Contract Law Update: Developments of Note

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This paper was presented at the
5th Edition Negotiating and Drafting Major Business Agreements Conference
Vancouver, B.C.

September 20–21, 2011

[1] I would like to thank my research associate, Willa Duplantis, Sophie Elliott and Kyla Schwartz (articled students), and our librarian, Susannah Tredwell, for their help in the preparation of this paper.

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CONTRACT LAW UPDATE: DEVELOPMENTS OF NOTE (2011)

Focus and Scope of This Paper

Each year I review judgments dealing with contract law issues looking for decisions of relevance to commercial lawyers and business leaders. Contract law principles typically do not change overnight; rather, they are modified incrementally. Where I find a case that illustrates an incremental change, I use it as a springboard for discussing the state of the law on the particular issue and how it affects commercial practice. I also consider private international law conventions and treaties that are en route to domestic implementation, and are therefore relevant to commercial practice.

This paper is not meant to be a comprehensive review of Canadian contract law principles. There are a number of excellent textbooks that take on that daunting task.[1]

This year, the topics I have chosen are:

- Unconscionability in commercial transactions;
- Unconscionability and exculpatory clauses post-*Tercon*;
- Impact of consumer protection legislation on mandatory arbitration/mediation clauses;
- Buy/sell clauses;
- Best efforts clauses (and their variants);
- Equitable mistake and contract rescission;
- Clauses affecting non-contracting related entities, privity and the corporate veil.

If I have not covered a topic of interest to you in this year's paper, I may have covered it in past papers (published in the materials for this seminar in prior years and on-line at http://www.lawsonlundell.com/Team/Lawyers/Lisa-Peters).

The topics covered in my prior updates are:

> **2010**: Fundamental breach; arbitration clauses; choice of court (forum selection) clauses; time of the essence clauses; economic duress; pre-incorporation contracts; illegal contracts.

[1] I recommend, for example, John D. McCamus. *The Law of Contracts* (Toronto: Irwin Law, 2005) and Angela Swan, *Canadian Contract Law*, 2nd ed. (Markham: LexisNexis, 2009).

2009: Enforceability of exculpatory clauses (exclusion clauses and limitation of liability clauses); illegal contracts and severance; good faith obligations in contract; frustration and *force majeure*; contract termination; privity of contract and third party beneficiaries.

2006: Good faith in contract law; assignment of contractual rights; mistake; rectification; entire agreement and exclusion clauses; termination clauses; frustration; severability of illegal provisions; penalty and liquidated damages clauses; unilateral contracts.

Unconscionability in Commercial Transactions

Historically, unconscionability has not played a major role in Canadian contract law, at least as it applies to commercial transactions. The cases assessing contracts from the perspective of whether they are unconscionable typically arise in a consumer transaction context or at least in a context where the plaintiff is a vulnerable individual (rather than a corporation or other business association). The party raising unconscionability will often be seeking to have the entire contract set aside.

In B.C.,[2] Part 2 of the *Business Practices and Consumer Protection Act*, S.B.C. 2004, c. 2, contains a statutory regime applicable to unconscionable acts or practices by suppliers. That regime applies to "consumer transactions", which are defined as follows:

> **"consumer transaction"** means
>
> (a) a supply of goods or services or real property by a supplier to a consumer for purposes that are primarily personal, family or household, or
>
> (b) a solicitation, offer, advertisement or promotion by a supplier with respect to a transaction referred to in paragraph (a),
>
> and, except in Parts 4 and 5, includes a solicitation of a consumer by a supplier for a contribution of money or other property by the consumer;

This statutory regime reverses the burden of proof,[3] requiring the supplier to prove that the unconscionable act or practice in question was not committed or engaged in. It also gives the Court considerable flexibility as to remedies.

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[2] There are similar regimes in other provinces' consumer legislation: see, for example, *Consumer Protection and Business Practices Act*, S.N.L. 2009, c. C-31.1, ss. 8-10.

The common law of unconscionability applies to transactions falling outside this regime.

What sort of conduct amounts to unconscionability at common law? In the oft-cited B.C. Court of Appeal decision in *Morrison v. Coast Finance Ltd.* (1965), 55 D.L.R. (2d) 710, Davey J.A. explained the concept as follows (at 712):

> …a plea that a bargain is unconscionable invokes relief against an unfair advantage gained by an unconscientious use of power by a stronger party against a weaker. On such a claim the material ingredients are proof of inequality in the position of the parties arising out of the ignorance, need or distress of the weaker, which left him in the power of the stronger, and proof of substantial unfairness in the bargain obtained by the stronger. On proof of these circumstances, it creates a presumption of fraud which the stronger must repel by proving that the bargain was fair, just and reasonable or perhaps by showing that no advantage was taken.

A subsequent B.C. Court of Appeal decision takes a different (and arguably inconsistent) approach to the assessment of unconscionablity. *Harry v. Kreutziger* (1978), 9 B.C.L.R. 166 (C.A.), involved an unsophisticated business person who sold his fishing boat and commercial fishing licence to the defendant at a significantly undervalued price. In Lambert J.A.'s concurring judgment, he boiled unconscionability down to a single question: "…whether the transaction, seen as a whole, is sufficiently divergent from community standards of commercial morality that it should be rescinded" (at 177).

As a recent B.C. Law Institute consultation paper notes,[4] subsequent cases lean slightly towards the *Morrison v. Coast Finance Ltd.* formulation, but a majority of the B.C. Court of Appeal endorsed the *Harry v. Kreutziger* formulation in *Gindis v. Brisbourne*, 2000 BCCA 73, leave to appeal refused, [2001] S.C.C.A. No. 145.

Some cases refer to both tests and purport to apply them both (rolling the notion of commercial morality into the assessment of the fairness of the bargain).

Despite Lambert J.A.'s invitation to assess unconscionability from the perspective of commercial morality, there are very few truly commercial cases where a finding of unconscionability was made, leading to rescission.

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[3] See subsection 9(2).

[4] *Consultation Paper on Proposals for Unfair Contracts Relief* (Vancouver: British Columbia Law Institute, 2010).

On the current state of B.C. law, it is open to an unhappy party to a commercial transaction to make a common law claim for rescission based on unconscionability My unscientific survey of existing cases suggests that unconscionability is most likely to be raised in insurance settlement, banking or franchise fact patterns. When dealing with unsophisticated parties (which can include corporations) in these settings, counsel and the larger enterprise need to be alive to the elements of unconscionability. Turning a blind eye to disadvantages of the opposite parties, such as illiteracy, lack of business knowledge or financial distress, could result in commercial uncertainty in the long run, with the transaction being vulnerable to attack on the grounds of unconscionability.

Where the complaining party received independent legal advice, a plea of unconscionability is unlikely to succeed; see the discussion in *Ma v. MIV Therapeutics Inc.*, 2004 BCCA 483.

Unconscionability and Exculpatory Clauses

The role of unconscionability in the court's assessment of the enforceability of exclusion clause is perhaps of more potential relevance to commercial practice.

In my paper last year I discussed the Supreme Court of Canada's decision in *Tercon Contractors Ltd. v. British Columbia (Transportation and Highways*), 2010 SCC 4, and the test the Court articulated for dealing with the application of exclusion clauses where there is a breach of the contract by a party *prima facie* entitled to rely on such clause, and an allegation by the innocent party that the breaching party should not be permitted to so rely.

The Court first must ask whether, as a matter of interpretation, the exclusion clause even applies to the circumstances established in evidence. If the exclusion clause does apply, the second step is to consider whether the exclusion clause was unconscionable and thus invalid at the time the contract was entered into.

If the answer to the second question is "no", then the court may consider whether it should nevertheless refuse to enforce the exclusion clause because of overriding public policy.

The Supreme Court of Canada in *Tercon* was not limiting its analysis to the consumer context or the context of individuals contracting with corporations. However, post-*Tercon*, unconscionability arguments as a means of evading exclusion clauses are surfacing primarily in cases involving plaintiffs who are individuals rather than corporations or other types of business associations. The provincial courts have been the primary testing ground for this component of the *Tercon* test.

Interestingly, the lower court judges do not refer to the tests for unconscionability articulated by the B.C. Court of Appeal when assessing exclusion clauses under the *Tercon* test.

Two recent cases dealt with home inspection contracts and clauses purporting to limit the liability of the inspection company to the amount of their fee.

In *Schiltroth v. RDS Enterprises o/a "Home-Alyze"*, 2010 SKPC 47, the inspector was negligent in failing to identify certain roof and eaves deficiencies. The plaintiffs claimed for the cost of rectifying those deficiencies. The contract in this case included both a sweeping exclusion clause and a provision limiting liability to an amount no greater than the price of the inspection and report.

The Saskatchewan Court found the clauses to be unconscionable and unenforceable. Scott J. noted that the plaintiffs were new to home buying and were not in an equal bargaining position. They signed the standard form contract after the work was done. The inspector did not explain the exclusion clause or limitation of liability.

In *Calder v. Jones*, 2010 BCPC 77, the inspector negligently failed to carry out a visual inspection of the home. However, the Court refused to relieve the plaintiffs from the effect of the clause in the contract limiting liability. The plaintiffs, the trial judge concluded, were bright articulate individuals who would have no difficulty understanding the plain language of the clause, so there was no inequality of bargaining power. The fact that the inspector did not bring the clause to their attention did not render the bargain unconscionable either.

In *Campbell v. 0698900 BC Ltd.*, 2010 BCPC 136, Campbell entered into a contract to store his travel and horse trailers at the defendant's storage lot. The standard form contract disclaimed bailee or warehouseman status on the part of the lessor, expressly set out that the lessor carried no insurance for the lessee's property, and had the lessee agree to hold the lessor harmless for any damage and exempted the lessor from liability for theft or damage to the property caused by acts or omissions by the lessor, its agents or anyone else.

The travel trailer was stolen from the lot. The plaintiff sued the defendant, arguing that it had to meet the standard of care of a bailee or, alternatively, failed to meet its duties under the *Occupiers Liability Act*. The defendant relied on the exemption language in the contract. The plaintiff argued that the clause should not be enforced by the court.

The trial judge found that in all the circumstances, the clause was not unconscionable and should be enforced. While the defendant was a numbered company and the plaintiff an individual who operated a small business, there was no evidence that the defendant was more sophisticated. The plaintiff received the contract in the mail and had ample time to read it and seek out advice if he wished. The contract was in plain language. There was evidence that the plaintiff had signed other similar standard form contracts with limitations of liability. There was some evidence of a representative of the defendant confirming with the plaintiff that he needed to obtain his own insurance and what he would be liable for.

Roy v. 1216393 Ontario Ltd., 2011 BCSC 465, involved a contract of purchase and sale for a residential lot to be developed as part of a subdivision in Vernon. The plaintiffs paid a 10% deposit. Unbeknowst to them, the defendant had already entered into a similar agreement with another couple for the same lot. The defendant had purported to cancel that agreement but the matter was in litigation. Subsequently, those other purchasers obtained an order for specific performance. The plaintiffs sought damages for breach of contact, since the lot was no longer available to them. The contract contained an exclusion clause that purported to limit the defendant's liability to liquidated damages equivalent to a return of the purchaser's deposit.

Josephson J. noted that there was appellate authority prior to *Tercon* finding such a clause to be unenforceable. He went on to apply the *Tercon* test and found that the exclusion clause was unconscionable and unenforceable under that test as well. It permitted the vendor to walk away from the contract with no consequence at all, while the purchasers would face significant consequences if they failed to comply with obligations imposed on them. From the purchasers' perspective, it made the purported contract no contract at all.

Bottom line: In a consumer transaction context, businesses and their advisors need to be aware of the applicable statutory unconscionability regime. Where the transaction is not a consumer transaction but one of the parties is an individual or small business enterprise, businesses using standard form contracts need to be aware of unconscionability as a basis for setting aside contracts and the desirability of adverse parties obtaining independent legal advice as a prophylactic measure.

Drafters of commercial agreements need to be alive to the role of unconscionability in the enforceability (or not) of exclusion and limitation of liability clauses. The case law to date suggests that courts will not balk at refusing to enforce exclusion clauses by finding them to be unconscionable and may be more receptive to this type of argument than an unconscionability claim seeking rescission of the entire agreement. Where enterprises relying on exemption and limitation of liability clauses bring them to the attention of their customers and give the customers an opportunity to review standard form contracts containing such clauses, they are more likely to be able to enforce them.

Buy/Sell Clauses

Buy/sell clauses, also referred to as shotgun clauses, are a common feature of shareholders' agreements. Such clauses are often the product of extensive negotiation, meaning that court decisions interpreting them may have little precedential value.

However, there are three appellate decisions from the past three years that do provide some helpful guidance on how courts will interpret such clauses.

In *942925 Alberta Ltd. v. Thompson*, 2008 ABCA 81, the issue was whether two shareholders could, in combination, make an effective joint offer under a shotgun clause. The article in question referred to a single shareholder as an "Offeror" and contemplated

an Offeror giving notice to one or more of the other shareholders ("Offeree" or "Offerees"). Thus, the Court held, while the article contemplated an offer to one or more shareholders, it did not contemplate the converse. The Court cited the decision of Virtue J. of the Alberta Court of Queen's Bench in *Trimac Ltd. v. C-I-L Inc*., [1987] 4 W.W.R. 719 at 727:[5]

> A shotgun buy-sell is strong medicine. One takes it strictly in accordance with the prescription or not at all.[6]

The principal question in *Aronowicz v. Emtwo Properties Inc.*, 2010 ONCA 96, was whether, in triggering a shotgun provision by delivering an offer to purchase, a shareholder owed fiduciary duties. The plaintiff and one of the individual defendants were brothers (Abraham and Harry), and parties to a unanimous shareholders' agreement ("USA"). Harry triggered the shotgun clause in the USA. After the transaction closed, Abraham learned that as part of the financing arrangements by which Harry raised the funds to buy him out, Harry had agreed to repay the loan by transferring three of the company's properties to the lender. Abraham took the position that Harry was obliged to disclose these financing details because, had he known of them, he could have responded differently in the shotgun process.

The defendants brought a successful summary judgment motion, so that the plaintiff's claim was dismissed in its entirety, and that result was upheld on appeal.

Mr. Justice Blair made the following helpful comments at paragraph 50:

> It is hard to conceive of a corporate/commercial mechanism less likely to attract the operation of fiduciary obligations than a shotgun buy/sell provision in a unanimous shareholder agreement. The same may be said for the operation of obligations to act reasonably, honestly and in good faith - other than the good faith obligation not to act in a fashion that eviscerates the very purpose of the agreement. A shotgun buy/sell provision is the quintessential corporate mechanism for the exercise of shareholder self-interest. Carefully drafted, it provides a delicate balance for the preservation of the parties' individual rights by ensuring that the pulling of the trigger

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[5] Varied on other grounds, [1987] 6 W.W.R. 66 (Alta. C.A.).

[6] See also *942925 Alberta Ltd. v. Thompson*, 2008 ABCA 81, where the Court stated at para. 21 that "a shareholder must strictly comply with the terms of a shotgun clause [buy-sell] in order to obtain its benefit".

> generates the best and highest price in exchange for the involuntary termination of the shareholders' relationship.

Zeubear Investments Ltd. v. Magi Seal Corporation, 2010 ONCA 825, dealt with two groups of shareholders in the defendant corporation, referred to by the Court as "the Harris group" and the "Geddes group". The shareholders' agreement between the two groups contained a shotgun clause.

In January 2010, the Harris group triggered the shotgun clause. The offer under the shotgun clause was either to purchase the Geddes group's shares or to sell its own shares to the Geddes group. In the former case, given that the Geddes group had originally purchased its shares with promissory notes, the offer contemplated that indebtedness would be set-off against the value, effectively meaning that there would be no cash consideration. The offer contemplated that on a sale of the Harris group's shares, the Geddes group would have to pay to redeem the first tranche of shares paid for with promissory notes and pay for the remainder of the Harris group's shares. While the Geddes group accepted the offer, choosing the option of purchasing the shares held by the Harris group, their acceptance indicated that the purchase price would be satisfied in accordance with the prescribed terms of the shareholders' agreement, which provided for partial payment only upon closing with the balance to be paid by way of promissory note. The Harris group took the position that the Geddes group's purported acceptance was invalid because it did not comply with the terms of the offer. The Harris group argued that because the acceptance was non-compliant, the Geddes group was deemed to have accepted the sell option pursuant to the express provisions of the shotgun provision.

The shotgun provision contained a paragraph entitled "Minimum Terms". It stated that, "Notwithstanding any other provision hereof...the Terms shall be deemed to provide, *inter alia*, that…" followed by a list of terms dealing with the purchase price.[7]

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[7] The clause read in part as follows:

> *Minimum Terms*. Notwithstanding any other provision hereof … the Terms shall be deemed to provide, *inter alia*, that: […]
>
> (c) payment of the Purchase Price for all of the Shares to be purchased pursuant to this section shall be made by delivering on completion:
>
> (i) at least 50.0% of the Purchase Price in cash or by certified cheque or bank draft; and
>
> (ii) a promissory note for the balance of the Purchase Price, which promissory note shall:
>
> A. bear interest at a fixed rate…;

The live issue then, was whether this list of terms were only minimum terms that had to be included in an offer in order to trigger the buy-sell process or whether they were deemed to be included in every offer as mandatory terms (and could not be tinkered with by an offeror).

The Geddes group applied to the Superior Court of Justice for an order declaring that its acceptance of the Harris group's offer to sell was validly made. That application was dismissed on the grounds that the provisions of the shareholders' agreement stipulated only the "minimum terms" which a shareholder was required to include in any shotgun offer. The applications judge held that the Geddes group's failure to reply in accordance with the terms of the Harris group's offer constituted a counteroffer rather than a valid acceptance. The Geddes group appealed from that decision.

The Court of Appeal held that the terms relating to the purchase price provided for in the shareholders' agreement were mandatory. From the offeror's perspective, these terms had to either be expressly included in any shotgun offer or they would be deemed to be included. The Harris group's offer was not invalid, but the terms as to payment in the shareholders agreement were incorporated into it. Therefore, the Geddes group validly accepted the offer by offering to pay on the precise terms set out in the deeming provision. The Court concluded that its interpretation was the commercially reasonable one and took the view that it was not commercially unreasonable to interpret the clause in a manner that, at least to some extent, leveled the buy-sell playing field between the parties. Had the Harris group's interpretation been accepted, the Harris group would have been able to purchase the Geddes group's shares without paying any money unless the Geddes group was able to pay close to $3 million within 90 days and pay out the promissory notes (a tall order).

Bottom line: Shareholders are entitled to act in a self-interested fashion when triggering a buy-sell clause. However, they must be careful that either as offeror or offeree, they understand and strictly comply with the terms of such a provision. If various modes of exercise are contemplated (*i.e.*, one offeror or two) they need to be built in expressly. Be

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B. be payable in full on or before the first (1st) anniversary of the date of completion;

C. be open for prepayment…; and

D. be secured by a pledge of all the Shares held by the purchaser, including the Shares being purchased and, where the purchaser is a Shareholder which is not an individual, the personal guarantee of its Principal(s).

careful with deeming provisions, as they may tie the hands of the offeror in structuring the offer.

Best Efforts Clauses

Parties to commercial agreements frequently include clauses that require a party to make "best efforts" to fulfill a condition or carry out particular obligations.

Over time, variations of the phrase "best efforts" to describe a performance obligation, have found their way into agreements. The common variations include: commercially reasonable efforts; reasonable commercial efforts; commercial best efforts; reasonable best efforts.

Lawsuits alleging that a party failed to fulfill the standard imposed in such a clause are quite common. Commercial solicitors and their clients clearly need to understand the standard against which the performance in question will be measured when a particular variation is adopted.

The leading case on what a "best efforts" obligation entails is *Atmospheric Diving Systems Inc. v. International Hard Suits Inc.* (1994), 89 B.C.L.R. (2d) 356 (S.C.). At paragraph 71 of that decision, Dorgan J. distilled the existing case law into seven propositions:

> 1. "Best efforts" imposes a higher obligation than a "reasonable effort".
>
> 2. "Best efforts" means taking, in good faith, all reasonable steps to achieve the objective, carrying the process to its logical conclusion and leaving no stone unturned.
>
> 3. "Best efforts" includes doing everything known to be usual, necessary and proper for ensuring the success of the endeavour.
>
> 4. The meaning of "best efforts" is, however, not boundless. It must be approached in the light of the particular contract, the parties to it and the contract's overall purpose as reflected in its language.
>
> 5. While "best efforts" of the defendant must be subject to such overriding obligations as honesty and fair dealing, it is not necessary for the plaintiff to prove that the defendant acted in bad faith.
>
> 6. Evidence of "inevitable failure" is relevant to the issue of

> causation of damage but not to the issue of liability. The onus to show that failure was inevitable regardless of whether the defendant made "best efforts" rests on the defendant.
>
> 7. Evidence that the defendant, had it acted diligently, could have satisfied the "best efforts" test is relevant evidence that the defendant did not use its best efforts.

The phrase “best efforts”, then, imposes a high standard of conduct. For that reason, contracting parties may negotiate for a less onerous standard by using the terminology “commercially reasonable efforts” or “reasonable commercial efforts” (in my view, these two are properly treated as synonyms).

The leading authorities on the meaning of “reasonable commercial efforts” are the trial and appeal decisions in *364511 Ontario Ltd. v. Darena Holdings Ltd* (1998), 55 O.T.C. 13 (Gen. Div.), var’d (1999), 120 O.A.C. 280.

Those decisions confirm that “reasonable commercial efforts” is a lower standard than “best efforts”. The trial judge resorted to dictionary definitions of “reasonable” and “commercial” and in doing so, made it clear that the use of the term “commercial” allows the party with the performance obligation to take into account its economic position and viability when deciding where to draw the line in terms of attempted performance of the obligation. These decisions also explain that the more relaxed standard of “reasonable commercial efforts” does not mean that the performing party can elect whether to perform or not. As a corollary, the party cannot, through its own actions, create a situation where it is impossible for it to perform.

Two subsequent B.C. decisions (both of which cited *364511 Ontario Ltd. v. Darena Holdings Ltd* with approval) illustrate what will or will not constitute “reasonable commercial efforts”. In *GC Parking Ltd. v. New West Ventures Ltd.*, 2004 BCSC 706, a purchaser under an “Offer to Purchase” was required to put forth “reasonable commercial efforts to obtain all governmental approvals and permits as may be required or considered desirable by the Purchaser, acting reasonably, in order to complete its proposed casino development”. Mr. Justice Burnyeat found that there was no obligation on the plaintiff to take the various necessary applications through to refusal, as to do so would have been expensive, time consuming and commercially irresponsible once it was apparent that the approvals would not be forthcoming.

In *Nelson v. 535945 British Columbia Ltd*., 2007 BCSC 1544, the defendant purchaser was obligated to use “all reasonable commercial efforts” to achieve an increased floor space ratio (“FSR”) through rezoning. Mr. Justice Ehrcke rejected the proposition that the word “all” imported a higher standard than “reasonable commercial efforts” (*i.e.*, a standard equivalent to “best efforts”). (Interestingly, there are English authorities to the contrary, expressly finding that “all reasonable endeavours” and “best endeavours” do

mean the same thing: see *Rhodia International Holdings Ltd. v. Huntsman International LLC*, [2007] EWHC 292 at para. 33, var'd on other grounds, [2007] EWCA Civ 621 and, most recently, *Jet2.com Limited v. Blackpool Airport Limited*, [2011] EWHC 1529 at para. 47 (Comm.)[8]).

Mr. Justice Ehrcke concluded that what the defendant was required to do was "to pursue the increased FSR up to the point where it became commercially unreasonable for them to proceed further." The plaintiff argued that the defendant had to, at minimum, make an application for rezoning to City Council. Based on expert evidence as to the political climate at the time, the history of approvals of increased density or height, and on conversations the defendant's representatives had with City planning staff, the trial judge found that the defendant's decision not to submit a formal application was commercially reasonable. He summed up at paragraph 54:

> The standard the defendant was required to meet under the Contract was to make "all reasonable commercial efforts" to achieve an FSR above 2.3 no later than August 31, 2005. They were not required to make all possible efforts. They were not required to make all efforts short of those that would be doomed to certain failure. The standard of reasonable commercial efforts allowed them to make reasonable business decisions in which they would weigh the cost of proceeding beyond the first stage of discussions with City planning staff against the cost of preparing a formal application to City Council. That is precisely what Anthem did. The defendant concluded that the political climate in the fall of 2004 was such that it would not be prudent from a business point of view to spend the many thousands of dollars it would have cost to pursue a formal application to Council, since the chance of success was too low.

What standard do the terms "reasonable best efforts" and "commercial best efforts" import? There is no case law that assists in placing these terms on a continuum that has "best efforts" on one end and "reasonable commercial efforts" at the other. Common sense suggests that "commercial best efforts" is somewhat less onerous the unmodified "best efforts" in that it may bring business judgment and economic interests of the performing party into the mix. "Reasonable best efforts" seems to me to be the most difficult variation of all to attribute meaning to. "Reasonable efforts" by itself denotes a lower standard than "best efforts" but it is not clear what parties might intend by combining the two.

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[8] We understand an appeal is underway from this decision.

Because contract interpretation is a contextual exercise, context is critical regardless of the standard chosen. Therefore, what constitutes a commercially reasonable effort in one case may not in another. Note that who the obligated party is may also be relevant in the interpretative exercise: government actors are entitled (and indeed required) to take into account the public interest, which will necessarily qualify what will amount to best efforts on their part. (See, for example, *Wentworth Developments Inc. v. Calgary (City)* (1998), 59 Alta. L.R. (3d) 265 (Q.B.)).

Bottom line: Pick the standard you are imposing as part of a performance obligation carefully. A "best efforts" obligation is considerably more onerous than a "reasonable commercial efforts" standard and, in particular, leaves little scope for the party subject to the obligation to exercise business judgment and take into account financial considerations in deciding when to stop making efforts to fulfill the obligation.

Equitable Mistake

In my 2006 paper, I reviewed the poorly understood distinction between common law and equitable mistake. As you may recall from your law school days, the decision in *Bell v. Lever Brothers Ltd.*, [1932] A.C. 161 (H.L.), has generally been interpreted as severely limiting the ability of a party to obtain an order setting aside a contract on the basis of a mistaken assumption at common law. It is only where there is an error that is fundamental in character, something fundamental going to the root of the contract, that the common law will find that there is no consensus *ad idem*, *i.e.*, the contract is void for mistake. One way of explaining the common law approach is that it distinguishes between mistakes that affect the intention to contract and mistakes that operate on the mistaken party's motive for contracting.

Pursuant to the common law rule, if there was consensus *ad idem*, in that the parties had agreed to the same terms on the same subject matter, no relief was available to a party who agreed to those terms based on a mistaken assumption.

A Lord Denning decision, *Solle v. Butcher*, [1950] 1 K.B. 671 (C.A.), formed the basis for parties seeking relief where they had made a mistaken assumption, and the so-called doctrine of equitable mistake.

In that case, the defendant agreed to let a flat to the plaintiff for £250 per year. The flat had previously been let at a rent of £140 per year. Both parties believed that because of substantial work done on the flat, it was freed from rent control that previously had applied. They were mistaken. The defendant could only charge the rent-controlled amount of £140 per year.

Lord Denning held that while there was a fundamental mistake as to the rent that could be charged, there was nonetheless an enforceable lease. However, he observed that in equity, a court could set aside a contract when it was unconscientious for the other party to take advantage of it.

He then made the following oft-cited statement (at 693):

> A contract is also liable in equity to be set aside if the parties were under a common misapprehension either as to facts or as to their relative and respective rights, provided that the misapprehension was fundamental and that the party seeking to set it aside was not himself at fault.

In *Great Peace Shipping Ltd. v. Tsavliris*, [2002] 4 All E.R. 689 (C.A.), the English Court restated the test for operative mistake at common law in a restrictive fashion. The Court went on to hold that the views expressed by Lord Denning in *Solle v. Butcher* were wrong, and irreconcilable with the majority opinions in *Bell v. Lever Brothers Ltd.*, and that the supposed equitable jurisdiction invoked in *Solle v. Butcher* and later English cases was a mere "chimera".

The English Court of Appeal made clear its view that the law ought to strive to uphold, rather than destroy, apparent contracts, and that the ability of a party to a contract to obtain rescission for mistake should be restricted accordingly.

In 2006, I wondered out loud whether Canadian judges would follow *Great Peace Shipping*. If the past five years of jurisprudence are any indication, it appears they will not and will keep Lord Denning's concept of equitable mistake alive.

In 2007, Mr. Justice Goudge of the Ontario Court of Appeal took the view, in *dicta*, that there was good reason for not adopting *Great Peace Shipping* in Canada: in his view, loss of the flexibility needed to correct unjust results in widely diverse circumstances would be a step backwards. (See *Miller Paving Limited v. B. Gottardo Construction Ltd.*, 2007 ONCA 422).

In two recent Alberta decisions, plaintiffs relied upon equitable mistake as the basis for rectifying or rescinding transactions that resulted in unforeseen tax consequences. In each case, the Court found grounds for either rescinding or rectifying the contracts.

In *Stone's Jewellery Ltd. v. Arora*, 2009 ABQB 656, the order rescinding land transfer agreements resulted in a $6 million tax savings. Madam Justice Strekaf indicated her awareness of the decision in *Great Peace Shipping* at paragraph 30, but held that the law had not changed in Canada, and that Canadian courts recognize a wider availability of equitable rescission for mistake than exists at common law.

Mr. Justice Graesser in *S&D International Group Inc. v. Canada (Attorney General)*, 2011 ABQB 230, did not expressly refer to *Great Peace Shipping*; he cited other cases in which equitable mistake gave rise to relief by way of rescission or rectification. While he noted that courts should be slow to use their equitable jurisdiction as a way of allowing parties to change the bargain they made or to use that jurisdiction as a means of effecting retroactive tax planning, he confirmed that that equitable jurisdiction continued to be

available in appropriate circumstances. In *S&D International Group Inc.*, the rectification order reduced the corporation's tax burden by amounts in the millions of dollars.

In *Romank v. Achtem*, 2009 BCSC 1757, Mr. Justice Barrow, without expressly referencing *Great Peace Shipping*, acknowledged that *Solle v. Butcher* was the subject of controversy in England. He then expressed the view that equitable mistake is still a feature of Canadian law.

Most recently, in *0707448 B.C. Ltd. v. Cascades Recovery Inc.*, 2011 BCSC 1065, Mr. Justice Silverman commented on the uncertainty as to whether equitable mistake still formed part of Canadian law in light of the decision in *Great Peace Shipping*. He held he did not have to decide the issue on the case before him.

Bottom line: A Canadian party seeking to rescind or rectify a contract on the basis of mistake can still rely on the broader concept of equitable mistake, raising a mistaken assumption rather than a mistake that goes to the parties' actual intention to contract. If the current trend continues, we will not follow England's lead in restricting relief for mistake to a narrow category of cases. The net result is more opportunity for buyer's (or seller's) remorse to give rise to a remedy and less commercial certainty.

Mandatory Arbitration/Mediation Clauses in Contracts of Adhesion

Cases dealing with pure contract law concepts do not frequently make their way to the Supreme Court of Canada ("SCC"). The SCC case of note this past year (from a contract law perspective) is *Seidel v. Telus Communications Inc.*, 2011 SCC 15. In *Seidel*, the SCC considered the enforceability of an arbitration clause in a consumer context.

Seidel involved a cellular phone services contract between Telus and a consumer, Ms. Seidel. Ms. Seidel alleged that Telus falsely represented how it calculated air time for billing purposes. She based her claim on both common law and statutory causes of action, including causes of action under the *Business Practices and Consumer Protection Act*, S.B.C. 2004, c. 2 ("*BPCPA*"). When Ms. Seidel applied to have her claim certified as a class action, Telus sought a stay on the basis of the arbitration clause in the contract. The arbitration clause provided that "any claim, dispute or controversy" would be determined by mediation or failing that, arbitration.

Telus relied in part on *Dell Computer Corp. v. Union des consommateurs*, 2007 SCC 34, which also dealt with an arbitration clause in a consumer contract. In *Dell*, the SCC dismissed the plaintiff's motion to institute a class action and sent his claim to arbitration on the basis that the arbitration clause in the contract was not prohibited by any Quebec legislation in force at the time the contract was entered into. (A prohibition is contained in the current Quebec legislation: see *Consumer Protection Act*, R.S.Q., c. P-40.1).

In *Seidel*, the SCC confirmed that arbitration clauses will be enforced in the absence of legislation prohibiting them, even in the context of contracts of adhesion. A majority of five-to-four held that the arbitration clause was not enforceable in relation to Ms. Seidel's claims under the *BPCPA*, but that it was enforceable in relation to her other statutory and common law claims. The majority grounded its decision in the legislative intent behind s. 172 of the *BPCPA*, which provides a right for a person, whether or not they are affected by any consumer transaction, to bring an action in the Supreme Court. The purpose of this provision is to enhance consumer protection by ensuring that complaints against suppliers are made public, and that suppliers can be enjoined from engaging in offending conduct against any consumer, not just the complainant.

The arbitration clause in *Seidel* also contained a class action waiver. The Court held that the waiver could not be severed from the arbitration clause and thus was also unenforceable in relation to Ms. Seidel's claims under the *BPCPA*. The net result is that Ms. Seidel's *BPCPA* claims could proceed to court as a class action but her other claims were required to go to arbitration.

Commercial lawyers seeking to include a class action waiver in a contract should keep severability in mind when drafting such provisions. *Seidel* does not directly rule on whether a properly drafted, separate waiver clause would be enforced or run afoul of B.C.'s consumer protection legislation. While U.S. jurisprudence has found class action waivers to be unconscionable, the SCC declined to consider this issue in *Seidel*.

Note that Ontario has invalidated arbitration clauses and class action waivers in relation to claims under consumer protection legislation (see *Consumer Protection Act*, S.O. 2002, c. 30, Sch. A, ss. 7(2) and 8(1)). Alberta requires ministerial approval of arbitration clauses for such claims (see *Fair Trading Act*, R.S.A. 2000, c. F-2, s. 16).

Bottom line: Solicitors drafting or reviewing consumer contracts need to be alive to consumer protection statutes (and the differences in such statutes across Canada) because they may invalidate arbitration clauses and class action waivers to the extent such clauses purport to apply to consumers' statutory claims.

Clauses Affecting Related, Non-Contracting Parties, Privity and the Corporate Veil

A very recent decision of Mr. Justice Sigurdson of the B.C. Supreme Court shines the spotlight on the practice of including language in restrictive covenants (or other clauses imposing obligations) that purports to "bind" (and I use that word loosely on purpose) not just the contracting entity, but its related entities. The case is of interest not because it articulates new principles, but because it underscores: 1) the importance of the express language chosen by the parties; and 2) the difficulty a party will face in seeking to rely on the narrow exceptions to the doctrine of privity or the concept of piercing the corporate veil if the express language does not capture all members of a corporate family.

The facts in *Emtwo Properties Inc. v. Cineplex (Western Canada) Inc.*, 2011 BCSC 1072, are somewhat complex. The plaintiffs E and T were successive assignees of the original landlord (Cadillac Fairview) under a lease of the Granville Cinema (the "Lease"). The original tenant Cineplex Odeon Canada (COC) assigned its interest to a wholly-owned subsidiary, Cineplex Western, through a series of transactions following upon a CCAA proceeding. COC then sold its assets, including the sole share in Cineplex Western, to a limited partnership (CELP). CELP subsequently acquired partnership units in the Famous Players Limited Partnership and thereby acquired the Scotiabank theatre in the same neighbourhood. Under a consent agreement with the Competition Commissioner, CELP assigned the Lease to Empire, but without limiting its liability under the Lease.

The Lease contained what is described as a radius clause (Clause 7.03), which read as follows:

> It is understood and agreed and it is a condition precedent to the execution of this Lease by the Landlord, that the Tenant acknowledges that the income of the Landlord is dependent upon the attraction of customers to the Leased Premises and the Shopping Centre. Therefore, the Tenant agrees that throughout the Term:
>
> > (a) it shall not, and
> >
> > (b) it shall not suffer or permit any Person under its control ~~or connected or affiliated with it;~~ whether as partner, shareholder (of five percent (5%) or more of the issued and outstanding shares of the Tenant), lender (unless such lender is a recognized public financial institution), employee or otherwise, to
>
> engage directly or indirectly in, or furnish any financial assistance to, any business which is the same as or similar to, or in competition with, the Tenant's business in the Leased Premises within any building or building complex, any portion of which is located within a radius of ... ~~two (2) miles~~ *1200 feet* from any point on the perimeter of the Leased Premises …
>
> To give effect to the foregoing, if the Tenant shall breach the foregoing covenant, or if another business as described in this Section is operated within the radius aforesaid, the Landlord, in addition to any other remedy available to it, is entitled to require that the gross revenue (calculated in the same manner as Gross Revenue) from and in respect of any

> such other business be included in the computation of Gross Revenue hereunder, as though such gross revenue had actually been made from the Leased Premises …

The Scotiabank theatre is within 1200 feet of the Granville Cinema. The plaintiffs took the position that Cineplex Western was liable under the radius clause by reason of CELP's operation of the Scotiabank theatre. Despite the fact that the clause referred to "any Person under its control" and CELP was the parent and Cineplex Western the subsidiary (rather than vice versa), the plaintiffs argued for a broad interpretation of the clause, saying that its intent was to impose a radius clause applicable to competition by any member of the Cineplex group. Plaintiffs' counsel argued that the words following the struck-out phrase provided an extended meaning of "control" for the purpose of the clause, which included shareholders of more than 5% of the shares in the tenant, Cineplex Western. The defendants argued that the key word was "control" and that the words that follow the strike-out simply described ways in which a third party might be found to be under the tenant's control. (Although, as the trial judge noted, the concept of a corporation (the tenant) controlling a 5% shareholder or lender is awkward in and of itself).

Mr. Justice Sigurdson reviewed the principles of contract interpretation, including that a negotiated commercial document should be construed in accordance with sound commercial principles and good business sense. He concluded that the ordinary meaning of "control" and "otherwise" undercut the plaintiffs' proposed interpretation. For the words starting "whether…" to amount to a deeming provision that resulted in an extended definition of "control", the word "otherwise" would have to be treated as surplusage. Thus, the control requirement must have been intended to be the overriding concept. Sigurdson J. held that he was entitled to consider the crossed-out words as an aid to resolving ambiguity and that those words supported the defendants' interpretation. Ultimately, while noting several times that neither proposed interpretation was entirely satisfactory, he held that the defendants' interpretation prevailed and since Cineplex Western did not control CELP, the radius clause was not triggered by CELP's operation of the Scotiabank theatre.

While it was not necessary, given this finding, for Mr. Justice Sigurdson to consider the plaintiffs' corporate veil argument, he addressed it in extensive *obiter*. Because Cineplex Western had no assets, the plaintiffs argued that if it was found liable, then CELP should be found responsible for Cineplex Western's liability by way of a lifting of the corporate veil.

Evidence was led as to the business relationship between Cineplex Western and CELP (and its predecessor COC). All gross revenues of Cineplex Western were deposited in the bank account of the parent. All expenses were paid by the parent. The parent made decisions about Cineplex Western's finances. All of Cineplex Western's officers were officers of the parent. Cineplex Western paid a management fee to the parent.

All this, said the plaintiffs, demonstrated that Cineplex Western was the mere alter ego of CELP and the corporate veil should therefore be pierced, with the Court treating Cineplex Western and CELP as a single entity. The plaintiffs advocated for a limited exception to the general rule of separate corporate personality where the subsidiary is "so utterly and entirely dominated by the parent corporation that it is a mere puppet of the parent" and took the position that this exception should apply even in the absence of fraud.

After a detailed review of the jurisprudence across Canada and textbook commentary, Mr. Justice Sigurdson concluded (at paragraph 128):

> The circumstances in which the Court will lift the veil and impose the contractual liability of a subsidiary on a parent require more than the exercise of total control by the parent over the subsidiary. The corporate veil will not be pierced absent conduct akin to fraud.

Bottom line: Drafters will continue to seek to bind or affect non-contracting parties, or bring home liability to a contracting party for the conduct of non-contracting parties, by way of expansive language. In doing so, however, the drafter must be alive to: 1) the importance of the words chosen in terms of what members of a corporate family will be captured; 2) the doctrine of privity and the scope of what are still very narrow exceptions to it; and 3) the general futility (absent fraudulent conduct) of "piercing the corporate veil" arguments as a means of bringing home liability to related entities that have separate legal personalities.

Legislative and Law Reform Developments

A broad range of legislation affects commercial agreements and highlighting all such legislative changes is beyond the scope of this paper. Instead, I will bring your attention to developments that might have escaped your notice to date.

New West Partnership Trade Agreement: The NWPTA is an accord among the Governments of British Columbia, Alberta and Saskatchewan that creates Canada's largest, barrier-free, interprovincial market. The NWPTA came into effect July 1, 2010 and will be fully implemented on July 1, 2013. The NWPTA essentially expands the geographic scope of TILMA. It is a must read for anyone contracting with or seeking to enter into contracts with government entities in the three provinces. Go to: http://www.newwestpartnershiptrade.ca/the_agreement.asp.

Model Law on Procurement: Government procurement is also a hot topic on the international stage. In July 2011, UNCITRAL released its Model Law on Public Procurement, which replaces the 1994 document. Go to: http://www.uncitral.org/uncitral/uncitral_texts/procurement_infrastructure/2011Model.html.

BCLI Unfair Contracts Relief Project: The B.C. Law Institute published a consultation paper on its Unfair Contracts Relief Project on December 14, 2010. The final project report will likely be published this fall. The project materials canvass a broad range of contract law subject-matters and contain proposals for legislative reform. Go to: http://www.bcli.org/bclrg/projects/unfair-contracts-relief.

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