

# CONTRACT LAW UPDATE: DEVELOPMENTS OF NOTE (2019)

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Lisa A. Peters, Q.C. | Lawson Lundell LLP  
Vancouver (+1) 604 631 9207 | Kelowna (+1) 778 738 2605  
[lpeters@lawsonlundell.com](mailto:lpeters@lawsonlundell.com)





## **CONTRACT LAW UPDATE: DEVELOPMENTS OF NOTE (2019)**

By Lisa A. Peters, Q.C.

Every year, I review decisions from the past 12 to 18 months dealing with contract law issues, looking for topics relevant to commercial practice that I can write about.<sup>1</sup> Some years there are sea changes to the law of contract as a result of appellate decisions. This is not one of those years. As a result, this year I revisit topics I addressed over a decade ago, explore some foundational principles of contract law as illustrated by recent cases and foreshadow developments I expect in the next 12 to 18 months.

This year's topics are:

- ✓ Notional severance and blue-pencil severance of illegal or unenforceable terms revisited (and updated);
- ✓ Implied contracts (contracts by conduct);
- ✓ The consequences of failing to pay notional consideration;
- ✓ The Supreme Court of Canada splits on the interpretation of indemnity clauses: *Resolute FP Canada Inc. v. Ontario (Attorney General)*, 2019 SCC 60;
- ✓ Entire agreement clauses; and
- ✓ Decisions on reserve at the Supreme Court of Canada.

A chart of the topics covered in my papers over the past ten years is attached as an appendix. Previous years' papers are available on the Lawson Lundell website.

### **Notional severance revisited and applied in a new context – enforcement of foreign judgments**

Where a contractual provision is unenforceable because enforcement would be contrary to a statute or the common law, rather than setting aside the entire contract, the courts may sever the offending provisions, while leaving the remainder of the contract intact. The appropriate remedy, *i.e.*, severance (and which kind) vs. voiding the contract, depends on the particular context and any relevant policy considerations. Severance engages policy

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<sup>1</sup> I would like to acknowledge the work of Alice Kim, who did her summer articles at Lawson Lundell in 2019 and attends the Allard School of Law, in combing over cases and articles to help me come up with this year's topics.

concerns because the court is being asked to assist one party to enforce an otherwise unenforceable provision.

As I outlined in my 2009 paper, at one time Canadian courts applied the so-called blue pencil doctrine (or technique), which permitted severance of an illegal contract term or portion thereof only if the agreement, after the offending wording was excised, constituted an agreement that could sensibly be enforced. Put another way, severance was only available under this test where the judge could strike out, by drawing a line through it, the portion of the contract they want to remove, leaving the portions that are not tainted by illegality, without affecting the meaning of the part remaining.

From 2004 forward,<sup>2</sup> the Supreme Court of Canada ("SCC") embraced the availability of notional severance, at least in relation to contractual terms providing for illegal interest, in circumstances where public policy ought to allow an otherwise illegal agreement to be partially enforced instead of being declared void *ab initio* and application of the blue-pencil technique would do violence to the intentions of the parties.

The Court enumerated factors to be considered in assessing the appropriateness of severance in a given case:

- (1) whether the purpose or policy of the law that the term offended 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; and
- (4) the potential for the party alleging that the term is unenforceable to enjoy an unjustified windfall.

In 2009,<sup>3</sup> the SCC elaborated on the availability of notional severance in the context of restrictive covenants, stating that it may be resorted to sparingly, and only in cases where

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<sup>2</sup> Beginning with *Transport North American Express Inc. v. New Solutions Financial Corp.*, 2004 SCC 7.

<sup>3</sup> *Shafron v. KRG Insurance Brokers (Western) Inc.*, 2009 SCC 6.

the part being removed is clearly severable, trivial and not part of the main purport of the restrictive covenant. The Court held that for policy reasons, notional severance should not be used when dealing with a restrictive covenant in an employment contract (although blue-pencil severance may be appropriate in limited circumstances).

The SCC also remarked that both types of severance involved altering the original contract between the parties, and that courts should be restrained in their application of severance because of the right of parties to freely contract and choose the words that determine their obligations and rights.<sup>4</sup>

Before discussing a 2019 case in which notional severance was applied in the context of an application to enforce a foreign judgment, I will explore what has happened in the intervening decade since I last wrote about the concept.

First, it is uncontroversial that blue-pencil severance is available in the context of unenforceable restrictive covenants in business contracts; see, for example, *GDL Solutions Inc. v. Walker*, 2012 ONSC 4378. It is also available in relation to other types of clauses, such as dispute resolution clauses.

Second, as implicitly recognized by the SCC in *Shafron v. KRG Insurance Brokers (Western) Inc.*, notional severance may be available in the context of restrictive covenants in business contracts that are not employment contracts. Notional severance is also potentially available in relation to other types of illegal or unenforceable clauses in business agreements.

Third, boilerplate severability clauses are given significant weight by the courts provided that the public policy considerations do not militate against severance as a remedy.

I will illustrate these principles with examples from recent case law.

Two Ontario Court of Appeal decisions from the past five years illustrate how the context of the given agreement and public policy considerations will factor into the availability of blue-pencil and notional severance in relation to an unenforceable clause.

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<sup>4</sup> *Ibid.* at para. 32.

In *2176693 Ontario Ltd. v. Cora Franchise Group Inc.*, 2015 ONCA 152, the Court upheld a lower court decision that a clause in franchise agreements requiring delivery of a release as a condition of the franchisees' assignment of their franchise agreements was unenforceable, as enforcement of the clause would result in a release contrary the s. 11 of the *Arthur Wishart Act (Franchise Disclosure)*<sup>5</sup> ("AWA"). The Court also agreed that striking down the clauses in their entirety was the appropriate remedy.

The franchisor argued that the application judge erred in failing to apply notional severance to read down the clause to require release by the franchisees of non-AWA claims only. The Court of Appeal disagreed. It took into account the context, namely franchise agreements, which were contracts of adhesion. It held that notional severance in this context could undermine the purpose of s. 11 of the AWA and that while striking down the clause in its entirety might give rise to some potential of a windfall to the franchisees, this factor did not outweigh the potential for abuse and subversion of the purposes of the AWA.

*PQ Licensing S.A. v. LPQ Central Canada Inc.*, 2018 ONCA 331, also involved a franchise agreement. The agreement contained a dispute resolution clause that provided for mediation as a precondition to arbitration. The clause required the mediation to be conducted in the State of Delaware. The franchise agreement was for the development of franchise locations in Ontario and Quebec.

When the franchisee delivered a notice of rescission, alleging breach of disclosure obligations under the AWA, the parties ended up in arbitration. The primary issue before the arbitrator was whether the arbitration was statute-barred by a limitation period. The franchisee also argued that the entire mediation provision in the agreement was void because, in requiring the parties to mediate in Delaware rather than Ontario, it breached s. 10 of the AWA.

The arbitrator held that the reference to Delaware was severable and that applying blue-pencil severance was consistent with the remedial purpose of the AWA in that it would be contrary to that purpose to void the entire provision and deny the franchisee its otherwise valid rights to mediate its claim. This approach was upheld by the Superior Court of Justice and by the Court of Appeal.

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<sup>5</sup> S.O. 2000, c. 3.

The Court of Appeal decision in *PQ Licensing* is also significant because of how the Court factored in the severability clause included in the agreement. That clause provided that in the event of any conflict between a provision in the agreement and any law, any affected provision will be "curtailed and limited only to the extent necessary to bring it within the requirement of the law." The Court of Appeal, referring to this clause, held that removal of the requirement to mediate in Delaware served to uphold the ADR process the parties agreed to. It would cure the illegality while remaining as close as possible to the intentions of the parties. In short, the Ontario courts applied the blue-pencil approach to severance.

Other decisions confirm that the presence of a severability clause is an important, albeit not overriding, consideration when the court is assessing whether or not to sever an offending provision.

In *Miller v. Convergys CMG Canada Limited*, 2014 BCCA 311,<sup>6</sup> Miller worked for the defendant for close to three years under his first contract of employment. In 2006, when he was promoted, he signed a second contract. The termination clause in the contract stipulated that he would be provided with notice pursuant to the *Employment Standards Act* ("ESA").<sup>7</sup> The contract also included a probation clause that denied him severance for 90 days (even though he had been previously employed by the same employer for close to three years). When he was terminated after seven years without cause, he sued for wrongful dismissal. The trial judge found that he was only entitled to severance under the ESA, rather than severance at common law.

The contract contained a severability clause reading as follows:

Each paragraph of this agreement and the attached Schedules are separate and distinct covenants, severable one from the other and if such covenant is determined to be invalid or unenforceable, such invalidity or unenforceability shall attach only to the covenant to the extent of such invalidity or unenforceability, and all other covenants shall continue in full force and effect.

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<sup>6</sup> Leave to appeal refused, [2014] S.C.C.A. No. 424.

<sup>7</sup> R.S.B.C. 1996, c. 113.

Miller argued that because the probation clause breached the ESA, the contract as a whole was unenforceable. The trial judge held that the probation clause did not apply to Miller given his pre-existing employment by the company, and that even if it did, it should be severed, citing the severability clause.

On appeal, Miller argued that the probation clause and termination clause dealt with the same subject matter and were inextricably intertwined. He relied primarily on cases dealing with contracts breaching minimum notice periods prescribed by the ESA, which the Court found distinguishable.

The Court outlined the relevance of the severability clause to its analysis as follows:

[42] Where the parties anticipated the possibility of severance and chose contractual language to govern this eventuality, severability is not just a remedial question. Before turning to remedy, the starting point must be to give effect to what the parties reasonably intended if a provision of the contract is found unenforceable by reason of illegality.

[43] The severability clause in the Agreement is unambiguous. It stipulates that the units of the Agreement are paragraphs, and each paragraph is a separate and distinct covenant severable from the others. In the event a paragraph is invalid, it provides that the offending provision should be read down to the extent of the invalidity and that all other provisions will remain in full force and effect. The clear intent is that if one clause becomes invalid, the balance of the contract should remain enforceable to the extent possible.

[44] The plain meaning of the severability clause should therefore be given effect if possible, and should inform the test set out by Fridman. The question becomes whether the removal of the probation clause affects the substance of the remainder of the Agreement. The answer does not depend on the similarity of subject matter between the probation clause and the termination clause as Mr. Miller contends, but on the impact of severance on the scope and intention of the Agreement.

[45] I am satisfied the trial judge made no error in concluding the probation clause could be severed from the Agreement. Its removal has no impact on the termination clause, the balance of the contract, or the employment relationship. By stipulating notice in accordance with the Act, the termination clause retains a virtually identical term regarding absence of notice for the first three months of employment. Thereafter, the requirement for notice in accordance with the Act is clear, and unaffected by the severance of the probation clause. Nor does the removal of that provision have any impact on the other terms of the Agreement.

[46] Further, I am not persuaded the presence of a broadly-worded severance clause in an employment contract is necessarily unfair to employees. In this case, the severability clause is not directed solely to the termination provisions, but is applicable to the Agreement in its entirety. It is not reasonable to interpret it as providing a "fallback provision" designed by Convergys in the hope of avoiding notice under the Act. The termination clause is clear that the parties intended the Act would govern severance entitlement. Mr. Miller received notice in compliance with that term.<sup>8</sup>

In a lengthy decision dealing with a dispute between parties to joint venture and related agreements with respect to ethylene production facilities they jointly owned (*Dow Chemical Canada ULC v. NOVA Chemicals Corporation*, 2018 ABQB 482), the Alberta Court of Queen's Bench both applied notional severance and gave significant weight to a severability clause.

One of the issues in the case, in which both parties alleged multiple breaches of contract by the other, was the alleged unenforceability of specific articles of the Operating and Services Agreement as being contrary to the *Competition Act*.<sup>9</sup>

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<sup>8</sup> Note that on different facts (where the termination clause itself breached the relevant Ontario statute by providing that the termination entitlement was only to be calculated on a base salary), the Ontario Court of Appeal held that the termination clause was void and that there was nothing that could properly be severed. Under this approach, the severability clause was not void, but was found to be inoperative in circumstances where the impugned clause purported to contract out of or waive an employment standard: see *North v. Metaswitch Networks Corporation*, 2017 ONCA 790.

<sup>9</sup> R.S.C. 1985, c. C-34. As unduly preventing or lessening competition contrary to s. 45(1).

Madam Justice Romaine found the provisions in question to be illegal under the *Competition Act*. However, she concluded that it was appropriate to apply notional severance so as to preserve the intention of the parties to the extent possible.

The OSA contained a severability clause that read as follows:

In the event that the whole or any portion of any section of this Agreement or the application thereof to any circumstances shall be held invalid, unenforceable or superseded to any extent, the remainder of the section in question, or its application to any circumstance other than that to which it has been held invalid or unenforceable and the remainder of this Agreement shall not be affected thereby and shall be valid and enforceable to the fullest extent permitted by law." [emphasis added by the trial judge]

Justice Romaine applied the factors articled in *Transport North American Express Inc. v. New Solutions Financial Corp.*<sup>10</sup> to the facts and concluded that they supported the application of notional severance to read down the impugned provisions to save them from illegality. She stressed that, in light of the severability clause, the clear intention of the parties was to have the remainder of any illegal provision and the agreement unaffected and valid and enforceable to the fullest extent permitted by law.

Now that we are caught up to 2018, I will address a 2019 decision that addresses severance in the context of enforcement of a foreign judgment.

In *Wei v. Li*, 2019 BCCA 114,<sup>11</sup> the plaintiff had obtained judgments from the Intermediate People's Court of Tangshan City in relation to debt owed by the corporate defendant and guaranteed by the individual defendants. When plaintiff brought an action to enforce the judgments in B.C., the defendants raised various conflict of law defences to the enforcement action (i.e., as to jurisdiction of the foreign court, the nature of the judgment as final and conclusive, an alleged breach of the principles of natural justice), all of which were rejected by the summary trial judge.

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<sup>10</sup> *Supra* note 2.

<sup>11</sup> Leave to appeal dismissed, 2019 CanLII 106996 (S.C.C.).

The plaintiff also argued that as the rate of interest running on the Chinese judgments exceeded the annual rate of 60% permitted by the *Criminal Code of Canada*, the Court should apply notional severance to reduce it to 60%. The defendants argued that the principle from *Transport North American Express* should not be applied to a foreign judgment and that the rate of interest should be governed by the *Court Order Interest Act*.<sup>12</sup>

The summary trial judge applied notional severance. On appeal the Court agreed with that approach:

[42] Ultimately, the matter comes down to a contest between two principles. On the one hand we have the general statement made in *Dingwall* (citing the older decision of the Supreme Court of Canada in *Livesley*) that where a foreign judgment carries interest, the interest provision is "treated as an integral part of the judgment debt, and the rate is accordingly calculated in conformity with the requirements of that law, whatever that rate may be." On the other hand, we have the more recent decision of the Supreme Court in *Transport v. New Solutions* adopting a "flexible" approach to s. 347 of the *Criminal Code* and rejecting the argument that notional severance amounts to 'rewriting' the parties' contract. *Transport v. New Solutions* did not involve a foreign judgment; *Dingwall* did not involve criminal interest. Counsel have not located a case directly on point. *Transport v. New Solutions* calls for the severance of a criminal rate of interest and its replacement by the rate of 60% where the four criteria discussed above are met. According to the summary trial judge's findings, they were met in this case. Why should notional severance not be available in respect of foreign judgments in the same way as it is for domestic judgments?

[43] Whatever solution is adopted, it is simply not open to a Canadian court to leave the interest provision in the Chinese Judgments as it is, notwithstanding that it is an "integral part" of the debt and the defendants agreed to it. Some "interference" is therefore inevitable. I see no principled reason why notional severance should not be available for foreign judgments, especially given that international comity is one of the objectives underlying

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<sup>12</sup> R.S.B.C. 1996, c. 79.

the enforcement of foreign judgments: see *Beals* at para. 28. If notional severance does not amount to a rewriting of the parties' contract in a domestic case, it seems to me that the same should be true of a foreign judgment where the *Transport* criteria are met. I therefore conclude that the summary trial judge did not err in law in applying *Transport v. New Solutions* to the Chinese Judgments in the case at bar.

Bottom line: 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 latter is not available in relation to restrictive covenants in employment contracts. Courts will be restrained in using severance because doing so amounts to rewriting the parties' agreement and therefore trenches on freedom of contract. The party seeking severance must address the factors from *Transport North American Express Inc. v. New Solutions Financial Corp.* and be alive to policy concerns that may militate against use of notional severance (or indeed the use of severance at all). A severability clause in the relevant contract will be given weight by courts in assessing whether severance is appropriate and which variety should be applied.

The B.C. Court of Appeal recently applied severance in relation to enforcement of a foreign judgment that provided for interest at a rate contrary to the *Criminal Code*. It will be interesting to see whether severance will be applied to some other perceived illegality in a foreign judgment that raises a recognized defence to enforcement under conflict of laws principles.

### **Implied contract (contracts by conduct)**

Contracts are not always written. Parties may enter into oral agreements. Further, conduct unaccompanied by any written or verbal undertaking could constitute an acceptance of a written or verbal offer so as to bind the acceptor thereto.

Finally, and perhaps more controversially, the offer itself may consist of conduct manifesting that offer and be accepted in kind. In other words, the contractual relationship is inferred from conduct of the parties indicating their consent and intention to be in such a relationship.

Cases use the terms implied contract, inferred contract or contract by conduct to describe either an offer accepted by conduct<sup>13</sup> or a contract where offer and acceptance, and indeed all the required elements of a contractual relationship, are manifested by conduct. In this paper, I will discuss the latter concept.

Some academics take the view that when courts found there to be an "implied contract" in older cases, they were really applying restitutive principles and that, in modern times, when one is alleging that because of its conduct in accepting goods or services from Party A, Party B must compensate Party A, the appropriate claim is in unjust enrichment.<sup>14</sup>

Of course, the elements of a claim in contract and a claim in unjust enrichment are very different. A party alleging a breach of contract must the existence of a valid contract (an intention to create legal relations; offer and acceptance; *consensus ad idem*; consideration; sufficient certainty of terms); a breach of the contract; and damages resulting therefrom. An action for unjust enrichment arises when three elements are satisfied: (1) an enrichment; (2) a corresponding deprivation; and (3) the absence of a juristic reason for the enrichment.

Because of this, it is easy to envisage scenarios where the elements of unjust enrichment as articulated by the SCC are not present, but it could be said that parties intended to bind themselves contractually and had a sufficient understanding of what the other party expected of them for a contract on those terms to be implied.

The following passage from the most recent edition of *Chitty on Contracts* situates implied contracts in contract law theory:<sup>15</sup>

Contracts may be either express or implied. The difference is not one of legal effect but simply of the way in which the consent of the parties is manifested. Contracts are express when their terms are stated in words by the parties. They are often said to be implied when their terms are not so stated, as, for example, when a passenger is permitted to board a bus: from the conduct of the parties the law implies a promise by the passenger to pay the fare, and a

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<sup>13</sup> See, for example, *O'Neill v. Kings County Construction Ltd.*, 2019 PECA 13, application for leave to appeal filed, 2019 CarswellPEI 104 (S.C.C.).

<sup>14</sup> See, for example, the discussion in G.H.L. Friedman, *The Law of Contract in Canada*, 6<sup>th</sup> ed., (Toronto: Carswell, 2011) at 10.

<sup>15</sup> Joseph Chitty Jr. and H.G. Beale, *Chitty on Contracts*, vol. 1 (London: Sweet & Maxwell, 2018) at §1-111.

promise by the operator of the bus to carry him safely to his destination. There may also be an implied contract when the parties make an express contract to last for a fixed term, and continue to act as though the contract still bound them after the term has expired. In such a case the court may infer that the parties have agreed to renew the express contract for another term or the court may infer an implied contract drawing on some of the terms of the earlier contract, but omitting others. Express and implied contracts are both contracts in the true sense of the term as they both arise from the agreement of the parties, though in one case the agreement is manifested in words and in the other case by conduct.

I am not convinced that the concept of implied contracts has been subsumed into the modern law of restitution.

Implied contracts or contracts by conduct are probably more common outside a commercial context. However, they can arise in a commercial context and therefore, it is important for clients to have an understanding as to how they may arise, so that operational personnel do not bypass protocols put in place for corporate contracting and end up binding the corporation to an implied contract. Based on my cursory review of textbooks and cases, parties may be less inclined to plead implied contract (which is not even discussed in many texts) and more inclined to plead unjust enrichment. However, pleas in the alternative are, in my view, still prudent.

The 2019 case I discuss below illustrates how the concept of an implied contract is still extant in very recent jurisprudence.

In a recent decision of the Ontario Superior Court, *G.E.X.R. v. Shantz Station Terminal*, 2019 ONSC 1914 ("GEXR"), Justice Braid stated:<sup>16</sup>

An implied contract is inferred by law, as a matter of reason and justice from the conduct and the circumstances surrounding the transaction. An implied contract is one inferred from the conduct of parties and arises where the plaintiff, without being requested to do so, renders services under circumstances indicating that he expects to be paid therefor; and the

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<sup>16</sup> At para. 108, citing *Smith v. Port Hood Harbour Authority* (1993), 123 N.S.R. (2d) 225 at 229 (S.C.).

defendant, knowing such circumstances, avails himself of the benefit of those services. It is an agreement which legitimately can be inferred from the intention of the parties as evidenced by the circumstances, ordinary course of dealing and common understanding.

Alternative claims were pleaded and pursued in *GEXR*. The plaintiff is a federally regulated railway company that operates a short-line track (the "Guelph Line") that it leases from Canadian National Railway, which track connects to that railway's main lines. The defendant Parrish and Heimbecker Limited ("P&H"), a grain company, built Shantz Station Terminal on the Guelph Line and used that location as an unloading facility.

In this litigation, *GEXR* sought to recover demurrage<sup>17</sup> in accordance with its published tariff for the delayed unloading of railcars at the Shantz Station Terminal. P&H refused to pay the charges on the basis that, in the absence of a contract, *GEXR* had no right to charge demurrage.

Prior jurisprudence confirmed that a contract of carriage that incorporated tariff terms was necessary for the railway in question to levy demurrage charges and that the mere provision of services, even under the structure of the *Canada Transportation Act*,<sup>18</sup> did not create a contract.

*GEXR* pleaded an express contract, in the alternative an implied contract, and in the further alternative that P&H was unjustly enriched.

There was a contract of carriage between CN and P&H and *GEXR* hauled freight as an agent of CN on the Guelph Line. CN paid *GEXR* a portion of the freight rate it was paid by P&H as a haulage fee. But *GEXR* was not a party to the contract of carriage and therefore, Justice Braid held, there was no express contract under which *GEXR* could charge demurrage.

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<sup>17</sup> As Justice Braid notes, demurrage is a charge levied when it takes longer than anticipated to load or unload goods in transit. Railway companies allow shippers a reasonable period of free time for loading or unloading railcars when equipment is placed at the shipper's disposal. When a shipper exceeds the time period to unload the freight and thereby withholds the railcars from transport service, the shipper may be liable to pay demurrage.

<sup>18</sup> S.C. 1996, c. 10.

In considering whether there was an implied contract, Justice Braid noted that the court must be satisfied that the parties have agreed to the essential terms of the contract and that courts are generally reluctant to find that an implied contract exists.

GEXR argued that a custom of the railroad industry gave rise to an implied contract on the facts. The railroad, it said, gives the shipper the right to use the line, which carries with it an assumption that the shipper will pay demurrage; the railroad issues a tariff that establishes the rate of demurrage; the obligation is assumed by the parties to exist; and the expectation of payment is created as a result.

Justice Braid did not expressly rule on whether such a custom existed. Instead, she found on the facts that even if such a custom existed, P&H explicitly rejected the custom from the time that Shantz Station Terminal began its operations. P&H had consistently and unequivocally refused to accept or pay GEXR demurrage charges that GEXR invoiced. Yet GEXR continued to perform despite this refusal; accordingly, she held, GEXR could not have a legitimate expectation or belief that they had a contract with P&H.

That left the alternative plea in unjust enrichment. Justice Braid found that GEXR had not established either an enrichment of P&H or a corresponding deprivation suffered by GEXR.

Bottom line: It is theoretically possible for parties to bind themselves to an implied contract by reason of their conduct. One scenario where this can occur is where a contract expires but the parties carry on performing pursuant to its terms. If this result is not desired, the drafter should make it clear that any extension of the contract must be in writing and, if appropriate, approved by the necessary person or corporate body. Operational personnel should be made aware that lack of formality will not necessarily preclude them from (perhaps inadvertently) binding their employer to contractual obligations by conduct. Another scenario where an implied contract may arise is where there a party can prove a custom in the particular industry from which the elements of a contract can be drawn and the parties engage in conduct consistent with the industry custom.

Where a party has provided goods or services without a written or oral contract in place, they should consider whether a plea of implied contract is plausible and also a plea of unjust enrichment.

## Failure to pay nominal consideration

It is common for contracts to provide for nominal consideration to be paid by one contracting party. Anecdotally, I understand that it is not uncommon for actual payment of that nominal consideration to never occur.

Two recent B.C. cases comment on the consequences of a failure to pay nominal consideration.

In *Jones v. Alberni-Clayoquot (Regional District)*, 2018 BCSC 216, property owned by the Joneses was subject to a 99-year lease in favour of the Regional District. The lease permitted the construction and maintenance of a pump house and water line that supplied water to the neighboring community. The Joneses applied to set aside the lease on a number of grounds. One ground was the failure of the Regional District to pay the annual amount stipulated in the lease of \$1 for four years.

Mr. Justice Dley held as follows:

[32] The payments were symbolic and the financial gain was nominal. The plaintiffs received other benefits, including the waiver of water tolls and parcel taxes. This was not a one-sided agreement.

[33] The failure to pay a nominal consideration does not render a contract invalid where it is clear that the parties intended the payment term to be immaterial and negligible for the completion of the agreement: *5240 Investments Ltd. v. Great Eagle Resources Ltd.*, 2013 BCSC 35 (CanLII) at paras. 105-106.

[34] The parties did not adhere to a consistent pattern of payments and there were prior occasions when the payments were in arrears. The Regional District was prepared to pay the arrears and interest, as soon as it received the First Notice. The Regional District tendered the full amount of the particularized arrears upon receiving the Second Notice. There is no suggestion that the failure to pay caused the plaintiffs any distress. I, therefore, conclude that arrears of \$4.00 over a four-year period did not render the lease invalid or unenforceable.

He went on to find that the Regional District was entitled to relief from forfeiture in any event.

In *Hall v. Osoyoos Indian Band*, 2018 BCSC 2379, the plaintiff sought a declaration that would require the defendant to issue her a certificate of purchase with respect to a house located on the Osoyoos Indian Reserve #1. Under a residential tenancy agreement, the parties agreed that once all required rental payments had been paid in full, the plaintiff had an option to pay \$1.00 to purchase the premises. Madam Justice Beames found that the plaintiff had made all required rental payments. The plaintiff admitted that she had not paid or offered to pay the \$1. In her mind, paying the required rental payments in full meant she had already paid for the house: she did not consider the \$1 to be relevant.

Madam Justice Beames held as follows (at para. 28):

With respect to the \$1 payment, I find that either that payment was not required, having been waived by the defendant, or that the defendant, if it insisted such a payment be made, was at liberty to withhold that sum from the allotments and distributions it was required to make to the plaintiff on an annual basis. [...] Had the defendant required strict compliance with the term that \$1 be paid in order to exercise the option, that should have been made clear to the plaintiff, preferably in writing or at least verbally in response to each of her five requests for her "title", or should have been paid by the defendant to itself from the plaintiff's funds when it became clear and obvious that the plaintiff intended to and was making every effort to exercise her option. The law is clear, in any event, that the failure to pay nominal consideration does not necessarily render a contract invalid, particularly when it is clear that the parties considered the payment to be immaterial and negligible, as I find it was here (*5240 Investments Ltd. v. Great Eagle Resources Ltd.*, 2013 BCSC 35 (CanLII) at para. 105; *Jones v. Alberni-Clayoquot (Regional District)*, 2018 BCSC 216 (CanLII), at para. 33).

The 2013 decision referred to in each of these 2018 decisions discusses the question of the consequence of a failure to pay nominal consideration in more detail.

In *5420 Investments Ltd. v. Great Eagle Resources Ltd.*, the plaintiff entered into a general security agreement with the defendant mining company. Great Eagle owned several registered mineral claims and leases in B.C. The plaintiff loaned funds to Great Eagle, backed by a General Security Agreement, under which Great Eagle's interest in a mineral tenure was collateral.

Two documents papering the relationship were a Loan and Participation Agreement ("LPA") and a postponement agreement ("PA"). Pursuant to the terms of each of the LPA and PA, the plaintiff was to pay \$10.00 in consideration. The \$10.00 was never paid.

The defendants argued that because of the failure to pay the nominal consideration, the LPA and PA were invalid and unenforceable.

Mr. Justice Greyell held:

[104] In my view, the \$10.00 consideration was a symbolic amount, not intended by the parties to be paid.

[105] The courts have generally not given much credence to an argument that failure to pay nominal consideration means the contract is invalid and unenforceable. The foundational case supporting this view is *Davidson v. Norstrant* (1921), 1921 CanLII 26 (SCC), 61 S.C.R. 493 (*Davidson*), where the majority held that in view of the intent of the parties, it was clear that the down payment term was immaterial and negligible for the purpose of completing the contract.

He went on to cite from a 2005 Alberta case<sup>19</sup> describing it as persuasive authority for dismissing an argument that a contract is rendered invalid for failure to pay nominal consideration. In that case, Mr. Justice Germain stated in part:

[78] Using somewhat standard legal drafting, the Draft Offer to Purchase indicated that the consideration was the sum of \$100.00 for the granting of an option to purchase the shares for \$700,000.00.

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<sup>19</sup> *621224 Alberta Ltd. v. 610042 Alberta Ltd.*, 2005 ABQB 606.

[79] The \$100.00 consideration was nominal consideration only.

[80] Lawyers have, for the last 200 years, attempted to make contracts in which there is an exchange of promises, more binding by throwing in nominal consideration.

[81] As these issues have been fought over the carcasses of disputed agreements in the courts, the legal drafting has tightened up such that usually the statement in today's document indicates that the nominal consideration is acknowledged to have been both received and adequate and the recipient is estopped from denying to the contrary. In this case, the nominal consideration was not so qualified.

[82] The defence attempts to illustrate that perhaps with an Option Agreement there is no other consideration for the time given to exercise the Option other than the nominal consideration and therefore the nominal consideration should in fact be paid.

[83] The cases, however, do not draw a distinction between Option Agreements and other forms of documentation. In *Davidson v. Norstrant*, 1921 CanLII 26 (SCC), [1921] 61 S.C.R. 493, 57 D.L.R. 377 (S.C.C.) the Supreme Court of Canada had to consider \$100.00 nominal consideration against a \$10,000.00 option.

[84] They concluded that the matter is one of intention, and there was no intention expressed that the parties would not be bound if the \$100.00 was not paid. Both parties understood that the down payment was immaterial and negligible.

Mr. Justice Greyell distinguished the decision in *Carlson v. Jorgenson Logging Co. Ltd.*, [1952] 3 D.L.R. 294 (B.C.S.C.), where the Court held that failure to pay nominal consideration rendered the contract *nudum pactum*. In that case, the consideration was a condition precedent for entering into the deal. The contract remained a unilateral contract up until the time when the option was exercised.

The actual substantive finding made by Greyell J. was that the parties did not intend for the \$10.00 consideration to pass between them and that there was other substantive consideration by way of the benefits each party derived from the terms of the LPA and PA.

Bottom line: Failure to pay nominal consideration provided for in a contract will not be fatal to the party seeking to subsequently enforce the contract. The only scenario where it will be clearly fatal is where payment of the consideration is a condition precedent for entering into the agreement.

The jurisprudence on point suggest that courts will strive to find a way to validate the contract notwithstanding such non-payment. Ways of doing so include finding that the parties waived payment of consideration or that there was other consideration passing between them (or the agreement was entered into under seal).

The finding in a number of cases that it was clear that the term providing for nominal consideration was immaterial and negligible appears to be a catch-all for describing these scenarios. This reality begs the question: what would a court do in a scenario where there was no other consideration (and the agreement was not under seal) and no waiver of payment of the consideration and a failure to pay the stipulated nominal consideration?

A boilerplate clause acknowledging the receipt and sufficiency of stipulated nominal consideration should discourage any arguments to the effect that non-payment of consideration results in an unenforceable contract (although the Court still considered the failure to pay consideration argument in the face of such a clause in *5420 Investments Ltd. v. Great Eagle Resources Ltd.*).

### **The SCC splits on the interpretation of an indemnity clause**

I typically do not cover cases in which the principles of contract interpretation are applied to a particular contract and factual matrix.

But, for obvious reasons, when the SCC weighs in on the interpretation of a particular type of clause, I feel the need to comment. As I discussed in prior papers, the SCC provided guidance on the principles of contract interpretation and appellate review of contract interpretation carried out by lower courts in *Sattva Capital Corp. v. Creston Moly Corp.*, 2014 SCC 53 and *Ledcor Construction Ltd. v. Northbridge Indemnity Insurance Co.*, 2016 SCC 37.

Most recently, in *Resolute FP Canada Inc. v. Ontario (Attorney General)*, 2019 SCC 60, the Court dealt with the interpretation of an indemnity clause (the "1985 Indemnity"), forming part of a settlement of litigation in which two First Nations sued owners of a pulp and paper mill (the "Dryden Mill") in relation to the mercury waste contamination of two rivers caused by the operation of that Mill. Ontario granted the 1985 Indemnity, which was a schedule to the settlement agreement. The other parties to the 1985 Indemnity were Reed Ltd. ("Reed") and Great Lakes Forest Products Limited ("Great Lakes").

The live question in the subsequent litigation was whether a successor owner of the Dryden Mill and a corporate successor to Great Lakes were entitled to recover compensation from Ontario under the 1985 Indemnity for the cost of complying with a Director's Order issued by the Ministry of the Environment in 2011 (under environmental legislation enacted subsequent to the execution of the 1985 Indemnity).

The key paragraph in the 1985 Indemnity read as follows:

1. Ontario hereby covenants and agrees to indemnify Great Lakes, Reed, International and any company which was at the Closing Date a subsidiary or affiliate company (whether directly or indirectly) of International, harmless from and against any obligation, liability, damage, loss, costs or expenses incurred by any of them after the date hereof as a result of any claim, action or proceeding, whether statutory or otherwise, existing at December 17, 1979 or which may arise or be asserted thereafter (including those arising or asserted after the date of this agreement), whether by individuals, firms, companies, governments (including the Federal Government of Canada and any province or municipality thereof or any agency, body or authority created by statutory or other authority) or any group or groups of the foregoing, because of or relating to any damage, loss, event or circumstances, caused or alleged to be caused by or with respect to, either in whole or in part, the discharge or escape or presence of any pollutant by Reed or its predecessors, including mercury or any other substance, from or in the plant or plants or lands or premises forming part of the Dryden assets sold by Reed Ltd. to Great Lakes under the Dryden Agreement (hereinafter referred to as "Pollution Claims"). It is hereby expressly acknowledged and agreed that in

respect of Ontario's covenant and agreement hereunder to indemnify Great Lakes that the term "Pollution Claims" shall include any obligation, liability, damage, loss, costs or expense incurred by Great Lakes as a result of any claim, action or proceeding resulting from or in connection with the indemnity agreement of even date herewith made between Great Lakes, Reed and International. [emphasis added]

Weyerhaeuser Company Limited ("Weyerhaeuser") had owned the Dryden Mill for a period of time and was named in the Director's Order. It was successful in obtaining a declaration in the lower court that the 1985 Indemnity required Ontario to compensate it. Resolute, the corporate successor to Great Lakes, sought leave to intervene and was successful, along with Weyerhaeuser, in obtaining summary judgment in the lower court. On appeal, the majority of the Court of Appeal held that the 1985 Indemnity applied to the Director's Order, but that Resolute was not entitled to indemnification and remitted Weyerhaeuser's entitlement to indemnification to the Superior Court. Mr. Justice Laskin wrote a lengthy dissent, which the majority in the SCC essentially adopted on appeal (the "Laskin Dissent").

Mr. Justice Laskin found that properly construed, the 1985 Indemnity was intended to cover only pollution claims brought by third parties and that first party regulatory claims, such as the Director's Order, did not fall within its scope.

The Laskin Dissent and the majority SCC ruling turned, to a large extent, on the ruling that the motion judge made errors of fact. One of the assets acquired by Weyerhaeuser was a waste disposal site, which was used as a solution to the pollution of the rivers. The Director's Order was issued in relation to the waste disposal site (as opposed to the Dryden Mill facilities more generally). The motion judge was found to have erred in finding that the waste disposal site continued to discharge mercury into the environment. This finding, in turn, founded his conclusion that these discharges could give rise to "pollution claims" within the meaning of that term in the 1985 Indemnity. The Laskin Dissent and the SCC found that the disposal site was not a source on ongoing mercury contamination or environmental liability and thus its creation would not give rise to pollution claim.

The majority SCC ruling went on to find that the motions judge made palpable and overriding errors in interpreting the scope of the 1985 Indemnity in context, including:

- Failing to consider the total context of the settlement agreement when determining the scope of the 1985 Indemnity, including the fact the former was limited to discharge of mercury and other pollutants into the river systems and the continued presence of such discharged pollutants in the related ecosystems.
- Failing to consider the context of two indemnities given by Ontario prior to 1985 in the context of the litigation brought by the First Nations.
- Making a palpable and overriding error of fact in finding that the 1985 Indemnity was provided in consideration for financial commitments made by the original Dryden Mill owner and that therefore it would commercially absurd for Ontario to be able to impose remediation costs on top of those financial commitments. The SCC found that the financial commitments were actually provided as part of an earlier indemnity. Therefore, it held, the motions judge mistakenly overemphasized the words "statutory or otherwise" in the 1985 Indemnity and misconstrued the bargain actually struck.
- Failing to consider the 1985 Indemnity as a whole, including the language that gave Ontario the right to elect to take carriage of the defence or participate in the defence of any pollution claim and required the indemnitees to cooperate in such defence. The SCC held that these provisions would be meaningless in relation to first party claims.

Three of the seven justices dissented (the "SCC Dissent"). They specifically, and in significant detail, rejected the errors of the motion judge identified by the majority.<sup>20</sup>

The SCC Dissent reads more like a trial judgment than a judgment on appeal; it is factually dense. The dissenting justices state that the motion judge's appreciation of the factual matrix is entitled to deference on appeal and then go on to find that he did consider the items in the factual matrix that the majority ruled he did not consider and that those items did not support the interpretation put forward by Ontario (and accepted by the SCC majority).

The dissenting justices reject the proposition that the motion judge made errors in his factual findings and go on to find that, in any event, these were minor and collateral findings

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<sup>20</sup> The SCC Dissent also deals with Ontario's argument that the motion judge's interpretation of the 1985 Indemnity had the effect of impermissibly fettering the Ontario Legislature's law-making power, rejecting this argument.

that could not possibly have had an overriding effect on the conclusion reached by the motion judge.

Neither the majority nor the dissenting judges say anything new about the principles of contractual interpretation.<sup>21</sup> They do not articulate unique contract interpretation principles applicable to indemnity clauses. While (subject to what I say below about one aspect of the SCC Dissent) the decision does not change contract law and is deeply rooted in its particular facts, it is striking for the following reasons:

- The willingness of the Court to grant leave on an appeal where the alleged errors involved issues of mixed fact and law and issues of pure fact;
- The willingness of the majority to wade into factual findings and carry out its own contract interpretation exercise, without showing deference to the motion judge's findings; and
- The schism between the majority and dissenting judges on virtually every point.

The portion of the SCC Dissent in which the justices considered whether Weyerhaeuser and Resolute were entitled to the benefit of the 1985 Indemnity could have some precedential value going forward. Some of the corporate history is necessary to understand this part of the reasons.

The original owner of the Dryden Mill was Dryden Paper Company Limited, which operated the Mill through Dryden Chemicals Limited. Those entities amalgamated to form Reed. Reed sold Dryden Mill to Great Lakes by way of an asset purchase agreement. Great Lakes was a indemnitee under a 1979 indemnity from Ontario as well as a 1982 indemnity related to the litigation with the First Nations.

Great Lakes was also a party to the 1985 Indemnity. That Indemnity contained an enurement clause under which the Indemnity was stated to be "binding upon and enure to the benefit of the respective successors and assigns of Ontario, Reed, Reed International and Great Lakes."

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<sup>21</sup> Note, however, the Alberta Court of Appeal recently picked up on comments made in the SCC Dissent, taking the position that *Sattva* does not mean that surrounding circumstances include all pre-contract negotiations (barring only evidence of subjective intention): *Alberta Union of Public Employees v. Alberta Health Services*, 2020 ABCA 4 at para. 32.

Reed amalgamated with other corporations and, ultimately, its successor corporation was dissolved in 1993. Great Lakes became Bowater Pulp and Paper Canada in 1998.

Subsequently, Weyerhaeuser bought the property where the Dryden Mill was situated along with certain related assets. The property conveyed included the waste disposal site. Weyerhaeuser sold the Dryden Mill to Domtar Inc. in 2007.

Bowater went through proceedings under the *Companies' Creditors Arrangement Act*.<sup>22</sup> It was authorized to transfer the waste disposal site to a numbered company, which then obtained court approval to abandon that site without liability. In 2012, Bowater became Resolute FP Canada Inc.

The motion judge held that the enurement clause in the 1985 Indemnity extended the rights and obligations under the 1985 Indemnity to Resolute as a **corporate successor** to Great Lakes and to Weyerhaeuser as both a **successor-in-title** to the Dryden Mill property and an **assignee** of the 1985 Indemnity under its asset purchase agreement with Bowater.

The majority of the Court of Appeal agreed with the conclusion that Weyerhaeuser had rights and obligations as assignee but held it did not as successor-in-title, taking the view that the enurement clause only referred to corporate successors. It went on to hold that Resolute could not claim the benefit of the enurement clause as the 1985 Indemnity had been assigned from Bowater to Weyerhaeuser, extinguishing Bowater's interest therein (leaving nothing to enure to Resolute as Bowater's corporate successor). The Laskin Dissent did not deal with this issue.

The SCC Dissent set out three sub-issues:

1. Can an indemnified party continue to enjoy the benefit of an indemnity after it assigns its rights thereunder absolutely to a third party?
2. Did Bowater actually assign the benefit of the 1985 Indemnity to Weyerhaeuser under the asset purchase agreement?
3. Was Weyerhaeuser a "successor" of Great Lakes under the enurement clause?

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<sup>22</sup> R.S.C. 1985, c. C-36.

The second sub-issue, which was answered in the negative by the SCC Dissent, is rooted in the details and wording of the asset purchase transaction. I will not discuss it here.

On the first sub-issue,<sup>23</sup> Resolute and Weyerhaeuser argued that there was no legal principle that required the Court of Appeal to apply what they dubbed the "hot potato" theory, in which only the singular legal owner of an indemnity may rely on it. They posited that all of Great Lakes' successors and assigns could continue to benefit in perpetuity from the 1985 Indemnity, even if they had assigned the benefit of the Indemnity to third parties.

While in one sense this was a question of contract interpretation, and therefore rooted in the particular wording in the 1985 Indemnity, the SCC Dissent used the opportunity to articulate basic principles. Citing the 7th edition of *Corbin on Contracts*,<sup>24</sup> which refers to the right of a promisee under a contract, who then assigns it, being extinguished and the right being recreated in the assignee, they stated that the starting place is that the effect of an absolute assignment of contractual right is to extinguish the assignor's right to call upon the obligation for him or herself, and to place that right in the hands of the assignee. The enurement clause simply referred to rights and obligations continuing for the benefit of successors and assigns. Nothing in the factual matrix or text, said the SCC Dissent, altered the foundational principle.

On sub-issue #3, Weyerhaeuser argued that the term "successor" encompassed both corporate successors of Great Lakes and successors-in-title to the Dryden Property. It relied, in part, on a case I discussed in my 2013 paper, *Brown v. Belleville (City)*, 2013 ONCA 148.<sup>25</sup>

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<sup>23</sup> On this sub-issue, for the purpose of argument, it was assumed that Bowater (Resolute) had assigned its rights under the 1985 Indemnity to Weyerhaeuser.

<sup>24</sup> John E. Murray, Jr., *Corbin on Contracts – Third Party Beneficiaries, Assignments, Joint and Several Contracts*, vol. 9, rev. ed. (Newark: LexisNexis, 2007) at 130.

<sup>25</sup> In that case, the contact in question was between a municipality and a landowner. Subsequent owners, who were not parties to the contract and were not assignees of the original owner, sought to enforce the covenant under which the municipality agreed to perpetually maintain and repair that part of a storm sewer drainage system on or near the landowners' property, despite their lack of privity. The Ontario Court of Appeal found that as successors-in-title of the original property owner, the plaintiffs were entitled to enforce the relevant covenant in the agreement. The Court only relied on the "principled exception" to privity described in the third-party-beneficiary cases in the alternative. Its primary finding was that the wording of the enurement clause unequivocally confirmed that the contracting parties intended and agreed that the benefit of the agreement would extend to an aggregation or class of persons that included successor land owners. Justice Cronk described the Court as "relaxing" the doctrine of privity in such a way as to not frustrate the reasonable expectations of the parties at the time the agreement was formed.

The majority in the Ontario Court of Appeal carefully distinguished the decision in *Brown v. Belleville* on the following grounds:<sup>26</sup>

- (i) The present case requires interpreting the term "successor" in reference to a corporation. *Brown*, on the other hand, dealt with interpreting "successor" in reference to an individual;
- (ii) In *Brown*, the agreement contained language that led this court to conclude that the parties intended successors-in-title would benefit from it. Specifically, the litigants in that case agreed the town's obligation to "make good damage" was linked to future owners of the land – "*to the property owner whoever that may be from time to time*": *Brown*, at para. 86 (emphasis in original). Weyerhaeuser cannot point to any similar language in the Ontario Indemnity that links the obligation to indemnify to the future owners of the WDS property; and
- (iii) The subsequent owners of the property in *Brown* brought a claim under the contract for specific performance of the agreement at a time when they owned the property. In the present case, Weyerhaeuser did not own the WDS at the time it sought the benefit of the Ontario Indemnity; it had conveyed the WDS back to Bowater more than a decade before.

The SCC Dissent essentially agreed with this analysis, confirming that when the term "successors" is used in a boilerplate clause like the enurement clause before it, that term generally denotes another corporation which, through merger, amalgamation or some other type of legal succession, assumes the burdens, and becomes vested with the rights, of the first corporation. It concluded that there was nothing in the language of the 1985 Indemnity or the factual matrix that supported an extension of the meaning to successors-in-title.

The SCC Dissent was careful to point out that they were not setting out a universal definition of the term successors and that, in other circumstances (such as those discussed in *Brown v. Belleville*) it may be possible for that term to refer to successors-in-title.

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<sup>26</sup> 2017 ONCA 1007 at para. 177.

Bottom line: Appellate courts vary in terms of the deference they are willing to show trial judges who engaged in contract interpretation. The decision in this case suggests there are strongly differing views among the current SCC justices on this issue.

Careful drafting is critical. In the context of an indemnity clause, the drafter needs to consider what types of claims are meant to be covered, e.g., statutory or common law, based on what type of actions or events, etc. Do you intend to cover claims between the contracting parties (i.e., first party or direct claims) or only third party claims? However, as this case illustrates, even relatively clear language can spawn divergent interpretations.

When you use the term successors, particularly in a boilerplate clause, it will likely be interpreted as referring only to corporate successors. If you intend it to cover successors-in-title, say so expressly.

### **Entire agreement clauses**

Entire agreement clauses are routinely included in commercial contracts with a view to excluding collateral contracts and pre-contractual representations not incorporated into the final agreement.

Their purpose is clear. As described by the Ontario Court of Appeal, an entire agreement clause is "generally intended to lift and distill the parties' bargain from the muck of the negotiations. In limiting the expression of the parties' intentions to the written form, the clause attempts to provide certainty and clarity."<sup>27</sup>

I have not chosen to deal with entire agreement clauses in any depth before because, frankly, the case law on point is somewhat muddled.

I have always taken the position that the enforceability of entire agreement clauses, as a type of exclusion clause, is to be assessed under the *Tercon* test.<sup>28</sup> Indeed, many cases support that position.<sup>29</sup>

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<sup>27</sup> *Soboczynski v. Beauchamp*, 2015 ONCA 282 at para. 43, leave to appeal refused, [2015] S.C.C.A. No. 243.

<sup>28</sup> *Tercon Contractors Ltd. v. British Columbia (Transportation and Highways)*, 2010 SCC 4.

<sup>29</sup> See for example *Ottawa Convention Centre Corporation v. treefort Hip Productions Inc.*, 2018 ONSC 5233; *Laidar Holdings Ltd. v. Lindt & Sprungli*, 2018 BCSC 66; *7326246 Canada Inc. v. Ajilon Consulting*; 2014 ONSC 28 (Div. Ct.); *Haliburton Forest & Wildlife Reserve Ltd. v. Toromont Industries Ltd.*, 2016 ONSC 3767; *Kielb v. National Money Mart Company*, 2015 ONSC 3790, aff'd 2017 ONCA 356.

And yet there are recent cases dealing with entire agreement clauses that do not refer to *Tercon* at all. Further, it is unclear the extent that jurisprudence identifying what I will call "exceptions" to the scope of such clauses co-exists with or is integrated into the *Tercon* test.

A recent decision of the Manitoba Court of Appeal is illustrative: *Virden Mainline Motor Products Limited v. Murray*, 2018 MBCA 82. While acknowledging the *Tercon* test and its application to exclusion clauses, the Court said that recent cases had "demonstrated a more moderate approach to entire agreement clauses where misrepresentation is alleged".<sup>30</sup> It went on to list factors to be taken into consideration such as whether the misrepresentation relates to a matter that is independent of the contract; whether it is a standard from contract; and whether there was inequality of bargaining power.

It is not clear to me whether the Court is saying that these are factors that should be taken into account under the prongs of the tripartite test in *Tercon* (for example, that the factors should influence interpretation of the scope of the clause by way of strict construction under prong #1 or that they feed into a finding of unconscionability under prong #2) or whether it is saying that there is a distinct "moderate approach" to assessing validity of entire agreement clauses outside *Tercon*. Ultimately, the Court gave effect to the entire agreement clause in a Share Purchase Agreement between sophisticated parties who had financial and legal advice.

There is a patchwork of fact scenarios where courts historically have declined to apply or enforce entire agreement clauses (outside the *Tercon* test). They include situations where: one party can be said to have been induced to enter into the contract by the pre-contractual misrepresentation upon which it now seeks to rely;<sup>31</sup> a party can prove the existence of a collateral agreement that does not conflict with the principal agreement in which the entire agreement clause is contained; a party proves a fraudulent misrepresentation.<sup>32</sup>

Justice Himel of the Ontario Divisional Court considered the extent to which the *Tercon* test subsumed the previous jurisprudence in *7326246 Canada Inc. and Kevin Gardiner v. Ajilon*

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<sup>30</sup> At para. 40.

<sup>31</sup> Some versions of this boilerplate clause specifically assert that no party has been induced by any representation, etc., except to the extent it has been reduced to writing and included as a term in the agreement.

<sup>32</sup> See the discussion of these lines of jurisprudence in Cynthia L. Elderkin & Julia S. Shin Doi, *Behind and Beyond Boilerplate: Drafting Commercial Agreements*, 4<sup>th</sup> ed. (Toronto: Thomson Reuters, 2018) at 51-64.

*Consulting*.<sup>33</sup> She considered, in particular whether the pre-existing law requiring notice of the clause, or even notice of its intended effect, be brought home to an unsophisticated counterparty during negotiations for that party to be barred from relying on a negligent misrepresentation that induced him or her to enter into the contract. Ultimately, she applied the *Tercon* test and found that the clause was unconscionable, but also held that if the *Tercon* test did not apply, the clause would be unenforceable under the prior jurisprudence.

The interaction of these “pre-existing exceptions” with the *Tercon* test is still, in my view, a work in progress.<sup>34</sup>

What is certain about entire agreement clauses?

First, as a general rule, they are to be strictly construed against the party seeking to rely on them.<sup>35</sup>

Second, they only operate retrospectively (absent an express statement that they also operate prospectively). In 2015, in *Soboczynski v. Beauchamp*,<sup>36</sup> the Ontario Court of Appeal confirmed this proposition, citing textbooks and articles to the effect that an entire agreement clause deals only with what was done or said before the agreement was made and seeks to exclude those statements and acts from muddying the interpretation of the agreement.

Finally, academics seem to agree that entire agreement clauses codify or are to the same effect as the parol evidence rule. Prior to the SCC decision in *Sattva*, there was confusion as to whether the parol evidence rule precluded resort to pre-contractual statements and conduct as part of the interpretative exercise. The Court explained that parol evidence rule does not bar evidence of the surrounding circumstances as part of the interpretative process. Therefore, neither should the presence of an entire agreement clause. However, evidence of surrounding circumstances is admitted to interpret the written contract, not to contradict or rewrite it.

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<sup>33</sup> *Supra* note 29.

<sup>34</sup> See the discussion of the uncertainty arising from the application of the *Tercon* test in Chris D.L. Hunt and Milad Javdan, “Apparitions of Doctrines Past: Fundamental Breach and Exculpatory Clauses in the Post-*Tercon* Jurisprudence” (2018) 60 CBLJ 309.

<sup>35</sup> *Feldstein v. 364 Northern Development Corporation*, 2017 BCCA 174 at para. 59.

<sup>36</sup> *Supra* note 27.

### **Bottom line:**

Entire agreement clauses are an important type of boilerplate clause used by commercial parties to preclude reliance on pre-contractual statements and conduct and to thereby provide commercial certainty. Unless explicit language to the contrary is used, they only operate retrospectively. They will be strictly construed, which is why they often include a lengthy list of what they exclude. While there are multiple authorities applying the *Tercon* test to the enforceability of entire agreement clauses, it is unclear the extent to which prior categories of case where entire agreement clauses were not enforced are subsumed under that test or continue outside that test.

### **Cases to be decided by the SCC**

Sometimes my paper comes out while key decisions are under reserve at the SCC, which is the case this year. Cases I expect to cover next year are:

*Uber Technologies Inc. v. Heller*:<sup>37</sup> The SCC decision in this case, which was heard by the Court on November 6, 2019, should shed light on the role of a court in determining the validity of an arbitration clause (agreement), including the extent to which the competence-competence principle applies to challenges to the validity of an arbitration clause (not just challenges to its scope). The Court should also weigh in on the governing test for determining that an arbitration clause is unconscionable and therefore unenforceable.

*Wastech Services Ltd. v. Greater Vancouver Sewerage and Drainage District*/<sup>38</sup> *C.M. Callow Inc. v. Zollinger*:<sup>39</sup> These two appeals were heard together on December 6, 2019. In *C.M. Callow*, the Court will have the opportunity to further address the scope of the duty of honest performance it articulated in *Bhasin v. Hrynew*, 2014 SCC 71. In *Wastech*, the Court will consider the duty of good faith in the context of one party's exercise of discretion.

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<sup>37</sup> Decision under appeal at 2019 ONCA 1. SCC File No. 38534.

<sup>38</sup> Decision under appeal at 2019 BCCA 66. SCC File No. 38601.

<sup>39</sup> Decision under appeal at 2018 ONCA 896. SCC File No. 38463.

*Chandos Construction Ltd. v. Deloitte Restructuring Inc.*:<sup>40</sup> The primary issue in this case, heard January 20, 2020, is whether the anti-deprivation rule exists in the common law of Canada or whether provisions in the *Bankruptcy and Insolvency Act*<sup>41</sup> constitute the entire code governing the enforceability of contractual provisions that impose consequences upon the insolvency of a contracting party. The majority in the Alberta Court of Appeal decided the case by focussing on this issue, and did not view the case as being a contract law case. The dissenting judgment, however, engaged in a lengthy analysis, informed by history, of judicial treatment of contractual stipulated-consequence-on-breach terms as penalties (as opposed to liquidated damages), rendering them contrary to public policy and unenforceable. Assuming the SCC addresses this issue, the decision will have ramifications beyond the insolvency context.

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<sup>40</sup> Decision under appeal at 2019 ABCA 32. SCC File No. 38571.

<sup>41</sup> R.S.C. 1985, c. B-3.

# **CONTRACT LAW**

## **DEVELOPMENTS OF NOTE SUMMARY OF TOPICS**

HEADINGS	2018	2017	2016	2015	2014	2013	2012	2011	2010
Links to Contract Law Paper by Year	<a href="https://www.lawsonlundell.com/assets/html/documents/Contract%20Law%20Update%20May%202019.pdf">https://www.lawsonlundell.com/assets/html/documents/Contract%20Law%20Update%20May%202019.pdf</a>	<a href="https://www.lawsonlundell.com/assets/html/documents/2017%20Contract%20Law%20Update%202015.pdf">https://www.lawsonlundell.com/assets/html/documents/2017%20Contract%20Law%20Update%202015.pdf</a>	<a href="http://www.lawsonlundell.com/media/news/550-Lisa%20Peters-20Contract%20Law%20Update%202015%20Final.pdf">http://www.lawsonlundell.com/media/news/550-Lisa%20Peters-20Contract%20Law%20Update%202015%20Final.pdf</a>	<a href="http://www.lawsonlundell.com/media/news/502-Contract%20Law%20Update%202015%20Final.pdf">http://www.lawsonlundell.com/media/news/502-Contract%20Law%20Update%202015%20Final.pdf</a>	<a href="http://www.lawsonlundell.com/media/news/461-Contract%20Law%20Update%202014%20Final.pdf">http://www.lawsonlundell.com/media/news/461-Contract%20Law%20Update%202014%20Final.pdf</a>	<a href="http://www.lawsonlundell.com/media/news/396-2013%20developments%20in%20ContractLawUpdate2012.pdf">http://www.lawsonlundell.com/media/news/396-2013%20developments%20in%20ContractLawUpdate2012.pdf</a>	<a href="http://www.lawsonlundell.com/media/news/323-ContractLawUpdate2011.pdf">http://www.lawsonlundell.com/media/news/323-ContractLawUpdate2011.pdf</a>	<a href="http://www.lawsonlundell.com/media/news/76-ContractLawUpdateDevelopmentsofNote2011LisaPeters.pdf">http://www.lawsonlundell.com/media/news/76-ContractLawUpdateDevelopmentsofNote2011LisaPeters.pdf</a>	<a href="http://www.lawsonlundell.com/media/news/101-ContractLaw%20Update.pdf">http://www.lawsonlundell.com/media/news/101-ContractLaw%20Update.pdf</a>
Acceptance by Conduct								X	
Anti-oral Amendment Clauses			X						
Arbitration Clauses	X	X			X	X	X	X	X
Automatic Renewal Clauses				X					
Best Effort Clauses								X	
Binding Effect and Enurement Clauses						X			
Buy/Sell Clauses									X
Choice of Court (Forum Selection) Clauses	X				X				X
Conditions Precedent						X			
Confidentiality Clauses				X					
Consideration in the Context of Contract Variations	X								
Continuing Breach of Contract			X		X				
Contract Interpretation			X						
Contract Termination									
Contracting with First Nations under the <i>Indian Act</i>							X		
Contractual References to Legislative Provisions	X								
Discretionary Powers			X						
Duty of Good Faith			X	X	X	X	X		

HEADINGS	2018	2017	2016	2015	2014	2013	2012	2011	2010
<b>Links to Contract Law Paper by Year</b>	<a href="https://www.lawsonlundell.com/assets/html/documents/Contract%20Law%20Update%20May%202024%2020219.pdf">https://www.lawsonlundell.com/assets/html/documents/Contract%20Law%20Update%20May%202024%2020219.pdf</a>	<a href="https://www.lawsonlundell.com/assets/html/documents/2017%20Contract%20Law%20Update%20Upd9.pdf">https://www.lawsonlundell.com/assets/html/documents/2017%20Contract%20Law%20Update%20Upd9.pdf</a>	<a href="http://www.lawsonlundell.com/media/news/550Lisa%20Peters%20Contract%20Law%20Update%20November%202015%20Final.pdf">http://www.lawsonlundell.com/media/news/550Lisa%20Peters%20Contract%20Law%20Update%20November%202015%20Final.pdf</a>	<a href="http://www.lawsonlundell.com/media/news/502Contract%20Law%20Update%202015%20Final.pdf">http://www.lawsonlundell.com/media/news/502Contract%20Law%20Update%202015%20Final.pdf</a>	<a href="http://www.lawsonlundell.com/media/news/461Contract%20Law%20Update%202014%20LP.pdf">http://www.lawsonlundell.com/media/news/461Contract%20Law%20Update%202014%20LP.pdf</a>	<a href="http://www.lawsonlundell.com/media/news/396Contract%20Law%20Update%202013%20Development.pdf">http://www.lawsonlundell.com/media/news/396Contract%20Law%20Update%202013%20Development.pdf</a>	<a href="http://www.lawsonlundell.com/media/news/323ContractLawUpdate2012.pdf">http://www.lawsonlundell.com/media/news/323ContractLawUpdate2012.pdf</a>	<a href="http://www.lawsonlundell.com/media/news/76ContractLaw%20Act%20Law%20UpdateDevelopmentofNote2011LisaPeters.pdf">http://www.lawsonlundell.com/media/news/76ContractLaw%20Act%20Law%20UpdateDevelopmentofNote2011LisaPeters.pdf</a>	<a href="http://www.lawsonlundell.com/media/news/101ContractLaw%20UpdateDeve20Update.pdf">http://www.lawsonlundell.com/media/news/101ContractLaw%20UpdateDeve20Update.pdf</a>
Duty of Honesty in Contractual Performance				X	X				
Efficient breach					X				
Economic Duress									X
Electronic Transactions and Equitable Mistake							X		
								X	
Exculpatory Clauses and Limitation of Liability Clauses	X			X	X	X	X	X	
Forum Selection Clauses	X								
Frustration and <i>Force Majeure</i>	X								
Fundamental Breach									X
Illegal Contracts									X
Implied Terms			X				X		
Legislative Developments of Liquidated Damages Clauses						X		X	
No Suit Clauses	X							X	
Options		X							
Pre-Incorporation Contracts									X
Privity of Contract							X	X	
Rectification	X								
Releases	X								
Rights of First Refusal		X							
Restrictive covenants					X				
Severability						X			
Smart Contracts	X	X							
Specific Performance						X			



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## VANCOUVER

Suite 1600 Cathedral Place  
925 West Georgia Street  
Vancouver, British Columbia  
V6C 3L2  
t 604.685.3456  
f 604.669.1620

## CALGARY

Suite 1100, 225-6th Avenue S.W.  
Brookfield Place  
Calgary, Alberta  
T2P 1N2  
t 403.269.6900  
f 403.269.9494

## KELOWNA

Suite 403 - 460 Doyle Avenue  
Kelowna, British Columbia  
V1Y 0C2  
t 778.738.2610

## YELLOWKNIFE

Suite 200 - 4915 - 48th Street  
Yellowknife, Northwest Territories  
X1A 2N6  
t 867.669.5500  
f 867.920.2206



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