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Contract Law Update

Developments of Note 2023

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As those familiar with this annual update know, each fall I undertake a review of decisions from the previous 12 to 18 months, looking for cases relevant to commercial practice.[1] If there are cases bringing about significant changes to the law of contract or if the Supreme Court of Canada ("SCC") weighs in on a contract law issue, I will write about those cases. But typically, I will also highlight cases that remind us of longstanding contract law principles and that illustrate how those apply in practice.

Because they are typically fact dependent, I generally do not deal with cases in which the issue was interpretation of contractual provisions or whether an enforceable contract had been made (unless they articulate more broadly applicable principles).

These are the topics I cover this year:

- Update on the principled exception to privity in favour of third party beneficiaries
- What's new with the duty of good faith in contract law
- Recent law on the interpretation and application of buy-sell (shotgun) clauses
- Notional severance revisited
- Offer and acceptance in the digital world

Update on the Principled Exception to Privity in favour of Third Party Beneficiaries

By now, we are all aware of the body of case law dealing with the "principled exception" to the doctrine of privity whereby third parties can benefit from provisions in a contract to which they are not a party. I wrote on this topic at some length in my 2012 update. Since over a decade has passed since then, it is time I revisited the topic.

The doctrine of privity provides that as a general rule, a contract cannot confer rights or impose obligations arising under it on any person other than the contracting parties.

It is primarily the "conferral of rights" portion of this proposition that litigants and courts have pushed back against. There are a number of contexts in which strict application of the doctrine of privity can be avoided because other doctrines provide a foundation for a claim by a third party beneficiary against the contractual promisor. Examples of what are often referred to as "exceptions" to the doctrine include agency, trust, and collateral contract.[2]

In addition, third parties may be able to fit within the "principled exception" articulated in jurisprudence from the SCC.

The two key SCC decisions on the principled exception are *London Drugs Ltd. v. Kuehne & Nagel International Ltd.*, [1992] 3 S.C.R. 299, and *Fraser River Pile & Dredge Ltd. v. Can-Dive Services Ltd.*, [1999] 3 S.C.R. 108.

[1] I would like to acknowledge the work of Katrina Bois, summer articled student, in carrying out research and identifying topics for this year's update.

[2] I commend to you the article by Professor M.H. Ogilvie for a detailed consideration of the principled exception in the jurisprudence: M.H. Ogilvie, "Re-defining Privity of Contract: *Brown v. Belleville (City),*" 2015 CanLIDocs 74 ("Ogilvie Article"). Professor Ogilvie takes the view that the so-called exceptions are not true exceptions but rather instances of other principles of law operating so as to permit so-called third parties to sue to enforce an agreement and that the operation of these principles does not impact on the narrow doctrines of privity and consideration, but rather defines the boundaries for the operation of the doctrine of privity.

In simple terms, those cases articulate two factors that the court must take into account when deciding whether the benefit of a contract should be extended to third parties in a particular case:

- Whether the parties to the contract intended to extend the benefit in question to the third party seeking to rely on the contractual provision; and
- Whether the activities performed by the third party seeking to rely on the contractual provision are the very activities contemplated as coming within the scope of the contract in general, or the provision in particular, again as determined by reference to the intention of the parties.

The majority of the SCC in *London Drugs* was careful to frame the exception narrowly. Mr. Justice Iacobucci stated:[3]

> Without doubt, major reforms to the rule denying third parties the right to enforce contractual provisions made for their benefit must come from the legislature. Although I have strong reservations about the rigid retention of a doctrine that has undergone systematic and substantial attack, privity of contract is an established principle in the law of contracts and should not be discarded lightly. Simply to abolish the doctrine of privity or to ignore it, without more, would represent a major change to the common law involving complex and uncertain ramifications.

In *Fraser River*, Justice Iacobucci (for the Court) reiterated this cautionary note, but went on to state that in appropriate circumstances, courts must not abdicate their judicial duty to decide on incremental changes to the common law necessary to address emerging needs and values in society. Permitting third-party beneficiaries to rely on a waiver of a subrogation clause (particularly given the language of the clause in that case) was, accordingly, an appropriate incremental change.

The main focus of my 2012 analysis was on the extent to which courts in particular provinces have seen fit to relax the narrow constraints of the principled exception and, in particular, to allow third party beneficiaries to use it as a sword (and pursue claims under the contract) rather than as a shield (as it was used in the SCC cases). I noted that B.C. courts had rejected such a change in the law, while Ontario courts had viewed the law as undergoing evolution.

The intervening 11 years have not resulted in clarity or uniformity in the approach to this issue.[4]

If anything, the 2013 decision of the Ontario Court of Appeal in *Brown v. Belleville*[5] (which I wrote about in my 2014 update) has complicated the analysis.

[3] At para. 43.

[4] Note that I will not consider cases dealing with statutory modification of the doctrine of privity in the context of consumer protection and sale of goods.

[5] 2013 ONCA 148.

What did the ONCA actually decide in *Brown v. Belleville*?[6]

That case involved an agreement whereby the municipality agreed to perpetually maintain and repair part of a storm sewer drainage system constructed on and near lands originally owned by a farmer named Sills, who in turn granted the municipality the right to enter onto his property to construct and maintain the drainage system. The covenant to maintain and repair was personal; it did not run with the land. The Browns were subsequent owners of the property; there had been no assignment of the benefit under the agreement nor had there been a novation. The agreement contained an enurement clause providing that it would "inure to the benefit of and be binding upon the parties hereto and their respective heirs". The Browns sued to enforce the agreement and the municipality defended, in part, on the basis that there was no privity of contract between it and the Browns.

The core finding of the ONCA, in my view, was that the broad and unqualified wording of the enurement clause constituted an express stipulation by the contracting parties that they intended the benefit of an agreement to be shared by future owners of Mr. Sills' land, as his successors or assigns by way of inheritance. On that basis, according to Justice Cronk, the Browns stepped into Mr. Sills' shoes and had standing to enforce the agreement as against the municipality as if they were the original covenantees.

Justice Cronk stated (at para. 83) that the enurement clause could not properly be termed an "exception" to the doctrine of privity, but also concluded that on the particular facts, strict application of the doctrine of privity would ignore the nature, stated purpose and express terms of the agreement and would allow the municipality to escape covenants to which it expressly consented.

As the Court acknowledged, it was not "technically necessary" for it to consider whether the facts fit within the principled exception to privity. However, Cronk J.A. went on to apply the test from the SCC decisions and found that they were satisfied on the facts. She went on to state:

> [110] I recognize that *London Drugs* and *Fraser River* were cases where the third-party beneficiaries sought to rely, by way of defence, on the benefit of the contractual provisions at issue to resist claims brought against them -- they were not seeking to enforce the affirmative benefit of the relevant contractual provisions.
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> [111] Nonetheless, it is my view that the Browns' status as the successors of the original covenantee under the Agreement affords them the right to seek to enforce the original covenantor's contractual obligations, as against the original covenantor. In effect, for the purpose of enforcement of the Agreement, the Browns are Mr. Sills and the City is Thurlow. Further, insofar as the performance of the City's obligations under the Agreement are concerned, there is a clear identity of interest between Mr. Sills and the Browns. As Mr. Sills's successors, the Browns stood ready to comply with the activity required of them under the Agreement -- the provision of access to their lands. In all these circumstances, the application of the principled exception to the privity rule advances the interests of justice.

[6] See the Ogilvie Article for a detailed discussion of this case.

So can a third party beneficiary now rely on the principled exception to enforce a contractual benefit in their favour outside of the particular factual situation in *Brown v. Belleville*?[7]

Based on my review of the case law, the answer is "no" in B.C. and "maybe" everywhere else.

I will start with the B.C. law, since it is, for the most part, consistent in rejecting any extension of the principled exception to allow a third party to enforce rights or benefits bestowed on it by contracting parties.

There are three appellate cases from B.C. rejecting the proposition that the principled exception can be used as a "sword": *RS II Productions Inc. v. B.C. Trade Development Corp.,* 2000 BCCA 674; *Kitimat (District) v. Alcan Inc*., 2006 BCCA 75; and *Holmes v. United Furniture Warehouse GP*, 2012 BCCA 227 (the "BCCA Trilogy").

These cases were all decided pre-*Brown v. Belleville*.

In the one BCCA decision post-*Brown v. Belleville*, while the Court referred to that decision, it found on the facts that there was no evidence that the landlord and tenant under a lease intended to extend the landlord's benefits under the lease (and the overholding tenancy) to beneficiaries of trusts of which the landlord may be or may become the trustee. Therefore, there was no basis for applying the principled exception to privity. Accordingly, the Court did not have to squarely address the fact that the appellant was seeking to use the principled exception as a "sword": *Price Security Holdings Inc. v. Klompas & Rothwell*, 2019 BCCA 36.[8]

Mr. Justice Tysoe stated in part:

> [45] Price Security submits the doctrine of privity should be relaxed in the circumstances of this case to conform with commercial reality and justice and notes, among other things, the lack of prejudice to the Tenant. Price Security takes this concept of commercial reality and justice from *London Drugs*, but the Supreme Court of Canada in that case did not hold that the concept dictated the abolishment of the doctrine. Rather, the Court used the concept to make an incremental change to the law; namely, the establishment of a principled exception to the doctrine, as was amplified in para. 32 of *Fraser River Pile* quoted above. Price Security does not meet the test for the principled exception.
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> [46] It may be that the relaxation of the doctrine of privity will not prejudice the Tenant. However, it must be borne in mind that Price Security made the decision to have the Property held in trust for it by the Landlord. It admits that it did so to achieve tax savings. If it wishes to take advantage of a trust structure,

[7] Professor Ogilvie takes the view that *Brown v. Belleville* "provides support" for the possibility of the principled exception permitting third parties to enforce agreements for their benefit; see Ogilvie Article at 743.

[8] The plaintiff in that case was suing for unpaid rent. It was the beneficiary under a trust pursuant to which the landlord of the subject property was trustee; however, the trust only came into existence after the lease had been executed. The chambers judge rejected all of the exceptions to privity relied upon by the plaintiff, including trust, agency and the principled exception. The Court of Appeal ordered a new trial on the issue of whether special circumstances existed that would permit a trust beneficiary to sue a third party in the place of the trustee. A second summary trial was held on the issue of whether the plaintiff, as the beneficiary of a trust, had standing to sue a third party debtor of the trust in its own name. On the second summary trial, the plaintiff's claim was dismissed on the basis it failed to establish the requisite special circumstances: *Price Security Holdings Inc. v. Klompas & Rothwell*, 2022 BCSC 152, but that result was overturned by the Court of Appeal on the basis that the trustee's failure to protect the plaintiff's beneficial interest in the unpaid rent, and the unjust enrichment of the tenant at the plaintiff's expense constituted special circumstances so as to support the beneficiary's standing to sue the tenant directly: 2023 BCCA 453.

> it should be prepared to accept the limitations of such a structure, particularly when it was open to it to ameliorate those limitations. […]
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> [47] I would not accede to Price Security's argument that the present circumstances meet the test for a principled exception to the doctrine of privity.

There are several trial level decisions citing the BCCA Trilogy or the SCC decisions and rejecting an argument that the principled exception allows a third party beneficiary to sue to enforce benefits under a contract.[9]

In *Burns v. Woodsdale Estates Ltd.,* 2015 BCSC 212, Mr. Justice Sigurdson distinguished *Brown v. Belleville* in circumstances where the plaintiff sought to enforce a positive obligation against a non-party to an easement agreement.[10]

In Alberta, the Court of Appeal on two occasions has referred to the issue of whether the principled exception could be used as a sword, but did not have to decide the issue: *Landex Investments Company v. John Volken Foundation*, 2008 ABCA 333 and *541788 Alberta Ltd v Bourgeois & Company Ltd.*, 2018 ABCA 310. In the latter case,[11] the trial judge, after noting that strict application of the doctrine of privity has been "severely criticized" stated, in *dicta*, that the law in Alberta had evolved with respect to the limitation of the principled exception to matters of defence. Therefore, had it been necessary to rule on the privity issue, he would have allowed the plaintiff to rely on the contract in question as a third party beneficiary and advance its claim on that basis. He stated that he was adopting the position of the Ontario Court of Appeal in *Brown v. Belleville.*

By contrast, in a 2015 decision of the trial court, Justice Renke stated that it had not been authoritatively determined whether the principled exception to the privity rules provides a sword, permitting a cause of action, or whether it only offers a shield: *Condominium Plan No 0125764 v. Amber Equities Inc*., 2015 ABQB 235.[12]

Most recently, in a 2023 decision, Justice Schlosser, citing neither the SCC decisions nor any appellate authorities, held that based on the language used in the agreement,[13] the

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[9] See, for example, *0980131 B.C. Ltd. v. The Owners, Strata Plan KAS2615,* 2019 BCSC 913; *Advantage Tool & Machine Ltd. v. Cross Industries Ltd*., 2023 BCSC 104.

[10] *Brown v. Belleville* was also distinguished in *British Columbia Synod of the Evangelical Lutheran Church in Canada v. Vancouver Chinese Lutheran Church*, 2017 BCSC 2333.

[11] 2017 ABQB 363.

[12] See also *Power v. Goodram*, 2012 ABQB 50.

[13] The clause in question read as follows:

> The Purchase Price for the Shares shall be the obligation of the Purchaser to ensure that the Corporate Licenceholder satisfies ("Satisfaction") the obligations and indebtedness (collectively, the "Indebtedness") of the Corporate Licenceholder as set out on Schedule "A" to this Agreement. The approximate amount of the Indebtedness as of the Closing Date is set out on Schedule "A" to this Agreement. Satisfaction means that the Purchaser shall ensure that a full release of such Indebtedness is obtained from the creditors ("Creditors") who hold the Indebtedness. In addition, Satisfaction shall mean the de-registration of any security held by the Creditors in regard to the indebtedness. The manner in which the Satisfaction is managed shall be in the sole discretion of the Purchaser on behalf of the Corporate Licenceholder. The Purchase Price for the Shares shall be the obligation of the Purchaser to ensure that the Corporate Licenceholder satisfies ("Satisfaction") the obligations and indebtedness (collectively, the "Indebtedness") of the Corporate Licenceholder as set out on Schedule "A" to this Agreement. The approximate amount of the Indebtedness as of the Closing Date is set out on Schedule "A" to this Agreement. Satisfaction means that the Purchaser shall ensure that a full release of such Indebtedness is obtained from the creditors ("Creditors") who hold the Indebtedness. In addition, Satisfaction shall mean the de-registration of any security held by the Creditors in regard to the indebtedness. The manner in which the Satisfaction is managed shall be in the sole discretion of the Purchaser on behalf of the Corporate Licenceholder.

contracting parties intended to extend a payment benefit to the plaintiff and to permit it to sue to recover the payment.

In *Mark T Johnson Professional Corporation v. Vanshaw Enterprises Ltd*., 2023 ABKB 534, the plaintiff was a lawyer's professional corporation that facilitated a transaction whereby the defendants purchased shares in a casino business. The agreement provided that the price for the shares consisted of an obligation on the purchasers to satisfy the indebtedness of the corporate licence holder as set out in a schedule. One of the debts listed in the schedule was the amount of $300,000 owed to the plaintiff law corporation.

When the law corporation was not paid, it sued the defendants. The defendants took the position that since the plaintiff was not a party to the contract, it could not sue on it. Justice Schlosser cited not *Brown v. Belleville*, but rather *dicta* from an older Ontario decision as follows:

> 11 As noted in *Coast-to-Coast Industrial Development Co.*, at paras 43 and 44:
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> > While the principled exception to privity of contract is not restricted to defensive provisions, it seems to me that it would take very clear language to find that a contracting party has assumed a liability to a third party, particularly where that liability is potentially unlimited.
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> 12 The language in this contract is very clear. Liability is not unlimited, potentially or otherwise.
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> 13 The intention of the parties was that Mr. Johnson would be paid. The purchasers agreed to pay him. It may have been open to the purchaser to negotiate a lower price, but the point of the exercise was to retire the vendor's debt to his lawyer.
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> 14 The contract was unequivocal that this benefit be extended to the plaintiff. The 'activities' are specifically described by the provision itself. The *Fraser River* exception applies. Any other approach would lead to a multiplicity of proceedings and likely cloud the issues, but with the same result.

What is the law in Ontario?

There is, of course, the decision in *Brown v. Belleville*.

Prior to that case, in *Arora v. Whirlpool Canada LP*, 2013 ONCA 657,[14] the Court of Appeal left the issue of the principled exception's availability as a sword to be decided another day, and held that it was unnecessary to decide whether it would endorse the approach of the BCCA in the BCCA Trilogy.

As noted above, *dicta* from the Ontario Superior Court of Justice ("ONSC") in *Coast-to-Coast Industrial Development Co. v. 1657483 Ontario Inc*., 2010 ONSC 2011, has been cited in other cases as opening the door to using the principled exception as a sword if there is very clear language providing for that result in the contract.

Post-*Brown v. Belleville*, decisions of the ONSC on this issue fall into four rough categories:

[14] Leave to appeal dismissed, 2014 CarswellOnt 3031 (S.C.C.).

1. Decisions that explicitly rely on *Brown v. Belleville* and take the view that going forward, the principled exception is flexible enough that it can be used as sword – *Seelster Farms v. Her Majesty in Right of Ontario*, 2020 ONSC 4013; *Gilani v. BMO Investments Inc*., 2021 ONSC 3589, leave to appeal dismissed, 2021 ONSC 5906 (Div. Ct.).[15]
2. Decisions finding that the principled exception cannot operate as a sword, *i.e*., as permitting a third party to sue to enforce a benefit–*Cass v. 1410088 Ontario Inc*., 2018 ONSC 5439; *Stevens v. Nexterra Substructures Incorporated*, 2022 ONSC 370.
3. Decisions that focus on the wording of an agreement and, on the particular facts, finding it is sufficient to give a third party an enforcement right–*Desco Plumbing and Heating Supply Inc. v. AVN Plumbing Limited*, 2020 ONSC 6728, rev'd in part (on other grounds), 2022 ONSC 6439 (Div. Ct.).
4. Decisions in which the court applies the criteria for application of the principled exception from the SCC decisions and finds they are not made out–*Golfnorth Properties Inc. v. Rebel Land*, 2019 ONSC 3479; *Bertrand v. Academic Medical Organization*, 2023 ONSC 3209; *Porter Airlines Inc. v. Nieuport Aviation Infrastructure Partners GP*, 2022 ONSC 5922.

In the cases in the last category, the court may be viewed as acknowledging the possibility of using the principled exception as a sword, since the plaintiff in each case was suing under agreements to which it was not a party.

In *Porter Airlines*, the Court cited the *dicta* passage from *Coast-to-Coast* (set out in the passage from *Mark T Johnson Professional Corporation v Vanshaw Enterprises Ltd*. set out above), before concluding that there was no clear language in the agreement showing that the parties intended to extend the benefit of the agreement to Porter or a right of enforcement thereunder.

In *Golfnorth*, the Court cited *Coast-to-Coast* and *Brown v. Belleville*, then concluded:

> [90] I do not read the Court's *obiter* comments in *Brown* as abrogating or dispensing with the law of privity, or altering the test laid down by the Supreme Court of Canada in *Fraser River* for application of the "principled exception" to the privity rule. Indeed, the Court in *Brown* went on to apply the principled exception test to the facts of that case at paras. 95-111.
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> [91] In my view, the first branch of the "principled exception" test is not satisfied in the case at bar. There is no evidence that the parties to the Agreements intended to extend the benefit in question under the Agreements to a non-party seeking to rely on the contractual provision.

There are also examples in the Ontario case law of a court being satisfied that the parties did not intend for the plaintiff to have rights under the principled exception because of a clause or clauses expressly disclaiming a right in third parties.[16]

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[15] Where there is an ascertainable group or class of persons to whom the conferral of a benefit is intended.

[16] In *Forvest Trust S.A. v. The Devine Entertainment Film Library Limited Partnership*, 2013 ONSC 3347, the relevant clause, entitled "Third Party Beneficiaries," read as follows:

> "The Vendor [Devine Corp.] and the Purchaser [Devine LP] intend that this Agreement shall not benefit or create any right or cause of action in, or on behalf of, any person, other than the parties to this Agreement

So perhaps the weight of authority in Ontario is in favour of the principled exception being used as a sword where the parties clearly intended that to be the case, although on my review of the case law, the matter is not entirely without controversy.

Bottom line

Reconciling the case law on the question of whether the principled exception to privity can be used as a sword, not just as a shield, is challenging.

In B.C., until the BCCA weighs in on the issue again, arguing that the principled exception allows a third party to enforce a contract will be an uphill battle in light of the BCCA Trilogy.

In Alberta, while there are at least two decisions in which an ABKB justice accepted a "sword argument", there is also ABKB authority to the contrary. Again, we will have to see what happens when the issue comes before the ABCA in the future.

If one accepts the proposition that the reasoning of Cronk J.A. in *Brown v. Belleville* applies outside the enurement clause in relation to land use context, then in Ontario, a third party can sue to enforce a right or benefit provided they are able to establish the two elements from the SCC cases, *i.e.,* the parties to the contract intended to extend the benefit in question to the third party seeking to rely on the contractual provision; and the activities performed by the third party seeking to rely on the contractual provision are the very activities contemplated as coming within the scope of the contract in general, or the provision in particular.

Subject to the uncertainty raised by the case law, contracting parties can influence the outcome by making plain their intention both that a third party is to benefit from particular rights under the contract and is to have standing to sue to enforce such rights. Conversely, if the parties do not want third parties be able to rely on the principled exception to privity (either as a shield or a sword), they can make that clear by inserting a clause to that effect.

Update on Good Faith Duties in Contract Law

Because the law on contractual duties of good faith continues to develop since the three key decisions of the SCC in 2014 (*Bhasin v. Hrynew*, 2014 SCC 71), 2020 (*C.M. Callow Inc. v. Zollinger*, 2020 SCC 45) and 2021 (*Wastech Services Ltd. v. Greater Vancouver Sewerage and Drainage District*, 2021 SCC 7), I review decisions on this topic every year so as to report anything new or noteworthy.

While there are no major developments to report from case law in 2023, I will report on cases dealing with three topics:

- Proof of loss;
- Where self-interest fits within the duty to exercise contractual discretion in good faith; and
- The relationship between "ordinary" contract law principles and the duty of good faith performance.

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and **no person, other than the parties to this Agreement, shall be entitled to rely on the provisions of this Agreement in any action, suit, proceeding, hearing or other forum".** [Emphasis added.]

Proof of Loss

As I reported in the supplement to my 2020 Update,[17] the majority of the SCC in *Callow* held that the appropriate measure of damages for a breach of the duty of honest performance is the usual expectation measure of damages for breach of contract, putting the innocent party in the position that they would have been had the contractual duty been fulfilled. Damages are to be measured against a defendant's least onerous means of performance.

The trial judge in *Callow* had found that had the defendant in that case (Baycrest) acted honestly in exercising its right of termination, and thus corrected the false impression of the plaintiff (Callow) as to the likelihood of his winter contract being renewed, the plaintiff would have taken proactive steps to bid on other contracts. This conclusion was based on evidence that Callow had opportunities to bid on other contracts for winter maintenance at other buildings, but did not do so given his misapprehension about the status of his contract with Baycrest. Damages were awarded representing the profit that would have been made on the contract plus the costs Callow incurred in leasing equipment in advance. The SCC found no palpable and overriding error in the trial court's approach to damages.

In the process of endorsing the trial judge's approach, Justice Kasirer, after referring to the evidence of Callow's other opportunities, stated:[18]

> In any event, even if I were to conclude that the trial judge did not make an explicit finding as to whether Callow lost an opportunity, it may be presumed as a matter of law that it did, since it was Baycrest's own dishonesty that now precludes Callow from conclusively proving what would have happened if Baycrest had been honest… (the "Callow Passage").

Justice Kasirer cited *Lamb v. Kincaid* (1907), 38 S.C.R. 516 at the end of this passage.

Lamb v. Kincaid was a case about removal and conversion of gold from a neighbouring property. The gold, once severed from the land, was deliberately intermixed with gold from the defendants' property. This conduct obviously made it difficult for the plaintiff to prove which gold came from its property. In that the defendants had destroyed the means of ascertaining the quantity of gold from the plaintiff's property, they were liable in damages for the total value of so much of the intermixed products as were not strictly proved to have come from the undisputed portion of the land.

Kasirer J. cited *Lamb v. Kincaid* again recently in *Ponce v. Société d'investissements Rhéaume ltée*, 2023 SCC 25, at para. 114, for the proposition that where a fact cannot be proved because of a party's dishonesty, that fact will be assumed to be true in the absence of evidence to the contrary.

Lamb v. Kincaid was also referenced in *XY, LLC v. Canadian Topsires Selection Inc*., 2016 BCSC 1095,[19] where Madam Justice Kirkpatrick quoted[20] from earlier reasons of Mr. Justice Kelleher as follows:

[17] https://www.lawsonlundell.com/assets/htmldocuments/Contract%20Law%20Update%20part%202%202020.pdf

[18] At para. 116.

[19] Appeal dismissed as abandoned, 2016 BCCA 469.

[20] At paras. 287-88.

> [278] The plaintiff bears the burden of proving a compensable loss. Where a defendant's wrongful conduct prevents the plaintiff from establishing the loss, adverse facts will be presumed: *Le Soleil* (S.C.) at paras. 286-287, aff'd *Le Soleil* (CA).
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> [279] Where the defendants fail to keep a record that would establish the actual measure of damages, the court may apply the principle *omnia praesumuntur contra spoliatorem* (all things are presumed against a wrongdoer). The principle has been applied by this Court: *Encorp Pacific Canada v. Rocky Mountain Return Center Ltd.*, 2008 BCSC 779. The origin of this legal principle has been traced to *Armory v. Delamirie* (1722), 1 Strange 504, 93 E.R. 664 (K.B.). In that case, the plaintiff gave the defendant a jewel for the purpose of having it assessed. The defendant failed to return it, and the court presumed the jewel to be of the best quality.

Justice Kirkpatrick then noted:

> [288] Other cases cited by XY in support of this principle arising from *Armory* (cited above) are: *Lamb v. Kincaid* (1907), 1907 CanLII 38 (SCC), …

I am not a damages scholar, but it seems to me that this passage deals with how wrongful conduct by the defendant may affect both proof of loss and quantification of damages by way of an adverse inference being drawn against the wrongdoer.

What I find challenging about the Callow Passage is that it is not entirely clear whether the Court was talking about causation of loss (proof a loss was caused by the breach of contract) or quantification of that loss by way of damages (or both).

The BCCA recently explained the difference between the two as follows:[21]

> [123]… *causation* and the *quantification* of loss are separate issues. The first must be proven by the plaintiff on a balance of probabilities—and it is thus framed as a question of fact. The second arises only after the first is proven and is more forgiving in the sense that it accommodates difficulty with assessing the extent of the loss.
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> [124] Three central propositions can be extracted from this discussion. First, proof of causation is an essential requirement in a claim for compensatory damages for breach of contract. Second, the issue of causation is distinct from the issue of the quantification of loss. Third, causation is a question of fact that must be addressed before turning to the issue of quantifying any loss.

Perhaps it does not matter which of these Kasirer J. was talking about in *Callow,* as it would appear that the principle *omnia praesumuntur contra spoliatorem* can be applied in relation to proof of loss or assessment of damages.

Another challenge in interpreting the Callow Passage is the reference to a "lost opportunity". The phrase "loss of opportunity" is used to refer to a particular type of claim for damages (also referred to as loss of chance) epitomized by the historical case of *Chaplin v. Hicks*, [1911] 2 K.B.

[21] In *Sharp v. Royal Mutual Funds Inc.*, 2021 BCCA 307, leave to appeal dismissed, 2022 CanLII 19055 (S.C.C.).

786 (Eng. C.A.).[22] On my read of *Callow*, the plaintiff recovered the full value of the lost contract, and as such his damages claim was not discounted to reflect contingencies as one would expect a loss of opportunity award of damages to be, although it may be that the trial court and SCC in *Callow* were satisfied that there were no such contingencies.[23]

That brings us to the decision of the Ontario Court of Appeal, *Bhatnagar v Cresco Labs Inc.,* 2023 ONCA 401. While it is a decision worth knowing about, all that really happened is that the ONCA shot down a creative interpretation of the Callow Passage.

In *Bhatnagar*, the appellants seized upon the Callow Passage to argue that the court is required to presume a loss of opportunity where there is a breach of the duty of honest performance, in circumstances where there is no proof of loss.

I will summarize the facts before commenting on the decision.

The Plaintiff ("180 Smoke") sold their shares through a share purchase agreement ("SPA") to CannaRoyalty Corp. ("Origin House"). Origin House paid $25 million on closing and the SPA provided for an additional $15 million over a three-year period, if certain milestones were met in the subsequent years, including revenue milestones (the "Milestone Payments").

The SPA also addressed the possible acquisition of Origin House by a third party. In the event that Origin House was sold during the three-year "earn-out period," 180 Smoke would be entitled to the amount of all future entitlements to unearned Milestone Payments.

On April 1, 2019, Origin House announced it had entered into an agreement under which Cresco would purchase Origin House. The transaction was expected to close in 2019, which would trigger the full payment of the Milestone Payments over the three-year earn-out period.

On October 20, 2019, Origin House learned that Cresco was proposing a new target closing date in January, 2020. The transaction closed in early January, 2020 and 180 Smoke was paid the earn-out period payments for 2020 and 2021.

The application judge found that Origin House breached its duty of honest performance by failing to advise the plaintiffs in October 2019 that Cresco was proposing to (and eventually did) move the closing of the Cresco Transaction to January of 2020, after having advised the plaintiffs on numerous occasions that the closing was expected to occur in 2019. However, the application judge made no award of damages. She found that even if the plaintiffs had been promptly advised of the change in the closing date, they would not have been able to meet the revenue targets or take steps to force the transaction to close by the end of 2019.

Justice Kimmel noted:

> [84] The presumption that the Supreme Court refers to in *Lamb* and *Callow* is one that deals with evidentiary difficulties, but it still requires an evidentiary premise. The injured party has an onus to prove the facts upon which damages

[22] In a loss of chance claim, once it is established that the defendant is liable for depriving the plaintiff of a non-trivial loss of chance, neither the fact that the benefit would have been contingent on the actions of a third party, nor any uncertainties and complexities that make it impossible to estimate precisely the plaintiff's likelihood of having secured the benefit, are a reason to deprive the plaintiff of compensatory damages. The plaintiff, having been wrongly deprived of a valuable benefit, is entitled to fair compensation for her or his loss, and the court must make its best estimate of the value of that loss: Harvin D. Pitch and Ronald M. Snyder, *Damages for Breach of Contract*, 2nd ed. (loose-leaf) (Toronto: Carswell, 1989--) at §4.2.

[23] Although there is no commentary to that effect in either decision.

> are estimated, but where the assessment is difficult because of the nature of the damages proved, that will not be a ground for refusing substantial damages. […]
>
> [85] It is not open to the vendors to argue that there was anything they could have done in October 2019 to enable 180 Smoke to achieve its Minimum or Target Revenue Thresholds for the First Earn-Out Period when their representatives conceded on cross-examination that by the time they resigned (which was before the closing date was moved to 2020), and despite their efforts made until then, there was little or no chance of those Revenue Thresholds being achieved in 2019. […]
>
> [88] Damages in a claim for breach of contract are supposed to put the vendors in the position they would have been if they had been told in October 2019 that the closing date had been moved to January 2020. The court does not need to know precisely what the vendors would have done and whether they would have succeeded, but there needs to be some evidentiary foundation upon which the court can conclude that there was a credible opportunity that could have resulted in the closing date being changed, or some other outcome could have been achieved to make up for their loss of the Revenue Milestone Payment for the First Earn-Out Period.
>
> [89] Inferences must be made based on facts that reasonably support them. There is in this case an absence of facts from which the court can reasonably infer that there were steps that the vendors could have taken to influence the parties to move the closing date to December 2019. That is not something that the court can infer lightly in a situation where minority shareholders who have signed a voting and lock-up agreement would be trying to influence the timing of a large cross-border public company Arrangement Transaction. The suggestion that they could have been "a fly in the ointment" in the context of the Arrangement Transaction is not a sufficient evidentiary threshold in these circumstances.

She held there was no evidence of lost opportunity on the part of 180 Smoke and she would not presume one.

The ONCA posed the question on appeal (and answered it) as follow:

> [1] Does the Supreme Court decision in *C.M. Callow Inc. v. Zollinger*, 2020 SCC 45, 452 D.L.R. (4th) 44, create a legal presumption of loss once the court finds a breach of the contractual duty of honest performance? The judge below concluded that finding such a breach does not relieve a claimant from having to show an evidentiary foundation on which the court can conclude there was a loss of opportunity. A central issue on this appeal is whether she erred in that conclusion. In my view, she did not.

The ONCA understood the majority decision in *Callow* to place the burden on the claimant to lead some evidence on which the court can find that the breach of the duty of honest performance resulted in the claimant failing to have a fair opportunity to protect its interests or caused it to lose an opportunity.[24]

[24] At para. 55.

The Court noted that the language used in the Callow Passage is permissive, not mandatory: the Court "may" presume a lost opportunity. Furthermore, it held, the Callow Passage must be read within paragraph 116 of *Callow* as a whole and in the context of the facts of that case. The SCC, according to the ONCA, explicitly found an evidentiary foundation for Callow's claim of "lost opportunity".

I think, perhaps, that what Justice Kasirer the SCC was talking about in *Callow* was proof of loss as opposed to quantification of damages. He was identifying an adverse inference that can be drawn against a wrongdoer whose dishonesty prevents a plaintiff from proving particular facts, but was not suggesting that a plaintiff in those circumstances is entirely relieved from its burden to lead evidence.

And one would expect, if the SCC was articulating a principle whereby there is an invariable presumption that a plaintiff has suffered loss once a breach of the duty of honest performance is proven (either generally or where the plaintiff alleges a loss of chance), it would have been more explicit. Even in true loss of opportunity/loss of chance cases, a plaintiff is not relieved from leading some evidence that that it was deprived of a chance to secure a significant benefit (that is not too remote from the parties' bargain) by the defendant's breach. While it may be impossible to prove an actual loss of the benefit, the plaintiff needs to demonstrate that it had a chance to obtain a benefit that would have existed but for the defendant's wrong and an estimated likelihood that the plaintiff would have actually secured the benefit.[25]

Cases considering the presumption against a wrongdoer in relation to proof of loss or damages do not suggest that the plaintiff is relieved of its burden to lead some evidence on both; rather they state that where the defendant's wrongdoing renders it unusually difficult for this burden to be discharged, although the burden does not shift from one party to the other, it may be met by application of a presumption of adverse facts against the wrongdoer.[26]

Claims for breach of contractual duties of good faith, it would seem then, are subject to the same principles as any other breach of contract claim in terms of causation, remoteness, proof of loss and quantification of damages.

Good Faith Exercise of Discretion and Self-Interest

The majority of the SCC in *Wastech*, after outlining the duty to exercise contractual discretion in good faith, stated in part:

> [73] …the role of the courts is not to ask whether the discretion was exercised in a morally opportune or wise fashion from a business perspective. The common law recognizes that "[c]ompetition between businesses regularly involves each business taking steps to promote itself at the expense of the other. . . . Far from prohibiting such conduct, the common law seeks to encourage and protect it" (*A.I. Enterprises Ltd. v. Bram Enterprises Ltd.*, 2014 SCC 12, [2014] 1 S.C.R. 177, at para. 31, citing *OBG Ltd. v. Allan*, [2007] UKHL 21, [2008] 1 A.C. 1, at para. 142). As a general matter, good faith should not be used as a pretext for scrutinizing motive (*Bhasin*, at para. 70).

[25] For another analysis of *Bhatnagar*, see the article by Jassmine Girgis: https://ablawg.ca/2023/11/07/there-is-no-presumption-of-loss/

[26] See, for example, *Le Soleil Hospitality Inc. v. Louie*, 2010 BCSC 1183 at paras. 286-7, aff'd 2011 BCCA 305, leave to appeal dismissed, 2012 CanLII 12781 (S.C.C.).

> [74] Not only does this deferential approach ensure "some elbow-room" for the "aggressive pursuit of self-interest" (C. Sappideen and P. Vines, eds., *Fleming's The Law of Torts* (10th ed. 2011), at para. 30.120; see also *A.I. Enterprises*, at para. 31), but it also prevents good faith from veering into "a form of *ad hoc* judicial moralism or 'palm tree' justice" (*Bhasin*, at para. 70). In this context, then, courts must only ensure parties have not exercised their discretion in ways unconnected to the purposes for which the contract grants that power.

The question that arises then is how aggressive can the pursuit of self-interest be without breaching the duty? As long as the defendant can establish that it exercised its discretion generally for the purpose for which it was granted, can they act with only their own interests in mind?

There are a few recent cases in which courts touched on this issue.

In *Cedar Peaks Investments Inc. v. 2167584 Alberta Corp*., 2023 ABKB 572, Cedar Peaks was a lender holding mortgages over two properties in Edmonton that were developed by the defendant numbered company ("216"). Cedar Peaks commenced foreclosure proceedings. A third party, Encore Master Builder Inc., held an unpaid vendor's lien. In anticipation of distribution of sales proceeds within the foreclosure proceedings, Cedar Peaks brought an application to determine the priority between its mortgage and Encore's vendor's lien caveat registered ahead of the mortgage in first place on title to the properties.

The contract at issue in the case was a purchase agreement between 216 and Encore. In that agreement, 216 agreed that Encore would be entitled to register an unpaid vendor's lien caveat against title. Encore agreed to "postpone this caveat in favour of a new mortgage by the Purchaser subject to the Purchaser meeting all of the conditions referred to above."

The lender required, as a condition of the financing it provided, that the mortgages be registered in first priority of all other encumbrances and liens or, alternatively, that any existing encumbrances and liens be postponed or subordinated to the mortgages. The mortgage funds were delivered on a trust condition to the same effect. But the postponement never happened and on discovering that the mortgages were behind the caveats on title, the lender made no further advances. Encore was prepared to postpone the caveats at that point, but only upon unconditional receipt of the second advance from the lender. In light of issues involving construction delays and construction defects, and 216's failure to make payments on the mortgages, the lender rejected the idea of advancing further funds in exchange for a postponement. The conditions to Encore's obligation to postpone its security were never met.

Cedar Peaks argued that the purchase agreement imposed an obligation on Encore to postpone the caveats to the mortgages. It also argued that Encore or its legal counsel failed to follow the trust conditions imposed.

Encore argued that its caveats were valid prior-registered interests on title and that Cedar Peaks was seeking to litigate around the apparent negligence of its former counsel.

The primary body of law considered in the judgment is a body of law to the effect that where an instrument provides for a postponement of interests in favour of a subsequent encumbrancer, that subsequent encumbrancer can enforce the right of postponement as a third-party beneficiary.

The law on good faith exercise of discretion came up because of how Encore framed its argument.

Encore asserted that the purchase agreement imposed a conditional obligation upon it to postpone the caveats to the mortgages but that it had an unfettered discretion as to when postponement would occur, and that its decision not to postpone the caveats was a commercially reasonable exercise of its discretion. Encore pointed out that the lender advanced the first mortgage draw with knowledge of its discretion and that the preconditions to postponement set out in the purchase agreement were not met. It said that there was no evidence that it acted in a manner which was ulterior or extraneous to its intentions under the purchase agreement. It argued that it had "some elbow-room for the aggressive pursuit of self-interest."

The Court noted that the application was not about breach of contract as between Encore and 216, but was rather about the equitable remedy available to the lender to require postponement of Encore's caveats. Therefore, it said, Cedar Peaks did not need to show that Encore acted capriciously or arbitrarily or otherwise acted in bad faith and thereby breached their contractual obligation (to 216) to postpone.

The application judge dealt with the failure of 216 to meet the preconditions to the postponement by finding that Encore could no longer insist on 216's performance of the preconditions where it had accepted the first draw mortgage funds.

He then went on to consider the cases on the exercise of contractual discretion in good faith. He found that the purpose and intent of the purchase agreement was to obtain draw mortgage financing for the use of Encore in building two new single-family homes. He held that Encore was not entitled to immunity from the consequences of the agreement to postpone based on 216's failure to meet the preconditions to postponement when that conduct affected Cedar Peak's security and where it accepted the first draw mortgage funds without protesting the request for a registrable postponement. Effectively, then, he found that the course of action chosen by Encore was not a good faith exercise of its discretion (to the extent it had discretion in all the circumstances).

In *1000249084 Ontario Inc. v. Andazesgishahr*, 2023 ONSC 5447, two individuals agreed to purchase and renovate a luxury home with one of them (P) holding title and living in the home but the other (M) having a 50% beneficial interest. Their relationship was governed by a co-tenancy agreement. It provided that the property could only be sold by mutual agreement.

When the relationship fell apart, P wanted to sell the house to pay out the mortgages. M did not.

When the second mortgage went into default, the plaintiff numbered company paid out the mortgage, taking an assignment of it. The plaintiff company was wholly owned by M's son, R.

The plaintiff sought an order for judgment and sale of the property by way of summary judgment.

P alleged that M was the true entity in control of the plaintiff and orchestrated the mortgage buy out. He also alleged that the plaintiff and M colluded and that the plaintiff purchased the mortgage in order to give unfair leverage to M in the dispute between M and P.

Judgment was granted in favour of the plaintiff, with the application judge concluding that P had failed to establish a genuine issue in relation to M controlling the plaintiff or as to the alleged collusion.

One of the arguments that P made is that the Court should draw the inference that M was deliberately trying to harm him because, while P was making good faith efforts to facilitate and sell the property and pay off the encumbrances and debts, M would not consent to a sale. This, P asserted, was a breach of the good faith obligation to act reasonably in the exercise of a discretion.

On three occasions, P provided M with frameworks for the sale of the property, each of which was rejected. The Court identified the imbalance (in favour of P) or risks to M in the first two proposals. While the main issues in the first two proposals were fixed in the third proposal, by that time the plaintiff had already set the motion down for a hearing. At that point there was a lack of trust between the parties caused, in part, by P having taken out a third mortgage without M's consent. The application judge held that M was entitled to act in his own best interests and was not required to agree to something that could undermine them (and so, apparently, did not breach the good faith duty).

It would be helpful if the cases confirmed that the aggressive pursuit of self-interest is only allowed where the exercise of discretion is for the purpose contemplated by the parties when they provided for such discretion. To date, they do not give us that guidance.

Good Faith Duties as Part of the "Ordinary" Law of Contract

The common law duties of good faith articulated by the SCC (sheltered under the organizing principle of good faith that leaves room for other such duties to be articulated) have been part of the contract law landscape for almost a decade.

Yet in *Amacon Alaska Development Partnership v. ARC Digital Canada Corp*., 2023 BCCA 34, leave to appeal dismissed, 2023 CanLII 80890 (S.C.C.), counsel for the appellant alleged a novel error of law by the trial judge: that the trial judge allowed the law of good faith to overwhelm contract law.

ARC Digital Canada Corp. ("ARC") was a tenant of commercial premises. Amacon Alaska Development Partnership ("Amacon") purchased the property and approached ARC about a possible early termination of the lease. ARC was open to negotiation and made it known that its two primary concerns were securing an alternative space and receiving reimbursement for its moving expenses.

Negotiations ensued and a lease modification agreement (the "Lease Modification Agreement") was drafted. It included a new termination date of June 30, 2019 and compensation to be paid to ARC in two installments. The first payment was due upon execution of the Lease Modification Agreement, and the second payment was conditional on ARC vacating the premises by the new termination date. ARC let Amacon know that it would only sign the Lease Modification Agreement once it had secured a new space. Amacon was aware that ARC was currently in negotiations for a potential space.

A few weeks later, on the day it signed a new lease, ARC signed the Lease Modification Agreement and returned it to Amacon. One week later, Amacon informed ARC that it would not sign the Lease Modification Agreement. Amacon did not provide an explanation and did not deliver the first installment. ARC began its claim against Amacon in April 2019.

Two days after the new termination date, in an "unannounced reversal of position,"[27] Amacon delivered a fully executed Lease Modification Agreement to ARC along with the first installment and a letter. In the letter, Amacon stated that ARC was not entitled to the second installment because it had not vacated the premises by June 30, 2019 and ARC was liable for double rent for the overholding period from July 1, 2019. ARC paid only normal rent and provided notice in September that it would vacate the premises by October 31, 2019.

At summary trial, the judge made credibility findings against Amacon and held they had not presented "any reasonable or intelligible commercial rationale"[28] for not signing the Lease Modification Agreement. She "expressly" found that the letter of July 2 was the "first indication by Amacon to ARC that Amacon agreed that it was bound by the [Agreement]."[29] The summary trial judge summarized the parties' positions:

> [79] By the delivery of the signed agreement and cheque on July 2, 2019, Amacon sought to essentially rewrite the Lease Modification Agreement to allow it to pay the first installment of $290,000 after the New Termination Date with the *ex post facto* result that ARC's performance in moving out by the New Termination Date was impossible.
>
> [80] ARC's later position, from a contractual point of view, sought a similar result in terms of rewriting the Lease Modification Agreement. ARC essentially sought to amend ARC's performance date in the Lease Modification Agreement to accord with Amacon's actual performance date. Hence, ARC then took the position that, upon payment of the first installment on July 2, 2019, the New Termination Date was delayed by that same period (3-4 months) and after ARC had vacated by that later date, Amacon was required to pay the second installment.
>
> [81] These unique and unusual circumstances could easily stand as a template for a challenging law school examination question, given the thorny issues that arise.

The summary trial judge made extensive findings of fact in relation to the duty of honest performance. She concluded that Amacon's conduct was dishonest, despite being based on "ordinary contract principles,"[30] and held that Amacon had breached its duty of good faith.

On appeal to the BCCA, Amacon argued that the summary trial judge erred by "expressly declining to apply 'ordinary contract principles' and instead allowing the law of good faith to overwhelm contract law."[31] The Court disagreed.

The BCCA noted that the good faith principles do not exist in a "realm beyond that of basic contract law"[32] and that they form a part of basic contract law. The Court held that the summary trial judge found Amacon had clearly breached its duty of honest performance by

[27] At para 15 (BCCA).

[28] 2021 BCSC 1652, at para. 35.

[29] At para 27 (BCCA). Emphasis on the word "first" is that of the summary trial judge in her reasons at para 52.

[30] At para 28 (BCCA). The summary trial judge was referring to Amacon's position based on the law of repudiation.

[31] At para 35.

[32] At para 68.

"simply"[33] applying the principles of good faith to Amacon's conduct in her analysis. The BCCA rejected the creative assertion that she had leapt over contract law in a single bound.

Bottom line

We already knew, from the decision in *Callow*, that damages for breach of the duty of honest performance attracts damages according to the ordinary contractual measure, *i.e.,* expectation damages.

Recent case law supports the proposition that when it comes to proof of loss and quantification of damages, claims for breach of the contractual duties of good faith are not treated differently from other breach of contract claims.

The duties set out in the good faith cases and the applicable principles articulated there do not exist in a "realm beyond that of basic contract law": they form a part of basic contract law.

When considering alleged breaches of the duty to exercise discretion in good faith, the role of the courts is not to ask whether the discretion was exercised in a morally opportune or wise fashion from a business perspective, and this means that there is "some elbow-room" for the "aggressive pursuit of self-interest." How the pursuit of self-interest interacts with the court's assessment of whether the exercise of discretion was reasonable, *i.e.,* exercised for the purpose for which it was granted, is still unclear and may ultimately be a matter of impression in any particular case.

Shotgun Clauses

I last wrote on buy-sell clauses, commonly referred to as shotgun clauses, in 2011. As I noted then, such clauses are common features of shareholders' agreements. Such clauses serve as a way to end a business relationship in a closely held company if the shareholder relationship breaks down.

A 2023 decision of Justice Winteringham of the B.C. Supreme Court[34] contains a useful review of the principles applicable to such clauses, drawing from a number of the leading appellate decisions on point.

In *Jeana Ventures Ltd. v. Garrow*, 2023 BCSC 1831, two individuals (Sallay and Garrow), through their closely-held companies, invested together to develop two residential properties in West Vancouver, B.C. When the investments failed, Sallay's company sued Garrow and Garrow counterclaimed. One of the issues was whether Sallay breached a buy/sell condition in each of the parties' two shareholders' agreements.

Justice Winteringham reviewed the existing jurisprudence on such clauses and the principles arising therefrom, including:

- Shotgun clauses help align the parties' interests by incentivizing the offeror to put forward a price as close to market value as possible, as, otherwise, they would risk selling at a discount or having to buy at a premium.
- The exercise of a shotgun clause does not itself attract a fiduciary duty.

[33] At para 69.
[34] Justice Winteringham was elevated to the BCCA on December 4th of 2023.

- By availing itself of a shotgun clause, the offeror is not unilaterally exercising a power or discretion that affects the offeree's legal interests.
- Shotgun clauses are viewed as harsh remedies. Accordingly, to engage a shotgun clause, the offeror must adhere to the pre-conditions agreed to in the contract. The courts require strict, but not perfect, compliance. Strict compliance will also be imposed on the offeree.
- A true shotgun clause, once exercised, is irrevocable. Its purpose is to force an end of the business relationship.

In this case, Justice Winteringham found that the purported exercise of the shotgun clause in one of two shareholders' agreement (by one of Garrow's corporations) was invalid, as it was not the entity that was a party to the agreement that purported to trigger the shotgun mechanism, but rather was a distinct corporate entity. She noted that corporations are distinct legal entities and cited *Holmes v. United Furniture Warehouse, supra*, for the proposition that the doctrine of privity generally prevents persons who are not parties to a contract from enforcing or benefitting from it. She held that this was not a case of requiring perfect compliance; it was not open to Garrow to rely on the legal structure the parties had set up when convenient and then disregard it when inconvenient. Thus, the claim in the counterclaim that the other party, Jeana Ventures Ltd., had breached the shotgun provision, was dismissed.

The shotgun provision in the second shareholders' agreement was invoked by the correct corporate entity. But after this purported exercise, the plaintiff became aware of frauds committed by the other party and that it had not contributed to the corporate vehicle (Sandhurst) as required by the parties' agreement.

Justice Winteringham held that there had been a fundamental breach of the Sandhurst shareholders' agreement and that it was therefore open to the plaintiff to elect to terminate the contract. She stated that not enforcing the contract in light of the lacking contribution–and, relatedly, the frauds–would achieve justice in the circumstances, concluding in part:

> 336 In light of the frauds, the plaintiff did not have any real basis to evaluate the Sandhurst SA shotgun clause. Accepting Jeana's claims that the defendants never contributed the funds they agreed to provide to the projects and lied about it, then it is true that their equity in the projects was unequal. The proper functioning and reciprocal nature of the shotgun clause assumes that the shareholders have equal information and similar shareholdings. Absent these elements, Jeana, the party with less information and greater equity, risked being bought out with the money it contributed to the projects, or being forced to pay a business partner that did not pay for its equity in the projects. In turn, the defendants could propose a price that either overvalued their share of the project or where they could simply pay Jeana with its own money. There is an injustice in allowing the defendants to benefit from a contract that they performed in bad faith.
>
> 337 Alternatively, I would find that the defendant's frauds themselves discharge the plaintiff from any obligation to comply with the Sandhurst SA shotgun clause. Fraud is a recognized a [*sic*] manner in which a part [*sic*] may resist the enforceability of a contract: *Douez v. Facebook, Inc*., 2017 SCC 33 at para. 28. Here, fraud was operative both as an inducement for the plaintiff to contract [and] as a means of obscuring the defendant's non-performance of

> key contractual obligations. That fraud directly impacted the plaintiff's ability to properly evaluate Mr. Garrow's September 20, 2020 offer.

The BCCA dealt with shotgun provisions in two 2022 decisions that are referenced by Winteringham J. in *Jeana Ventures*.

In *Wolverton Pacific Partnership v. Triple F Investments Ltd*., 2022 BCCA 262, the parties were shareholders in a closely held corporation (471469 B.C. Ltd.), with their relationship governed by a shareholders' agreement containing a shotgun clause. The shotgun clause required the instigating shareholder to make an offer to "all" of the other shareholders. Following execution of the agreement, the number of directors in the company was decreased and new shareholders were brought in. One of the shareholders (Triple F) made an offer under the shotgun mechanism to all existing shareholders after these corporate changes.

Wolverton, another shareholder, tried to oppose the offer by saying it was now impossible to strictly comply with the terms of the agreement since: (1) the clause stipulating that there be disagreement in relation to a matter that required unanimous board agreement could not be satisfied as they were operating with fewer directors than contemplated in the agreement, and (2) since some of the original shareholders had sold to the new shareholders, the offer could not be made to "all" of the shareholders as required in the agreement.

The BCCA rejected both of these arguments. On the second argument, it held as follows:

> 55 To invoke the buy-sell clause, Triple F is required to make an offer to "all of the other Shareholders". If the New Shareholders are not bound by the Shareholders Agreement, the compulsory nature of the offer would apply to WPP alone. If the New Shareholders are bound by the agreement, they would also be bound by the compulsory buy-out provisions. Triple F made the offer to all the existing shareholders, which includes the remaining original shareholder WPP, so they have complied with the strict requirements of the clause under either scenario. Whether the New Shareholders consider themselves to be bound by the Shareholders Agreement and if so, how they will respond to the offer, are matters to be determined. They do not affect the validity of the offer, which complies with the requirements of the Shareholders Agreement.[35]

In *Blackmore Management Inc. v. Carmanah Management Corporation*, 2022 BCCA 117,[36] the appeal raised the issue of whether a shotgun offer made pursuant to the compulsory buy-sell provision of a shareholders' agreement was revocable within the contractual election period.

The chambers judge had found that the shotgun offer was revocable, relying on the general principle that an offer to contract can be revoked prior to acceptance (unless the parties have specifically agreed otherwise) and the fact that the shareholders' agreement did not contain any language suggesting that a compulsory buyout offer was irrevocable.

[35] Presumably the parties settled the issue of whether the agreement bound the New Shareholders as there is no subsequent decision.

[36] Leave to appeal to the SCC was filed but discontinued.

The BCCA found that the chambers judge made a palpable and overriding error and interpreted the agreement differently, pointing to the following indicia that the parties intended an offer under the shotgun mechanism to be irrevocable:

- The steps outlined in the clause, ending with a provision whereby the recipient shareholder would be deemed to have accepted the offer to sell if it failed to make its election to either buy the other party's (or parties') interest under the terms and conditions in the offer or sell its interest to the instigating shareholder under those same terms and conditions. The shotgun process thereby had to continue once initiated: the recipient of an offer could not avoid the process by failing to make an election.
- The surrounding circumstances, including the commercial context and the interpretative principle of commercial reasonableness. Since the commercial purpose of a shotgun clause is to provide a mechanism for shareholders to terminate their relationship by forcing a sale of one shareholder's interest in the company, an interpretation that would allow the shotgun process to be unilaterally stopped once triggered is inconsistent with this objective.
- Further, an important feature of a shotgun mechanism is that each party has an incentive to make their offer as close to market value as possible because the instigator does not know whether it will be required to buy or sell. An interpretation that would make the offer revocable would allow a shareholder to attempt to buy shares at a below-market rate and then revoke if it became apparent that the recipient shareholder was going to elect to buy them out.
- The parties were experienced business people, with counsel, who must be taken to understand the consequences and risks of triggering the shotgun mechanism. It is not for the court to rescue a party who later regrets contractual arrangements that were carefully designed and accepted by the parties.

The recent decision in *Leeder Automotive Inc. v. Warwick*, 2023 ONCA 726, is worth reading for a number of reasons:

- It distinguishes compulsory shotgun clauses (that can be used to initiate a sale of shares against an unwilling vendor) from buy-sell mechanisms with built-in off ramps, which the Court treats as akin to rights of first refusal.
- It wrestles with the question (which may be primarily an academic question) of whether invocation of a buy-sell mechanism and a response to it by the counterparty gives rise to a standalone contract.
- It summarizes the law on the question of whether there is such a thing as a partial repudiation (which confirms that there is not).

In this case, the unanimous shareholders' agreement (the "USA") contained a buy-sell mechanism with the following elements:

- Before any shareholder solicited third-party offers for their shares, they had to offer their shares for sale internally (*i.e.*, as a right of "first consideration"). That is, a shareholder had to give written notice to the other shareholders, and to the Corporation, of their intention to sell.

- The Corporation then was entitled to purchase the shares by providing written notice. If the Corporation did not provide written notice, the other shareholders were entitled to purchase the shares. If the other shareholders did not do so, the offeror of the shares was entitled to sell their shares to a third party.
- Once the buy-sell mechanism was triggered, Article 12 of the USA provided for the manner in which the valuation of the shares was to be determined. In summary, the Corporation's auditors or accountants were to prepare financial statements using generally accepted accounting principles ("GAAP"), the Corporation's real estate was to be appraised by an independent expert agreed upon by the shareholders, and the Corporation's goodwill was to be determined using the formula contained in Article 12.3. The fair market value of the shares was to be determined by adding up the value of the Corporation's assets, including its goodwill and the value of its real estate.

Warwick gave notice of his intention to sell all of his shares in the Corporation. Around the same time, four other minority shareholders also provided their notices. The Corporation agreed to buy the shares, but ultimately the relationship between Warwick and the Corporation's CEO broke down and Warwick refused to sell his shares. The Corporation brought an application seeking to compel Warwick to complete the transaction. Warwick defended on the basis that the Corporation had repudiated the share purchase transaction by failing to close the transaction in the stipulated time period and by relying on valuations of the Corporation's property and goodwill respectively that Warwick said were not carried out in compliance with Article 12.

The application judge found that the failure to close the transaction on time was technical and did not amount to repudiation, but that each of the failures to comply with Article 12 were sufficient in its own right to amount to repudiation. Whereas Article 12.2 required the Corporation and the shareholders to agree upon an independent business valuator, the Corporation did not consult Warwick and unilaterally chose the valuator. The valuations done of the properties were also done in advance of the Valuation Date specified in the USA.

Under Article 12.1, in preparing the valuation of the business, the valuator was required to use GAAP applied on a basis consistent with those used in the preceding fiscal year. Instead, the valuation report was unaudited and did not apply GAAP. Further, the Corporation instructed the valuator to remove a $5,000,000 settlement the Corporation had received in the Volkswagen TDI emissions scandal from the calculation of net annual income.

In the trial court, the parties agreed that the notice given by Warwick, coupled with the Corporation's response, constituted a standalone contract incorporating the terms of the buy-sell provision. When, following the hearing, while judgment was under reserve, the decision in *Blackmore* was issued, the Corporation's counsel brought that decision to the application judge's attention and emphasized its position that the initiated share-purchase transaction created a separate contract (which it said was not revocable). Warwick agreed it was a separate contract but asserted that it had been repudiated.

The application judge, however, relied on the following passage from *Blackmore* to conclude that there was only one contract, *i.e.,* the USA:

> 31 I am not persuaded that the invocation of a shotgun clause is either an exercise of a contractual option or an offer to form a new contract. Rather, to invoke a shotgun clause is to rely on a term of an existing contract by which the parties have agreed to a compulsory buyout procedure. As a result, whether the respondents were entitled to

revoke the shotgun offer depends on the proper interpretation of the shareholders' agreement as a whole.

In *Blackmore,* the BCCA went on to interpret the shotgun clause in the context of the shareholders' agreement as a whole.

On appeal in *Leeder*, the Corporation had new counsel, who argued that the application judge was correct in finding that the buy-sell mechanism did not create a separate contract. The reason for making that argument was that the law does not recognize the concept of partial repudiation; accordingly, there was no basis for the application judge finding that there was repudiation of the contract that justified relieving Warwick from completing the transaction.

The ONCA found that the application judge had made a palpable and overriding error in concluding that the buy-sell mechanism did not give rise to a standalone agreement, but concluded that she was correct in finding that the agreement was breached in a number of respects, amounting to repudiation.

The ONCA then had to explain the approach of the BCCA in *Blackmore.* It concluded that the question of whether the shotgun mechanism gave rise to a standalone agreement played a minor role in that case; rather, the focus of the BCCA in *Blackmore* was on the effect of a compulsory buyout procedure contained in a shotgun provision. The ONCA does not expressly state that the BCCA got it wrong.

There was no allegation of repudiation in *Blackmore* and thus the question of whether there was a standalone agreement or only one agreement (the shareholders' agreement) was not as significant as it was in *Leeder.* In *Leeder,* the application judge's conclusion that there was no standalone contract gave rise to a problem in her analysis–the fact that the law does not recognize the concept of partial repudiation. Accordingly, said the ONCA, the application judge could not have properly found that while the share-purchase transaction was merely an implementation of the USA, the transaction "agreement" was repudiated.

The ONCA compared the buy-sell mechanism before it and the one under consideration in *Blackmore* and concluded they were substantively different. Whereas the mechanism in *Blackmore* was compulsory, the mechanism in *Leeder* contained "little that was compulsory" according to the ONCA, at least until the Corporation or other shareholders elected to purchase the offered shares. The mechanism had built-in exit ramps, including where the Corporation declined to purchase the shares and where other shareholders did the same. In that circumstance, the shareholder could sell the shares to a third party.

The ONCA found that the clause before it was akin to a right of first refusal, giving rise to a new contractual arrangement built on an offer to sell and the acceptance of that offer. Thus, the triggering of the buy-sell mechanism did not force a sale as the shotgun clause did in *Blackmore*. Instead, the buy-sell mechanism required an acceptance of the seller's offer by the Corporation (or by other shareholders) and in this way the mechanism differed fundamentally from the shotgun clause in *Blackmore*. Therefore the application judge should not have relied on the analysis in *Blackmore*.

That the buy-sell mechanism in this case had to give rise to a standalone contract was illustrated by the fact that the mechanism could lead to a share sale to a third party who was not a party to the USA, noted the Court.

Bottom line

Buy-sell mechanisms in shareholders' agreements involving sophisticated parties are not boilerplate and are often crafted to fit the particular parties and circumstances.

The appellate decisions dealing with these types of provisions over the past two years underscore how some may be framed as compulsory mechanisms that can be used to initiate a sale of shares against an unwilling vendor (which are aptly described as shotgun clauses), whereas others may be framed as non-compulsory (and more akin to a right of first refusal), in the sense that they include off-ramps, such as the ultimate right of the initiating shareholder to sell their shares to third parties in certain circumstances.

The interpretative principles that apply to the former type (true shotgun clauses) are helpfully set out in the 2023 BCSC decision in *Jeana Ventures Ltd. v. Garrow.*

There is some dissonance in the law in terms of whether a standalone contract is formed once the buy-sell mechanism is initiated and responded to by the receiving party. The determination of that issue may, ultimately, be a question of contract interpretation in a given case.

Revisiting Notional Severance

I last provided an update on the concept of notional severance in 2019.[37]

I will not repeat here everything I said there other than to summarize the key takeaways:

- Severance is available as a remedy to salvage contract provisions that would otherwise be unenforceable as contrary to statute or common law unless policy concerns dictate to the contrary.
- There are two types of severance: blue-pencil and notional. The former involves removing part of a contractual provision in circumstances where the part being removed is clearly severable, trivial and not the main purport of the provision in question. The latter is more flexible, in that the court may use it to read down a contractual provision so as to make it legal and enforceable.
- A party seeking severance must address the factors from *Transport North American Inc. v. New Solutions Financial Corp.*, [2004] 1 S.C.R. 249, and be alive to policy concerns that may militate against the use of notional severance (or indeed the use of severance at all).
- Because both types of severance involve altering the original contract between the parties, court should be restrained in their use of severance because of the rights of parties to freely contract and choose the words that determine their obligations and rights.
- Notional severance is not available to cure overbroad restrictive covenants in employment contracts,[38] but is available in the context of unenforceable restrictive covenants in business contracts.

[37] https://www.lawsonlundell.com/assets/htmldocuments/Contract%20Law%20Update%20-%20Developments%20of%20Note%202019.pdf
[38] For a recent application of that proposition, see *Skyscope Technologies Inc. v. Jia*, 2023 BCSC 1288.

A significant portion of the jurisprudence on severance arises in the context of loans that breach the criminal interest rate provision (s. 347) of the *Criminal Code*.[39] The past three years are no exception.

In two recent decisions, the B.C. Court of Appeal clarified the mechanics of notional severance as it should be applied in this context.

In *Forjay Management Ltd. v. 625536 B.C. Ltd*., 2020 BCCA 70,[40] the parties had entered into a second mortgage agreement for a one-year term. The nominal interest rate on the mortgage was 12%, but of the $10 million amount secured by the mortgage, $4 million represented fees paid to the lenders (two fees of $2 million each). The trial judge found that the second mortgage provided for a criminal interest rate, contrary to s. 347(1) of the *Criminal Code*, and fashioned a remedy that severed one of the $2 million lender/broker fees, increased the nominal mortgage rate from 12% to 18%, and ordered that the overall effective annual interest rate was not to exceed 40%.

The BCCA held that the trial judge had, by combining notional severance with modification of terms, misunderstood the "spectrum of remedies" established in *Transport North.*[41] In its analysis, the Court referred to an article authored by Professor Waddams where he wrote:

> … I would hope that the references to a flexible remedy and a spectrum do not imply that a judge might select any interest rate between zero and 60% according to his or her view of the culpability of the lender and the appropriate punishment. This would be, in my opinion, to make the rights of the parties to a civil dispute depend too much on considerations more appropriate to the criminal law. I would suggest also that "order" or "disposition" might be a better word in this context than "remedy". The court is not here granting a remedy to the borrower for the lender's wrong; still less is it granting a remedy to the lender for any wrong of the borrower's. It is enforcing a contract, but, for reasons of public policy, not to its full extent, and the question in issue is, "To what extent does public policy prevent enforcement of this contract?" The answer will vary with the circumstances of the case, but this is not the same as saying that it is discretionary.
>
> [Emphasis added by the BCCA.][42]

The BCCA agreed with Professor Waddams' perspective and held that a judge's discretion is limited to choosing among three remedies. These are: voiding the contract *ab initio*, striking out/severing particular provisions of the contract ("blue-pencil severance"), and reading the interest rate down to the legal rate of 60% ("notional severance").

In this case, having determined that the rate exceeded the criminal interest rate and that the contract should not be declared void *ab initio* based on the surrounding circumstances, the options were to either sever particular terms of the contract *or* read-down the interest to an effective annual rate of 60%.

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[39] R.S.C. 1985, c. C-46. "Criminal rate" is defined in s. 347(2) to mean an effective annual rate of interest calculated in accordance with generally accepted actuarial practices and principles that exceeds sixty per cent on the credit advanced under an agreement or arrangement.

[40] Leave to appeal dismissed, 2020 CanLII 71311 (S.C.C.).

[41] *Forjay*, at para. 44, citing *Transport North*, at para. 238.

[42] *Ibid.* at para 58, citing S.M. Waddams, "Illegal Contracts, Severance and Public Policy" (2005) 42 Can. Bus. L.J. 278 at 281.

In a subsequent case, *Community Savings Credit Union v. Bodnar,* 2022 BCCA 263, the Court applied *Forjay* to a fact pattern involving overdraft fees charged by credit unions that, to the extent they exceeded the amount of $5.00 per transaction, had to be factored into the interest rate for the purposes of the *Criminal Code*.

The plaintiffs in this class proceeding alleged that overdraft fees charged by eight credit unions until 2003 frequently resulted in effective interest rates that exceeded the 60% legal limit established by s. 347 of the *Criminal Code*. The *Criminal Code* explicitly defines "overdraft charge" to mean "a charge not exceeding five dollars for the creation of or increase in an overdraft, imposed by a credit union…"[43] Under this provision, charges exceeding $5.00 per transaction for overdrafts are considered to be interest. Until 2003, the defendant credit unions, unaware of this provision, imposed higher overdraft charges. Where overdrafts were small or outstanding for short periods of time, the resulting interest rate exceeded the criminal interest rates.

The plaintiffs sought damages for unjust enrichment or under provincial consumer protection legislation. The trial judge determined that where the imposition of the overdraft charges served to increase the effective interest rate beyond the permitted 60%, the credit unions were unjustly enriched at the expense of the members who paid the charges. He was of the view that an equitable remedy would be to allow the credit unions to retain only $2.50 of the overdraft charge in respect of each transaction.

On appeal, the BCCA had to address the law on notional severance because the only juristic reason capable of supporting the enrichment lay in the contractual arrangements between the credit unions and their members. Only to the extent that the law was prepared to enforce those contracts would they justify the enrichment of the credit unions.[44]

The Court relied on the *Transport North* framework, which sets out how a court can sever unlawful provisions from a contract, and *Forjay* for its clarification on the available remedies. In *Transport North*, the SCC confirmed that there are:

> …four considerations relevant to the determination of whether public policy ought to allow an otherwise illegal agreement to be partially enforced rather than being declared void *ab initio* in the face of illegality of contract:
>
> 1. whether the purpose or policy of s. 347 would be subverted by severance;
>
> 2. whether the parties entered into the agreement for an illegal purpose or with an evil intention;
>
> 3. the relative bargaining positions of the parties and their conduct in reaching the agreement;
>
> 4. the potential for the debtor to enjoy an unjustified windfall.[45]

The BCCA did not consider these four considerations to be a checklist, but rather viewed each as a reflection of "different concerns underlying the exercise of discretion."[46] The first consideration recognizes that a judge's discretion cannot be allowed to override the legislative intent of the *Criminal Code* provision. The second consideration takes into account

[43] In s. 347(2).
[44] At para 54.
[45] *Transport North*, relying on *William E. Thomson Associates Inc. v. Carpenter*, 1989 CanLII 185 (Ont. C.A.).
[46] *Bodnar*, *supra* at para 70.

"the broader goals of the criminal law and regulation."[47] The third consideration "recognizes that the law is aimed at preventing lenders from exploiting vulnerable or desperate borrowers."[48] The fourth consideration reflects a desire to avoid exploitation of the lender by the borrower; the borrower should not be able to exploit a lender's unknowing violation of the criminal interest rate provision to obtain a windfall.[49] The four considerations are designed to place transactions on a spectrum.

Applying the law to the trial judge's decision, the BCCA found that the trial judge erred by adding a fifth consideration when it said that "the Credit Unions ought not to be disincentivized from being proactive in ensuring their agreements comply with the *Criminal Code*."[50] The Court rejected this additional consideration as the four considerations already allow a court to take into account the need for deterrence and for disincentives to violate a law. The addition of this fifth consideration would cause considerations of deterrence to have a disproportionate effect on the remedy.

Relying on the framework clarified in *Forjay*, the BCCA found that the trial judge incorrectly "fashioned a remedy that is not one of the three found…to be available."[51] Applying the law to the case, the BCCA found the simplest way to apply severance was to reduce the overdraft charge on each transaction to the legal amount of $5.00 as defined in the *Criminal Code*. In doing so, the Court acknowledged that while the remedies outlined in *Forjay* did not include a reduction of an overdraft charge, the remedy was "consistent with the underlying rationale of *Forjay* and was the most reasonable way to notionally sever the loan agreements to make them lawful."[52]

Bottom line

Notional severance is typically the go-to remedy when courts are dealing with agreements that have the effect of imposing a criminal interest rate. But the availability of that remedy does not give the judge *carte blanche* to adjust the interest rate in any fashion they deem appropriate.

Rather, in the criminal interest rate context, notional severance permits the judge to read the criminal interest rate down to the lawful rate of 60%.

I have not reviewed the cases dealing with notional severance and restrictive covenants in commercial agreements, and therefore will not comment on any guidance that exists in that case law as to what notional severance allows in that context. Given the length of this paper, I will leave that topic for another day.

Offer and Acceptance in the Digital Age

The proposition that an offer to contract can be made and accepted by digital means (where the offer does not require a specific form of acceptance) is not controversial in 2023.

[47] *Ibid.* at para 71.

[48] *Ibid*. at para 72.

[49] *Ibid.* at para. 73.

[50] *Ibid.* at para 83, citing the lower level decision.

[51] *Bodnar*, *supra* at para 86.

[52] *Bodnar*, *supra* at para 92.

Courts have looked at emails as evidence of the necessary communication of acceptance: see, for example, *Vancouver Canucks Limited Partnership v. Canon Canada Inc*., 2015 BCCA 144, *Code Red Security v. Sheraton Centre Toronto Hotel*, 2021 ONSC 7212, and *Bouttell v. T-Bay Movers Corporation*, 2018 ONSC 5532. Clickwrap agreements, whereby a purchaser indicates acceptance by clicking on "I Agree," or something similar, are ubiquitous online.

A 2023 decision of the Saskatchewan Court of King's Bench has garnered lots of commentary because the necessary acceptance was communicate by way of an emoji.

In *South West Terminal Ltd. v Achter Land and Cattle Ltd.*, 2023 SKKB 116, the plaintiff purchased grain from the defendant using deferred grain contracts for many years. The defendant company was owned by Chris Achter. In March 2021, the plaintiff texted Mr. Achter and his father with a request to purchase grain at a set price with delivery in "Oct/Nov/Dec."[53] After a telephone call with Mr. Achter's father, the plaintiff drafted a contract providing for delivery in November. After signing the contract, the plaintiff took a photo and texted the contract to Mr. Achter with the message "please confirm flax contract."[54] Mr. Achter texted back with a "thumbs-up" emoji. Mr. Achter and his company did not deliver the flax grain in November.

At trial, the main issue was whether there was a valid contract between the parties. The Court began its analysis by reviewing the law as set out in *Ethiopian Orthodox Tewahedo Church of Canada St. Mary Cathedral v Aga*.[55] The Court then reviewed the relationship of the parties. The SKKB noted that the parties had a pattern of entering into deferred delivery contracts, that both knew to be valid and binding. In the past, each time the plaintiff had texted the contract to the defendant, he would do so with the request to confirm. Mr. Achter replied by texting "'looks good', 'ok' or 'yup.'"[56] The Court found the parties clearly understood the curt words to mean confirmation of the contract and not simply acknowledgement of its receipt, as argued by the defendant.

The Court noted that it did not matter what Mr. Achter thought the emoji meant, but rather what an "informed bystander would understand."[57] The Court rejected Mr. Achter's version of events "as the circumstances leading up to the conversation (multiple previous contract negotiations resulting in contracts) support [the Plaintiff's] recollection."[58] The trial judge concluded that a reasonable bystander, knowing all the background, would have an objective belief that a contract had been formed.

The trial judge further found that an emoji is "an action in electronic form" that can be used to allow to express acceptance as contemplated under the *The Electronic Information and Documents Act*."[59]

The Court rejected the Defendant's public policy argument that, by allowing a thumbs-up emoji to constitute acceptance, the Court will open the flood gates to numerous claims asking for interpretation of various emojis. The trial judge agreed the case was novel, but found "nevertheless this Court cannot (nor should it) attempt to stem the tide of technology

[53] At para 5.

[54] At para 6.

[55] 2021 SCC 22 at para 35 [*Aga*].

[56] *Achter*, at para. 21.

[57] *Ibid*. at para. 29.

[58] *Ibid*. at para. 35.

[59] *Ibid.* at para.37, referencing *The Electronic Information and Documents Act*, *2000*, S.S. 2000, c. E-7.22.

and common usage – this appears to be the new reality in Canadian society and courts will have to be ready to meet the new challenges that may arise from the use of emojis and the like."[60]

The SKKB found the parties entered into a legally binding contract. The Court then turned its attention to whether the use of the emoji was enough to meet the requirements of the *Sale of Goods Act,* which requires "some note or memorandum in writing" and "signed by the party to be charged."[61] While the Court accepted that an emoji is a non-traditional way to sign a contract, under the circumstances of the case, an emoji was a "valid way to convey the two purposes of a signature"[62] as required by the *Sale of Goods Act*.

Bottom line

An offeror can stipulate a mode by which the offer must be accepted. Statutory provisions may require acceptance in writing and also that the acceptance be signed.

Absent such requirements, acceptance may be found to have occurred by conduct.

Acceptance leading to a binding contract is routinely carried out nowadays by electronic means. When considering whether an acceptance by electronic means suffices (where the contract is not clear on the topic), make sure you consult any statute applicable to the type of contract and also the electronic transactions statute in force in the relevant province or territory. The latter may provide a means of complying with requirements in the former; conversely, the former may be framed in such a way as to preclude electronic communications being treated as documents "in writing" or to preclude email or other electronic signature as being equivalent to traditional "wet" signatures.

[60] *Ibid*. at para. 40.

[61] *Ibid.* at para 54 referencing *The Sale of Goods Act*, R.S.S. 1978, c. S-1.

[62] *Ibid.* at para 63.

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Contract Law Developments of Note Summary of Topics

Headings	2022	2021	2020	2019	2018	2017	2016	2015	2014
Links to Contract Law Paper by Year	Link	Link	Link	Link	Link	Link	Link	Link	Link
Acceptance by Conduct									
Anti-oral Amendment Clauses							X		
Arbitration Clauses	X				X	X			X
Automatic Renew Clauses								X	
Best Efforts Clauses	X								
Binding Effect and Enurement Clauses									
Buy/Sell Clauses									
Conditions Precedent									
Confidentiality Clauses							X		
Consideration in the Context of Contract Variations					X				
Constitutions/bylaws of voluntary associations as contracts	X								
Continuing Breach of Contract							X	X	
Continuing Interpretation				X			X		X
Contract Termination									

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Headings	2022	2021	2020	2019	2018	2017	2016	2015	2014
Links to Contract Law Paper by Year	Link	Link	Link	Link	Link	Link	Link	Link	Link
Contracting with First Nations under the *Indian Act*									
Contracts with government	X								
Contractual References to Legislative Provisions					X				
Discretionary Powers							X		
Duties of Good Faith (see supplements)	X	X	X				X	X	X
Efficient breach									X
Economic Duress									
Electronic Transactions									
Entire Agreement Clauses				X					X
Equitable Mistake									
Exculpatory Clauses and Limitation of					X			X	X
Forum Selection Clauses			X		X	X			X

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Headings	2022	2021	2020	2019	2018	2017	2016	2015	2014
Links to Contract Law Paper by Year	Link	Link	Link	Link	Link	Link	Link	Link	Link
Frustration and *Force*					X				
Fundamental Breach									
Illegal Contracts									
Implied Terms and Implied Contracts				X			X		
Inconsistent Terms			X						
Indemnity Clauses				X					
Liquidated Damages									
Mistake			X						
Mitigation									
No Suit Clauses						X			
"No Waiver" Clauses		X							
Nomincal Consideration				X					
Non est Factum		X							
Options							X		
Ordinary course of business covenants	X								
Penalty Clauses							X		
Perpetual Contracts		X							
Pre-Incorporation Contracts		X							

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Headings	2022	2021	2020	2019	2018	2017	2016	2015	2014
Links to Contract Law Paper by Year	Link	Link	Link	Link	Link	Link	Link	Link	Link
Privity of Contract									
Rectification	X		X			X			
Releases		X				X			
Rescission	X								
Rights of First Refusal							X		
Restrictive covenants									X
Severability				X					
Smart Contracts					X	X		X	X
Specific Performance									
Standard of Review on Contract Interpretation Issues							X		X
Statutory Illegality									
Statutory Warranties Under the International Sale of Goods Act				X					
Stipulated-Consequence-on-In-solvency Clauses			X						
Time of the Essence Clauses									
Unconscionability		X	X	X				X	X

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We hope that the information in this Contract Law update is helpful and we look forward to speaking with you.

Please reach out to Lisa A. Peters, K.C. if you have any questions or require further information.

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