforceability of penalty clauses which have not been previously accounted for, courts should be conservative in expanding the scope of enforceability of such clauses. Courts should continue to employ the traditional *Dunlop* test and modify it incrementally to clarify the proper application of the test and to bring the test in line with the policy considerations relating to the enforceability of such clauses.