Court File No. CV-16-11549-00CL

ONTARIO
SUPERIOR COURT OF JUSTICE
[COMMERCIAL LIST]

IN THE MATTER OF THE COMPANIES' CREDITORS ARRANGEMENT ACT, R.S.C. 1985, c. C-36, AS AMENDED

AND IN THE MATTER OF A PLAN OF COMPROMISE OR ARRANGEMENT OF URBANCORP (WOODBINE) INC. AND URBANCORP (BRIDLEPATH) INC., THE TOWNHOUSES OF HOGG'S HOLLOW INC., KING TOWNS INC., NEWTOWNS AT KINGTOWNS INC., AND DEAJA PARTNER (BAY) INC. (COLLECTIVELY, THE "APPLICANTS")

AND IN THE MATTER OF TCC/URBANCORP (BAY) LIMITED PARTNERSHIP

RESPONDING BOOK OF AUTHORITIES OF STEFANO SERPA AND ADRIAN SERPA

(Home Buyer Damage Claims)

April 5, 2017

FOGLER, RUBINOFF LLP
Lawyers
77 King Street West, TD Centre
Suite 3000, North Tower
Toronto, ON M5K 1G8

Vern W. DaRe(LSUC #32591E)
Tel: (416) 941-8842
Fax: (416) 941-8852
Email: vdare@foglers.com

Lawyers for Stefano Serpa and Adrian Serpa

TO: SERVICE LIST

CCAA PROCEEDINGS OF URBANCORP (WOODBINE) INC., URBANCORP (BRIDLEPATH) INC. ET AL.

SERVICE LIST
(UPDATED OCTOBER 25, 2016)

TO: **WEIRFOULDS LLP**
The TD Bank Tower, Suite 4100
66 Wellington Street West
Toronto, ON M5K 1B7

Edmond F.B. Lamek / Danny M. Nunes
Tel: 416-947-5042 / 416-619-6293
Email: elamek@weirfoulds.com / dnunes@weirfoulds.com

Lawyers for the Urbancorp CCAA Entities

AND TO: **KSV ADVISORY INC.**
150 King Street West, Suite 2308
Toronto, ON M5H 1J9

Bobby Kofman / Noah Goldstein / Robert Harlang
Tel: 416-932-6228 / 416-932-6027 / 416-932-6225
Email: bkofman@ksvadvisory.com / ngoldstein@ksvadvisory.com / rharlang@ksvadvisory.com

The Proposal Trustee

AND TO: **DAVIES WARD PHILLIPS & VINEBERG LLP**
155 Wellington Street West
Toronto, ON M5V 3J7

Jay Swartz / Robin B. Schwill / Dina Milivojevic
Tel: 416-597-4107 / 416-597-4194 / 416-367-7460
Email: jswartz@dwpv.com / rschwill@dwpv.com / dmilivojevic@dwpv.com

Lawyers for KSV Advisory Inc., in its capacity as the Proposal Trustee

AND TO: **BENNETT JONES LLP**
3400 One First Canadian Place
P.O. Box 130
Toronto, ON M5X 1A4

S. Richard Orzy / Raj S. Sahni
Tel: 416-777-5737 / 416-777-4804
Email: Orzyr@bennettjones.com / SahniR@bennettjones.com

Lawyers for Alan Saskin and Urbancorp Inc.

AND TO: **BLAKE, CASSELS & GRAYDON LLP**
199 Bay Street
Suite 4000, Commerce Court West
Toronto, ON M5L 1A9

Steve Weisz / Silvana M. D'Alimonte / Michael McGraw
Tel: 416-863-2616 / 416-863-3860 / 416-863-4247
Email: steven.weisz@blakes.com / smda@blakes.com / michael.mcgraw@blakes.com

Lawyers for Laurentian Bank of Canada

AND TO: **ROBINS APPLEBY LLP**
120 Adelaide Street West, Suite 2600
Toronto, ON M5H 1 Tl

Leor Margulies / Dominique Michaud
Tel: 416-360-3372 / 416-360-3795
Email: lmargulies@robapp.com / dmichaud@robapp.com

Lawyers for Terra Firma Capital Corporation

AND TO: **TEPLITSKY, COLSON LLP**
70 Bond Street, Suite 200
Toronto, ON M5B 1X3

James M. Wortzman / J. Ventrella / Catherine Allen
Tel: 416-865-5315
Email: jwortzman@teplitskycolson.com / jventrella@teplitskycolson.com / callen@teplitskycolson.com

Lawyers for Atrium Mortgage Investment Corporation

AND TO: **FOGLER, RUBINOFF LLP**
77 King Street West
TD Centre North Tower
Suite 3000, P.O. Box 95
Toronto, ON M5K I G8

Vern W. DaRe
Tel: 416-941-8842
Email: vdare@foglers.com

Lawyers for Adrian Serpa and Stefano Serpa

AND TO: **TRENT MORRIS BARRISTER**
336-20 De Boers Drive
Toronto, ON M3J OH1

Trent Morris
Tel: 647-366-6837
Email: trent@trentmorris.ca

Lawyer for six purchasers of pre-construction homes

AND TO: **TORYS LLP**
79 Wellington Street West, 30th Floor
Box 270, TD South Tower
Toronto, ON M5K 1 N2

Adam M. Slavens
Tel: 416-865-7333
Email: aslavens@torys.com

Lawyers for Tarion Warranty Corporation

AND TO: **DICKINSON WRIGHT LLP**
199 Bay Street, Suite 2200, Commerce Court
Toronto, ON M5L 1G4

Lisa Corne / David Preger
Tel: 416-646-4608 / 416-646-4606
Email: lcorne@dickinsonwright.com / dpreger@dickinsonwright.com

Lawyers for certain purchaser of pre-construction units

AND TO: **DEPARTMENT OF JUSTICE CANADA**
Suite 3400
130 King Street West
Toronto, ON M5X 1 K6

Fozia Chaudary
Tel: 416-952-7722
Email: fozia.chaudary@justice.gc.ca

AND TO: **MINISTRY OF FINANCE**
77 Bay Street, 11th Floor
Toronto, ON M5G 2C8

Kevin O'Hara
Tel: 416-327-8463
Email: Kevin.Ohara@ontario.ca

AND TO: **GOLDMAN SLOAN NASH & HABER LLP**
480 University Ave Suite 1600
Toronto, Ontario M5G 1V2

Mario Forte / Robert Drake
Tel: 416 597 6477 / 416-597-5014
Email: forte@gsnh.com / drake@gsnh.com

Lawyers for Fuller Landau LLP, Proposal Trustee to Alan Saskin

AND TO: **DELZOTTO ZORZI, LLP**
4810 Dufferin Street, Suite D
Toronto, ON M3H 5S8

Robert W. Calderwood / Sabrina Adamski
Tel.: 416-665-5555
E-mail: rcalderwood@dzlaw.com / sadamski@dzlaw.com

Lawyers for Furkin Construction Inc. and GMF Consulting Inc.

AND TO: **FULLER LANDAU LLP**
151 Bloor Street West
Toronto, ON M5S 1S4

Gary Abrahamson / Adam Erlich / Ken Pearl
Tel: 416-645-6500
Email: GAbrahamson@FullerLLP.com / AErlich@FullerLLP.com / KPearl@FullerLLP.com

Proposal Trustee to Alan Saskin

AND TO: **DENTONS CANADA LLP**
400-77 King Street West, TD Centre
Toronto, ON M5K 0A1

Neil Rabinovitch / Kenneth Kraft
Tel: 416-863-4656 / 416-863-4374
Email: neil.rabinovitch@dentons.com / kenneth.kraft@dentons.com

Lawyers for Adv. Gus Gissin, in his capacity as the Court-appointed Israeli Functionary of Urbancorp Inc.

AND TO: **TORYS LLP**
79 Wellington Street West, Suite 3000
Toronto, ON M5K 1N2

Scott Bomhof
Tel: 416-865-7370
Email: sbomhof@torys.com

Lawyers for First Capital Realty Inc.

AND TO **FARBER FINANCIAL GROUP**
150 York Street, Suite 1600
Toronto, ON M5H 3S5

Hylton Levi
Tel: 416.496.3070
Email: hlevy@farberfinancial.com

3434636

index

TABLE OF CONTENTS

Tab Case Law and Secondary Sources

tab 1

Tercon Contractors Ltd. v. British Columbia (Transportation and Highways), [2010] 1 SCR 69, 2010 SCC 4 (CanLII)

Date: 2010-02-12
Docket: 32460
Other citations: 315 DLR (4th) 385; [2010] 3 WWR 387; 100 BCLR (4th) 201; 65 BLR (4th) 1; 281 BCAC 245; 397 NR 331; [2010] CarswellBC 296; EYB 2010-169491; JE 2010-321; [2010] SCJ No 4 (QL); 86 CLR (3d) 163
Citation: Tercon Contractors Ltd. v. British Columbia (Transportation and Highways), [2010] 1 SCR 69, 2010 SCC 4 (CanLII), <http://canlii.ca/t/27zz2>, retrieved on 2017-03-15

SUPREME COURT OF CANADA

CITATION: Tercon Contractors Ltd. *v.* British Columbia (Transportation and Highways), 2010 SCC 4, [2010] 1 S.C.R. 69

DATE: 20100212
DOCKET: 32460

BETWEEN:

Tercon Contractors Ltd.
Appellant
and
Her Majesty The Queen in Right of the Province of British Columbia, by her Ministry of Transportation and Highways
Respondent
– and –
Attorney General of Ontario
Intervener

CORAM: McLachlin C.J. and Binnie, LeBel, Deschamps, Fish, Abella, Charron, Rothstein and Cromwell JJ.

REASONS FOR JUDGMENT: Cromwell J. (LeBel, Deschamps, Fish and Charron JJ. concurring)
(paras. 1 to 80)

DISSENTING REASONS: (paras. 81 to 142) Binnie J. (McLachlin C.J. and Abella and Rothstein JJ. concurring)

Tercon Contractors Ltd. *v.* British Columbia (Transportation and Highways), 2010 SCC 4, [2010] 1 S.C.R. 69

Tercon Contractors Ltd.
Appellant

v.

Her Majesty The Queen in Right of the Province of British Columbia, by her Ministry of Transportation and Highways
Respondent

and

Attorney General of Ontario
Intervener

Indexed as: Tercon Contractors Ltd. *v.* British Columbia (Transportation and Highways)

2010 SCC 4

File No.: 32460.

2009: March 23; 2010: February 12.

Present: McLachlin C.J. and Binnie, LeBel, Deschamps, Fish, Abella, Charron, Rothstein and Cromwell JJ.

ON APPEAL FROM THE COURT OF APPEAL FOR BRITISH COLUMBIA

Contracts — Breach of terms — Tender — Ineligible bidder — Exclusion of liability clause — Doctrine of fundamental breach — Province issuing tender call for construction of highway — Request for proposals restricting qualified bidders to six proponents — Province accepting bid from ineligible bidder — Exclusion clause protecting Province from liability arising from participation in tendering process — Whether Province breached terms of tendering contract in entertaining bid from ineligible bidder — If so, whether Province's conduct fell within terms of exclusion clause — If so, whether court should nevertheless refuse to enforce the exclusion clause because of unconscionability or some other contravention of public policy.

The Province of British Columbia issued a request for expressions of interest ("RFEI") for the design and construction of a highway. Six teams responded with submissions including Tercon and Brentwood. A few months later, the Province informed the six proponents that it now intended to design the highway itself and issued a request for proposals ("RFP") for its construction. The RFP set out a specifically defined project and contemplated that proposals would be evaluated according to specific criteria. Under its terms, only the six original proponents were eligible to submit a proposal; those received from any other party would not be considered. The RFP also included an exclusion of liability clause which provided: "Except as expressly and specifically permitted in these Instructions to Proponents, no Proponent shall have any claim for compensation of any kind whatsoever, as a result of participating in this RFP, and by submitting a Proposal each Proponent shall be deemed to have agreed that it has no claim." As it lacked expertise in drilling and blasting, Brentwood entered into a pre-bidding agreement with another construction company ("EAC"), which was not a qualified bidder, to undertake the work as a joint venture. This arrangement allowed Brentwood to prepare a more competitive proposal. Ultimately, Brentwood submitted a bid in its own name with EAC listed as a "major member" of the team. Brentwood and Tercon were the two short-listed proponents and the Province selected Brentwood for the project. Tercon successfully brought an action in damages against the Province. The trial judge found that the Brentwood bid was, in fact, submitted by a joint venture of Brentwood and EAC and that the Province, which was aware of the situation, breached the express provisions of the tendering contract with Tercon by considering a bid from an ineligible bidder and by awarding it the work. She also held that, as a matter of construction, the exclusion clause did not bar recovery for the breaches she had found. The clause was ambiguous and she resolved this ambiguity in Tercon's favour. She held that the Province's breach was fundamental and that it was not fair or reasonable to enforce the exclusion clause in light of the Province's breach. The Court of Appeal set aside the decision, holding that the exclusion clause was clear and unambiguous and barred compensation for all defaults.

Held (McLachlin C.J. and Binnie, Abella and Rothstein JJ. dissenting): The appeal should be allowed. The Court agreed on the appropriate framework of analysis but divided on the applicability of the exclusion clause to the facts.

The Court: With respect to the appropriate framework of analysis the doctrine of fundamental breach should be "laid to rest". The following analysis should be applied when a plaintiff seeks to escape the effect of an exclusion clause or other contractual terms to which it had previously agreed. The first issue is whether, as a matter of interpretation, the exclusion clause even applies to the circumstances established in evidence. This will depend on the court's interpretation of the intention of the parties as expressed in the contract. If the exclusion clause applies, the second issue is whether the exclusion clause was unconscionable and thus invalid at the time the contract was made. If the exclusion clause is held to be valid at the time of contract formation and applicable to the facts of the case, a third enquiry may be raised as to whether the court should nevertheless refuse to enforce the exclusion clause because of an overriding public policy. The burden of persuasion lies on the party seeking to avoid enforcement of the clause to demonstrate an abuse of the

freedom of contract that outweighs the very strong public interest in their enforcement. Conduct approaching serious criminality or egregious fraud are but examples of well-accepted considerations of public policy that are substantially incontestable and may override the public policy of freedom to contract and disable the defendant from relying upon the exclusion clause. Despite agreement on the appropriate framework of analysis, the court divided on the applicability of the exclusion clause to the facts of this case as set out below.

Per LeBel, Deschamps, Fish, Charron and Cromwell JJ.: The Province breached the express provisions of the tendering contract with Tercon by accepting a bid from a party who should not even have been permitted to participate in the tender process and by ultimately awarding the work to that ineligible bidder. This egregious conduct by the Province also breached the implied duty of fairness to bidders. The exclusion clause, which barred claims for compensation "as a result of participating" in the tendering process, did not, when properly interpreted, exclude Tercon's claim for damages. By considering a bid from an ineligible bidder, the Province not only acted in a way that breached the express and implied terms of the contract, it did so in a manner that was an affront to the integrity and business efficacy of the tendering process.

Submitting a compliant bid in response to a tender call may give rise to "Contract A" between the bidder and the owner. Whether a Contract A arises and what its terms are depends on the express and implied terms and conditions of the tender call and the legal consequences of the parties' actual dealings in each case. Here, there is no basis to interfere with the trial judge's findings that there was an intent to create contractual obligations upon submission of a compliant bid and that only the six original proponents that qualified through the RFEI process were eligible to submit a response to the RFP. The tender documents and the required ministerial approval of the process stated expressly that the Province was contractually bound to accept bids only from eligible bidders. Contract A therefore could not arise by the submission of a bid from any other party. The trial judge found that the joint venture of Brentwood and EAC was not eligible to bid as they had not simply changed the composition of their team but, in effect, had created a new bidder. The Province fully understood this and would not consider a bid from or award the work to that joint venture. The trial judge did not err in finding that in fact, if not in form, Brentwood's bid was on behalf of a joint venture between itself and EAC. The joint venture provided Brentwood with a competitive advantage in the bidding process and was a material consideration in favour of the Brentwood bid during the Province's evaluation process. Moreover, the Province took active steps to obfuscate the reality of the true nature of the Brentwood bid. The bid by the joint venture constituted "material non-compliance" with the tendering contract and breached both the express eligibility provisions of the tender documents, and the implied duty to act fairly towards all bidders.

When the exclusion clause is interpreted in harmony with the rest of the RFP and in light of the commercial context of the tendering process, it did not exclude a damages claim resulting from the Province unfairly permitting an ineligible bidder to participate in the tendering process. The closed list of bidders was the foundation

of this RFP and the parties should, at the very least, be confident that their initial bids will not be skewed by some underlying advantage in the drafting of the call for tenders conferred only upon one potential bidder. The requirement that only compliant bids be considered and the implied obligation to treat bidders fairly are factors that contribute to the integrity and business efficacy of the tendering process. The parties did not intend, through the words found in this exclusion clause, to waive compensation for conduct, like that of the Province in this case, that strikes at the heart of the tendering process. Clear language would be necessary to exclude liability for breach of the implied obligation, particularly in the case of public procurement where transparency is essential. Furthermore, the restriction on eligibility of bidders was a key element of the alternative process approved by the Minister. When the statutory provisions which governed the tendering process in this case are considered, it seems unlikely that the parties intended through this exclusion clause to effectively gut a key aspect of the approved process. The text of the exclusion clause in the RFP addresses claims that result from "participating in this RFP". Central to "participating in this RFP" was participating in a contest among those eligible to participate. A process involving other bidders — the process followed by the Province — is not the process called for by "this RFP" and being part of that other process is not in any meaningful sense "participating in this RFP".

Per McLachlin C.J. and Binnie, Abella and Rothstein JJ. (dissenting): The Ministry's conduct, while in breach of its contractual obligations, fell within the terms of the exclusion compensation clause. The clause is clear and unambiguous and no legal ground or rule of law permits a court to override the freedom of the parties to contract with respect to this particular term, or to relieve Tercon against its operation in this case. A court has no discretion to refuse to enforce a valid and applicable contractual term unless the plaintiff can point to some paramount consideration of public policy sufficient to override the public interest in freedom of contact and defeat what would otherwise be the contractual rights of the parties. The public interest in the transparency and integrity of the government tendering process, while important, did not render unenforceable the terms of the contract Tercon agreed to.

Brentwood was a legitimate competitor in the RFP process and all bidders knew that the road contract would not be performed by the proponent alone and required a large "team" of different trades and personnel to perform. The issue was whether EAC would be on the job as a major sub-contractor or identified with Brentwood as a joint venture "proponent" with EAC. Tercon has legitimate reason to complain about the Ministry's conduct, but its misconduct did not rise to the level where public policy would justify the court in depriving the Ministry of the protection of the exclusion of compensation clause freely agreed to by Tercon in the contract.

Contract A is based not on some abstract externally imposed rule of law but on the presumed (and occasionally implied) intent of the parties. At issue is the intention of the actual parties not what the court may project in hindsight would have been the intention of reasonable parties. Only in rare circumstances will a court relieve a party from the bargain it has made.

The exclusion clause did not run afoul of the statutory requirements. While the *Ministry of Transportation and Highways Act* favours "the integrity of the tendering process", it nowhere prohibits the parties from negotiating a "no claims" clause as part of their commercial agreement and cannot plausibly be interpreted to have that effect. Tercon — a sophisticated and experienced contractor — chose to bid on the project, including the risk posed by an exclusion of compensation clause, on the terms proposed by the Ministry. That was its prerogative and nothing in the "policy of the Act" barred the parties' agreement on that point.

The trial judge found that Contract A was breached when the RFP process was not conducted by the Ministry with the degree of fairness and transparency that the terms of Contract A entitled Tercon to expect. The Ministry was at fault in its performance of the RFP, but the process did not thereby cease to be the RFP process in which Tercon had elected to participate.

The interpretation of the majority on this point is disagreed with. "[P] articipating in this RFP" began with "submitting a Proposal" for consideration. The RFP process consisted of more than the final selection of the winning bid and Tercon participated in it. Tercon's bid was considered. To deny that such participation occurred on the ground that in the end the Ministry chose a Brentwood joint venture (an ineligible bidder) instead of Brentwood itself (an eligible bidder) would be to give the clause a strained and artificial interpretation in order, indirectly and obliquely, to avoid the impact of what may seem to the majority *ex post facto* to have been an unfair and unreasonable clause.

Moreover, the exclusion clause was not unconscionable. While the Ministry and Tercon do not exercise the same level of power and authority, Tercon is a major contractor and is well able to look after itself in a commercial context so there is no relevant imbalance of bargaining power. Further, the clause is not as draconian as Tercon portrays it. Other remedies for breach of Contract A were available. The parties expected, even if they did not like it, that the "no claims" clause would operate even where the eligibility criteria in respect of the bid (including the bidder) were not complied with.

Finally, the Ministry's misconduct did not rise to the level where public policy would justify the court in depriving the Ministry of the protection of the exclusion of compensation clause freely agreed to by Tercon in the contract.

Cases Cited

By Cromwell J.

Applied: *M.J.B. Enterprises Ltd. v. Defence Construction (1951) Ltd.*, 1999 CanLII 677 (SCC), [1999] 1 S.C.R. 619; *Martel Building Ltd. v. Canada*, 2000 SCC 60 (CanLII), [2000] 2 S.C.R. 860; **considered:** *Hunter Engineering Co. v. Syncrude Canada Ltd.*, 1989 CanLII 129 (SCC), [1989] 1 S.C.R. 426; *Cahill (G.J.) & Co. (1979) Ltd. v. Newfoundland and Labrador (Minister of Municipal and Provincial Affairs)*, 2005 NLTD 129 (CanLII), 250 Nfld. & P.E.I.R. 145; *Guarantee Co. of North*

America v. Gordon Capital Corp., 1999 CanLII 664 (SCC), [1999] 3 S.C.R. 423; *Fraser Jewellers (1982) Ltd. v. Dominion Electric Protection Co.* (1997), 1997 CanLII 4452 (ON CA), 34 O.R. (3d) 1; **referred to:** *Canadian Pacific Hotels Ltd. v. Bank of Montreal*, 1987 CanLII 55 (SCC), [1987] 1 S.C.R. 711; *Double N Earthmovers Ltd. v. Edmonton (City)*, 2007 SCC 3 (CanLII), [2007] 1 S.C.R. 116; *Hillis Oil and Sales Ltd. v. Wynn's Canada, Ltd.*, 1986 CanLII 44 (SCC), [1986] 1 S.C.R. 57.

By Binnie J. (dissenting)

Hunter Engineering Co. v. Syncrude Canada Ltd., 1989 CanLII 129 (SCC), [1989] 1 S.C.R. 426; *The Queen in right of Ontario v. Ron Engineering & Construction (Eastern) Ltd.*, 1981 CanLII 17 (SCC), [1981] 1 S.C.R. 111; *M.J.B. Enterprises Ltd. v. Defence Construction (1951) Ltd.*, 1999 CanLII 677 (SCC), [1999] 1 S.C.R. 619; *Naylor Group Inc. v. Ellis-Don Construction Ltd.*, 2001 SCC 58 (CanLII), [2001] 2 S.C.R. 943; *Martel Building Ltd. v. Canada*, 2000 SCC 60 (CanLII), [2000] 2 S.C.R. 860; *Double N Earthmovers Ltd. v. Edmonton (City)*, 2007 SCC 3 (CanLII), [2007] 1 S.C.R. 116; *Tercon Contractors Ltd. v. British Columbia* (1993), 9 C.L.R. (2d) 197, aff'd [1994] B.C.J. No. 2658 (QL); *Karsales (Harrow) Ltd. v. Wallis*, [1956] 1 W.L.R. 936; *Guarantee Co. of North America v. Gordon Capital Corp.*, 1999 CanLII 664 (SCC), [1999] 3 S.C.R. 423; *ABB Inc. v. Domtar Inc.*, 2007 SCC 50 (CanLII), [2007] 3 S.C.R. 461; *Re Millar Estate*, 1937 CanLII 10 (SCC), [1938] S.C.R. 1; *Plas-Tex Canada Ltd. v. Dow Chemical of Canada Ltd.*, 2004 ABCA 309 (CanLII), 245 D.L.R. (4th) 650.

Statutes and Regulations Cited

Ministry of Transportation and Highways Act, R.S.B.C. 1996, c. 311, ss. 4, 23.

Authors Cited

Hall, Geoff R. *Canadian Contractual Interpretation Law*. Markham, Ont.: LexisNexis, 2007.

Kain, Brandon, and Douglas T. Yoshida. "The Doctrine of Public Policy in Canadian Contract Law", in Todd L. Archibald and Randall Scott Echlin, eds., *Annual Review of Civil Litigation, 2007*. Toronto: Thomson Carswell, 2007, 1.

McCamus, John D. *The Law of Contracts*. Toronto: Irwin Law, 2005.

Waddams, S. M. *The Law of Contracts*, 5th ed. Aurora, Ont.: Canada Law Book, 2005.

APPEAL from a judgment of the British Columbia Court of Appeal (Donald, Mackenzie and Lowry JJ.A.), 2007 BCCA 592 (CanLII), 73 B.C.L.R. (4th) 201, 40 B.L.R. (4th) 26, 289 D.L.R. (4th) 647, [2008] 2 W.W.R. 410, 249 B.C.A.C. 103, 414 W.A.C. 103, 66 C.L.R. (3d) 1, [2007] B.C.J. No. 2558 (QL), 2007 CarswellBC 2880, setting aside a decision of Dillon J., 2006 BCSC 499 (CanLII), 53 B.C.L.R. (4th) 138, [2006] 6 W.W.R. 275, 18 B.L.R. (4th) 88, 51 C.L.R. (3d) 227,

[2006] B.C.J. No. 657 (QL), 2006 CarswellBC 730. Appeal allowed, McLachlin C.J. and Binnie, Abella and Rothstein JJ. dissenting.

Chris R. Armstrong, *Brian G. McLean*, *William S. McLean* and *Marie-France Major*, for the appellant.

J. Edward Gouge, *Q.C.*, *Jonathan Eades* and *Kate Hamm*, for the respondent.

Malliha Wilson and *Lucy McSweeney*, for the intervener.

The judgment of LeBel, Deschamps, Fish, Charron and Cromwell JJ. was delivered by

CROMWELL J. —

I. Introduction

[1] The Province accepted a bid from a bidder who was not eligible to participate in the tender and then took steps to ensure that this fact was not disclosed. The main question on appeal, as I see it, is whether the Province succeeded in excluding its liability for damages flowing from this conduct through an exclusion clause it inserted into the contract. I share the view of the trial judge that it did not.

[2] The appeal arises out of a tendering contract between the appellant, Tercon Contractors Ltd., who was the bidder, and the respondent, Her Majesty the Queen in Right of the Province of British Columbia, who issued the tender call. The case turns on the interpretation of provisions in the contract relating to eligibility to bid and exclusion of compensation resulting from participation in the tendering process.

[3] The trial judge found that the respondent (which I will refer to as the Province) breached the express provisions of the tendering contract with Tercon by accepting a bid from another party who was not eligible to bid and by ultimately awarding the work to that ineligible bidder. In short, a bid was accepted and the work awarded to a party who should not even have been permitted to participate in the tender process. The judge also found that this and related conduct by the Province breached the implied duty of fairness to bidders, holding that the Province had acted "egregiously" (2006 BCSC 499 (CanLII), 53 B.C.L.R. (4th) 138, at para. 150). The judge then turned to the Province's defence based on an exclusion clause that barred claims for compensation "as a result of participating" in the tendering process. She held that this clause, properly interpreted, did not exclude Tercon's claim for damages. In effect, she held that it was not within the contemplation of the parties

that this clause would bar a remedy in damages arising from the Province's unfair dealings with a party who was not entitled to participate in the tender in the first place.

[4] The Province appealed and the Court of Appeal reversed (2007 BCCA 592 (CanLII), 73 B.C.L.R. (4th) 201). Dealing only with the exclusion clause issue, it held that the clause was clear and unambiguous and barred compensation for all defaults.

[5] On Tercon's appeal to this Court, the questions for us are whether the successful bidder was eligible to participate in the request for proposals ("RFP") and, if not, whether Tercon's claim for damages is barred by the exclusion clause.

[6] In my respectful view, the trial judge reached the right result on both issues. The Province's attempts to persuade us that it did not breach the tendering contract are, in my view, wholly unsuccessful. The foundation of the tendering contract was that only six, pre-selected bidders would be permitted to participate in the bidding. As the trial judge held, the Province not only acted in a way that breached the express and implied terms of the contract by considering a bid from an ineligible bidder, it did so in a manner that was an affront to the integrity and business efficacy of the tendering process. One must not lose sight of the fact that the trial judge found that the Province acted egregiously by "ensuring that [the true bidder] was not disclosed" (para. 150) and that its breach "attacke[d] the underlying premise of the [tendering] process" (para. 146), a process which was set out in detail in the contract and, in addition, had been given ministerial approval as required by statute.

[7] As for its reliance on the exclusion clause, the Province submits that the parties were free to agree to limitations of liability and did so. Consideration of this submission requires an interpretation of the words of the clause to which the parties agreed in the context of the contract as a whole. My view is that, properly interpreted, the exclusion clause does not protect the Province from Tercon's damage claim which arises from the Province's dealings with a party not even eligible to bid, let alone from its breach of the implied duty of fairness to bidders. In other words, the Province's liability did not arise from Tercon's participation in the process that the Province established, but from the Province's unfair dealings with a party who was not entitled to participate in that process.

[8] I would allow the appeal and restore the judgment of the trial judge.

II. Brief Overview of the Facts

[9] I will have to set out more factual detail as part of my analysis. For now, a very brief summary will suffice. In 2000, the Ministry of Transportation and Highways (also referred to as the "Province") issued a request for expressions of interest ("RFEI") for designing and building a highway in northwestern British Columbia. Six teams made submissions, including Tercon and Brentwood Enterprises Ltd. Later that year, the Province informed the six proponents that it now intended to design the highway itself and would issue a RFP for its construction.

[10] The RFP was formally issued on January 15, 2001. Under its terms, only the six original proponents were eligible to submit a proposal. The RFP also included a clause excluding all claims for damages "as a result of participating in this RFP" (s. 2.10).

[11] Unable to submit a competitive bid on its own, Brentwood teamed up with Emil Anderson Construction Co. ("EAC"), which was not a qualified bidder, and together they submitted a bid in Brentwood's name. Brentwood and Tercon were the two short-listed proponents and the Ministry ultimately selected Brentwood as the preferred proponent.

[12] Tercon brought an action seeking damages, alleging that the Ministry had considered and accepted an ineligible bid and that, but for that breach, it would have been awarded the contract. The trial judge agreed and awarded roughly $3.5 million in damages and prejudgment interest. As noted, the Court of Appeal reversed and Tercon appeals by leave of the Court.

III. Issues

[13] The issues for decision are whether the trial judge erred in finding that:

1. the Province breached the tendering contract by entertaining a bid from an ineligible bidder.

2. the exclusion clause does not bar the appellant's claim for damages for the breaches of the tendering contract found by the trial judge.

IV. Analysis

A. *Was the Brentwood Bid Ineligible?*

[14] The first issue is whether the Brentwood bid was from an eligible bidder. The judge found that the bid was in substance, although not in form, from a joint venture of Brentwood and EAC and that it was, therefore, an ineligible bid. The Province attacks this finding on three grounds:

(i) a joint venture is not a legal person and therefore the Province could not and did not contract with a joint venture;

(ii) it did not award the contract to EAC and EAC had no contractual responsibility to the Province for failure to perform the contract;

(iii) there was no term of the RFP that restricted the right of proponents to enter into joint venture agreements with others; this arrangement merely left Brentwood, the original proponent, in place and allowed it to enhance its ability to perform the work.

[15] While these were the Province's main points, its position became more wide-ranging during oral argument, at times suggesting that it had no contractual obligation to deal only with eligible bidders. It is therefore necessary to take a step back and look at that threshold point before turning to the Province's more focussed submissions.

1. The Province's Contractual Obligations in the Bidding Process

[16] The judge found, and it was uncontested at trial, that only the six original proponents that qualified through the RFEI process were eligible to submit a response to the RFP. This finding is not challenged on appeal, although there was a passing suggestion during oral argument that there was no contractual obligation of this sort at all. The trial judge also held, noting that this point was uncontested, that a joint venture between Brentwood and EAC was ineligible to bid. This is also not contested on appeal. These two findings are critical to the case and provide important background for an issue that is in dispute, namely whether the Brentwood bid was ineligible. It is, therefore, worth reviewing the relevant background in detail. I first briefly set out the legal framework and then turn to the trial judge's findings.

2. Legal Principles

[17] Submitting a compliant bid in response to a tender call *may* give rise to a contract — called Contract A — between the bidder and the owner, the express terms of which are found in the tender documents. The contract may also have implied terms according to the principles set out in *Canadian Pacific Hotels Ltd. v. Bank of Montreal*, 1987 CanLII 55 (SCC), [1987] 1 S.C.R. 711; see also *M.J.B. Enterprises Ltd. v. Defence Construction (1951) Ltd.*, 1999 CanLII 677 (SCC), [1999] 1 S.C.R. 619, and *Martel Building Ltd. v. Canada*, 2000 SCC 60 (CanLII), [2000] 2 S.C.R. 860. The key word, however, is "may". The Contract A/Contract B framework is one that arises, if at all, from the dealings between the parties. It is not an artificial construct imposed by the courts, but a description of the legal consequences of the parties' actual dealings. The Court emphasized in *M.J.B.* that whether Contract A arises and if it does, what its terms are, depend on the express and implied terms and conditions of the tender call in each case. As Iacobucci J. put it, at para. 19:

> What is important . . . is that the submission of a tender in response to an invitation to tender may give rise to contractual obligations, quite apart from the obligations associated with the construction contract to be entered into upon the acceptance of a tender, depending upon whether the parties intend to initiate contractual relations by the submission of a bid. If such a contract arises, its terms are governed by the terms and conditions of the tender call. [Emphasis added.]

3. The Trial Judge's Findings Concerning the Existence of Contract A

[18] The question of whether Tercon's submission of a compliant bid gave rise to contractual relations between it and the Province was contested by the Province at trial. The trial judge gave extensive reasons for finding against the Province on this issue. We are told that the Province did not pursue this point in the Court of Appeal but instead premised its submissions on the existence of Contract A. The Province took the same approach in its written submissions in this Court. However, during oral argument, there was some passing reference in response to questions that there was no Contract A. In light of the position taken by the Province on its appeal to the Court of Appeal and in its written submissions in this Court, it is now too late to revisit whether there were contractual duties between Tercon and the Province. Even if it were open to the Province to make this argument now, I can see no error in legal principle or any palpable and overriding error of fact in the trial judge's careful reasons on this point.

[19] The trial judge did not mechanically impose the Contract A/Contract B framework, but considered whether Contract A arose in light of her detailed analysis of the dealings between the parties. That was the right approach. She reviewed in detail the provisions of the RFP which supported her conclusion that there was an intent to create contractual relations upon submission of a compliant bid.

She noted, for example, that bids were to be irrevocable for 60 days and that security of $50,000 had to be paid by all proponents and was to be increased to $200,000 by the successful proponent. Any revisions to proposals prior to the closing date had to be in writing, properly executed and received before the closing time. The RFP also set out detailed evaluation criteria and specified that they were to be the only criteria to be used to evaluate proposals. A specific form of alliance agreement was attached. There were detailed provisions about pricing that were fixed and non-negotiable. A proponent was required to accept this form of contract substantially, and security was lost if an agreement was not executed. The Ministry reserved a right to cancel the RFP under s. 2.9 but in such event was obliged to reimburse proponents for costs incurred in preparing their bids up to $15,000 each. Proponents had to submit a signed proposal form, which established that they offered to execute an agreement substantially in the form included in the RFP package. Further, they acknowledged that the security could be forfeited if they were selected as the preferred proponent and failed to enter into good faith discussions with the Ministry to reach an agreement and sign the alliance agreement.

[20] In summary, as the trial judge found, the RFP set out a specifically defined project, invited proposals from a closed and specific list of eligible proponents, and contemplated that proposals would be evaluated according to specific criteria. Negotiation of the alliance construction contract was required, but the negotiation was constrained and did not go to the fundamental details of either the procurement process or the ultimate contract.

[21] There is, therefore, no basis to interfere with the judge's finding that there was an intent to create contractual obligations upon submission of a compliant bid. I add, however, that the tender call in this case did not give rise to the classic Contract A/Contract B framework in which the bidder submits an irrevocable bid and undertakes to enter into Contract B on those terms if it is accepted. The alliance model process which was used here was more complicated than that and involved good faith negotiations for a Contract B in the form set out in the tender documents. But in my view, this should not distract us from the main question here. We do not have to spell out all of the terms of Contract A, let alone of Contract B, so as to define all of the duties and obligations of both the bidders and the Province. The question here is much narrower: did contractual obligations arise as a result of Tercon's compliant bid and, if so, was it a term of that contract that the Province would only entertain bids from eligible bidders? The trial judge found offer, acceptance and consideration in the invitation to tender and Tercon's bid. There is no basis, in my respectful view, to challenge that finding even if it were open to the Province to try to do so at this late stage of the litigation.

4. The Trial Judge's Finding Concerning Eligibility

[22] It was not contested at trial that only the six original proponents that qualified through the RFEI process were eligible to bid. This point is not in issue on appeal; the question is what this eligibility requirement means. It will be helpful, therefore, to set out the background about this limited eligibility to bid in this tendering process.

[23] To begin, it is worth repeating that there is no doubt that the Province was contractually bound to accept bids only from eligible bidders. This duty may be implied even absent express stipulation. For example, in *M.J.B.*, the Court found that an implied obligation to accept only compliant bids was necessary to give business efficacy to the tendering process, noting, at para. 41, that a bidder must expend effort and incur expense in preparing its bid and must submit bid security and that it is "obvious" that it makes "little sense" for the bidder to comply with these requirements if the owner "is allowed, in effect, to circumscribe this process and accept a non-compliant bid". But again, whether such a duty should be implied in any given case will depend on the dealings between the parties. Here, however, there is no need to rely on implied terms. The obligation to consider only bids from eligible bidders was stated expressly in the tender documents and in the required ministerial approval of the process which they described.

[24] As noted, in early 2000, the Province issued a RFEI based on a design-build model; the contractor would both design and build the highway. The RFEI contemplated that a short list of three qualified contractors, or teams composed of contractors and consultants, would be nominated as proponents. Each was to provide a description of the legal structure of the team and to describe the role of each team member along with the extent of involvement of each team member as a percentage of the total scope of the project and an organization chart showing each team member's role. Any change in team management or key positions required notice in writing to the Province which reserved the right to disqualify the proponent if the change materially and negatively affected the ability of the team to carry out the project.

[25] Expressions of interest ("EOI") were received from six teams including Tercon and Brentwood. The evaluation panel and independent review panel recommended a short list of three proponents with Tercon topping the evaluation. Brentwood was evaluated fifth and was not on the short list. Brentwood was known to lack expertise in drilling and blasting and so its EOI had included an outline of the key team members with that experience. EAC did not participate and had no role in the Brentwood submission. The results of this evaluation were not communicated and the process did not proceed because the Province decided to design the project itself and issue an RFP for an alliance model contract to construct the highway.

[26] It was clear from the outset that only those who had submitted proposals during the RFEI process would be eligible to submit proposals under the RFP. This was specified in the approval of the process by the Minister of Transportation and Highways ("Minister") before the RFP was issued. It is worth pausing here to briefly look at the Minister's role.

[27] Pursuant to s. 23 of the *Ministry of Transportation and Highways Act*, R.S.B.C. 1996, c. 311, the legislation in force at the relevant time, the Minister was required to invite public tenders for road construction unless he or she determined that another process would result in competitively established costs for the work. The section provided:

> **23** (1) The minister must invite tenders by public advertisement, or if that is impracticable, by public notice, for the construction and repair of all government buildings, highways and public works, except for the following:
>
> . . .
>
> (c) if the minister determines that an alternative contracting process will result in competitively established costs for the performance of the work.
>
> (2) The minister must cause all tenders received to be opened in public, at a time and place stated in the advertisement or notice.
>
> (3) The prices must be made known at the time the tenders are opened.
>
> (4) In all cases where the minister believes it is not expedient to let the work to the lowest bidder, the minister must report to and obtain the approval of the Lieutenant Governor in Council before passing by the lowest tender, except if delay would be injurious to the public interest.
>
> . . .

[28]These provisions make clear that the work in this case had to be awarded by public tender, absent the Minister's approval of an alternative process, and had to be awarded to the lowest bidder, absent approval of the Lieutenant Governor in Council. As noted, ministerial approval was given for an alternative process under s. 23(1)(c). The Minister issued a notice that, pursuant to that section, he approved the process set out in an attached document and had determined it to be an alternative contracting process that would result in competitively established costs for the performance of the work. The attached document outlined in seven numbered paragraphs the process that had been approved.

[29]The document described the background of the public RFEI (which I have set out earlier), noting that *only those firms identified through the EOI process would be eligible to submit proposals for the work* and that they would receive invitations to do so. The Minister's approval in fact referred to the firms who had been short-listed from the RFEI process as being eligible. If this were taken to refer only to the three proponents identified by the evaluation process of the RFEI, Tercon would be included but Brentwood would not. However, no one has suggested that anything turns on this and it seems clear that ultimately all six of the RFEI proponents — including both Tercon and Brentwood — were intended to be eligible. The ministerial approval then briefly set out the process. Proposals "by short-listed firms" were to be evaluated "using the considerations set out in the RFP".

[30]It is clear, therefore, that participation in the RFP process approved by the Minister was limited to those who had participated in the RFEI process.

[31]The Province's factum implies that the Minister approved inclusion of the exclusion clause in the RFP. However, there is no evidence of this in the record before the Court. The Minister's approval is before us. It is dated as having been prepared on August 23, 2000 and signed on October 19, 2000, and approves a process outlined in a two-page document attached to it. It says nothing about exclusion of the Province's liability. The RFP, containing the exclusion clause in issue here, is dated January 15, 2001 and was sent out to eligible bidders under cover of a letter of the same date, some three months after the Minister's approval.

[32]The RFP is a lengthy document, containing detailed instructions to proponents, required forms, a time schedule of the work, detailed provisions concerning contract pricing, a draft of the ultimate construction contract and many other things. Most relevant for our purposes are the terms of the instructions to proponents and in particular the eligibility requirements for bidders.

[33]The RFP reiterates in unequivocal terms that eligibility to bid was restricted as set out in the ministerial approval. It also underlines the significance of the identity of the proponent. In s. 1.1, the RFP specifies that only the six teams involved in the RFEI would be eligible. The term "proponent", which refers to a bidder, is defined in s. 8 as "a team that has become eligible to respond to the RFP as described in Section 1.1 of the Instructions to Proponents". Section 2.8(a) of the RFP stipulates that *only* the six proponents qualified through the RFEI process were eligible and that *proposals received from any other party would not be considered.* In

short, there were potentially only six participants and "Contract A" could not arise by the submission of a bid from any other party.

[34]The RFP also addressed material changes to the proponent, including changes in the proponent's team members and its financial ability to undertake and complete the work. Section 2.8(b) of the RFP provided in part as follows:

> If in the opinion of the Ministry a material change has occurred to the Proponent since its qualification under the RFEI, including if the composition of the Proponent's team members has changed . . . or if, for financial or other reasons, the Proponent's ability to undertake and complete the Work has changed, then the Ministry may request the Proponent to submit further supporting information as the Ministry may request in support of the Proponent's qualification to perform the Work. If in the sole discretion of the Ministry as a result of the changes the Proponent is not sufficiently qualified to perform the Work then the Ministry reserves the right to disqualify that Proponent, and reject its Proposal.

[35]The proponent was to provide an organization chart outlining the proponent's team members, structure and roles. If the team members were different from the RFEI process submission, an explanation was to be provided for the changes: s. 4.2(b)i). A list of subcontractors and suppliers was also to be provided and the Ministry had to be notified of any changes: s. 4.2(e).

[36]The RFP provided proponents with a mechanism to determine whether they remained qualified to submit a proposal. If a proponent was concerned about its eligibility as a result of a material change, it could make a preliminary submission to the Ministry describing the nature of the changes and the Ministry would give a written decision as to whether the proponent was still qualified: s. 2.8 (b).

[37]Brentwood tried to take advantage of this process. The trial judge thoroughly outlined this, at paras. 17-23 of her reasons. In brief, Brentwood lacked expertise in drilling and blasting and by the time the RFP was issued, it faced limited local bonding capacity due to commitments to other projects, a shorter construction period, the potential unavailability of subcontractors and limited equipment to perform the work. It in fact considered not bidding at all. Instead, however, it entered into a pre-bidding agreement with EAC that the work would be undertaken by a joint venture of Brentwood and EAC and that upon being awarded the work, they would enter into a joint venture agreement and would share 50/50 the costs, expenses, losses and gains. The trial judge noted that it was common in the industry for contractors to

agree to a joint venture on the basis of a pre-bid agreement with the specifics of the joint venture to be worked out once the contract was awarded and that Brentwood and EAC acted consistently throughout in accordance with this industry standard.

[38]Brentwood sent the Province's project manager, Mr. Tasaka, a preliminary submission as provided for in s. 2.8(b) of the RFP, advising of a material change in its team's structure in that it wished to form a joint venture with EAC. This was done, the trial judge found, because Brentwood thought it would be disqualified if it submitted a proposal as a joint venture without the Ministry's prior approval under this section of the RFP. The Province never responded in writing as it ought to have according to s. 2.8(b).

[39]It seems to have been assumed by everyone that a joint venture of Brentwood and EAC was not eligible because this change would not simply be a change in the composition of the bidder's team, but in effect a new bidder. Without reviewing in detail all of the evidence referred to by the trial judge, it is fair to say that although Brentwood ultimately submitted a proposal in its own name, the proposal in substance was from the Brentwood/EAC joint venture and was evaluated as such. As the trial judge concluded:

> The substance of the proposal was as a joint venture and this must have been apparent to all. The [project evaluation panel] approved Brentwood/EAC as joint venturers as the preferred proponent. The [panel] was satisfied that Tercon had the capacity and commitment to do the job but preferred the joint venture submission of Brentwood/EAC. [para. 53]

[40]There was some suggestion by the Province during oral argument that the trial judge had wrongly imposed on it a duty to investigate Brentwood's bid, a duty rejected by the majority of the Court in *Double N Earthmovers Ltd. v. Edmonton (City)*, 2007 SCC 3 (CanLII), [2007] 1 S.C.R. 116. In my view, the trial judge did no such thing. As her detailed findings make clear, the Province: (1) fully understood that the Brentwood bid was in fact on behalf of a joint venture of Brentwood and EAC; (2) thought that a bid from that joint venture was not eligible; and (3) took active steps to obscure the reality of the situation. No investigation was required for the Province to know these things and the judge imposed no duty to engage in one.

5. The Province's Submissions

[41]I will address the Province's first two points together:

(i) a joint venture is not a legal person and therefore the Province could not and did not contract with a joint venture; and

(ii) it did not award the contract to EAC and EAC had no contractual responsibility to the Province for failure to perform the contract.

[42]I cannot accept these submissions. The issue is not, as these arguments assume, whether the Province contracted with a joint venture or whether EAC had contractual obligations to the Province. The issue is whether the Province considered an ineligible bid; the point of substance is whether the bid was from an eligible bidder.

[43]At trial there was no contest that a bid from a joint venture involving an ineligible bidder would be ineligible. The Province's position was that there was no need to look beyond the face of the bid to determine who was bidding: the proposal was in the name of Brentwood and therefore the bid was from a compliant bidder. Respectfully, I see no error in the trial judge's rejection of this position. There was a mountain of evidence to support the judge's conclusions that first, Brentwood's bid, in fact if not in form, was on behalf of a joint venture between itself and EAC; second, the Province knew this and took the position that it could not consider a bid from or award the work to that joint venture; third, the existence of the joint venture was a material consideration in favour of the Brentwood bid during the evaluation process; and finally, that steps were taken by revising and drafting documentation to obfuscate the reality of the situation.

[44]Brentwood was one of the original RFEI proponents and was of course eligible to bid, subject to material changes in the composition of its team. EAC had not submitted a proposal during the RFEI process. It had been involved in advising the Ministry in relation to the project in 1998 and, in the fall of 2000, the Ministry had asked EAC to prepare an internal bid for comparison purposes (although EAC did not do so) as EAC was not entitled to bid on the Project.

[45]As noted earlier, after the RFP was issued, Brentwood and EAC entered into a pre-bidding agreement that provided that the work would be undertaken in the name of Brentwood/Anderson, a joint venture, that the work would be sponsored and managed by the joint venture and that upon being awarded the contract, the parties would enter into a joint venture agreement. Brentwood advised the Ministry in writing that it was forming a joint venture with EAC "to submit a more competitive price"; this fax was in effect a preliminary submission contemplated by s. 2.8(b) of the RFP and was written, as the trial judge found, because Brentwood

assumed that it could be disqualified if it submitted a proposal as a joint venture unless prior arrangements had been made. The Province never responded in writing to this preliminary submission, as required by s. 2.8(b). There were, however, discussions with the Province's project manager, Mr. Tasaka who, the trial judge found, understood that a joint venture from Brentwood and EAC would not be eligible. As the judge put it, the Province's position appears to have been that the Brentwood/EAC proposal could proceed as long as the submission was in the name of Brentwood.

[46]In the result, EAC was listed in the ultimate submission as a "major member" of the team. The legal relationship with EAC was not specified and EAC was listed as a subcontractor even though, as the trial judge found, their relationship bore no resemblance to a standard subcontractor agreement. The trial judge found as facts — and these findings are not challenged — that Brentwood and EAC always intended between themselves to form a joint venture and to formalize that arrangement once the contract was secured, and further, that the role of EAC was purposefully obfuscated in the bid to avoid an apparent conflict with s. 2.8(a) of the RFP.

[47]During the selection process, it became clear that the bid was in reality on behalf of a joint venture. The project evaluation panel ("PEP") requested better information than provided in the bid about the structure of the business arrangements between Brentwood and EAC. Brentwood responded by disclosing the pre-bid agreement between them to form a 50/50 joint venture if successful. The PEP understood from this that Brentwood and EAC had a similar interest in the risk and reward under the contract and that this helped satisfy them that the "risk/reward" aspect of the alliance contract could be negotiated with them flexibly. The PEP clearly did not consider EAC to be a subcontractor although shown as such in the bid. In its step 6 report, the PEP consistently referred to the proponent as being a joint venture of Brentwood and EAC or as "Brentwood/EAC" and the trial judge found that it was on the basis that they were indeed a joint venture that PEP approved Brentwood/EAC as the preferred proponent. This step 6 report was ultimately revised to refer only to the Brentwood team as the official proponent. The trial judge found as a fact that this revision was made because "it was apparent that a joint venture was not eligible to submit a proposal" (para. 56).

[48]The findings of the trial judge and the record make it clear that it was no mere question of form rather than a matter of substance whether the bidder was Brentwood with other team members or, as it in fact was, the Brentwood/EAC joint venture. As she noted, at para. 121 of her reasons, the whole purpose of the joint venture was to allow submission of a more competitive price than it would have been able to do as a proponent with a team as allowed under s. 2.8(b) of the RFP. The joint venture permitted a 50/50 sharing of risk and reward and co-management of the

project while at the same time avoiding the restrictions on subcontracting in the tendering documents. As the judge put it, the bid by the joint venture constituted "material non-compliance" with the tendering contract: ". . . the joint venture with EAC allowed Brentwood to put forward a more competitive price than contemplated under the RFEI proposal. This went to the essence of the tendering process" (para. 126).

[49]The Province suggests that the trial judge's reasons allow form to triumph over substance. In my view, it is the Province's position that better deserves that description. It had a bid which it knew to be on behalf of a joint venture, encouraged the bid to proceed and took steps to obfuscate the reality that it was on behalf of a joint venture. Permitting the bid to proceed in this way gave the joint venture a competitive advantage in the bidding process, and the record could not be clearer that the joint venture nature of the bid was one of its attractions during the selection process. The Province nonetheless submits that so long as only the name of Brentwood appears on the bid and ultimate Contract B, all is well. If ever a submission advocated placing form above substance, this is it.

[50]It is true that the Province had legal advice and did not proceed in defiance of it. However, the facts as found by the trial judge about this legal advice hardly advance the Province's position. The judge found that the Province's lawyer was not aware of the background relevant to the question of whether the Brentwood bid was eligible, never reviewed the proponent eligibility requirements in the RFP and was not asked to and did not direct his mind to the question of eligibility. As the trial judge put it, the lawyer "appears to have operated on the assumption that Brentwood had been irreversibly selected" (para. 70).

[51]The Brentwood/EAC joint venture having been selected as the preferred proponent, negotiations for the alliance contract ensued. The trial judge found that by this time, all agreed that a joint venture was not an eligible proponent and the Ministry was taking the position that the contract could not be in the name of the joint venture. Brentwood and EAC executed a revised pre-contract agreement that provided, notwithstanding the letter of intent from the Ministry addressed to Brentwood indicating that the legal relationship between them would be contractor/subcontractor, the contract would be performed and the profits shared equally between them. The work was to be managed by a committee with equal representation, the bond required by the owner was to be provided by both parties and EAC indemnified Brentwood against half of any loss or cost incurred as a result of performance of the work. According to schedule B4 of the RFP, all subcontracts were to be attached to the RFP but no contract between Brentwood and EAC was ever provided or attached to the proposal.

[52]The Province has identified no palpable and overriding error in these many findings of fact by the trial judge. I conclude, therefore, that we must approach the case on the basis of the judge's finding that the bid was in fact, if not in form, submitted by a joint venture of Brentwood and EAC, that the Ministry was well aware of this, that the existence of the joint venture was a material consideration in favour of the bid during the evaluation process and that by bidding as a joint venture, Brentwood was given a competitive advantage in the bidding process.

[53]I reject the Ministry's submissions that all that matters is the form and not the substance of the arrangement. In my view, the trial judge's finding that this bid was in fact on behalf of a joint venture is unassailable.

[54]I turn to the Province's third point:

(iii) there was no term of the RFP that restricted the right of proponents to enter into joint venture agreements with others; this arrangement merely left Brentwood, the original proponent in place and allowed it to enhance its ability to perform the work.

[55]This submission addresses the question of whether the joint venture was an eligible bidder. The Province submits that it is, arguing that s. 2.8(b) of the RFP shows that the RFP contemplated that each proponent would be supported by a team, that the composition of the team might change and that the Province under that section retained the right to approve or reject changes in the team of any proponent. I cannot accept these submissions.

[56]Section 2.8 must be read as a whole and in light of the ministerial approval which I have described earlier. Section 2.8(a), consistent with that approval, stipulates that only the six proponents qualified through the RFEI process were eligible to submit responses and that proposals from any other party "shall not be considered". The word "proponent" is defined in s. 8 as a team that has become eligible to respond to the RFP. The material change provisions in s. 2.8(b) should not be read as negating the express provisions of the RFP and the ministerial approval of the process. When read as a whole, the provisions about material change do not permit the addition of a new entity as occurred here. The process actually followed was not the one specified in the bidding contract and was not authorized by the statute because it was not the one approved by the Minister.

[57]Moreover, even if one were to conclude (and I would not) that this change from the Brentwood team that participated in the RFEI to the Brentwood/EAC joint venture by whom the bid was submitted could fall within the material change provisions of s. 2.8(b), the Province never gave a written decision to permit this change as required by that provision. As the trial judge noted, in fact the Province's position was that such a bid would not be eligible and its agents took steps to obfuscate the true proponent in the relevant documentation.

[58]The trial judge also found that there was an implied obligation of good faith in the contract and that the Province breached this obligation by failing to treat all bidders equally by changing the terms of eligibility to Brentwood's competitive advantage. This conclusion strongly reinforces the trial judge's decision about eligibility. Rather than repeating her detailed findings, I will simply quote her summary at para. 138:

> The whole of [the Province's] conduct leaves me with no doubt that the [Province] breached the duty of fairness to [Tercon] by changing the terms of eligibility to Brentwood's competitive advantage. At best, [the Province] ignored significant information to its [i.e. Tercon's] detriment. At worst, the [Province] covered up its knowledge that the successful proponent was an ineligible joint venture. In the circumstances here, it is not open to the [Province] to say that a joint venture was only proposed. Nor can the [Province] say that it was unaware of the joint venture when it acted deliberately to structure contract B to include EAC as fully responsible within a separate contract with Brentwood, so minimizing the [Province's] risk that the contract would be unenforceable against EAC if arrangements did not work out. . . . The [Province] was . . . prepared to take the risk that unsuccessful bidders would sue: this risk did materialize.

[59]To conclude on this point, I find no fault with the trial judge's conclusion that the bid was in fact submitted on behalf of a joint venture of Brentwood and EAC which was an ineligible bidder under the terms of the RFP. This breached not only the express eligibility provisions of the tender documents, but also the implied duty to act fairly towards all bidders.

B. *The Exclusion Clause*

1. Introduction

[60]As noted, the RFP includes an exclusion clause which reads as follows:

2.10 . . .

> Except as expressly and specifically permitted in these Instructions to Proponents, no Proponent shall have any claim for compensation of any kind whatsoever, as a result of participating in this RFP, and by submitting a Proposal each Proponent shall be deemed to have agreed that it has no claim. [Emphasis added.]

[61]The trial judge held that as a matter of construction, the clause did not bar recovery for the breaches she had found. The clause, in her view, was ambiguous and, applying the *contra proferentem* principle, she resolved the ambiguity in Tercon's favour. She also found that the Province's breach was fundamental and that it was not fair or reasonable to enforce the exclusion clause in light of the nature of the Province's breach. The Province contends that the judge erred both with respect to the construction of the clause and her application of the doctrine of fundamental breach.

[62]On the issue of fundamental breach in relation to exclusion clauses, my view is that the time has come to lay this doctrine to rest, as Dickson C.J. was inclined to do more than 20 years ago: *Hunter Engineering Co. v. Syncrude Canada Ltd.*, 1989 CanLII 129 (SCC), [1989] 1 S.C.R. 426, at p. 462. I agree with the analytical approach that should be followed when tackling an issue relating to the applicability of an exclusion clause set out by my colleague Binnie J. However, I respectfully do not agree with him on the question of the proper interpretation of the clause in issue here. In my view, the clause does not exclude Tercon's claim for damages, and even if I am wrong about that, the clause is at best ambiguous and should be construed *contra proferentem* as the trial judge held. As a result of my conclusion on the interpretation issue, I do not have to go on to apply the rest of the analytical framework set out by Binnie J.

[63]In my view, the exclusion clause does not cover the Province's breaches in this case. The RFP process put in place by the Province was premised on a closed list of bidders; a contest with an ineligible bidder was not part of the RFP process and was in fact expressly precluded by its terms. A "Contract A" could not arise as a result of submission of a bid from any other party. However, as a result of how the Province proceeded, the very premise of its own RFP process was missing, and the work was awarded to a party who could not be a participant in the RFP process. That is what Tercon is complaining about. Tercon's claim is not barred by the exclusion clause because the clause only applies to claims arising "as a result of participating in [the] RFP", not to claims resulting from the participation of other, ineligible parties. Moreover, the words of this exclusion clause, in my view, are not effective to limit liability for breach of the Province's implied duty of fairness to bidders. I will explain my conclusion by turning first to a brief account of the key legal principles and then to the facts of the case.

2. Legal Principles

[64]The key principle of contractual interpretation here is that the words of one provision must not be read in isolation but should be considered in harmony with the rest of the contract and in light of its purposes and commercial context. The approach adopted by the Court in *M.J.B.* is instructive. The Court had to interpret a privilege clause, which is somewhat analogous to the exclusion clause in issue here. The privilege clause provided that the lowest or any tender would not necessarily be accepted, and the issue was whether this barred a claim based on breach of an implied term that the owner would accept only compliant bids. In interpreting the privilege clause, the Court looked at its text in light of the contract as a whole, its purposes and commercial context. As Iacobucci J. said, at para. 44, "the privilege clause is only one term of Contract A and must be read in harmony with the rest of the tender documents. To do otherwise would undermine the rest of the agreement between the parties."

[65]In a similar way, it is necessary in the present case to consider the exclusion clause in the RFP in light of its purposes and commercial context as well as of its overall terms. The question is whether the exclusion of compensation for claims resulting from "participating in this RFP", properly interpreted, excludes liability for the Province having unfairly considered a bid from a bidder who was not supposed to have been participating in the RFP process at all.

3. Application to This Case

[66]Having regard to both the text of the clause in its broader context and to the purposes and commercial context of the RFP, my view is that this claim does not fall within the terms of the exclusion clause.

[67]To begin, it is helpful to recall that in interpreting tendering contracts, the Court has been careful to consider the special commercial context of tendering. Effective tendering ultimately depends on the integrity and business efficacy of the tendering process: see, e.g., *Martel*, at para. 88; *M.J.B.*, at para. 41; *Double N Earthmovers*, at para. 106. As Iacobucci and Major JJ. put it in *Martel*, at para. 116, "it is imperative that all bidders be treated on an equal footing . . . . Parties should at the very least be confident that their initial bids will not be skewed by some underlying advantage in the drafting of the call for tenders conferred upon only one potential bidder."

[68]This factor is particularly weighty in the context of public procurement. In that context, in addition to the interests of the parties, there is the need for transparency for the public at large. This consideration is underlined by the statutory provisions which governed the tendering process in this case. Their purpose was to assure transparency and fairness in public tenders. As was said by Orsborn J. (as he then was) in *Cahill (G.J.) & Co. (1979) Ltd. v. Newfoundland and Labrador (Minister of Municipal and Provincial Affairs)*, 2005 NLTD 129 (CanLII), 250 Nfld. & P.E.I.R. 145, at para. 35:

> The owner — in this case the government — is in control of the tendering process and may define the parameters for a compliant bid and a compliant bidder. The corollary to this, of course, is that once the owner — here the government — sets the rules, it must itself play by those rules in assessing the bids and awarding the main contract.

[69]One aspect that is generally seen as contributing to the integrity and business efficacy of the tendering process is the requirement that only compliant bids be considered. As noted earlier, such a requirement has often been implied because, as the Court said in *M.J.B.*, it makes little sense to think that a bidder would comply with the bidding process if the owner could circumscribe it by accepting a non-compliant bid. Respectfully, it seems to me to make even less sense to think that eligible bidders would participate in the RFP if the Province could avoid liability for ignoring an express term concerning eligibility to bid on which the entire RFP was premised and which was mandated by the statutorily approved process.

[70]The closed list of bidders was the foundation of this RFP and there were important competitive advantages to a bidder who could side-step that limitation. Thus, it seems to me that both the integrity and the business efficacy of the tendering process support an interpretation that would allow the exclusion clause to operate compatibly with the eligibility limitations that were at the very root of the RFP.

[71]The same may be said with respect to the implied duty of fairness. As Iacobucci and Major JJ. wrote for the Court in *Martel*, at para. 88, "[i]mplying an obligation to treat all bidders fairly and equally is consistent with the goal of protecting and promoting the integrity of the bidding process." It seems to me that clear language is necessary to exclude liability for breach of such a basic requirement of the tendering process, particularly in the case of public procurement.

[72]The proper interpretation of the exclusion clause should also take account of the statutory context which I have reviewed earlier. The restriction on

eligibility of bidders was a key element of the alternative process approved by the Minister. It seems unlikely, therefore, that the parties intended through this exclusion clause to effectively gut a key aspect of the approved process. Of course, it is true that the exclusion clause does not bar all remedies, but only claims for compensation. However, the fact remains that as a practical matter, there are unlikely to be other, effective remedies for considering and accepting an ineligible bid and that barring compensation for a breach of that nature in practical terms renders the ministerial approval process virtually meaningless. Whatever administrative law remedies may be available, they are not likely to be effective remedies for awarding a contract to an ineligible bidder. The Province did not submit that injunctive relief would have been an option, and I can, in any event, foresee many practical problems that need not detain us here in seeking such relief in these circumstances.

[73]The Province stresses Tercon's commercial sophistication, in effect arguing that it agreed to the exclusion clause and must accept the consequences. This line of argument, however, has two weaknesses. It assumes the answer to the real question before us which is: what does the exclusion clause mean? The consequences of agreeing to the exclusion clause depend on its construction. In addition, the Province's submission overlooks its own commercial sophistication and the fact that sophisticated parties can draft very clear exclusion and limitation clauses when they are minded to do so. Such clauses contrast starkly with the curious clause which the Province inserted into this RFP. The limitation of liability clause in *Hunter*, for example, provided that "[n]otwithstanding any other provision in this contract or any applicable statutory provisions neither the Seller nor the Buyer shall be liable to the other for special or consequential damages or damages for loss of use arising directly or indirectly from any breach of this contract, fundamental or otherwise" (p. 450). The Court found this to be clear and unambiguous. The limitation clause in issue in *Guarantee Co. of North America v. Gordon Capital Corp.*, 1999 CanLII 664 (SCC), [1999] 3 S.C.R. 423, provided that legal proceedings for the recovery of "any loss hereunder shall not be brought . . . after the expiration of 24 months from the discovery of such loss" (para. 5). Once again, the Court found this language clear. The Ontario Court of Appeal similarly found the language of a limitation of liability clause to be clear in *Fraser Jewellers (1982) Ltd. v. Dominion Electric Protection Co.* (1997), 1997 CanLII 4452 (ON CA), 34 O.R. (3d) 1. The clause provided in part that if the defendant "should be found liable for loss, damage or injury due to a failure of service or equipment in any respect, its liability shall be limited to a sum equal to 100% of the annual service charge or $10,000.00, whichever is less, as the agreed upon damages and not as a penalty, as the exclusive remedy" (p. 4). These, and many other cases which might be referred to, demonstrate that sophisticated parties are capable of drafting clear and comprehensive limitation and exclusion provisions.

[74]I turn to the text of the clause which the Province inserted in its RFP. It addresses claims that result from "participating in this RFP". As noted, the limitation on who could participate in this RFP was one of its premises. These words

must, therefore, be read in light of the limit on who was eligible to participate in this RFP. As noted earlier, both the ministerial approval and the text of the RFP itself were unequivocal: only the six proponents qualified through the earlier RFEI process were eligible and *proposals received from any other party would not be considered.* Thus, central to "participating in this RFP" was participating in a contest among those eligible to participate. A process involving other bidders, as the trial judge found the process followed by the Province to be, is not the process called for by "this RFP" and being part of that other process is not in any meaningful sense "participating in this RFP".

[75]The Province would have us interpret the phrase excluding compensation "as a result of participating in this RFP" to mean that compensation is excluded that results from "submitting a Proposal". However, that interpretation is not consistent with the wording of the clause as a whole. The clause concludes with the phrase that "by submitting a Proposal each Proponent shall be deemed to have agreed that it has no claim". If the phrases "participating in this RFP" and "submitting a Proposal" were intended to mean the same thing, it is hard to understand why different words were used in the same short clause to express the same idea. The fact that the Minister had approved a closed list of participants strengthens the usual inference that the use of different words was deliberate so as not to exclude compensation for a departure from that basic eligibility requirement.

[76]This interpretation of the exclusion clause does not rob it of meaning, but makes it compatible with other provisions of the RFP. There is a parallel between this case and the Court's decision in *M.J.B.* There, the Court found that there was compatibility between the privilege clause and the implied term to accept only compliant bids. Similarly, in this case, there is compatibility between the eligibility requirements of the RFP and the exclusion clause. Not any and every claim based on any and every deviation from the RFP provisions would escape the preclusive effect of the exclusion clause. It is only when the defect in the Province's adherence to the RFP process is such that it is completely outside that process that the exclusion clause cannot have been intended to operate. What is important here, in my view, is that the RFP in its conception, in its express provisions and in the statutorily required approval it was given, was premised on limiting eligibility to the six proponents in the RFEI process. Competition among others was not at all contemplated and was not part of the RFP process; in fact, the RFP expressly excluded that possibility. In short, limiting eligibility of bidders to those who had responded to the RFEI was the foundation of the whole RFP. As the judge found, acceptance of a bid from an ineligible bidder "attacks the underlying premise of the process" established by the RFP: para. 146. Liability for such an attack is not excluded by a clause limiting compensation resulting from participation in this RFP.

[77]This interpretation is also supported by another provision of the RFP. Under s. 2.9, as mentioned earlier, the Province reserved to itself the right to unilaterally cancel the RFP and the right to propose a new RFP allowing additional bidders. If the exclusion clause were broad enough to exclude compensation for allowing ineligible bidders to participate, there seems to be little purpose in this reservation of the ability to cancel the RFP and issue a new one to a wider circle of bidders. It is also significant that the Province did not reserve to itself the right to accept a bid from an ineligible bidder or to unilaterally change the rules of eligibility. The RFP expressly did exactly the opposite. None of this, in my opinion, supports the view that the exclusion clause should be read as applying to the Province's conduct in this case.

[78]To hold otherwise seems to me to be inconsistent with the text of the clause read in the context of the RFP as a whole and in light of its purposes and commercial context. In short, I cannot accept the contention that, by agreeing to exclude compensation for participating in this RFP process, the parties could have intended to exclude a damages claim resulting from the Province unfairly permitting a bidder to participate who was not eligible to do so. I cannot conclude that the provision was intended to gut the RFP's eligibility requirements as to who may participate in it, or to render meaningless the Minister's statutorily required approval of the alternative process where this was a key element. The provision, as well, was not intended to allow the Province to escape a damages claim for applying different eligibility criteria, to the competitive disadvantage of other bidders and for taking steps designed to disguise the true state of affairs. I cannot conclude that the parties, through the words found in this exclusion clause, intended to waive compensation for conduct like that of the Province in this case that strikes at the heart of the integrity and business efficacy of the tendering process which it undertook.

[79]If I am wrong about my interpretation of the clause, I would hold, as did the trial judge, that its language is at least ambiguous. If, as the Province contends, the phrase "participating in this RFP" could reasonably mean "submitting a Proposal", that phrase could also reasonably mean "competing against the other eligible participants". Any ambiguity in the context of this contract requires that the clause be interpreted against the Province and in favour of Tercon under the principle *contra proferentem*: see, e.g., *Hillis Oil and Sales Ltd. v. Wynn's Canada, Ltd.*, 1986 CanLII 44 (SCC), [1986] 1 S.C.R. 57, at pp. 68-69. Following this approach, the clause would not apply to bar Tercon's damages claim.

V. Disposition

[80]I conclude that the judge did not err in finding that the Province breached the tendering contract or in finding that Tercon's remedy in damages for

that breach was not precluded by the exclusion clause in the contract. I would therefore allow the appeal, set aside the order of the Court of Appeal and restore the judgment of the trial judge. The parties advise that the question of costs has been resolved between them and that therefore no order in relation to costs is required.

The reasons of McLachlin C.J. and Binnie, Abella and Rothstein JJ. were delivered by

[81]BINNIE J. (dissenting) — The important legal issue raised by this appeal is whether, and in what circumstances, a court will deny a defendant contract breaker the benefit of an exclusion of liability clause to which the innocent party, not being under any sort of disability, has agreed. Traditionally, this has involved consideration of what is known as the doctrine of fundamental breach, a doctrine which Dickson C.J. in *Hunter Engineering Co. v. Syncrude Canada Ltd.*, 1989 CanLII 129 (SCC), [1989] 1 S.C.R. 426, suggested should be laid to rest 21 years ago (p. 462).

[82]On this occasion we should again attempt to shut the coffin on the jargon associated with "fundamental breach". Categorizing a contract breach as "fundamental" or "immense" or "colossal" is not particularly helpful. Rather, the principle is that a court has no discretion to refuse to enforce a valid and applicable contractual exclusion clause unless the plaintiff (here the appellant Tercon) can point to some paramount consideration of public policy sufficient to override the public interest in freedom of contact and defeat what would otherwise be the contractual rights of the parties. Tercon points to the public interest in the transparency and integrity of the government tendering process (in this case, for a highway construction contract) but in my view such a concern, while important, did not render unenforceable the terms of the contract Tercon agreed to. There is nothing inherently unreasonable about exclusion clauses. Tercon is a large and sophisticated corporation. Unlike my colleague Justice Cromwell, I would hold that the respondent Ministry's conduct, while in breach of its contractual obligations, fell within the terms of the exclusion clause. In turn, there is no reason why the clause should not be enforced. I would dismiss the appeal.

I. Overview

[83]This appeal concerns a contract to build a $35 million road in the remote Nass Valley of British Columbia (the "Kincolith project"). The respondent Ministry accepted a bid from Brentwood Enterprises Ltd. that did not comply with the terms of tender. Tercon, as the disappointed finalist in the bidding battle, seeks compensation equivalent to the profit it expected to earn had it been awarded the contract.

[84]Tercon alleged, and the trial judge found, that although the winning bid was submitted in the name of Brentwood (an eligible bidder), Brentwood in fact intended, with the Ministry's knowledge and encouragement, to do the work in a co-venture with an ineligible bidder, Emil Anderson Construction Co. ("EAC"). The respondent Ministry raised a number of defences including the fact that the formal contract was signed in the name of Brentwood alone. This defence was rejected in the courts below. The Ministry's substantial defence in this Court is that even if it failed to abide by the bidding rules, it is nonetheless protected by an exclusion of compensation clause set out clearly in the request for proposals ("RFP"). The clause provided that "no Proponent shall have any claim for compensation of any kind whatsoever, as a result of participating in this RFP" and that "by submitting a Proposal each Proponent shall be deemed to have agreed that it has no claim" (s. 2.10 of the RFP).

[85]The appeal thus brings into conflict the public policy that favours a fair, open and transparent bid process, and the freedom of contract of sophisticated and experienced parties in a commercial environment to craft their own contractual relations. I agree with Tercon that the public interest favours an orderly and fair scheme for tendering in the construction industry, but there is also a public interest in leaving knowledgeable parties free to order their own commercial affairs. In my view, on the facts of this case, the Court should not rewrite — nor should the Court refuse to give effect to — the terms agreed to by the parties.

[86]I accept, as did the courts below, that the respondent Ministry breached the terms of its own RFP when it contracted with Brentwood, knowing the work would be carried out by a co-venture with Brentwood and EAC. The addition of EAC, a bigger contractor with greater financial resources than Brentwood, created a stronger competitor for Tercon than Brentwood alone. However, I also agree with the B.C. Court of Appeal that the exclusion of compensation clause is clear and unambiguous and that no legal ground or rule of law permits us to override the freedom of the parties to contract (or to decline to contract) with respect to this particular term, or to relieve Tercon against its operation in this case.

II. The Tendering Process

[87]For almost three decades, the law governing a structured bidding process has been dominated by the concept of Contract A/Contract B initially formulated in *The Queen in right of Ontario v. Ron Engineering & Construction (Eastern) Ltd.*, 1981 CanLII 17 (SCC), [1981] 1 S.C.R. 111. The analysis advanced by Estey J. in that case was that the bidding process, as defined by the terms of the

tender call, may create contractual relations ("Contract A") prior in time and quite independently of the contract that is the actual subject matter of the bid ("Contract B"). Breach of Contract A may, depending on its terms, give rise to contractual remedies for non-performance even if Contract B is never entered into or, as in the present case, it is awarded to a competitor. The result of this legal construct is to provide unsuccessful bidders with a *contractual* remedy against an owner who departs from its own bidding rules. Contract A, however, arises (if at all) as a matter of interpretation. It is not imposed as a rule of law.

[88]In *Ron Engineering*, the result of Estey J.'s analysis was that as a matter of contractual interpretation, the Ontario government was allowed to retain a $150,000 bid bond put up by Ron Engineering even though the government was told, a little over an hour after the bids were opened, that Ron Engineering had made a $750,058 error in the calculation of its bid and wished to withdraw it. Estey J. held:

> The contractor was not asked to sign a contract which diverged in any way from its tender but simply to sign a contract in accordance with the instructions to tenderers and in conformity with its own tender. [p. 127]

In other words, harsh as it may have seemed to Ron Engineering, the parties were held to their bargain. The Court was not prepared to substitute "fair and reasonable" terms for what the parties had actually agreed to.

[89]In *M.J.B. Enterprises Ltd. v. Defence Construction (1951) Ltd.*, 1999 CanLII 677 (SCC), [1999] 1 S.C.R. 619, Contract A included a "privilege" clause which stated that the owner was not obliged to accept the lowest or *any* tender. The Court implied a term, based on the presumed intention of the parties, that notwithstanding the privilege clause, only compliant bids were open to acceptance. While the owner was not obliged to accept the lowest compliant bid, the privilege clause did not, as a matter of contractual interpretation, give the owner "the privilege" of accepting a non-compliant bid. *M.J.B.* stops short of the issue in the present appeal because in that case, there was a breach of Contract A but no clause purporting to exclude liability on the part of the owner to pay compensation in the event of a Contract A violation.

[90]In *Naylor Group Inc. v. Ellis-Don Construction Ltd.*, 2001 SCC 58 (CanLII), [2001] 2 S.C.R. 943, the Court enforced the rules of the bid depository system against a contractor whose bid was based on what turned out to be a mistaken view of its collective bargaining status with the International Brotherhood of Electrical Workers. The Court again affirmed that "[t]he existence and content of Contract A will depend on the facts of the particular case" (para. 36). Ellis-Don sought relief from its bid on the basis of a labour board decision rendered subsequent

to its bid that upheld, to its surprise, the bargaining rights of the union. This Court held that no relief was contemplated in the circumstances under Contract A and none was afforded, even though this was a costly result when viewed from the perspective of Ellis-Don.

[91]In *Martel Building Ltd. v. Canada*, 2000 SCC 60 (CanLII), [2000] 2 S.C.R. 860, citing *M.J.B.*, the Court implied a term in Contract A obligating the owner to be fair and consistent in the assessment of tender bids. On the facts, the disappointed bidder's claim of unfair treatment was rejected.

[92] Finally, in *Double N Earthmovers Ltd. v. Edmonton (City)*, 2007 SCC 3 (CanLII), [2007] 1 S.C.R. 116, the unsuccessful bidder claimed that Edmonton had accepted, in breach of Contract A, a competitor's non-compliant bid to provide heavy equipment of a certain age to move refuse at a waste disposal site. The Court refused to imply a term "requiring an owner to investigate to see if bidders will really do what they promised in their tender" (para. 50). Accepting the existence of a duty of "fairness and equality", the majority nevertheless held that "[t]he best way to make sure that all bids receive the same treatment is for an owner to weigh bids on the basis of what is actually in the bid, not to weigh them on the basis of subsequently discovered information" (para. 52). In other words, the majority's interpretation of the express terms of Contract A was enforced despite Double N Earthmovers' complaint of double dealing by the owner.

[93]On the whole, therefore, while *Ron Engineering* and its progeny have encouraged the establishment of a fair and transparent bidding process, Contract A continues to be based not on some abstract externally imposed rule of law but on the presumed (and occasionally implied) intent of the parties. Only in rare circumstances will the Court relieve a party from the bargain it has made.

[94]As to implied terms, *M.J.B.* emphasized (at para. 29) that the focus is "the intentions of the actual parties". A court, when dealing with a claim to an implied term, "must be careful not to slide into determining the intentions of reasonable parties" (emphasis in original). Thus, "if there is evidence of a contrary intention, on the part of either party, an implied term may not be found on this basis".

[95]Tercon is a large and experienced contractor. As noted by Donald J.A. in the B.C. Court of Appeal, it had earlier "successfully recovered damages from the [Ministry] on a bidding default in a previous case" (2007 BCCA 592 (CanLII), 73 B.C.L.R. (4th) 201, at para. 15). See *Tercon Contractors Ltd. v. British Columbia*

(1993), 9 C.L.R. (2d) 197 (B.C.S.C.), aff'd [1994] B.C.J. No. 2658 (QL) (C.A.). Thus Tercon would have been more sensitive than most contractors to the risks posed by an exclusion of compensation clause. It nevertheless chose to bid on the project on the terms proposed by the Ministry.

III. Tercon's Claim for Relief From the Exclusionary Clause It Agreed to

[96]In these circumstances, the first question is whether there is either a statutory legal obstacle to, or a principled legal argument against, the freedom of these parties to contract out of the obligation that would otherwise exist for the Ministry to pay compensation for a breach of Contract A. If not, the second question is whether there is any other barrier to the court's enforcement of the exclusionary clause in the circumstances that occurred. On the first branch, Tercon relies on the *Ministry of Transportation and Highways Act*, R.S.B.C. 1996, c. 311 ("*Transportation Act*" or the "Act"). On the second branch, Tercon relies on the doctrine of fundamental breach.

A. *The Statutory Argument*

[97]Section 4 of the *Transportation Act* provides that before awarding a highway contract, "the minister must invite tenders in any manner that will make the invitation for tenders reasonably available to the public", but then provides for several exceptions: "The minister need not invite tenders for a project . . . if . . . (c) the minister believes that an alternative contracting process will result in a competitively established cost for the project". Here the required ministerial authorization was obtained for an "alternative process". The reason is as follows. As noted by Cromwell J., the Ministry's original idea was to use a "design-build" model where a single contractor would design and build the highway for a fixed price. The Ministry issued a request for expressions of interest ("RFEI") which attracted six responses. One was from Tercon. Another was from Brentwood. EAC declined to bid because it did not think the "design-build" concept was appropriate for the job.

[98]On further reflection, the Ministry decided not to pursue the design-build approach. It decided to design the highway itself. The contract would be limited to construction, as EAC had earlier advocated. EAC was not allowed to bid despite the Ministry coming around to its point of view on the proper way to tender the project. The Ministry limited bidding on the new contest to the six respondents to the original RFEI, all of whom had been found capable of performing the contract. But to do so, it needed, and did obtain, the Minister's s. 4 approval.

[99]A question arose during the hearing of the appeal as to whether the Minister actually approved an "alternative process" that not only restricted eligibility to the six participants in the RFEI process (an advantage to Tercon and the other five participants), but also contained the "no claims" clause excluding compensation for non-observance of its terms (no doubt considered a disadvantage). In its factum, the Ministry states:

> In this case, the Minister approved an alternate process under [s. 4(2) of the B.C. *Transportation Act*]. That process was set out in the Instructions to Proponents, which included the No Claim Clause. Having been approved by the Minister, the package (including the No Claim Clause) complied with section 4 of the *Transportation Act*. [para. 70]

[100] Tercon argued at the hearing of this appeal that as a matter of *law*, Contract A could not have included the exclusion clause because

> [t]he policy of the [*Transportation Act*] is to ensure that the Ministry is accountable; to preserve confidence in the integrity of the tendering process. To ensure that is so and that the Minister is accountable, the Ministry must be held liable for its breach of Contract A in considering and accepting a proposal from the joint venture . . . .
>
> . . .
>
> **MADAM JUSTICE ABELLA:** Can I just ask you one question. Is it your position, sir, that you can never have -- that a government can never have a no claims clause?
>
> **MR. McLEAN:** Yes. Under this statute because of the policy of the statute. [Transcript, at p. 27]

[101] While it is true that the Act favours "the integrity of the tendering process", it nowhere prohibits the parties from negotiating a "no claims" clause as part of their commercial agreement, and cannot plausibly be interpreted to have that effect.

[102] In the ordinary world of commerce, as Dickson C.J. commented in *Hunter*, "clauses limiting or excluding liability are negotiated as part of the general contract. As they do with all other contractual terms, the parties bargain for the consequences of deficient performance" (p. 461). Moreover, as Mr. Hall points out, "[t]here are many valid reasons for contracting parties to use exemption clauses, most notably to allocate risks" (G. R. Hall, *Canadian Contractual Interpretation Law* (2007), at p. 243). Tercon, for example, is a sophisticated and experienced contractor and if it decided that it was in its commercial interest to proceed with the bid despite

the exclusion of compensation clause, that was its prerogative and nothing in the "policy of the Act" barred the parties' agreement on that point.

[103] To the extent Tercon is now saying that as a matter of *fact* the Minister, in approving the RFP, did not specifically approve the exclusion clause, and that the contract was thus somehow *ultra vires* the Ministry, this is not an issue that was either pleaded or dealt with in the courts below. The details of the ministerial approval process were not developed in the evidence. It is not at all evident that s. 4 *required* the Minister to approve the actual terms of the RFP. It is an administrative law point that Tercon, if so advised, ought to have pursued at pre-trial discovery and in the trial evidence. We have not been directed to any exploration of the matter in the testimony and it is too late in the proceeding for Tercon to explore it now. Accordingly, I proceed on the basis that the exclusion clause did not run afoul of the statutory requirements.

B. *The Doctrine of the Fundamental Breach*

[104] The trial judge considered the applicability of the doctrine of fundamental breach. Tercon argued that the Ministry, by reason of its fundamental breach, had forfeited the protection of the exclusion of compensation clause.

[105] The leading case is *Hunter* which also dealt with an exclusion of liability clause. The appellants Hunter Engineering and Allis-Chalmers Canada Ltd. supplied gearboxes used to drive conveyor belts at Syncrude's tar sands operations in Northern Alberta. The gearboxes proved to be defective. At issue was a broad exclusion of warranty clause that limited time for suit and the level of recovery available against Allis-Chalmers (i.e. no recovery beyond the unit price of the defective products). Dickson C.J. observed: "In the face of the contractual provisions, Allis-Chalmers can only be found liable under the doctrine of fundamental breach" (p. 451).

[106] This doctrine was largely the creation of Lord Denning in the 1950s (see, e.g., *Karsales (Harrow) Ltd. v. Wallis*, [1956] 1 W.L.R. 936 (C.A.)). It was said to be a rule of law that operated independently of the intention of the parties in circumstances where the defendant had so egregiously breached the contract as to deny the plaintiff substantially the whole of its benefit. In such a case, according to the doctrine, the innocent party was excused from further performance but the defendant could still be held liable for the consequences of its "fundamental" breach even if the parties had excluded liability by clear and express language. See generally

S. M. Waddams, *The Law of Contracts* (5th ed. 2005), at para. 478; J. D. McCamus, *The Law of Contracts* (2005), at pp. 765 *et seq.*

[107] The five-judge *Hunter* Court was unanimous in the result and gave effect to the exclusion clause at issue. Dickson C.J. and Wilson J. both emphasized that there is nothing inherently unreasonable about exclusion clauses and that they should be applied unless there is a compelling reason not to give effect to the words selected by the parties. At that point, there was some divergence of opinion.

[108] Dickson C.J. (La Forest J. concurring) observed that the doctrine of fundamental breach had "spawned a host of difficulties" (p. 460), the most obvious being the difficulty in determining whether a particular breach is fundamental. The doctrine obliged the parties to engage in "games of characterization" (p. 460) which distracted from the real question of what agreement the parties themselves intended. Accordingly, in his view, the doctrine should be "laid to rest". The situations in which the doctrine is invoked could be addressed more directly and effectively through the doctrine of "unconscionability", as assessed at the time the contract was made:

> It is preferable to interpret the terms of the contract, in an attempt to determine exactly what the parties agreed. If on its true construction the contract excludes liability for the kind of breach that occurred, the party in breach will generally be saved from liability. Only where the contract is unconscionable, as might arise from situations of unequal bargaining power between the parties, should the courts interfere with agreements the parties have freely concluded. [p. 462]

Dickson C.J. explained that "[t]he courts do not blindly enforce harsh or unconscionable bargains" (p. 462), but "there is much to be gained by addressing directly the protection of the weak from over-reaching by the strong, rather than relying on the artificial legal doctrine of 'fundamental breach'" (p. 462). To enforce an exclusion clause in such circumstances could tarnish the institutional integrity of the court. In that respect, it would be contrary to public policy. However, a *valid* exclusion clause would be enforced according to its terms.

[109] Wilson J. (L'Heureux-Dubé J. concurring) disagreed. In her view, the courts retain some residual discretion to refuse to enforce exclusion clauses in cases of fundamental breach where the doctrine of *pre*-breach unconscionability (favoured by Dickson C.J.) did not apply. Importantly, she rejected the imposition of a general standard of reasonableness in the judicial scrutiny of exclusion clauses, affirming that "the courts . . . are quite unsuited to assess the fairness or reasonableness of contractual provisions as the parties negotiated them" (p. 508).

Wilson J. considered it more desirable to develop through the common law a *post*-breach analysis seeking a "balance between the obvious desirability of allowing the parties to make their own bargains . . . and the obvious undesirability of having the courts used to enforce bargains in favour of parties who are totally repudiating such bargains themselves" (p. 510).

[110] Wilson J. contemplated a two-stage test, in which the threshold step is the identification of a fundamental breach where "the foundation of the contract has been undermined, where the very thing bargained for has not been provided" (p. 500). Having found a fundamental breach to exist, the exclusion clause would *not* automatically be set aside, but the court should go on to assess whether, having regard to the circumstances of the breach, the party in fundamental breach should escape liability:

> Exclusion clauses do not automatically lose their validity in the event of a fundamental breach by virtue of some hard and fast rule of law. They should be given their natural and true construction so that the meaning and effect of the exclusion clause the parties agreed to at the time the contract was entered into is fully understood and appreciated. But, in my view, the court must still decide, having ascertained the parties' intention at the time the contract was made, whether or not to give effect to it in the context of subsequent events such as a fundamental breach committed by the party seeking its enforcement through the courts. . . . [T]he question essentially is: in the circumstances that have happened should the court lend its aid to A to hold B to this clause? [Emphasis added; pp. 510-11.]

[111] Wilson J. reiterated that "as a general rule" courts should give effect to exclusion clauses *even in the case of fundamental breach* (p. 515). Nevertheless, a residual discretion to withhold enforcement exists:

> Lord Wilberforce [in *Photo Production Ltd. v. Securicor Transport Ltd.*, [1980] A.C. 827 (H.L.)] may be right that parties of equal bargaining power should be left to live with their bargains regardless of subsequent events. I believe, however, that there is some virtue in a residual power residing in the court to withhold its assistance on policy grounds in appropriate circumstances. [Emphasis added; p. 517.]

Wilson J. made it clear that such circumstances of disentitlement would be rare. She acknowledged that an exclusion clause might well be accepted with open eyes by a party "very anxious to get" the contract (p. 509). However, Wilson J. did not elaborate further on what such circumstances might be because she found in *Hunter* itself that no reason existed to refuse the defendant Allis-Chalmers the benefit of the exclusion clause.

[112] The fifth judge, McIntyre J., in a crisp two-paragraph judgment, agreed with the conclusion of Wilson J. in respect of the exclusion clause issue but found it "unnecessary to deal further with the concept of fundamental breach in this case" (p. 481).

[113] The law was left in this seemingly bifurcated state until *Guarantee Co. of North America v. Gordon Capital Corp.*, 1999 CanLII 664 (SCC), [1999] 3 S.C.R. 423. In that case, the Court breathed some life into the dying doctrine of fundamental breach while nevertheless affirming (once again) that whether or not a "fundamental breach prevents the breaching party from continuing to rely on an exclusion clause is a matter of construction rather than a rule of law" (para. 52). In other words, the question was whether the parties *intended* at the time of contract formation that the exclusion or limitation clause would apply "in circumstances of contractual breach, whether fundamental or otherwise" (para. 63). The Court thus emphasized that what was important was not the label ("fundamental or otherwise") but the intent of the contracting parties when they made their bargain. "The only limitation placed upon enforcing the contract as written in the event of a fundamental breach", the Court in *Guarantee Co.* continued,

> would be to refuse to enforce an exclusion of liability in circumstances where to do so would be unconscionable, according to Dickson C.J., or [note the disjunctive "or"] unfair, unreasonable or otherwise contrary to public policy, according to Wilson J. [Emphasis added; para. 52.]
>
> (See also para. 64.)

What has given rise to some concern is not the reference to "public policy", whose role in the enforcement of contracts has never been doubted, but to the more general ideas of "unfair" and "unreasonable", which seemingly confer on courts a very broad after-the-fact discretion.

[114] The Court's subsequent observations in *ABB Inc. v. Domtar Inc.*, 2007 SCC 50 (CanLII), [2007] 3 S.C.R. 461, should be seen in that light. *Domtar* was a products liability case arising under the civil law of Quebec, but the Court observed with respect to the common law:

> Once the existence of a fundamental breach has been established, the court must still analyse the limitation of liability clause in light of the general rules of contract interpretation. If the words can reasonably be interpreted in only one way, it will not be open to the court, even on grounds of equity or reasonableness, to declare the clause to be unenforceable since this would amount to rewriting the contract negotiated by the parties. [Emphasis added; para. 84.]

While the *Domtar* Court continued to refer to "fundamental breach", it notably repudiated any judicial discretion to depart from the terms of a valid contact upon vague notions of "equity or reasonableness". It did not, however, express any doubt about the residual category mentioned in *Guarantee Co.*, namely a refusal to enforce an exclusion clause on the grounds of public policy.

[115] I agree with Professor Waddams when he writes:

> [I]t is surely inevitable that a court must reserve the ultimate power to decide when the values favouring enforceability are outweighed by values that society holds to be more important. [para. 557]

[116] While memorably described as an unruly horse, public policy is nevertheless fundamental to contract law, both to contractual formation and enforcement and (occasionally) to the court's relief *against* enforcement. As Duff C.J. observed:

> It is the duty of the courts to give effect to contracts and testamentary dispositions according to the settled rules and principles of law, since we are under a reign of law; but there are cases in which rules of law cannot have their normal operation because the law itself recognizes some paramount consideration of public policy which over-rides the interest and what otherwise would be the rights and powers of the individual.
>
> (*Re Millar Estate*, 1937 CanLII 10 (SCC), [1938] S.C.R. 1, at p. 4)

See generally B. Kain and D. T. Yoshida, "The Doctrine of Public Policy in Canadian Contract Law", in T. L. Archibald and R. S. Echlin, eds., *Annual Review of Civil Litigation, 2007* (2007), 1.

[117] As Duff C.J. recognized, freedom of contract will often, but not always, trump other societal values. The residual power of a court to decline enforcement exists but, in the interest of certainty and stability of contractual relations, it will rarely be exercised. Duff C.J. adopted the view that public policy "should be invoked only in clear cases, in which the harm to the public is substantially incontestable, and does not depend upon the idiosyncratic inferences of a few judicial minds" (p. 7). While he was referring to public policy considerations pertaining to the nature of the *entire contract*, I accept that there may be well-accepted public policy considerations that relate directly to the nature of the *breach*, and thus trigger the court's narrow jurisdiction to give relief against an exclusion clause.

[118] There are cases where the exercise of what Professor Waddams calls the "ultimate power" to refuse to enforce a contract may be justified, even in the commercial context. Freedom of contract, like any freedom, may be abused. Take the case of the milk supplier who adulterates its baby formula with a toxic compound to increase its profitability at the cost of sick or dead babies. In China, such people were shot. In Canada, should the courts give effect to a contractual clause excluding civil liability in such a situation? I do not think so. Then there are the people, also fortunately resident elsewhere, who recklessly sold toxic cooking oil to unsuspecting consumers, creating a public health crisis of enormous magnitude. Should the courts enforce an exclusion clause to eliminate contractual liability for the resulting losses in such circumstances? The answer is no, but the contract breaker's conduct need not rise to the level of criminality or fraud to justify a finding of abuse.

[119] A less extreme example in the commercial context is *Plas-Tex Canada Ltd. v. Dow Chemical of Canada Ltd.*, 2004 ABCA 309 (CanLII), 245 D.L.R. (4th) 650. The Alberta Court of Appeal refused to enforce an exclusion clause where the defendant Dow knowingly supplied defective plastic resin to a customer who used it to fabricate natural gas pipelines. Instead of disclosing its prior knowledge of the defect to the buyer, Dow chose to try to protect itself by relying upon limitation of liability clauses in its sales contracts. After some years, the pipelines began to degrade, with considerable damage to property and risk to human health from leaks and explosions. The court concluded that "a party to a contract will not be permitted to engage in unconscionable conduct secure in the knowledge that no liability can be imposed upon it because of an exclusionary clause" (para. 53). (See also McCamus, at p. 774, and Hall, at p. 243.) What was demonstrated in *Plas-Tex* was that the defendant Dow was so contemptuous of its contractual obligation and reckless as to the consequences of the breach as to forfeit the assistance of the court. The public policy that favours freedom of contract was outweighed by the public policy that seeks to curb its abuse.

[120] Conduct approaching serious criminality or egregious fraud are but examples of well-accepted and "substantially incontestable" considerations of public policy that may override the countervailing public policy that favours freedom of contract. Where this type of misconduct is reflected in the breach of contract, all of the circumstances should be examined very carefully by the court. Such misconduct may disable the defendant from hiding behind the exclusion clause. But a plaintiff who seeks to avoid the effect of an exclusion clause must identify the overriding public policy that it says outweighs the public interest in the enforcement of the contract. In the present case, for the reasons discussed below, I do not believe Tercon has identified a relevant public policy that fulfills this requirement.

[121] The present state of the law, in summary, requires a series of enquiries to be addressed when a plaintiff seeks to escape the effect of an exclusion clause or other contractual terms to which it had previously agreed.

[122] The first issue, of course, is whether as a matter of interpretation the exclusion clause even *applies* to the circumstances established in evidence. This will depend on the Court's assessment of the intention of the parties as expressed in the contract. If the exclusion clause does not apply, there is obviously no need to proceed further with this analysis. If the exclusion clause applies, the second issue is whether the exclusion clause was unconscionable at the time the contract was made, "as might arise from situations of unequal bargaining power between the parties" (*Hunter*, at p. 462). This second issue has to do with contract formation, not breach.

[123] If the exclusion clause is held to be valid and applicable, the Court may undertake a third enquiry, namely whether the Court should nevertheless refuse to enforce the valid exclusion clause because of the existence of an overriding public policy, proof of which lies on the party seeking to avoid enforcement of the clause, that outweighs the very strong public interest in the enforcement of contracts.

IV. Application to the Facts of This Case

[124] I proceed to deal with the issues in the sequence mentioned above.

A. *Did the Ministry Breach Contract A?*

[125] The trial judge found that the parties intended to create contractual relations at the bidding stage (i.e. Contract A): 2006 BCSC 499 (CanLII), 53 B.C.L.R. (4th) 138, at para. 88. I agree with that conclusion. If there were no intent to form Contract A, there would be no need to exclude liability for compensation in the event of its breach.

[126] The Ministry argued that Contract A was not breached. It was entitled to enter into Contract B with Brentwood and it did so. There was no privity between the Ministry and EAC. The Ministry would have had no direct claim against EAC in the event of deficient performance. I accept as correct that Brentwood, having obtained Contract B, was in a position of considerable flexibility as to how and with whom it carried out the work. Nevertheless, it was open to the trial judge to conclude,

as she did, that the RFP process was not conducted by the Ministry with the degree of fairness and transparency that the terms of Contract A entitled Tercon to expect. At the end of an unfair process, she found, Contract B was not awarded to Brentwood (the eligible bidder) but to what amounted to a joint venture consisting of Brentwood and EAC. I therefore proceed with the rest of the analysis on the basis that Contract A was breached.

B. *What Is the Proper Interpretation of the Exclusion of Compensation Clause and Did the Ministry's Conduct Fall Within Its Terms?*

[127] It is at this stage that I part company with my colleague Cromwell J. The exclusion clause is contained in the RFP and provides as follows:

> **2.10** . . .
>
> Except as expressly and specifically permitted in these Instructions to Proponents, no Proponent shall have any claim for compensation of any kind whatsoever, as a result of participating in this RFP, and by submitting a Proposal each Proponent shall be deemed to have agreed that it has no claim.

In my view, "participating in this RFP" began with "submitting a Proposal" for consideration. The RFP process consisted of more than the final selection of the winning bid and Tercon participated in it. Tercon's bid *was* considered. To deny that such participation occurred on the ground that in the end the Ministry chose a Brentwood joint venture (ineligible) instead of Brentwood itself (eligible) would, I believe, take the Court up the dead end identified by Wilson J. in *Hunter*:

> . . . exclusion clauses, like all contractual provisions, should be given their natural and true construction. Great uncertainty and needless complications in the drafting of contracts will obviously result if courts give exclusion clauses strained and artificial interpretations in order, indirectly and obliquely, to avoid the impact of what seems to them *ex post facto* to have been an unfair and unreasonable clause. [p. 509]

Professor McCamus expresses a similar thought:

> . . . the law concerning exculpatory clauses is likely to be more rather than less predictable if the underlying concern is openly recognized, as it is in *Hunter*, rather than suppressed and achieved indirectly through the subterfuge of strained interpretation of such terms. [p. 778]

[128] I accept the trial judge's view that the Ministry was at fault in its performance of the RFP, but the conclusion that the process thereby ceased to be the RFP process appears to me, with due respect to colleagues of a different view, to

be a "strained and artificial interpretatio[n] in order, indirectly and obliquely, to avoid the impact of what seems to them *ex post facto* to have been an unfair and unreasonable clause".

[129] As a matter of interpretation, I agree with Donald J.A. speaking for the unanimous court below:

> The [trial] judge said the word "participating" was ambiguous. With deference, I do not find it so. The sense it conveys is the contractor's involvement in the RFP/contract A stage of the process. I fail to see how "participating" could bear any other meaning. [Emphasis added; para. 16.]

Accordingly, I conclude that on the face of it, the exclusion clause applies to the facts described in the evidence before us.

C. *Was the Claim Excluding Compensation Unconscionable at the Time Contract A Was Made?*

[130] At this point, the focus turns to contract formation. Tercon advances two arguments: firstly, that it suffered from an inequality of bargaining power and secondly, (as mentioned) that the exclusion clause violates public policy as reflected in the *Transportation Act*.

(1) Unequal Bargaining Power

[131] In *Hunter*, Dickson C.J. stated, at p. 462: "Only where the contract is unconscionable, as might arise from situations of unequal bargaining power between the parties, should the courts interfere with agreements the parties have freely concluded." Applying that test to the case before him, he concluded:

> I have no doubt that unconscionability is not an issue in this case. Both Allis-Chalmers and Syncrude are large and commercially sophisticated companies. Both parties knew or should have known what they were doing and what they had bargained for when they entered into the contract. [p. 464]

While Tercon is not on the same level of power and authority as the Ministry, Tercon is a major contractor and is well able to look after itself in a commercial context. It need not bid if it doesn't like what is proposed. There was no relevant imbalance in bargaining power.

(2) Policy of the *Transportation Act*

[132] As mentioned earlier, Tercon cites and relies upon the policy of the Act which undoubtedly favours the transparency and integrity of the bidding process. I have already discussed my reasons for rejecting Tercon's argument that this "policy" operates as a bar to the ability of the parties to agree on such commonplace commercial terms as in the circumstances they think appropriate. In addition, the exclusion clause is not as draconian as Tercon portrays it. Other remedies for breach of Contract A (specific performance or injunctive relief, for example) were available.

[133] In this case, injunction relief *was* in fact a live possibility. Although Tercon was not briefed on the negotiations with other bidders, the trial judge found that Glenn Walsh, the owner of Tercon, "had seen representatives of EAC with Brentwood following [the Brentwood/EAC interviews with the Ministry and Bill Swain of Brentwood]", and when asked whether Tercon was going to sue, Walsh had said "no" without further comment. Had Tercon pushed for more information and sought an injunction (as a matter of private law, not public law), at that stage the exclusion clause would have had no application, but Tercon did not do so. This is not to say that estoppel or waiver applies. Nor is it to say that injunctive relief would be readily available in many bidding situations (although if an injunction had been sought here, the unavailability of the alternative remedy of monetary damages might have assisted Tercon). It is merely to say that the exclusion clause is partial, not exhaustive.

[134] The Kincolith road project presented a serious construction challenge on a tight time frame and within a tight budget. Contract A did not involve a bid for a fixed price contract but for the right to negotiate the bid details once the winning proponent was selected. In such a fluid situation, *all* participants could expect difficulties in the contracting process. Members of the construction bar are nothing if not litigious. In the circumstances, the bidders might reasonably have accepted (however reluctantly) the Ministry's need for a bidding process that excluded compensation, and adjusted their bids accordingly. The taxpayers of British Columbia were not prepared to pay the contractor's profit twice over — once to Brentwood/EAC for actually building the road, and now to Tercon, even though in Tercon's case the "profit" would be gained without Tercon running the risks associated with the performance of Contract B. The Court should not be quick to declare such a clause, negotiated between savvy participants in the construction business, to be "contrary to the Act".

D. *Assuming the Validity of the Exclusion Clause at the Time the Contract Was Made, Is There Any Overriding Public Policy That Would Justify the Court's Refusal to Enforce It?*

[135] If the exclusion clause is not invalid from the outset, I do not believe the Ministry's performance can be characterized as so aberrant as to forfeit the protection of the contractual exclusion clause on the basis of some overriding public policy. While there is a public interest in a fair and transparent tendering process, it cannot be ratcheted up to defeat the enforcement of Contract A in this case. There *was* an RFP process and Tercon participated in it.

[136] Assertions of ineligible bidders and ineligible bids are the bread and butter of construction litigation. If a claim to defeat the exclusion clause succeeds here on the basis that the owner selected a joint venture consisting of an eligible bidder with an ineligible bidder, so also by a parity of reasoning should an exclusion clause be set aside if the owner accepted a bid ineligible on other grounds. There would be little room left for the exclusion clause to operate. A more sensible and realistic view is that the parties here expected, even if they didn't like it, that the exclusion of compensation clause would operate even where the eligibility criteria in respect of the bid (including the bidder) were not complied with.

[137] While the Ministry's conduct was in breach of Contract A, that conduct was not so extreme as to engage some overriding and paramount public interest in curbing contractual abuse as in the *Plas-Tex* case. Brentwood was not an outsider to the RFP process. It was a legitimate competitor. All bidders knew that the road contract (i.e. Contract B) would not be performed by the proponent alone. The work required a large "team" of different trades and personnel to perform. The issue was whether EAC would be on the job as a major sub-contractor (to which Tercon could not have objected) or identified with Brentwood as a joint venture "proponent" with EAC. All bidders were made aware of a certain flexibility with respect to the composition of any proponent's "team". Section 2.8(b) of the RFP provided that if "a material change has occurred to the Proponent since its qualification under the RFEI, including if the composition of the Proponent's team members has changed, . . . the Ministry may request [further information and] . . . reserves the right to disqualify that Proponent, and reject its Proposal". Equally, "[i]f a qualified Proponent is concerned that it has undergone a material change, the Proponent can, at its election, make a preliminary submission to the Ministry, in advance of the Closing Date, and before submitting a Proposal. . . . The Ministry will, within three working days of receipt of the preliminary submission give a written decision as to whether the Proponent is still qualified to submit a Proposal."

[138] The RFP issued on January 15, 2001. The Ministry was informed by Brentwood of a "proposed material change to our team's structure" in respect of a joint venture with EAC by fax dated January 24, 2001. From the Ministry's perspective, the change was desirable. EAC was a bigger company, had greater expertise in rock drilling and blasting (a major part of the contract) and a

stronger balance sheet. EAC was identified in Brentwood's amended proposal as a sub-contractor. In the end, the Ministry did not approve the January 14, 2001 request, presumably because it doubted that a change in the "composition of the Proponent's team's members" could , according to the terms of the RFP, include a change in the Proponent itself.

[139] The Ministry did obtain legal advice and did not proceed in defiance of it. On March 29, 2001, the Ministry noted in an internal e-mail that a Ministry lawyer (identified in the e-mail) had come to the conclusion that the joint venture was not an eligible proponent but advised that Contract B could lawfully be structured in a way so as to satisfy both Brentwood/EAC's concerns and avoid litigation from disappointed proponents.

[140] I do not wish to understate the difference between EAC as a sub-contractor and EAC as a joint-venturer. Nor do I discount the trial judge's condemnation of the Ministry's lack of fairness and transparency in making a Contract B which on its face was at odds with what the trial judge found to be the true state of affairs. Tercon has legitimate reason to complain about the Ministry's conduct. I say only that based on the jurisprudence, the Ministry's misconduct did not rise to the level where public policy would justify the court in depriving the Ministry of the protection of the exclusion of compensation clause freely agreed to by Tercon in the contract.

[141] The construction industry in British Columbia is run by knowledgeable and sophisticated people who bid upon and enter government contracts with eyes wide open. No statute in British Columbia and no principle of the common law override their ability in this case to agree on a tendering process including a limitation or exclusion of remedies for breach of its rules. A contractor who does not think it is in its business interest to bid on the terms offered is free to decline to participate. As Donald J.A. pointed out, if enough contractors refuse to participate, the Ministry would be forced to change its approach. So long as contractors are willing to bid on such terms, I do not think it is the court's job to rescue them from the consequences of their decision to do so. Tercon's loss of anticipated profit is a paper loss. In my view, its claim is barred by the terms of the contract it agreed to.

V. Disposition

[142] I would dismiss the appeal without costs.

Appeal allowed, MCLACHLIN C.J. *and* BINNIE, ABELLA *and* ROTHSTEIN JJ. *dissenting.*

Solicitors for the appellant: McLean & Armstrong, West Vancouver.

Solicitor for the respondent: Attorney General of British Columbia, Victoria.

Solicitor for the intervener: Attorney General of Ontario, Toronto.

---

tab 2

7326246 Canada Inc. and Kevin Gardiner v. Ajilon Consulting, 2014 ONSC 28 (CanLII)

Date: 2014-02-04
Docket: 433/12
Other citation: [2014] OJ No 538 (QL)
Citation: 7326246 Canada Inc. and Kevin Gardiner v. Ajilon Consulting, 2014 ONSC 28 (CanLII), <http://canlii.ca/t/g2zd9>, retrieved on 2017-03-15

CITATION: 7326246 Canada Inc. and Kevin Gardiner v. Ajilon Consulting, 2014 ONSC 28
DIVISIONAL COURT FILE NO.: 433/12
DATE: 20140204

ONTARIO

SUPERIOR COURT OF JUSTICE

DIVISIONAL COURT

BETWEEN:	)	
7326246 Canada Inc. and Kevin Gardiner	)	Robert J. Drake, for the Plaintiffs (Respondents)
Plaintiff (Respondent)		
– and –		
Ajilon Consulting, a division of Ajilon Canada Inc.		John-Paul Alexandrowicz, for the Defendant (Appellant)
Defendant (Appellant)	)	
	)	**HEARD:** December 17, 2013

HIMEL J.

Introduction

[1] 7326246 Canada Inc. ("7326246") and Kevin Gardiner sued Ajilon Consulting ("Ajilon") for damages for negligent misrepresentation. The matter proceeded to trial before Deputy Judge M.O. Mungovan of the Small Claims Court. On April 20, 2012, the trial judge found in favour of the plaintiff in the amount of $16,800 and costs in the amount of $2,573.14. Ajilon appeals the judgment and asks that the appeal be allowed and that the decision be set aside and the action be dismissed with costs.

[2] The case was tried along with another claim against Ajilon by a plaintiff whose factual circumstances and legal issues were similar. In an order made by this court, this appeal and the appeal involving the other plaintiff were ordered to be heard together.

Factual Background

[3] Ajilon is a federally incorporated company which provides information technology ("IT") consulting services to a number of clients, one of which is Loblaw Companies Ltd. ("Loblaw"). Loblaw began using Ajilon's services in 2007, often on a project basis. The Business Analyst staffing group at Loblaw retained Ajilon in 2009 to provide consultants on a contract basis, as well as permanent staffing. Ajilon's practice was to locate consultants to provide the services, require them to incorporate, and have the consultant corporation sign an agreement as an independent contractor with Ajilon.

[4] In January 2010, Mark Healey was hired as a Business Development Manager at Ajilon and was assigned the Loblaw account. Late in January, Mr. Healey was contacted by Angela Walker, a senior manager at Loblaw, to locate five additional Senior Business Analysts ("BA") for her team. Mr. Healey's group made contact with potential consultants and arranged for them to meet with Jimmy Kahn, a senior manager at Loblaw.

[5] Kevin Gardiner ("Gardiner") is an officer and principal of the corporate plaintiff 7326246. He applied for a position to work at Loblaw as a Senior Business Analyst through Ajilon, interviewed successfully, and was offered the position through Ajilon. He signed an Incorporated Contractor Agreement with Ajilon (the "agreement") which provided for an initial term of six months commencing on February 10, 2010 and ending on August 13, 2010.

[6] Prior to receiving the offer from Loblaw, Mr. Gardiner had started a four month contract with a company called ESP. However, he believed that the Loblaw opportunity was a better one and notified ESP on February 3, 2010 that he was accepting another position but could still offer some services to ESP. Mr. Gardiner sent a copy of his incorporation certificate to Ajilon, signed Ajilon's standard independent contractor agreement and returned it to Ajilon. He arranged to meet with the Human Resources department at Loblaw to provide information for background checks.

[7] The agreement signed by Mr. Gardiner on behalf of 7326246 was to engage the consultant corporation as an independent contractor. It provided that background and security checks had to be completed. It stated that the company would only be

paid for hours actually worked and approved according to proper invoices. It was silent on the amount of work that would be received, leaving this to the client's discretion. A termination clause provided for termination for any reason upon the provision of same day written notice. It also contained an entire agreement clause.

[8] On February 9, 2010, one day before the consultants were to start work, Mr. Healey received an email from Ms. Spadafora, an IT recruiter with the Human Resources department at Loblaw, advising that they were pushing Mr. Gardiner's start date back by one week to February 17. On February 16, Mr. Healey emailed Ms. Spadafora reminding her that the five consultants were starting in her group the next day and that her signature was still needed on the agreements. Later that day Mr. Healey received an email from Ms. Walker indicating that "due to some recent possible changes" within her group, they were still assessing the need for additional BAs and that Loblaw was postponing Mr. Gardiner's and the other consultants' start date again. This time, no new date was given. Mr. Healey responded that he believed there were five exceptions to the moratorium on engagements, one being Mr. Gardiner, and he also noted that he and the other consultants were already signed up to contracts. However, Mr. Healey only received an email which reiterated that there was some uncertainty. The correspondence continued over the week.

[9] During this period, Mr. Gardiner had been in touch with Ajilon through Ms. Mehandiratta. On February 23, 2010, Mr. Healey emailed the consultants including Mr. Gardiner and advised that they should pursue other opportunities while he tried to get a firm commitment from Loblaw regarding start dates. On March 5, 2010, Ajilon sent letters to the consultants, including Mr. Gardiner, terminating their agreements. The reason given was that Loblaw no longer required his services. No services had ever been provided. 7326246 and Mr. Gardiner commenced an action against Ajilon for damages for negligent misrepresentation.

Decision of the court below

[10] Deputy Judge Mungovan heard the trial over two days. In his decision, he outlined the elements of the tort of negligent misrepresentation as set out in the leading authority of *Queen v. Cognos*, 1993 CanLII 146 (SCC), [1993] 1 S.C.R. 87. Having heard the evidence of Mr. Gardiner and read the emails sent back and forth between him and Ajilon, he found that Mr. Gardiner was relying on what the representatives of Ajilon had said to him "about a job in Loblaws." He applied the test in *Hercules Managements Ltd. v. Ernst & Young*, 1997 CanLII 345 (SCC), [1997] 2 S.C.R. 165, and found that the indicia of "reasonable reliance" had been proven: Ajilon had a direct financial interest in the transaction as it stood to gain from a successful placement of Mr. Gardiner in Loblaw; its employees possessed special skills, judgment or knowledge when dealing with Loblaw's staffing needs; its advice on Loblaw's offer was given to Mr. Gardiner in the course of Ajilon's business, as it was done in the context of work; and the information was requested by Mr. Gardiner. Thus, he found that a duty of care existed between Ajilon and Mr. Gardiner's corporation. The trial judge then held that Mr. Gardiner placed foreseeable reasonable and justifiable reliance on representations made by Ajilon. He also found that the duty extended to Mr. Gardiner's corporation as Ajilon's representative had dealt with both him and his corporation throughout.

[11] The trial judge found that the representation made to 7326246 was misleading as it portrayed to Mr. Gardiner that there was a "job" for him at Loblaw when there was no firm commitment from that company that they would "employ" Mr. Gardiner as a Senior Business Analyst. He noted that on February 16, 2010, Loblaw had communicated second thoughts about increasing its existing complement of business analysts.

[12] The trial judge went on to find that Ajilon, through Ms. Mehandiratta, acted negligently in making this representation. This conduct had to be considered against an objective standard with reference to a reasonable person. He held that Ajilon had breached the standard of care by representing to Mr. Gardiner that he had secured a place at Loblaw as a Senior Business Analyst "when in fact that was far from the case." He held that Ms. Mehandiratta should have cautioned him about the uncertainty of the position since there was no certainty until an official at Loblaw had "signed off on a candidate's hire."

[13] Deputy Judge Mungovan held that Mr. Gardiner relied upon the representations in advising Mr. Stern of ESP that he had been offered another position and was accepting it. He held that his reliance was "not rash but reasonable on his part" in that he had received an email from Ms. Mehandiratta on February 3, 2010, in which she congratulated him on having been offered the position and made it sound like it was a certainty.

[14] On the issue of damages, he found that Mr. Gardiner had left a four month contract at ESP for a warehouse manager position at $4,200 per month with a possibility of full time employment. He calculated the damages at four months at $4,200 per month, for a total of $16,800. He also found that Ajilon terminated its agreement with Mr. Gardiner and his company effective March 5, 2010, and that Mr. Gardiner then tried to find work. On June 1, 2010, he found a job with Armtec-Brooklin Concrete. The trial judge found that he had made an effort to mitigate his company's damages.

[15] Finally, on the question of whether the entire agreement clause in the agreement prevented Mr. Gardiner from bringing the action, the Deputy Judge found that the negligent misrepresentation was made by Ms. Mehandiratta, acting on behalf of Ajilon, in stating that there was a job for Mr. Gardiner as a Senior Business Analyst at Loblaw. The trial judge considered the "entire agreement" clause in the agreement and held that, while it did not specifically use the word "representation", any representations would be covered by the word "understandings" which was mentioned in the clause. However, he went on to hold that the clause would only be enforceable where the parties to the contract are "sophisticated commercial parties" and that Mr. Gardiner was not a sophisticated commercial party and was not knowledgeable about technical legal aspects of contracts. Moreover, he held it was unenforceable because it was not specifically brought to Mr. Gardiner's attention by Ajilon prior to signing the contract.

Positions of the parties

[16] The appellant argues that the trial judge erred by mischaracterizing the evidence and finding that Mr. Gardiner had a "job" – Ajilon did not have a firm

commitment from Loblaw that they would "employ" Mr. Gardiner. In fact, Mr. Gardiner was offered a position through his company as an information technology consultant pursuant to an independent contractor agreement, not as an employee. By mischaracterizing the nature of the offer, the trial judge mischaracterized the representation that was made to Mr. Gardiner.

[17] Ajilon argues that the trial judge further erred by failing to consider the evidence presented by Ajilon regarding the representation that was made which showed, it submits, that it was not a negligent misrepresentation as at the time it was made, the offer made was true and accurate. In fact, Mr. Gardiner was asked to meet Ms. Spadafora on February 4, 2010, to provide the information for backgrounds checks. Even when the start date was pushed back, Loblaw still intended to proceed and the only pending step was a signature on the contracts. It was only on February 16, 2010, after Mr. Healey contacted Ms. Walker, that Mr. Healey became aware that Loblaw was not sure that it was going ahead to hire the five consultants. While there was evidence regarding communications between representatives of Loblaw and Ajilon instructing Ajilon to make the offer to Mr. Gardiner, the relationship between Loblaw and Ajilon and the terms of the consulting arrangements were inherently uncertain in nature.

[18] The appellant also argues that the trial judge erred in law and made incorrect findings of fact in finding that the entire agreement clause in the agreement did not bar the action for negligent misrepresentation. It submits that the trial judge erred in law and made incorrect findings of fact in finding that Mr. Gardiner was not a "sophisticated commercial entity/party."

[19] The appellant takes the position that, where the credibility of a witness was not in issue, it is open to an appellate court to review findings of fact by a trial judge if they were based on the failure to consider relevant evidence or a misapprehension of the evidence: see *Schreiber Brothers Ltd. v. Currie Products Ltd.*, 1980 CanLII 11 (SCC), [1980] 2 S.C.R. 78, at para. 10. Where the trier has made unreasonable findings of fact based on a misapprehension of the evidence and where the misapprehension is material to significant findings of fact, a new trial should be ordered: see *Apelowicz Management Inc. v. Griffiths*, 2010 ONSC 1410 (CanLII), at para. 23.

[20] Ajilon submits that the proposition that an appellate court should not lightly interfere with the findings of fact by a trial judge is subject to the trial judge correctly characterizing the evidence: see *Remo Valente Real Estate Ltd. v. Beauchamp*, [1996] O.J. No. 2040 (Sup. Ct.), at para. 1. In summary, on the evidentiary issues Ajilon takes the position that the trial judge failed to consider the evidence called by Ajilon that the representation did not constitute a negligent misrepresentation and erred in mischaracterizing Ajilon's evidence concerning the nature of the opportunity that was offered to Mr. Gardiner.

[21] The respondent argues that the trial judge properly weighed the evidence and applied the law in concluding that the appellant had made a negligent misrepresentation about the nature and existence of the Senior Business Analyst position at Loblaw. It submits that Mr. Gardiner was congratulated about an offer from Loblaw but was never told that the offer was subject to a final approval or was

conditional in any way. In fact, at the time of Ms. Mehandiratta's email on February 3, 2010, the paperwork for final approval had not even been submitted to Loblaw. The agreement he signed with Ajilon set a start date of February 10, 2010. When that date arrived but the position had not materialized, he was told the start date was delayed one week to February 17. On February 16, he was told that he would not start the following day.

[22] The respondent was never cautioned that the position had not been approved and may not ever be approved. Mr. Gardiner takes the position that, on the contrary, Ajilon's approach was to assure him that the work at Loblaw had been offered and the start date was imminent. That there were problems with Loblaw's approval was not communicated to him until February 19, 2010, and even then, Mr. Healey said that matters still remained undecided at that point. No clear indication on the status of the work was given until he received a notice of termination. The respondent takes the position that there never was a position ready for him and that Loblaw never had made an "offer" capable of acceptance.

The standard of review

[23] The appellant submits that the applicable standard of review on questions of law is correctness. For questions of fact, the standard is palpable and overriding error. A palpable and overriding error is defined as "clear to the mind or plain to see": see *Housen v. Nikolaisen*, 2002 SCC 33 (CanLII), [2002] 2 S.C.R. 235, at paras. 5, 8, 10, 26.

[24] The respondent submits that the standard of palpable and overriding error applies equally whether the disputed determination relates to credibility concerning "primary" facts, "inferred" facts or to global conclusions based on assessments of the evidence as a whole: see *L.(H.) v. Canada (Attorney General)*, 2005 SCC 25 (CanLII), [2005] 1 S.C.R. 401, at paras. 53-54. An appellate court will not interfere with the trial judge's findings of fact unless the error can be identified and shown to have affected the result. The respondent further argues that it is for the trial judge to weigh the evidence and deference should be given. An appellate court should only intervene if the finding is "clearly wrong", "unreasonable" or "unsupported by the evidence".

[25] The trial judge's application of the test of for negligent misrepresentation raises questions of mixed fact and law reviewable on the standard of palpable and overriding error. Whether the entire agreement clause precludes liability for negligent misrepresentation is a question of law reviewable on a standard of correctness.

The Test for Negligent Misrepresentation

[26] The Supreme Court held in *Queen v. Cognos*, at p. 110, that for a claim to succeed based on the tort of negligent misrepresentation, five elements must be present. They are as follows:

> (1) there must be a duty of care based on a "special relationship" between the representor and the representee; (2) the representation in question must be untrue, inaccurate or misleading; (3) the representor must have acted negligently in making said representation; (4) the representee must have

relied, in a reasonable manner, on said negligent misrepresentation; and (5) the reliance must have been detrimental to the representee in the sense that damages resulted.

Analysis

(1) Did Ajilon owe a duty of care to Mr. Gardiner and his company?

[27] The appellant does not submit that the trial judge erred in finding a duty of care based on a special relationship between the appellant and the respondent. As the trial judge noted, the agreement was between Ajilon, the recruiting agency, and the consultant although the consultant was to provide the services for Loblaw and work at one of Loblaw's premises. The trial judge noted that this requirement for negligent misrepresentation has become "a duty based generally on 'foreseeable reasonable reliance'." Based on the evidence, the trial judge could easily have concluded that there was foreseeable reasonable reliance by the respondents on Ajilon's representation. Ajilon's representative, Mark Healey showed he understood this when he told Loblaw that "there may be issues because we already have [the consultants] signed up to contracts", and that he did not want to lose them to other opportunities. Only later did he inform the consultants, including Mr. Gardiner, that they should pursue other opportunities.

(2) Was the representation untrue, inaccurate or misleading?

[28] This element of negligent misrepresentation requires that the representation be untrue, inaccurate or misleading at the time that it was made. The trial judge held that the representation by Ms. Mehandiratta was "misleading" because she did not have a firm commitment that they would "employ" Mr. Gardiner as a Senior Business Analyst. On February 3, 2010, Mr. Gardiner was congratulated via telephone about the Loblaw offer and later that day was told to contact Loblaw's HR department for the criminal and job reference checks. These communications were based upon the email from Mr. Kahn of Loblaw to Mr. Healey of Ajilon, instructing Ajilon to extend an offer to Mr. Gardiner. What Mr. Gardiner was not told until much later was that the position was still waiting on a final approval from Loblaw. In an email dated February 16, Ms. Walker advised Mr. Healey that Loblaw was "having second thoughts about increasing its existing complement of business analysts" and yet Mr. Gardiner was not advised to pursue other opportunities until February 23.

[29] The appellant submits that the court must consider the inherently uncertain nature of consulting contracts and that the nature of the industry and the types of contracts used mean that an offer is never a certainty. Ajilon submits that there was no job, the opportunity was not secure and that there was no real representation as Ajilon was simply passing on the information that Loblaw had given it. The respondent argues that Ajilon was not led astray by Loblaw, as it knew sign-off was required and yet insisted on obtaining commitments from the potential analysts that drew them away from other opportunities without letting them know the true nature of the situation.

[30] The appellant makes much of the fact that Mr. Gardiner was an independent contractor, not a traditional employee, and consequently the trial judge

misapprehended the position when he described it as a "job" or "employment" in his reasons. It submits that independent contractor arrangements are flexible, not secure and there are risks that the business opportunity may not materialize or that the opportunity may change. Ajilon argues that the trial judge mischaracterized the opportunity as a "job" or "employment" when, in fact, it was an independent contractor arrangement which had no certainty. The appellant submits that the trial judge erred in finding that the representation was misleading because Ajilon did not have a firm commitment from Loblaw that they would "employ" Mr. Gardiner at the time they made the offer – Loblaw was never to be Mr. Gardiner's "employer".

[31] Regardless of the nature of the industry and the potential risks inherent in this type of offer, Ajilon represented an offer of work to Mr. Gardiner and gave him all the details of it, save for one—that the opportunity still required official approval. In the context of the communications between the appellant and the respondent, the trial judge found that the representations were untrue, inaccurate and misleading and I agree with this finding.

(3) Did the representor act negligently in making the representation?

[32] The failure to divulge relevant information is important in determining whether a misrepresentation was negligently made. Where the representor does not know or could not have known pertinent information when the misrepresentation was made, the misrepresentation would not be negligent: see *Lesage v. Canadian Forest Products Ltd.*, 2009 BCSC 1427 (CanLII), at paras. 87-89, aff'd, 2011 BCCA 259 (CanLII).

[33] Here, the trial judge found that Ms. Mehandiratta represented to Mr. Gardiner that he had secured a position as a Senior Business Analyst but failed to caution him that there was no certainty until Loblaw signed off. Ajilon argues that it is common in the context of the IT consulting industry for organizations to require flexibility and that needs are largely project-based, meaning that they can change or may fail to materialize altogether. The appellant argues that Mr. Gardiner should have been aware that the offer was not certain and, consequently, the appellant's failure to state this was not negligent. The appellant says that at the time the offer was made, Ajilon did not know that subsequent internal changes at Loblaw might impact any planned IT projects. Therefore, Ajilon did not act negligently in declining to warn Mr. Gardiner that the contract or statement of work had yet to be signed off on.

[34] Ajilon also submits that it is common to engage consultants without official paperwork and since the company had recently done this with eight consultants in the same group and no issues had resulted, it was reasonable to represent that Mr. Gardiner had been offered the position without expressly saying that the contract had not yet been signed.

[35] The respondents claim Ajilon should have known and did know that the contract still needed final approval, and that this meant the prospect of work for Mr. Gardiner was not yet certain. Ajilon's failure to disclose this made its misrepresentation regarding the certainty of the offer negligent.

[36] These submissions were all put to the trial judge. He concluded that, in making representations to the respondents, Ajilon breached the standard of care by representing that Mr. Gardiner had secured a position at Loblaw when Ajilon knew that was not the case. That conclusion was reasonable in the circumstances.

(4) Did the representee rely in a reasonable manner on the negligent misrepresentation?

[37] If it is doubtful that the misrepresentee would have acted any differently had the representation not been made, then this element will not be made out. The trial judge held that there was no doubt that Mr. Gardiner relied upon Ajilon's representation that there was a job for him at Loblaw as he left a position elsewhere. He found his reliance was reasonable. The trial judge referred to the fact that Ajilon sent a number of emails to Mr. Gardiner confirming the position.

[38] The appellant argues that Mr. Gardiner preferred the position at Loblaw to the job at ESP and was willing to take the risk of that position not materializing. The appellant argues that he did not rely on Ajilon's alleged representation and that it was unreasonable for him to believe the position was a certainty. Rather, they argue Mr. Gardiner was aware of the nature of the independent contractor arrangement. Again, the appellant argues that the mischaracterization of the opportunity as a "job" caused the trial judge to fail to consider the opportunity in an appropriate context.

[39] Counsel for the respondent points to the direct evidence that, had Mr. Gardiner been informed that the opportunity was not certain and was not yet approved, he would have kept the other position.

[40] The trial judge found that Ajilon intended for Mr. Gardiner to rely on its representations and make himself exclusively available for the Loblaw position. It was negligent for Ajilon to make statements about the position and then not accept the responsibility for the intended effect of such statements. In my view, it was open to the trial judge to reach this determination on the evidence.

(5) Was the reliance detrimental to the representee in the sense that damages resulted?

[41] The trial judge found that Mr. Gardiner was entitled to damages for the loss of the position at ESP. Although he had not yet passed the background checks for the Loblaw position, these were formalities and no issue with those checks was raised by Loblaw. It was not reckless to leave the other position before completion.

[42] The evidence was that Mr. Gardiner left a contract where he was to be paid for four months at $4,200 per month. When Ajilon terminated the agreement, Mr. Gardiner looked for work and found a job with Armtech-Brooklin Centre commencing on June 1, 2010.

[43] The trial judge held that he was satisfied with Mr. Gardiner's efforts to mitigate. He ordered damages for the amount of the contract that he rejected in order to take the Loblaw's position. The trial judge did not err in making his conclusions on damages.

The entire agreement clause

[44] Clause 30 of the agreement signed by Mr. Gardiner on behalf of himself and the plaintiff reads as follows:

> This Agreement constitutes the entire agreement between the Parties pertaining to the consulting engagement set forth herein and supersedes all prior negotiations, understandings and agreements between the Parties, written or oral ....

[45] The appellant argues that the entire agreement clause specifically precludes reliance on representations and operates as a bar to negligent misrepresentation claims: see *Corfax Benefits Systems Ltd. v. Fiducie Desjardins Inc.* (1997), 1997 CanLII 12195 (ON SC), 37 O.R. (3d) 50 (Gen. Div.), at p. 6; *McNeely v. Herbal Magic Inc.*, 2011 ONSC 4237 (CanLII), at paras. 10 and 19; *No. 2002 Taurus Ventures Ltd. v. Intrawest Corp.*, 2007 BCCA 228 (CanLII), at para. 59.

[46] The trial judge referred to the entire agreement clause and found that, while the word "representation" does not appear in the clause, the word "understandings" does. He was satisfied that the representation relied upon probably did fall into the category of an understanding and, in any event, to conclude otherwise would "constitute a distinction without a difference." In my view the trial judge did not err in this conclusion.

[47] He then relied on the authority of *McNeely* for the proposition that an entire agreement clause is enforceable to preclude liability for a negligent misrepresentation where the parties to such a contract are "sophisticated commercial parties." He held that Mr. Gardiner was not a sophisticated commercial party in the sense of understanding a contractual clause such as this. He noted that "only a lawyer" would understand the importance of an entire agreement clause in this context, and therefore the clause could not be enforced to preclude Ajilon's liability for the negligent misrepresentation.

[48] The appellant argues that *McNeely* does not stand for the proposition that the parties must be "sophisticated commercial parties" for an entire agreement provision to be enforced. Rather, it should be enforced unless it can be said that the clause is unconscionable or unfair, or unreasonable. The trial judge failed to establish the legal doctrine for striking the entire agreement clause down.

[49] The appellant thus argues that the trial judge applied the incorrect legal test by requiring that the parties be sophisticated commercial entities/parties and by narrowly defining a sophisticated commercial entity/party as a lawyer. The appellant argues that the trial judge erred in finding that Mr. Gardiner was not a "sophisticated commercial party" when he had previous experience in the IT industry as an independent contractor.

[50] The respondent argues that if the word representation is not in the clause, it cannot cover liability for misrepresentations. However, there is no suggestion that the trial judge made an error of law in finding otherwise. The respondent also submits that there are two situations in which a judge might not enforce an entire agreement

clause: where a party was not a sophisticated commercial party and where the representation went to the heart of the contract. The respondent submits that both of these concepts apply in the case at bar.

[51] The problem of determining whether an entire agreement clause can preclude liability for a negligent misrepresentation is one that lies on the shifting sands between tort and contract. An entire agreement clause is similar to but distinct from a general exculpatory, or exclusionary, clause. In general, "both types of clauses have the effect of excluding liabilities of various kinds and are capable of producing unjust results": see John D. McCamus, *The Law of Contracts*, 2nd ed. (Toronto: Irwin Law Inc., 2012), at p. 372. More specifically, an exculpatory clause limits or excludes "liability for damages for breach of contract or for a tort connected to the contract", while an entire agreement clause "seeks to exclude liability for statements other than those set out in the written contract and is sometimes referred to as an exclusion clause": see *Shelanu Inc. v. Print Three Franchising Corp.* (2003), 2003 CanLII 52151 (ON CA), 64 O.R. (3d) 533 (C.A.), at para. 31. Where the issue is the effect of an entire agreement clause on a party's liability in tort for a negligent misrepresentation, there appears to be little practical difference between its effect and that of an exculpatory clause.

[52] The precise relationship between the two types of clauses may seem an arcane point but it has ramifications given the Supreme Court of Canada's new approach to the application of exclusionary clauses in *Tercon Contractors Ltd. v. British Columbia (Transportation and Highways)*, 2010 SCC 4 (CanLII), [2010] 1 S.C.R. 69. In *Tercon*, the province of British Columbia sought to preclude liability to a large construction contractor for a breach of a tendering contract by way of an exclusion clause found in that contract. Both parties were held to be "sophisticated" commercial parties: at paras. 73, 82. The court was unanimous that a new approach should be applied when a party "seeks to escape the effect of an exclusion clause or other contractual terms to which it had previously agreed": at para. 121. Four members of the court dissented on the application of the new approach to the facts but the important aspect for this case is the approach itself.

[53] Under the former approach to exclusionary clauses, courts sometimes applied the doctrine of fundamental breach to hold an exclusionary clause unenforceable but this was undesirable as it often served to obscure the real grounds motivating judicial decision making. The new approach, described in *Tercon* at paras. 122-3, places the focus squarely on unconscionability and public policy:

> The first issue, of course, is whether as a matter of interpretation the exclusion clause even applies to the circumstances established in evidence. This will depend on the Court's assessment of the intention of the parties as expressed in the contract. If the exclusion clause does not apply, there is obviously no need to proceed further with this analysis. If the exclusion clause applies, the second issue is whether the exclusion clause was unconscionable at the time the contract was made, "as might arise from situations of unequal bargaining power between the parties" (*Hunter*, at p. 462). This second issue has to do with contract formation, not breach.

> If the exclusion clause is held to be valid and applicable, the Court may undertake a third enquiry, namely whether the Court should nevertheless refuse to enforce the valid exclusion clause because of the existence of an overriding public policy, proof of which lies on the party seeking to avoid enforcement of the clause, that outweighs the very strong public interest in the enforcement of contracts.

[54] This new approach whereby a court may determine that a specific exculpatory term within an otherwise valid contract is unconscionable and, therefore, unenforceable has been called the "unconscionable term" doctrine by John D. McCamus in *The Law of Contracts*, Ch. 11, Section D(6). Among the innovations to contract law potentially implied by the adoption of this doctrine is the ability of a court to strike an unconscionable term from a contract while upholding the remainder of the agreement as valid. As this is not a remedy at issue in this particular case, its availability need not be dealt with here. What is necessary, however, is to determine whether the *Tercon* approach applies to entire agreement clauses as well as exculpatory clauses, a point on which the decision itself is silent. The appellant argues that if the entire agreement clause is unconscionable, unfair or unreasonable, then the entire agreement clause will be unenforceable. The authority for this would have to come from an application of the *Tercon* approach to entire agreement clauses.

[55] The approach adopted by the Supreme Court in *Tercon* combines two previous approaches to the construction of exclusionary causes laid out in *Hunter Engineering Co. v. Syncrude Canada Ltd.*, 1989 CanLII 129 (SCC), [1989] 1 S.C.R. 426, where the court split on the doctrine to apply if not applying fundamental breach. In *Hunter*, Dickson C.J.C. preferred the doctrine of unconscionability because it would allow courts to focus on whether factors such as inequality of bargaining power meant an exclusionary clause should be held unenforceable. This notion seems to have become step two in the *Tercon* analysis. Justice Wilson, held that the courts must reserve some discretion to hold an exclusionary clause unfair and unreasonable in light of events subsequent to the formation of the contract, since unconscionability is only concerned with inequality of bargaining power and circumstances as they stood at the time the contract was made. This notion seems to have become step three in the *Tercon* analysis.

[56] In *Shelanu* the Ontario Court of Appeal held, at paras. 31-32, that entire agreement clauses should be construed using the principles of construction normally applied to exculpatory clauses. This decision came after *Hunter* but before *Tercon* and, accordingly, it described the framework for the construction of exclusionary clauses according to the *Hunter* approach. The question that remains is whether the *Tercon* approach, which seems to combine both elements of the framework from *Hunter*, applies to an entire agreement clause such as the one in this case absent direct authority.

[57] There are reasons to believe that it should. M.H. Ogilvie, writing prior to *Tercon*, argues that "entire agreement clauses pose the same policy issues as exclusion clauses" and for this reason "they are not at all mysterious": see M.H. Ogilvie, "Entire Agreement Clauses: Neither Riddle nor Enigma" (2008) 87 Can. Bar Rev. 625, at p. 632. Where a misrepresentation induces the agreement containing the entire agreement clause, these issues can include the sophistication of the parties and the

provision of notice to unsophisticated parties. Ogilvie argues, at p. 626, that "whether the contract in question is induced by negligent or fraudulent misrepresentation, the outcome for entire agreement clauses should be the same as in the case of exclusion clauses generally ..." where the clauses are generally enforced to preclude negligent misrepresentation in the context of negotiated contracts by sophisticated parties.

[58] Similarly, entire agreement clauses found in contracts induced by a negligent misrepresentation have generally been found to be unenforceable in the context of an unsophisticated party unless notice of the clause, or even notice of the clause's intended effect, was brought home to the unsophisticated party during bargaining: see *Beer v. Townsgate 1 Ltd.* (1997), 1997 CanLII 976 (ON CA), 152 D.L.R. (4th) 671 (Ont. C.A.), at para. 29; *Zippy Print Enterprises Ltd. v. Pawliuk* (1994), 1994 CanLII 1756 (BC CA), 100 B.C.L.R. (2d) 55, at para. 45; *Roberts v. Montex Development Corporation* (1979), 1979 CanLII 452 (BC SC), 100 D.L.R. (3d) 660 (B.C.S.C.).

[59] McCamus speculates that the so called unconscionable term doctrine from *Tercon* may have application to clauses traditionally subjected to "special notice" requirements. Of these, entire agreement clauses are the most likely. He writes about such clauses at p. 444:

> Of these provisions, perhaps the most likely candidate for subjection to the new doctrine is the "entire agreement" clause. Known to be a "trap for the unwary," entire agreement clauses have often been held to be enforceable only where Canadian courts are satisfied that the significance of the clause was brought home to the affected party ... It should be noted, however, that the "special notice" doctrine is applied only sparingly to signed agreements on the assumption that the signature constitutes a binding assent to all the written terms. It may be, then, that the new doctrine will play an important role in striking down unfair terms in signed agreements where there is no realistic expectation that the written terms have been either read or, if read, understood by the signing party. In other words, the doctrine of unconscionable term may provide a common law device, long awaited by some, that can ameliorate the harsh impact of unfair terms in boilerplate or "adhesion" contracts, offered particularly in the context of consumer transactions on a take-it-or-leave-it basis.

[60] This passage illuminates the importance of the trial judge's factual findings that Ajilon did not notify Mr. Gardiner of the entire agreement clause and that there could not have been any realistic expectation that he would have understood its importance without it being brought home to him. While the standard form contract as a whole was not strictly offered to Mr. Gardiner on a "take-it-or-leave-it basis", the enforcement of this particular clause would nevertheless impose a "harsh impact" on him.

[61] In my view, the *Tercon* analysis should be used to determine whether the entire agreement clause precludes Ajilon's liability for negligent misrepresentation. For this reason, I apply this approach.

[62] On step one, the trial judge concluded that the entire agreement clause did apply to negligent misrepresentations by use of the word "understandings" and I have already indicated I will not interfere with this finding.

[63] Step two of the question is focused on whether the clause is unconscionable. Unconscionability requires the combination of inequality of bargaining power and the use of that inequality by the stronger party to obtain an improvident bargain: see *Mundinger v. Mundinger* (1968), 1968 CanLII 250 (ON CA), [1969] 1 O.R. 606 (Ont. C.A.), at p. 610. In *ABB Inc. v. Domtar Inc.*, 2007 SCC 50 (CanLII), [2007] 3 S.C.R. 461, the Supreme Court wrote, at para. 82, that "[u]nder the doctrine of unconscionability, a limitation of liability clause will be unenforceable where one party to the contract has abused its negotiating power to take undue advantage of the other." Here, I consider the standard form nature of the agreement, the importance of the clause in light of Ajilon's knowledge that they were keeping Mr. Gardiner in abeyance without a final approval of the position from Loblaw, and the lack of any notice regarding the clause. While the appellant argues that Mr. Gardiner was not unsophisticated because of his experience as a contractor in the IT industry, the key points are that the clause took on outsized importance given the uncertainty of the Loblaw position and that his access to information regarding this uncertainty was controlled by Ajilon. I conclude that Ajilon used its stronger informational position in the circumstances to obtain Mr. Gardiner's supposed consent to an improvident clause.

[64] Step three of the analysis need not be undertaken given my finding on step two but, in any event, it may well be that the clause is also unenforceable on the public policy ground that recruitment companies should be prevented from leading potential recruits to believe they have secured work when they have not. This would not lead to an unduly restrictive operating environment for recruitment companies. Ajilon could have acknowledged to Mr. Gardiner and the other consultants the uncertainty in the situation with Loblaw and still tried to sell them on the merits of the positions and their eventual placement which served Ajilon's financial interests. The consultants may well have chosen to disregard other opportunities in favour of the potential but uncertain Loblaw positions.

[65] If I am wrong in applying the *Tercon* analysis to the entire agreement clause, the trial judge's ruling on this issue must still be upheld under the traditional jurisprudence. As the foregoing discussion has shown, he did not err in determining that the sophistication of the parties and the lack of specific notice are relevant considerations in the case law on entire agreement clauses. While the trial judge went too far in stating that "only a lawyer" could have understood the importance of the clause – non-lawyers are certainly capable of understanding a clause like this if its significance is brought home to them – it is important to note that Ajilon gave no notice of the clause whatsoever. This cannot be sufficient notice given Ms. Langley's unsophisticated nature with respect to the clause.

Result

[66] In his reasons, the trial judge correctly set out the test for a claim founded in negligent misrepresentation. He reviewed the five factors and applied the law to the evidence before him. The entire agreement clause cannot preclude liability in these

circumstances because it is unenforceable under the *Tercon* approach. Even if the *Tercon* approach does not apply, the trial judge did not err in determining the clause was unenforceable because Mr. Gardiner was an unsophisticated party and did not have notice of the clause. The trial judge made no reviewable error that would warrant intervention by this court. The appellant primarily asks this court to re-weigh the evidence and reconsider the matter, but that is not the function of this court.

[67] For these reasons, the appeal is dismissed. If the parties are unable to agree on costs, they may file written submissions according to the following timetable: the respondent by February 21, 2014 and the appellant by February 28, 2014.

Himel J.

Date: February 4, 2014

CITATION: 7326246 Canada Inc. and Kevin Gardiner v. Ajilon Consulting, 2014 ONSC 28
DIVISIONAL COURT FILE NO.: 433/12
DATE: 20140204

ONTARIO

SUPERIOR COURT OF JUSTICE

DIVISIONAL COURT

BETWEEN:

7326246 Canada Inc. and Kevin Gardiner

Plaintiff (Respondent)

– and –

Ajilon Consulting, a division of Ajilon Canada Inc.

Defendant (Appellant

REASONS FOR JUDGMENT

Himel J.

Released: February 4, 2014

tab 3

ESSENTIALS OF
CANADIAN LAW

THE LAW OF CONTRACTS

JOHN D. McCAMUS

Professor of Law
Osgoode Hall Law School, York University

role of the doctrine at common law as an instrument of such a policy is, at best, a limited one. The doctrine has, however, been given statutory expression in a number of provincial legislative schemes that do implement broadly based policies of this kind.[198]

2) Elements of Unconscionability

In order to set aside a transaction on the ground of unconscionability, one must establish both inequality of bargaining power in the sense that one party is incapable of adequately protecting his or her interests and undue advantage or benefit secured as a result of that inequality by the stronger party. The combination of these two factors is well illustrated in the leading case of *Morrison v. Coast Finance Ltd.*[199] The plaintiff was an elderly widow, Mrs. Morrison, preyed upon by two young men, Lowe and Kitely. A woman of modest means, Morrison's principal income came from renting out three rooms in her home. Kitely had been a roomer for a month or two before he and Lowe successfully persuaded Morrison to mortgage her home to the defendant finance company in order to be able to lend the monies thereby secured to Lowe and Kitely. The monies were to be used by Lowe to repay a loan advanced to him by the same finance company and by the two men to each buy a car from a related automobile company that operated as a car dealer. Kitely was an alcoholic; the two men represented to Morrison that her loan to them would enable Kitely to make a start in the automobile sales business. The transaction was handled by one Crawford, the office manager for both the finance company and the automobile company. Under his supervision, the cheque for the proceeds of the mortgage was endorsed by Morrison in favour of Lowe and Kitely, who in turn returned the cheque to Crawford. Crawford deposited the amount in the account of the automobile company, from which amount the outstanding balance on Lowe's loan was restored to the finance company. The unfairness of the transaction was no doubt evident to Crawford who, later that day or the next day, required Lowe to execute a promissory note in favour of Morrison for the amount advanced and further, required the execution of conditional sale contracts for the two cars in question between the automobile company and Lowe and Kitely and assigned the vendor's interest therein to Morrison. As Davey J.A. observed, "[T]he extreme folly of this old woman mortgaging her home in order to borrow money which she could not repay out of her own resources, for the purpose

198 See below this Chapter, section D(6).
199 Above note 195.

more broadly to all consumer transactions in which commercial parties are providing goods and services to ordinary or non-business consumers. With respect to such transactions, the statutes typically provide remedies where such transactions have been induced by misrepresentation[276] or where the transaction is determined by a court to be unconscionable. To assist the court in making the latter determination, a number of the statutes set out lists of factors that may be taken into account. The lists vary to some extent from one statute to another but the Ontario list, which is illustrative, sets out the following factors:

(i) that the consumer is not reasonably able to protect his or her interest because of physical infirmity, ignorance, illiteracy, inability to understand the language of an agreement or similar factors,
(ii) that the price grossly exceeds the price of which similar goods or services are readily available to like consumers,
(iii) that the consumer is unable to receive a substantial benefit from the subject-matter of the consumer representation,
(iv) that there is no reasonable probability of payment of the obligation in full by the consumer,
(v) that the proposed transaction is excessively one-sided in favour of someone other than the consumer,
(vi) that the terms or conditions of the transaction are so adverse to the consumer as to be inequitable,
(vii) that he or she is making a misleading statement of opinion on which the consumer is likely to rely to his or her detriment,
(viii) that he or she is subjecting the consumer to undue pressure to enter into the transaction.[277]

Where the supplier "knows or ought to know"[278] of the presence of one or more of these factors, a finding of unconscionability may be made. The statutes typically provide both civil redress in the form of rescis-

---

Consumer Protection Act, 2002, S.O. 2002, c. 30, Sch. A (to come into force on proclamation)); *Business Practices Act*, R.S.P.E.I. 1988, c. B-7. See generally E.P. Belobaba, "Unfair Trade Practices Legislation: Symbolism and Substance in Consumer Protection" (1977) 15 Osgoode Hall L.J. 327.

276 See Chapter 10, section I.

277 *Business Practices Act*, R.S.O 1990, c. B.18, s. 2(2). The Ontario Act adopts the awkward device of providing relief only where there has occurred an "unconscionable consumer representation" thus suggesting that in addition to one or more of the listed factors, there must be a representation of some kind made by the supplier. Presumably, however, any representation made in the unconscionable circumstances would suffice and this requirement should normally be easily met.

278 *Ibid.*

clauses"[90] in its agreement with the plaintiff. In the view of the Alberta Court of Appeal, such conduct was unconscionable and the exculpatory clauses could not be relied upon by the defendant.

The doctrine is likely to receive more ready application in the context of consumer transactions. Thus, suppliers of vehicles that are so defective as not to be in workable condition may not be able to hide behind an exculpatory clause.[91] A more difficult fact situation is posed by *Solway v. Davis Moving & Storage Inc.*[92] The plaintiffs had entered into a contract with the defendant moving company to remove and store their household goods before delivering them to their new home. The plaintiffs had understood that the goods would be stored in a locked trailer in the defendant's parking lot. The trailer was, however, left on the street to facilitate snow removal on the lot and the trailer and its contents were stolen from that location. The terms of the agreement were stipulated by statute and included a limitation of liability clause limiting the defendant's liability to a modest sum per pound. A majority of the Ontario Court of Appeal applied the fundamental breach doctrine on the ground that it would be unconscionable, unfair or unreasonable to allow the defendant to rely on the clause in these circumstances. The plaintiff was therefore allowed to recover the substantial losses resulting from the theft. The case is, however, a difficult one. The clause was stipulated by statute and might be thought to represent a reasonable allocation of risk between the owner of the chattels, who knows their value, and the moving company, who will not likely have such knowledge. Further, in this particular case, it appears that the plaintiffs were aware of the nature of the limitation of liability and, indeed, had taken out some additional insurance. For reasons such as these, Carthy J.A., in dissent, would not have applied fundamental breach doctrine.[93]

---

90 *Ibid.* at para. 54.

91 See, for example, *Scarborough Tire & Spring Service Ltd. v. Campbell Graphics Inc.* (1994), 17 B.L.R. (2d) 118 (Ont. Ct. Gen. Div.); *Bagnell's Cleaners & Launderers Ltd. v. Eastern Automobile Co.* (1991), 111 N.S.R. (2d) 51 (S.C.T.D.). These cases do not, however, refer to the *Hunter* analysis.

92 Above note 84.

93 For criticism of the majority opinion from a law and economics perspective, see A.J. Duggan, "Stolen Goods, A Cruise Disaster and a Right of Way Gone Wrong: Three Unconscionable Contracts Cases from a Law and Economics Perspective" (2004) 40 Can. Bus. L.J. 3. A similar exchange of views occurred in a Nova Scotia case involving two commercial parties. See *Atlas Supply Co. of Canada Ltd. v. Yarmouth Equipment Ltd.* (1991), 103 N.S.R. (2d) 1 (S.C.A.D.), leave to appeal to S.C.C. granted and discontinued, [1991] S.C.C.A. No. 256 (sale of franchise—misleading projections of future business—"merger" and "independent investigation" clauses held unconscionable). For criticism, see V.W.

Finally, it appears to be accepted that the application of the unconscionable or unfair and unreasonable test does not, if successfully met, lead to the rescission of the agreement. The cases applying *Hunter* assume that the effect of fundamental breach doctrine, if applicable, is to withhold the application of the term to the particular fact situation rather than to rescind either the agreement itself or the particular term.

E. CONCLUSION

The nature and scope of the doctrine of fundamental breach has varied over time in both England and in Canada. In England, with the enactment of the *Unfair Contract Terms Act 1977*,[94] the evolution of the doctrine appears to have been completed. With the discretion conferred by that statute on the courts to control the application of exculpatory clauses in consumer contracts and other standard form agreements, the need for a common law doctrine conferring a similar discretion has disappeared. Accordingly, under English law, the doctrine of fundamental breach appears to have settled into a simple matter of applying the usual techniques of contract interpretation, including the principle of *contra proferentum*, to exculpatory clauses in agreements not subject to the legislation. In common law Canada, in the absence of similar legislation, the courts have persisted, however, in developing a common law device for controlling the application of disclaimer clauses. Nonetheless, there remain some similarities between the English and Canadian versions of the doctrine. In both systems, in the case of an ordinary commercial transaction, a construction approach will be followed. Further, it appears that in both systems, an exculpatory clause will not be applied or interpreted in such fashion as to render nugatory or illusory the obligations of one party.[95] Further, Canadian courts continue to interpret clauses strictly on the basis of the *contra proferentum* principle.[96]

DaRe, "Atlas Unchartered: When Unconscionability 'Says It All'" (1996) 27 Can. Bus. L.J. 426. And see *F. Mendelssohn v. Normand Ltd.*, above note 5 (parked car—attendant promising to lock the car—car not locked with resulting theft of valuables left in the car—garage owner not protected by exculpatory clause).

94 Above note 30.

95 This principle was accepted by the Supreme Court of Canada in *Beaufort Realties* case, above note 64 and by Wilson J. in *Hunter*, above note 8 at 510.

96 *Canadian Pacific Forest Products Ltd. v. Belships (Far East) Shipping (Pte.) Ltd.* (1999), 175 D.L.R. (4th) 449 (Fed. C.A.) (*contra proferentum* or strict construction approach not overtaken by the decision in *Hunter Engineering*). See also *Meditek Laboratory Services Ltd. v. Purolator Courier Ltd.* (1995), 125 D.L.R.

tab 4

ATLAS UNCHARTERED: WHEN UNCONSCIONABILITY 'SAYS IT ALL'

*Vern W. DaRe**

In *Atlas Supply Co. of Canada Ltd. v. Yarmouth Equipment Ltd.*[1], the Nova Scotia Court of Appeal adopted a rather liberal, if not controversial, approach to the unconscionability doctrine. The court applied the doctrine to a commercial contract and refused to enforce the contract's exclusion clauses because they were held to be unconscionable. A similar approach to commercial exclusion clauses divided the Supreme Court of Canada in *Hunter Engineering Co. v. Syncrude Canada Ltd.*[2], and as a result whether the doctrine applies in commercial situations remains an open question. Despite the reluctance of the Supreme Court, several other courts have followed the initiative in *Atlas Supply* and taken a more robust view of the unconscionability doctrine.[3] This development has not, however,

---

* Associate, McInnes, Cooper and Robertson, Halifax. For their encouragement, comments and critiques, the assistance of Donald Harris, Philip H. Osborne, Jacob S. Ziegel and an anonymous second reader are gratefully acknowledged. I am especially indebted to Elio and Frances McLeod-McCluskey DaRe for their support. The views expressed, however, are those of the writer.

1 (1991), 103 N.S.R. (2d) 1, 37 C.P.R. (3d) 38 (C.A.); leave to appeal to S.C.C. granted 108 N.S.R. (2d) 270*n*, 38 C.P.R. (3d) vi; notice of discontinuance of appeal filed April 1, 1992, [1991] S.C.C.A. No. 256 (*Atlas Supply* is cited hereafter to N.S.R.).

2 In the leading decision of *Hunter Engineering Co. v. Syncrude Canada Ltd.* (1989), 57 D.L.R. (4th) 321, [1989] 1 S.C.R. 426 (hereafter *Hunter Engineering*), it was only in *obiter dicta* that the Supreme Court of Canada recognized the doctrine of unconscionability in commercial contracts. While Chief Justice Dickson and Justice La Forest were willing to adopt unconscionability as a test for the validity of exemption clauses, Justices Wilson and L'Heureux-Dubé contested the merits of the doctrine on the grounds of the considerable uncertainty it would create in commercial affairs. Accordingly, the Supreme Court has yet to apply the doctrine and its scope remains to be defined. For a review of the decision, see R. Flannigan, "Hunter Engineering: The Judicial Regulation of Exculpatory Clauses" (1990), 69 Can. Bar Rev. 514.

3 For example, several decisions have applied the unconscionability doctrine in a commercial setting: *Gateway Realty Ltd. v. Arton Holdings Ltd.* (1992), 112 N.S.R. (2d) 180, 307 A.P.R. 180 (C.A.); *Catre Industries Ltd. v. Alberta* (1989), 63 D.L.R. (4th) 74, 99 A.R. 321 (C.A.) (exemption clause upheld); reversing 97 A.R. 1 (Q.B.); leave to appeal to S.C.C. refused 65 D.L.R. (4th) vii, 105 A.R. 254*n*.

been without its critics[4] and it has generated a veritable "unconscionability" industry.[5]

As the unconscionability doctrine is reshaped in commercial settings, the debate generated over its discretionary scope needs to be reconsidered. This is the purpose of the present comment on *Atlas Supply.* Part I provides a legal analysis, and Part II an economic analysis. Part III concludes with some lessons from the decision. The debate over unconscionability and its tangled relationship with the problems of collateral warranties, misrepresentation, parol evidence and exemption clauses, are clearly important messages from the decision. These lessons should also prove valuable in helping to settle the commercial application of the doctrine.[6]

I. LEGAL ANALYSIS

1. The Facts

As part of its restructuring in Atlantic Canada, Imperial Oil, through its subsidiary, Atlas Supply of Canada ("Atlas"), began to convert its auto parts agencies into franchise operations. John Murphy, the owner of Yarmouth Equipment Ltd., was singled out as a prospective franchisee for the Yarmouth area. Before the contract was entered into, Atlas made some projections of probable future volumes of business, which turned out to be erroneous. Atlas' regional manager, John MacDougall, who made the projections, did not inform the franchisee that Atlas' head office took a less optimistic view of probable sales. The original projections were prepared by R.M. Ritchie, Imperial's national sales manager, from the head office in Toronto and estimated an annual profit of

---

4 See, for example, Donald Harris, *Remedies in Contract and Tort* (London, Weidenfeld and Nicolson, 1988); H. Beale and T. Dugdale, "Contracts Between Businessmen: Planning and the Use of Contractual Remedies" (1975), 2 Brit. J. Law and Soc. 45; V.W. DaRe, "Judicial Discretion under the Unfair Contract Terms Act: The Economics of Standard Form Exemption Clauses" (Diploma in Law Thesis, Oxford University, 1991) [unpublished].

5 The academic debate surrounding the unconscionability doctrine has generated an extensive literature. It is reviewed in J.A. Manwaring, "Unconscionability: Contested Values, Competing Theories and Choice of Rule in Contract Law" (1993), 25 Ottawa L. Rev. 235.

6 The significance of the decision is noted by S.M. Waddams in "Unconscionability, Implied Terms and Good Faith", Denault and Colton, eds., *Meredith Lectures: Franchising* (Montreal, Yvon Blais, 1992). At p. 420, he points out that "the principle of unconscionability, exemplified in the *Atlas* case, will have a far-reaching effect when combined with the principles of interpretation".

$11,000 for the Yarmouth franchise.[7] On this basis, Ritchie concluded that the franchise was not viable. However, these projections were modified by MacDougall, who presented Murphy with the modified projections instead.

The modified projections differed significantly from the original ones and were misleading in several ways.[8] For example, Murphy was not told that sales in the Yarmouth agency had been declining in recent years. A profit projection of $33,000, instead of $11,000, was presented to Murphy. Also he was not told that he would personally have to work full time to meet the profit projection, that the figure was based on him not drawing any salary from the business, and that he was expected to own an existing business. When Murphy inquired as to the source of the figures, he was told by MacDougall that they were prepared scientifically by the head office. MacDougall acknowledged that he knew Murphy would not check the projections.

Atlas also failed to review the financial position of Yarmouth Equipment Ltd. before entering into the contract. However, it requested a personal guarantee from Murphy, and had "merger"[9] and "independent investigation"[10] clauses included in the franchise

---

[7] *Atlas Supply*, *supra*, footnote 1, at pp. 31-32, paras. 142 to 144. The original projection was based on two fundamental presumptions: the franchise would operate on its own rather than in combination with an existing business and it would employ three individuals on a full-time basis.

[8] *Ibid.* The modified projections were based on alternatives considered by MacDougall, namely that the franchise operate in conjunction with an existing business, Yarmouth Equipment Ltd., that it employ two full-time employees and that the individual franchisee be the third full-time worker, although he would not draw a salary from the franchise.

[9] *Ibid.*, at p. 10, para. 43. The text of the "entire agreement" or "merger" exclusion clause was provided under cl. 2.06 of the Franchise Agreement:

> *Entire Agreement* — This Agreement, any documents incorporated by reference herein and the Schedules hereto constitute the entire agreement between the parties pertaining to the subject matter hereof and supersede all prior agreements, understandings, negotiations and discussions with respect to the subject matter hereof whether oral or written. Except as provided herein, there are no conditions, representations, warranties, undertakings, inducements, promises or agreements, whether direct, indirect, collateral, express or implied made by ATLAS to the Franchisee.

[10] *Ibid.*, at p. 11, para. 43. The text of the "independent investigation" clause under cl. 18.10 of the Franchise Agreement read as follows:

> *Investigation* — The Franchisee acknowledges that it has conducted an independent investigation of the Franchised Business and ATLAS and recognizes that the business venture contemplated by this Agreement involves business risks and that its success will be largely dependent upon the business ability of the Franchisee. Atlas expressly disclaims the making of and the Franchisee acknowledges that it has not received any warranty or guarantee, express or implied, as to the potential volume, profits or success of the Franchised Business.

The second sentence disclaiming the warranty and specifically the sales and profit

agreement. Murphy also provided a guarantee to his bank to enable Yarmouth Equipment Ltd. to secure the necessary financing for the franchise agreement. The franchise eventually failed with sales far below the modified projections.

Atlas sued on the agreement and on the personal guarantee given by Murphy. Murphy counterclaimed for damages resulting from the failure of the business. Both suits were successful. Judgment was given in favour of Atlas against the corporate franchisee Yarmouth Equipment, which was by then insolvent, and Murphy, as the individual franchisee, obtained judgment on his counterclaim.

2. Trial Judge

The trial judge held that Atlas provided grossly inaccurate information of a "viable" franchise which it knew was going to be relied upon unchecked. The projections therefore constituted a collateral warranty and the warranty was breached.[11] The "merger" clause could not be relied upon because it was in conflict with the fact that representations had been given outside the contract.[12] Also, Atlas could not disassociate itself from its regional manager, MacDougall, who had induced Murphy to enter into the contract by making the representations.[13] Neither could it rely on the "independent investigation" clause of the agreement, stating that the franchisee had made his own investigation, because it knew that Murphy had not conducted any investigation. The trial judge also found that MacDougall knew that Murphy lacked the resources and ability to conduct an independent investigation of the projections.[14]

Yarmouth Equipment Ltd. was held liable for stock purchased from Atlas in an amount agreed upon by the parties. The judge also found that Yarmouth's insolvency was not the fault of Atlas. However, in refusing to take back the stock of Yarmouth Equipment, Atlas had compromised Murphy's rights as personal guarantor of the franchise and therefore his guarantee was discharged.

---

projections is actually an elaboration of the merger clause. For the sake of clarity and to maintain a distinction between the two clauses, the references throughout this paper to the "independent investigation" clause mean the first sentence of the clause, and references to the "merger" clause include the second sentence.

11 *Ibid.*, at p. 10, para. 40.

12 *Ibid.*, at p. 12, paras. 49 and 50.

13 *Ibid.*

14 *Ibid.*

Murphy was also held to be entitled to the return of his franchise payment and to damages for his start-up costs.[15]

3. Court of Appeal

On appeal, the issues before the court were not limited to the status of the exclusionary clauses and whether the modified projections constituted a warranty. The novel issue[16] before the court indeed the central one, was whether the doctrine of unconscionability undermined the effect of the personal guarantee and commercial exclusion clauses.

(a) Majority Judgment

In holding as it did, the majority of the Court of Appeal allowed the appeal in part. First, it confirmed the lower court decision that the modified projections constituted a warranty which had been breached by Atlas. Atlas was held to be in a superior position to Murphy with respect to possessing and understanding the projected information.[17] Second, the majority held that Atlas could not rely on the exclusionary clauses because it would be unconscionable to enforce the clauses in the circumstances. Third, unlike the trial judge, the majority held that Murphy, as individual guarantor, should be partly liable for his guarantee to Atlas, but only to the extent of the value of the franchisee's inventory received from Atlas. Finally it upheld Murphy's entitlement to the return of his franchise payment and start-up costs ($23,500).

Unconscionability dominated the court's attention. The majority judgment adopted an interventionist approach under the doctrine. The leading authorities, *Morrison v. Coast Finance Ltd.*[18], *Lloyd's Bank Ltd. v. Bundy*[19] and *Harry v. Kreutziger*[20] were cited[21] with

---

15 *Ibid.*, at pp. 24 to 26, paras. 104 to 111.

16 *Ibid.*, at p. 30, para. 140. The issue of unconscionability was not pleaded or raised at trial. The Court of Appeal, however, provided a brief adjournment so that the issue could be considered.

17 *Ibid.*, at p. 10, paras. 40 to 42. As discussed in Part II, the idea of comparative advantage as it relates to risk allocation between contracting parties is an important one in law and economics literature.

18 (1965), 55 D.L.R. (2d) 710, 54 W.W.R. 257 (B.C.C.A.) (hereafter *Morrison*).

19 [1975] Q.B. 326, [1974] 3 All E.R. 757 (C.A.) (hereafter *Bundy*). Lord Denning's decision was modified and adopted in Canada as one element of unconscionability.

20 (1978), 95 D.L.R. (3d) 231, 9 B.C.L.R. 166 (C.A.) (hereafter *Kreutziger*).

21 The court referred to these decisions in *Atlas Supply* at p. 19, para. 80, as the "most frequently cited cases respecting the principle of unconscionability".

approval. Reference was also made to the decision in *Hunter Engineering* as supporting a doctrine of unconscionability even in commercial contexts.[22] Matthews J.A. also cited the leading academic authorities.[23] He acknowledged that the leading cases turned on their particular facts and that as a result it was difficult to generalize and to set guidelines for the application of the doctrine.[24]

Notwithstanding its reluctance to formulate a test, the majority was rather generous, although mechanical, in its application of the leading tests of unconscionability. The two-step process outlined by Waddams[25] and elaborated in *Morrison* was adopted and applied in a haphazard manner. Unconscionability is reduced to two basic elements under this approach — inequality of bargaining power and exploitation by the stronger party. As the court pointed out, the bargaining inequality may arise from the ignorance, need or distress of the weaker party, or the domination, undue pressure or misrepresentation of the stronger party. But inequality is only one element of the doctrine. There must also be proof of substantial unfairness of the bargain. Thus, both procedural and substantive elements were adopted by the court. However, it was also willing to dispense with formalities and apply the single, reformulated and related[26] test in

---

22 The court acknowledged, however, *ibid.*, at pp. 13 and 14, paras. 57 to 61, that the Supreme Court of Canada was divided over the issue. See, for example, *Hunter Engineering*, *supra*, footnote 2.

23 Reference was made to Waddams, *The Law of Contracts*, 2nd ed. (Toronto, Canada Law Book, 1984) at pp. 13 to 15, paras. 55, 56, 61 and 62, and Fridman, *The Law of Contract in Canada* (Toronto, Carswell, 1986) at pp. 16 and 20, paras. 66, 67, 68, 70, 71 and 84, to elaborate the principles of unconscionability.

24 The point was elaborated by Matthews J.A. in *Atlas Supply* at p. 15, para. 65, as follows: "The task of determining whether acts are unconscionable is at times difficult because the meaning of the word is far from precise. I suggest that it cannot be determined by recourse to a dictionary or precedents. Those can assist but they cannot precisely apply. The answer must be found within the particular facts of the case: the result will differ as do the facts."

25 After reviewing Waddams, Matthews J.A. concluded, *ibid.*, at p. 15, para. 62 as follows: "I am inclined to a similar approach in the instant case. We must explicitly address 'concerns of unconscionability and inequality of bargaining power' in order to determine the force to be given to relevant clauses in the agreement and, in particular 2.06 and 18.10."

26 As Matthews J.A. indicated, *ibid.*, at p. 19, para. 80: "These cases represent somewhat different approaches to unconscionability, however, all of them are interrelated. In *Morrison* the traditional view of unconscionability (pre-*Bundy*) was applied. As earlier mentioned, *Bundy* focused more on the inequality of the bargaining positions of the parties. However, all three have a similar base." With regard to the single test based on community standards of commercial morality in *Kreutziger*, Matthews J.A. at pp. 20-21, paras. 84 to 85, considered it a fairly simple test for determining unconscionability that "cut through the artificial concepts surrounding this aspect of contract law".

Kreutziger based on "community standards of commercial morality". The court therefore considered each test of unconscionability as related, and equally applicable to the facts.

So, despite its concern for certainty in commercial contracts[27] and the "sparing"[28] use of the doctrine to avoid exclusion clauses, the moral framework of the particular judge played a significant role in the application of the doctrine. This subjectivity is apparent when contrasting the fact-finding approaches in the majority and minority judgments.

For the majority, the facts of the case were clearly conducive to a finding of unconscionability. Applying the above tests, the court set aside the exclusion clauses. The first step was finding proof of inequality between the parties. For the majority, this stemmed from the lack of commercial sophistication, ignorance and precarious financial position of Murphy. As to his lack of business acumen, the court recognized that Murphy had limited education,[29] retailing experience[30] and resources for market studies and sales projections.[31] On the other hand, Atlas, as Imperial Oil's subsidiary, was considered much more sophisticated because of its affiliation with a "large corporation", its "access to substantial resources for market studies" and its "great experience in the sales field".[32] The inequality between the parties was also rooted in asymmetric information contributing to the ignorance of the weaker party and domination of the stronger. As Matthews J.A. indicated, "there is an inequality of bargaining power due to one party not being informed of all of the relevant and pertinent information".[33] Specifically, Atlas' failure to disclose the original projections to Murphy and its effort to mislead him with modified projections were held to be the main sources of asymmetric information between the parties. Combining these consideration

---

27 The concern of Matthews J.A. for contractual certainty in commercial relations was expressed in *Atlas Supply* at p. 23, para. 98, as follows: "Business people entering into a contract must have some certainty that its provisions will be applied and that courts will refrain from rewriting the contract."

28 *Ibid.*, p. 24, para. 101 (Matthews J.A.).

29 *Ibid.*, p. 4, para. 8. Murphy had a high school equivalent education.

30 *Ibid.* The court recognized that while Murphy was not new to business, he had "little or no retail experience".

31 *Ibid.*, at p. 23, para. 95. The court upheld the trial judge's finding in this regard that "Murphy did not have the resources and ability to check out the Atlas financial forecast".

32 *Ibid.*, at p. 28, para. 126 (Freeman J.A.).

33 *Ibid.*, at p. 17, para. 74. As discussed in Part II, the role of asymmetric information in risk allocation is significant in law and economics literature.

with Yarmouth's precarious financial position,[34] Matthews J.A. found Murphy to be in a position of inequality.

The second step involved finding proof of exploitation, undue influence or an unfair bargain. Again, asymmetric information, or the non-disclosure and modification of the original projections, provided the central basis for this finding.[35] The enforcement of the exclusion and independent investigation clauses would be exploitative under these circumstances. The majority found that Atlas was aware that Murphy did not independently investigate the projections and lacked the ability and resources to investigate the projections, and that he had entered the franchise agreement relying exclusively on the accuracy of the projections.[36] MacDougall encouraged this unconfirmed reliance by emphasizing the "scientific" basis of the projections.[37] The majority attacked the "merger" clause on similar grounds. Atlas could not have its "cake and eat it too" by warranting profit and sale projections it knew to be inaccurate and then protecting itself from liability under the merger clause.[38] This would produce an unfair bargain by shifting the risk of losses completely on the weaker party, Murphy.[39] The majority therefore found sufficient proof of the second element of unconscionability to strike down the exclusion clauses.[40]

In his concurring judgment, Freeman J.A. seemed to dispense with the two-step process altogether and simply applied the single "community standards of commercial morality" test of unconscionability. He bluntly characterized the transaction as "offensive to conscience".[41] He also favoured unconscionability as a stand-alone doctrine, a concept underlying other doctrines and better suited than the more anachronistic or fictitious doctrines of intervention. After reviewing the facts, he concluded that: "There are echoes here of the old doctrine of fundamental breach, failed consideration, mistake,

---

34 *Ibid.*, at p. 12, para. 47.

35 *Ibid.*, at p. 23, para. 95. As Matthews J.A. pointed out, "the appellant had information which would have dissuaded any but the foolhardy to enter into the agreement and it withheld that information from Murphy".

36 *Ibid.*, at p. 12, para. 48.

37 *Ibid.*

38 *Ibid.*, at p. 24, para. 101.

39 *Ibid.*, at p. 28, para. 129. (Freeman J.A.)

40 *Ibid.*, at pp. 23 and 24, paras. 96-103.

41 *Ibid.*, at p. 28, para. 127.

breach of collateral warranty, reliance on the seller's skill and judgment. *However the concept of unconscionability says it all.*"[42]

(b) Minority Judgment

If characterized as a "swinging pendulum",[43] the minority judgment provided a noticeable shift from that of the majority. Indeed, upon reading Justice Hallett's dissenting judgment, the reader could be excused for doubting whether the same facts were actually before the entire court. He adopted a non-interventionist approach, and viewed the franchise agreement as the result of "full freedom of contract"[44] between parties experienced in business.[45] He therefore dismissed breach of warranty and unconscionability as grounds for not enforcing the personal guarantee and exclusionary clauses. He also dismissed Murphy's claim to damages for franchise and start-up expenses. Instead, he held Murphy fully liable for his personal guarantee to Atlas in the agreed amount of $206,344 owed by Yarmouth Equipment. To reach these conclusions, Hallett J.A. took into account and interpreted facts determined by his own view of commercial morality.

On the warranty issue, he provided several reasons for refusing to characterize the sale and profit projections as a collateral warranty. First, the term "projections" was self-explanatory to the parties as experienced business people. Projection was understood to mean estimate, guess, speculation, and certainly not a guarantee of success or an "iron-clad" prediction.[46] Every business person knows how unreliable projections can be, he reminded us. Second, Atlas was not in a better position to Murphy nor did it have a comparative advantage to possess and guarantee the projected information. Instead, both parties were capable of assessing, and had the personnel for reviewing, the projected information.[47] Third, Murphy never requested that the verbal projections be expressly warranted under the franchise agreement and, given the written disclaimer, the

---

42 *Ibid.* (my emphasis).

43 The phrase is borrowed from Atiyah, *Essays on Contract* (Oxford, Clarendon Press, 1979), c. 12, p. 355. It refers to the competing ideologies that have shaped judicial and legislative approaches to contract law.

44 *Supra*, footnote 1, at p. 39, para. 164.

45 *Ibid.*, at p. 28, para. 132.

46 *Ibid.*, at p. 30, para. 138.

47 *Ibid.*, at p. 35, para. 153.

parol evidence rule governed.[48] Finally, Hallett J.A. distinguished this case from the English Court of Appeal's decision in *Esso Petroleum Co. v. Mardon*,[49] where a collateral warranty was found, on the basis that the franchise agreement in *Esso Petroleum* did not have any exclusion clauses.[50] Not only were they present in the Atlas franchise agreement, they were also incorporated into the contract *after* the verbal projections had been given,[51] were written in clear and understandable language,[52] and reflected the normal business practice of not warranting sale and profit projections.[53]

Hallett J.A. also rejected negligent misrepresentation as a ground of intervention.[54] In his view, there was no special relationship between the parties that created a duty of care on Atlas' part. This was not a contract for professional services. Rather, it was merely a standard business contract between experienced parties.[55] Furthermore, the merger clause prevented the assumption of a duty of care and therefore a claim in negligence.[56]

Hallett J.A. also dismissed commercial sophistication as a factor in applying the first step of the unconscionability test. Unlike Matthews J.A., he placed significant weight on Murphy's former ownership and partnership experiences,[57] his resources and personnel,[58] and the fact that neither party was experienced in retail sales or franchise operations.[59] Nevertheless, Hallett J.A. acknowledged that a degree of bargaining inequality existed between the parties.

---

48 *Ibid.*, at p. 39, para. 164. Hallett J.A. does not explicitly refer to the parol evidence rule.

49 [1976] 2 All E.R. 5. (hereafter *Esso Petroleum*).

50 *Atlas Supply*, at p. 30, para. 136.

51 *Ibid.*, at p. 30, para. 135.

52 *Ibid.*, at p. 30, para. 139.

53 *Ibid.*, at p. 41, para. 174.

54 *Ibid.*, at p. 29, para. 134. Although neither the trial judge nor Freeman J.A. develop the argument, there is a suggestion in *obiter* that Atlas was negligent in making the projections; see p. 29, para. 134 for comments regrding the trial judge's findings and p. 27, para. 120 where Freeman J.A. stated that "Atlas had not exercised a reasonable standard of care". Negligent misrepresentation, however, was not developed as a basis for intervention since the trial judge relied primarily on breach of warranty and Freeman J.A. on unconscionability.

55 *Ibid.*, at p. 29, para. 134.

56 *Ibid.*

57 *Ibid.*, at p. 31, para. 141. For example, one of Murphy's former companies had annual sales of approximately $1.2 million and equity in excess of $200,000. Another one of his companies owned eight apartment buildings.

58 *Ibid.*, at p. 35, para. 153. More specifically, Murphy's employees were former employees of the Atlas Yarmouth operation and, according to Hallett J.A., they would have been invaluable in the assessment of the projections and proposed franchise.

59 *Ibid.*, at p. 36, para. 155.

This alone did not satisfy the legal tests of unconscionability, however. Applying the second step of the *Morrison* test, he concluded that there was nothing exploitative or "substantially unfair" about the non-disclosure of the original projections, and the failure to warrant the modified projections.[60]

Specifically, he rejected equating asymmetric or unequal information between the parties with unconscionability. The original projections were considered obsolete and irrelevant.[61] Also, the modified projections were viewed as a risk of doing business and hardly "scientific".[62] In addition, non-disclosure of the assumptions underlying the modified projections concerning the manpower,[63] organization[64] and sales[65] of the franchise, was similarly rejected as being exploitative or unconscionable. Finally, Murphy's familiarity with the Yarmouth area, and the fact that he had a lawyer and one month to review the contract before signing it, were further considerations against a finding of unconscionability based on asymmetric information.[66] Accordingly, Hallett J.A. concluded that the second element of the *Morrison* test was not met under these circumstances.[67]

Applying the other test based on "community standards of commercial morality", he concluded, for the same reasons, that there was nothing unconscionable about enforcing the exclusion clauses in the franchise agreement.[68]

---

60 *Ibid.*, at p. 41, para. 176.

61 *Ibid.*, at pp. 37-38, para. 159.

62 *Ibid.*, at p. 38, para. 161.

63 *Ibid.*, at pp. 32 and 40, paras. 146, 168 and 169. MacDougall's failure to inform Murphy that he would have to work, employ two full-time workers, and combine an existing business for the franchise to be viable was held not to be unconscionable. No one represented to Murphy that he would not have to work, and it was Murphy's responsibility to assess the time required to supervise the combined business, according to Hallett J.A. who also held that manpower decisions were within Murphy's discretion.

64 *Ibid.*, at p. 32, paras. 145 and 146. As for Murphy not having been informed that the projections presupposed a combined rather than a stand-alone business, Hallett J.A. held that Murphy knew the franchise was to be operated in combination with his existing business and that this was obvious from the terms of the franchise agreement.

65 *Ibid.*, at p. 38, para. 163. Atlas' failure to disclose to Murphy that sales of its Yarmouth operation had been declining in recent years was not considered unconscionable. Hallett J.A. held that Murphy's employees, as former employees of Atlas' Yarmouth operation, had known this and informed Murphy, and accordingly that this allowed him to discount the sale and profit projections.

66 *Ibid.*, at p. 39, para. 164.

67 *Ibid.*, at p. 41, para. 176.

68 *Ibid.*, at p. 41, para. 174.

Despite reaching a different conclusion on the commercial morality of the transaction, Hallett J.A. did agree with the majority on one point: judicial restraint should characterize the application of the unconscionability doctrine. For Justice Matthews unconscionability should only be used "sparingly" to avoid an exclusionary clause[69] since business people entering contracts "must have some certainty that its provisions will be applied and that courts will refrain from rewriting the contract".[70] The uncertainty posed by unconscionability stemmed from the indeterminate, subjective and fact-based nature of the doctrine or, as he indicated, from a "far from precise" term that "cannot be determined by recourse to a dictionary or precedents" but instead "must be found within the particular facts of the case".[71] Not surprisingly, Hallett J.A. supported the view that courts should be very "slow to set aside a contract on the ground of unconscionability", particularly if it is "a business contract made by experienced business people".[72] This consensus on restraint, however, was more theoretical than real given the conflicting application of the doctrine, or the "swinging pendulum".

4. Unchartered Territory

The preceding review of the judgments in *Atlas Supply* indicates a reluctance on the court's part to tackle and clarify the unsettled principles of collateral warranty, parol evidence, unconscionability and misrepresentation.[73] This apparent reluctance is combined with some questionable application of these legal principles to the facts of the case.

The warranty issue provides the first example. In rejecting the existence of a collateral warranty, Hallett J.A.'s approach was rather rigid, formalistic and insensitive to the findings of the trial judge and leading case law. In applying Lord Moulton's judgment

---

69 *Ibid.*, at p. 24, para. 101.

70 *Ibid.*, at p. 23, para. 98.

71 *Ibid.*, at p. 15, para. 65.

72 *Ibid.*, at p. 30, para. 141.

73 The complexity and uncertainty of these legal concepts are well documented by several law reform commissions. See, for example, the Ontario Law Reform Commission in its *Report on the Amendment of the Law of Contract* (1987), cc. 6, 8, 11 and 12; The Law Reform Commission of British Columbia in its *Report on Parol Evidence Rule* (1979); and, most recently, the Manitoba Law Reform Commission in its *Report on Pre-Contractual Misstatements* (1994).

in *Heilbut, Symons & Co. v. Buckleton*,[74] the trial judge found a clear intention on Atlas' part to warrant the accuracy of the modified profit and sale projections. While determining intent is often difficult, the trial judge's findings were nevertheless justified. Murphy was led to believe that the projections were based on sound and reputable methods, or done "scientifically" and as a result of investigation and research. His precarious financial position, lack of resources to assess the projections and reliance on their accuracy are also important. These considerations were not given sufficient weight by Hallett J.A. and they undermine his finding that the parties considered the projections as mere estimates and nothing more. They also undermine the significance of his finding that Murphy made no request for such a warranty. In the face of verbal reassurances from MacDougall, and the expertise of a huge multinational corporation backing the accuracy of the projections, Murphy's omission becomes less significant.

As for the exemption clauses defeating the collateral warranty, such an interpretation is only plausible if the clauses are examined in isolation and on the basis of a narrow reading of *Esso Petroleum*. However, examined in a broader context, the clauses were in direct conflict with Atlas' reassurances mentioned above. They were also boilerplate clauses in a standard form contract and were not incorporated as a result of specific bargaining and negotiations between the parties. Equally unconvincing is Hallett J.A.'s distinction of *Esso Petroleum* on the basis that, unlike this case, the franchise agreement had no exemption clause. While accurate, there have nevertheless been several cases where an exemption clause was held to be nullified by the collateral warranty.[75] Hallett J.A.'s judgment would have been more persuasive if these cases had been examined and distinguished or explained. In truth, the facts in *Esso Petroleum* were strikingly similar to the facts here,[76] and it

[74] [1913] A.C. 30 (H.L.), at p. 47.

[75] See, for example, *Couchman v. Hill*, [1947] 1 All E.R. 103 (C.A.); *Mendelssohn v. Normand, Ltd.*, [1969] 2 All E.R. 1215 (C.A.); *Murray v. Sperry Rand Corp.* (1979), 96 D.L.R. (3d) 113, 23 O.R. (2d) 456 (H.C.).

[76] In *Esso Petroleum, supra*, footnote 49, at p. 14, Lord Denning held the sales forecasts to constitute a warranty under similar circumstances to the present case:

> Now, I would quite agree with counsel for Esso that it was not a warranty — in this sense — that it did not *guarantee* that the throughput *would be* 200,000 gallons. But, nevertheless, it was a forecast made by a party, Esso, who had special knowledge and skill. It was the yardstick . . . by which they measured the worth of a filling station. They knew the facts. They knew the traffic in the town. They knew the throughput of comparable stations. They had much experience and expertise at their disposal. They were in a much better position than Mr. Mardon to make a

seems problematic to distinguish *Esso Petroleum* on the ground that it did not contain an exemption clause.[77] The significant precedential value of the decision, combined with the broader context surrounding the inclusion of the exclusion clauses, therefore challenge Hallett J.A.'s refusal to recognize the existence of a collateral warranty based on the modified projections.

The majority's finding of a collateral warranty is, however, hardly enlightening. The general problem is that by assuming unconscionability "says it all", the court neglects to consider or develop other legal principles. First, like Hallett J.A., the court distinguished *Esso Petroleum* on the ground that the contract contained no exemption clause.[78] As noted above, the rigid distinction is problematic since the facts and issues in *Esso Petroleum* are similar to *Atlas Supply* and deserved fuller consideration. The majority's second omission was the failure to fully consider the parol evidence rule.[79] The oversight is disturbing since the parol evidence rule represents another ground for denying the existence of a collateral warranty,[80] and therefore should have been a central consideration of the court in finding one. The rule dictates the primacy of the written exclusion clauses over MacDougall's verbal projections on the assumption that had the oral projections been considered important they would have been written down. This is a dangerous assumption, given that the clauses were boilerplate provisions in a standard form contract and, in the absence of specific bargaining, may not have reflected the parties' intentions at all.

Nevertheless, under similar circumstances, the Supreme Court of Canada has demonstrated a strong commitment to the rule.[81]

---

forecast. It seems to me that if such a person makes a forecast — intending that the other should act on it and he does act on it — it can well be interpreted as a warranty that the forecast is sound and reliable in this sense that they made it with reasonable care and skill.

77 For a discussion of collateral warranties and their overriding effect, see McLauchlan, "The Inconsistent Collateral Contract" (1976), 3 Dalhousie L.J. 136.

78 *Atlas Supply*, *supra*, at p. 13, para. 53.

79 *Ibid.*, at p. 13, para. 54. Matthews J.A. makes a passing reference to the parol evidence rule without fully considering or explaining it and the many exceptions it has generated.

80 Based on the formulation in *Goss v. Lord Nugent* (1833), 5 B & Ad. 58 at pp. 64-65, 110 E.R. 713, the common formulation of the parol evidence rule is that where a contract has been reduced to writing, extrinsic evidence is inadmissible to add to, vary or contradict the writing.

81 *Hawrish v. Bank of Montreal*, [1969] S.C.R. 515; *Bauer v. Bank of Montreal* (1980), 110 D.L.R. (3d) 424, [1980] 2 S.C.R. 102; *Carman Construction Ltd. v. Canadian Pacific Railway Co.* (1982), 136 D.L.R. (3d) 193, [1982] 1 S.C.R. 958.

Others have been less enthusiastic and have expressed a concern about the potential hardship caused by a strict application of the rule. For this reason, many exceptions to it have been adopted by lower courts.[82] Some law reform agencies have recommended its relaxation or even abolition.[83] It is surprising that the majority in the present case neglected to give these developments the close analysis they deserved.

The omission points to a third failure — the lack of consideration given to more selective grounds of intervention. As noted, one line of exceptions to the parol evidence rule is misrepresentation, whether innocent, negligent or fraudulent. It is surprising that the court did not base its intervention on these grounds rather than

---

[82] The exceptions are numerous and some include misrepresentation, whether innocent, negligent or fraudulent; *non est factum*; partly oral and partly written contracts or oral promise as a collateral warranty; see Waddams, *The Law of Contracts*, 2nd ed. (Toronto, Canada Law Book, 1994), pp. 225-28. As the author points out at p. 227, these various techniques were brought together and put forward as a new general rule by Lord Denning in *Mendelssohn v. Normand, Ltd.*, *supra*, footnote 75. It has been followed in several Canadian cases. See, for example, *Gallen v. Allstate Grain Co. Ltd.* (1984), 9 D.L.R. (4th) 496 at p. 517, 53 B.C.L.R. 38 (C.A.) *per* Anderson J.A.; leave to appeal to S.C.C. refused 56 N.R. 233 *sub nom. Allstate Grain Co. v. Guichon*; *Canadian Acceptance Corp. Ltd. v. Mid-Town Motors Ltd.* (1970), 72 W.W.R. 365 (Sask. Dist. Ct.); *Hyndman v. Jenkins* (1981), 29 Nfld. & P.E.I.R. 331, 16 C.C.L.T. 296 (P.E.I.S.C.). The oft-cited passage from Lord Denning at p. 1218 is as follows:

> Such a statement is binding on the company. It takes priority over any printed condition. There are many cases in the books when a man has made, by word of mouth, a promise or a representation of fact, on which the other party acts by entering into the contract. In all such cases the man is not allowed to repudiate his representation by reference to a printed condition . . . nor is he allowed to go back on his promise by reliance on a written clause . . . The reason is because the oral promise or representation has a decisive influence on the transaction — it is the very thing which induces the other to contract — and it would be most unjust to allow the maker to go back on it. The printed condition is rejected because it is repugnant to the express oral promise or representation. As Devlin, J. said . . . "It is illusory to say — 'we promise to do a thing, but we are not liable if we do not do it' ". To avoid this illusion, the law gives the oral promise priority over the printed clause.

Phillimore L.J., in the same case, expressed a similar view at p. 1220: "Whether one regards that promise as a representation or whether one regards it as a collateral term of the contract, or whether one regards the contract as being partly oral and partly in writing . . . it seems to me it can make no real difference."

[83] See, for example, English Law Reform Commission, Working Paper No. 70, *Law of Contracts: The Parol Evidence Rule* (1976), recommending the abolition of the rule; Ontario Law Reform Commission, *Report on Amendment of the Law of Contract* (1987), recommending the abolition of the rule and that "conclusive effect should not be attached to merger and integration clauses" (Recommendation No. 35, pp. 161-163); Law Reform Commission of British Columbia, Report No. 44, *The Parol Evidence Rule* (1979), also recommending the abolition of the rule.

the more amorphous doctrine of unconscionability. Misrepresentations by the franchisor are a common technique for challenging franchise projections.[84] Innocent misrepresentation of the effect or content of a document, or conduct that "gives a false impression", is another basis for relief.[85] So are negligent misrepresentation[86] and the *Hedley Byrne* doctrine.[87] Still another is fraud: "fraud . . . unravels everything".[88] For example, an attempt to unjustly rely on a signed document induced by an oral statement or promise has been held to be fraudulent. This reasoning is illustrated in *Long v. Smith*[89] where Boyd C. admitted evidence of an oral promise modifying a signed document and said: "This assertion as to the whole being in writing cannot be used as an instrument of fraud; the plaintiff cannot ignore the means by which he obtained the contract sued upon, falsify his own undertaking, and, by the help of the court, fasten an unqualified engagement on the defendant."[90]

Surely the "sugar coating" of the original projections called for a closer consideration of these legal principles by the court. On the question of negligent misrepresentation, however, the court provided little analysis. Freeman J.A. seems to suggest that Atlas was negligent in the preparation of the modified projections although he failed to cite or examine any relevant case law. Both Matthews J.A. and Hallett J.A. applied the Ontario Court of Appeal's decision in *Sodd Corp.*[91] in a rather limited manner. In that case, the court applied *Esso Petroleum*, and distinguished *Nunes Diamonds*[92], for the proposition that an action for negligent misrepresentation is available even though a contractual relationship exists.

---

84 See, for example, John Southerst, "Beware of those 'sample' franchise figures" *The [Toronto] Globe and Mail*, June 5, 1995, p. B5.

85 *Free Ukrainian Society (Toronto) Credit Union Ltd. v. Hnatkiw* (1964), 44 D.L.R. (2d) 633 (Ont. C.A.).

86 *Sodd Corp. v. Tessis* (1977), 79 D.L.R. (3d) 632, 17 O.R. (2d) 158 (C.A.).

87 *Hedley Byrne & Co. v. Heller & Partners Ltd.*, [1964] A.C. 465 (H.L.). The literature on *Hedley Byrne* is extensive and a small sample includes C.R. Symmons, "The Problem of the Applicability of Tort Liability to Negligent Misstatements in Contractual Situations: A Critique on the *Nunes Diamonds* and *Sealand* Cases" (1975), 21 McGill L.J. 79; J.S. Ziegel, "Tortious Liability for Pre-contractual and Intra-contractual Misrepresentations" (1975-76), 1 C.B.L.J. 259.

88 *Per* Farwell J. in *May v. Platt*, [1900] 1 Ch. 616 at p. 623, quoted by Kellock J. in *Farah v. Barki*, [1955] 2 D.L.R. 657, [1955] S.C.R. 107.

89 (1911), 23 O.L.R. 121 (Div. Ct.).

90 *Ibid.*, p.127.

91 *Supra*, footnote 86.

92 *Nunes (J.) Diamonds Ltd. v. Dominion Electric Protection Co.* (1972), 26 D.L.R. (3d) 699, [1972] S.C.R. 769. In *Nunes Diamonds*, the Supreme Court of Canada, in a majority decision delivered by Pigeon J., held at pp. 727-28 that *Hedley Byrne* is inapplicable "where the relationship between the parties is governed by a contract, unless the negli-

By adopting *Sodd Corp.*, Matthews J.A. accepted the coexistence of tortious and contractual liability in the present case.[93] However, rather than pursue and develop negligent misrepresentation, and elaborate on the nature of that coexistence, he restricted his analysis primarily to unconscionability.

Hallett J.A. distinguished *Sodd Corp.* from *Atlas Supply* on several grounds. Unlike that decision, *Atlas Supply* involved clearly drafted exclusion clauses; the disclaimer was executed *after* the verbal projections; and there was no special relationship between the parties.[94] For these reasons the exclusion clauses were held to prevent a duty of care from arising and therefore a claim in negligence. There are several problems with this reasoning. First, it is problematic just how "clear" the technical and legal language of the clauses would have been to Murphy. Secondly, while the disclaimer did not precede the verbal projections, it was not communicated contemporaneously either. That is, no one at Atlas made it clear to Murphy, at the time the verbal projections were made to him, that they were not warranted. Given the reassurances to the contrary and the subsequent inclusion of the boilerplate clauses, it is even doubtful whether Murphy would have appreciated, at the time of signing the contract, that the representations were not warranted. Thirdly, the Supreme Court of Canada has recently rejected the restrictive approach of confining the duty of care to professionals who are in the business of giving advice.[95] It is thus difficult to accept Hallett J.A.'s use of *Sodd Corp.* as a precedent for not

---

gence relied on can properly be considered as 'an independent tort' unconnected with the performance of the contract".

93 *Atlas Supply, supra*, footnote 1, pp. 17-18, paras. 75 and 76.

94 *Ibid.*, p. 29, para. 134.

95 The Supreme Court has indicated a willingness to recognize a duty of care between contractual negotiators. Of significance is *Queen v. Cognos Inc.* (1993), 99 D.L.R. (4th) 626, [1993] 1 S.C.R. 87, where the employer's negligent misrepresentation to a prospective employee, in the course of negotiations, led to a contract of employment. The court recognized that the employer was under a duty of care not to negligently misrepresent the nature of the employment opportunity to the prospective employee. The court refused to provide a definitive explanation of the characteristics of the "special relationship" which gives rise to a duty of care but noted that the case displayed a number of relevant criteria. Iacobucci J. stated at p. 108: "It was foreseeable that the appellant would be relying on the information given during the hiring interview in order to make his career decision. It was reasonable for the appellant to rely on said representations. There is nothing before this court that suggests that the respondent was not, at the time of the interview or shortly thereafter, assuming responsibility for what was being represented . . .".

applying the principles of tortious liability for negligent misrepresentation to the present facts. Recent Supreme Court of Canada jurisprudence clearly favours a more robust role for the *Hedley Byrne* doctrine in respect of pre-contractual obligations than demonstrated by the entire court in *Atlas Supply.*

The court should have also considered much more carefully whether Atlas' actions were fraudulent. The modified projections were described variously as "mere guesswork", "unbased optimism" and "careless", but the findings fell short of fraud. The court should have considered the Ontario Court of Appeal decision in *Standard Investments*[96] at this point. In that decision, the court adopted an identification doctrine and reformulated it in a corporate context as follows: the acts and intentions of two or more officers of a company, within their respective fields of operation, are to be treated as the company's acts and intentions. This idea of combining and attributing each officer's knowledge and conduct to the company, or the "aggregation principle",[97] has the potential of broadening corporate liability. The court in *Atlas Supply* should have considered more carefully the combined conduct of Atlas' agents, Ritchie and MacDougall, to decide whether a case of fraud could be attributed against Atlas. However, as Ziegel points out, the *Standard Investments* doctrine does not impose a "blanket liability".[98] Whether it even applies to the present case is uncertain. Unlike *Atlas Supply, Standard Investments* involved a fiduciary relationship between the parties.[99]

---

96 *Standard Investments Ltd. v. Canadian Imperial Bank of Commerce* (1985), 22 D.L.R. (4th) 410, 52 O.R. (2d) 473 (C.A.), leave to appeal to S.C.C. refused 53 O.R. (2d) 663*n*, 15 O.A.C. 237*n*.

97 J.S. Ziegel, "Bankers' Fiduciary Obligations and Chinese Walls: A Further Comment on *Standard Investments Ltd. v. Canadian Imperial Bank of Commerce*" (1986-87), 12 C.B.L.J. 211 at p. 222.

98 *Ibid.*

99 The franchisor/franchisee relationship is that of independent contractors, and not of a fiduciary relationship. The leading authority is the Supreme Court of Canada decision in *Jirna Ltd. v. Mister Donut of Canada Ltd.* (1973), 40 D.L.R. (3d) 303, [1975] 1 S.C.R. 2. However, as Frank Zaid has pointed out in *Canadian Franchise Guide* (Toronto, Carswell, 1983) at p. 6-407, "this is not to say that in an appropriate case a franchisee could not argue that there is an implied fiduciary duty in a franchise relationship such that franchisors should be bound by specially imposed duties and obligations . . . The *Jirna* case can be distinguished on its facts . . . and it is interesting to speculate as to whether the Court might have found differently and implied a fiduciary duty had the franchisee in the *Jirna* case been ill-informed, inexperienced and naive".

The reason the majority failed to consider these legal principles is because "unconscionability says it all". Not only is it a stand-alone doctrine, it is a "concept" which underlies these other legal principles. Therefore, it should replace them and be paramount. There is no need to explain and elaborate breach of collateral warranty, even if it was the basis of the trial judge's decision. Atlas may have been negligent or fraudulent but there is no need to examine *Hedley Byrne* or *Standard Investments*, since "unconscionability says it all". It is surely not enough to assert that these principles are "anachronistic" and "fictitious" techniques of intervention without subjecting at least some of them, if not all of them, to analysis.

The failure to provide this analysis diverts attention from more compact solutions. *Atlas Supply* could have been decided on the more established grounds of breach of collateral warranty and misrepresentation. The additional unconscionability terminology — such as, the agreement was "offensive to conscience", regard must be had to "the particular facts of the case", and the exclusionary clause produces "an unconscionable bargain" — just confuses the analysis. What exactly was commercially immoral about Atlas' conduct? Was it the negligent preparation of the projection figures? Was it the conduct of MacDougall and/or Ritchie? Or was it the illusion of warranting projections and denying them in the same transaction? It is suggested that the selective grounds of collateral warranty and misrepresentation were more responsive to these issues than the blunt instrument of unconscionability.

The use of unconscionability as a "catch-all" principle demonstrates another flaw. Not only does it divert attention from other legal principles, it is not very predictable or certain as a stand-alone doctrine.[100] What is unconscionable obviously depends on one's perspective, and contrasting Hallett J.A.'s non-interventionist freedom of contract approach with Matthews J.A.'s interventionist paternalistic approach, it is apparent that a judge's philosophical

---

100 Leff was more eloquent about the problems of unconscionability when he pointed out in "Unconscionability and the Code: The Emperor's New Clause" (1967), 115 U. Pa. L. Rev. 485 at pp. 557-59: "One may suggest that first (and less important) it tends to permit to make the true bases of decisions more hidden to those trying to use them as the basis of future planning. But more important, it tends to permit a court to be nondisclosive about the basis of its decision even to itself . . . [W]hen you forbid a contractual practice, you ought to have the political nerve to do so with some understanding (and some disclosure) of what you are doing . . . Subsuming problems is not as good as solving them, and may in fact retard solutions instead."

starting point makes the doctrine just as uncertain and unpredictable as the other legal principles. Even when applied by one judge, however, the doctrine may be confused. For example, Matthews J.A. is not entirely consistent in his usage. At times he refers to Atlas as engaging in "unconscionable conduct", and at other parts of the decision he refers to an "unconscionable bargain".

Given this uncertainty, it is not unreasonable to turn to economic analysis for guidance and instruction.[101] Its focus on bargaining inequalities, information asymmetries, problematic risk allocations, and uncertain incentives[102] were precisely the issues before the court in *Atlas Supply.*

II. ECONOMIC ANALYSIS

The significance of economics to contract law derives from a common concern with exchanges.[103] While neither uncontroversial[104] nor uniform in its considerations,[105] the economic perspective

101 Not every one agrees on the significance of the economic approach to legal analysis. According to Manwaring, *supra*, footnote 5, at p. 295, "the theory provides little guidance to decision-making".

102 In economic jargon these problems arise when there is a "market failure" or the market deviates to such an extent from conditions of perfect competition that some intervention is justified to correct these problems. See Akerlof, "The Market for 'Lemons': Quality, Uncertainty and the Market Mechanism" (1970), 84 Q.J. Econ. 488; Beales, Craswell and Salop, "The Efficient Regulation of Consumer Information" (1981), 24 J.L. & Ec. 491.

103 Kronman and Posner, "Introduction: Economic Theory and Contract Law", in Kronman and Posner, eds., *The Economics of Contract Law* (Boston, Little, Brown, 1979) at p. 1, where the authors note: "Since buying and selling . . . are quintessentially economic activities, it would seem that economics should have something useful to say to students of contract law."

104 The economic analysis of law has been criticised on several grounds: for the indeterminacy, subjectivity and manipulability of its efficiency norm, see for example, Kennedy, "Cost Benefit Analysis of Entitlement Problems: A Critique" (1981), 33 Stan. L. Rev. 387; for its focus on unimportant values, see for example, Dworkin, "Is Wealth a Value?" (1980), 9 J. Leg. Stud. 181; and for its arbitrary exclusion of alternative ways of looking at the world, see for example, Michelman, "Reflections on Professional Education, Legal Scholarship, and the Law and Economics Movement"(1983), 33 J. Legal Educ. 197. As one law and economics scholar acknowledged: "any one-value view of the world is likely to prove, at the limit, self-defeating"; M.J. Trebilcock, "Law and Economics" (1993), 16(2) Dalhousie L.J. 360 at p. 376.

105 There is no single economic paradigm. For example, the economic approaches concentrating on the market may focus on different aspects of the marketplace: its efficiency, see, for example, the Chicago-based analysis of Kronman and Posner, *supra*, footnote 103; its failures, see, for example, the liberal-based analysis of Beales, Craswell and Salop, *supra*, footnote 102; or its informal mechanisms, see, for example, the transaction cost approach of Williamson, "The Organisation of Work" (1980), 1 J. Econ. Behaviour and Organ. 5; MacNeil, "The Many Futures of Contract" (1974), 47 Southern Cal. L. Rev. 691.

still shares a core set of principles around the concept of "efficiency".[106] It is in the context of efficiency theory that the legal issues in *Atlas Supply* are reconsidered here. The court imposed compulsory terms on Atlas: disclosure, investigation and warranty obligations. These included the obligations to disclose the original projections, investigate the franchisee's resources and financial stability, and guarantee the modified sale and profit projections. Whether this intervention was "efficient" is now considered.

1. Efficiency Theory

For an economist, "efficiency" is a term of art. It may refer to Pareto efficiency or Kaldor-Hicks efficiency. The former is concerned with private exchanges and whether both parties stand to benefit from the exchange. The latter concentrates on collective decisions and whether the gains or benefits from the decision exceed the losses or costs. Pareto efficiency measures resource allocation through voluntary exchanges such as commercial contracts, while Kaldor-Hicks measures allocations under collective decisions such as judicial or legislative intervention.[107]

More specifically, Pareto efficiency asks whether the particular exchange will make someone better off while making no one worse off. Any exchange which enhances the utility of at least one person without reducing the utility of another is said to improve social welfare. When a position has been reached where it is not possible to engage in further exchanges without someone becoming worse off, the resulting exchange is said to be "Pareto-efficient".[108]

By favouring voluntary private exchanges, Pareto economists make certain presumptions about human behaviour and the market process. Contracting parties are presumed to act rationally, individually and subjectively. The market allows them to assess a proposed exchange in light of the market price. If they are willing to pay and consent to the exchange then the exchange is considered

---

106 What follows is a rather selective outline of the economic perspective. For a fuller account of the economic approach, see Cooter and Ulen, *Law and Economics* (Glenview, Ill., Scott, Foresman and Company, 1988).

107 Harris, *supra*, footnote 4, pp. 6-10.

108 *Ibid.*

to be in both parties' interests and to enhance the wealth of society. Consequently, when two parties are observed entering a contract, the presumption is that both considered the exchange as making them better off, otherwise they would not have entered the contract. An efficient exchange or contract therefore becomes one that the parties mutually contracted for. Free exchange is presumed to move resources to their highest valued use. Of course, all this presupposes a competitive marketplace.[109]

The presumption is a rebuttable one. Economists refer to a list of market failures, and corresponding contract failures. These failures include monopoly (unequal bargaining power), externalities (third party effects) and "asymmetric" information (fraud, misrepresentation, breach of collateral warranty)[110]. In *Atlas Supply*, unequal bargaining power and asymmetric information were the central failures under consideration.

Market failures encourage corrective measures and external interference with private exchange or collective-decision making, such as legislative or judicial intervention. In *Atlas Supply*, the intervention came under the unconscionability doctrine, although other jurisdictions have passed franchise legislation to deal with informational problems. This renders the Pareto criterion of limited value because at least one person is worse off by the intervention. Economists suggest a cost-benefit analysis or Kaldor-Hicks efficiency test under these circumstances. This method asks whether those who benefit or gain from a collective decision could, in theory, compensate the losers from the decision and still be better off.[111] The question then becomes whether the net effect of these decisions maximizes social welfare.

---

109 Roberts, "Perfectly and Imperfectly Competitive Markets", in Eatwell, Milgate and Newman, eds., *The New Palgrave: Allocation, Information and Markets* (Macmillan Press Ltd., 1989).

110 Cooter and Ulen, *supra*, footnote 106, pp. 227-35. "Asymmetric" or "private" information simply means that not everyone is equally informed about a particular matter. For example, when one contracting party knows more than the other about a particular risk, the information is said to be distributed asymmetrically in the market.

111 Although Kaldor-Hicks efficiency acknowledges that some parties will suffer losses, it does not actually require the winners to compensate the losers. For a more detailed explanation of this notion of efficiency, see Fischoff and Cox, "Conceptual Framework for Regulatory Benefits Assessment" in Bentkover, Covello and Mumpower, eds., *Benefits Assessment: The State of the Art* (Boston, D. Reidel Publishing, 1986) at pp. 63-65.

While Pareto[112] and Kaldor-Hicks[113] notions of efficiency have been subjected to serious criticism, they are still instructive when applied to the jurisprudence. Considering wider notions of efficiency from another perspective can only reveal that "any one-value view of the world" (including a legal one) is likely to prove limited.[114] What follows is another view of *Atlas Supply.*

2. Applying the Economic Perspective

Contract serves several economic functions that are important in assessing the decision in *Atlas Supply.* At the heart of these functions is the certainty created by contract law. This certainty enables parties to minimize transaction costs, share risk, and incorporate difficult or idiosyncratic values. Another function relates to identifying "market failures" and providing an economically grounded set of excuses for intervention. Within a Pareto framework, imperfect information or externalities (*i.e.*, monopoly, unequal bargaining power) are likely to provide the central grounds of intervention. Whatever legal form the intervention takes, judicial or legislative, Kaldor-Hicks "cost-benefit" considerations are also important to the analysis.

---

112 Besides the general criticisms already noted, *supra*, footnote 104, there are some particular to the Pareto criterion. As Trebilcock points out, *supra*, footnote 104, at p. 365, one "objection to the concept of Pareto efficiency, even on its own terms, is that concepts of voluntariness, complete information, and (absence of) externalities upon which it is predicated are extraordinarily vague and to an important extent indeterminate". For an excellent critique of the normative justifications for Pareto efficiency, see also Jules Coleman, *Markets, Morals and the Law* (Cambridge University Press, 1988), pp. 97 to 129.

113 For a general criticism of Kaldor-Hicks efficiency, see Trebilcock, *supra*, footnote 104. More particular to this notion of efficiency are the problems it poses for collective decision-makers. Cost-benefit analysis may be difficult, if not impossible, in some instances particularly given the problem of third-party effects or externalities. Even in a contractual relationship, the two parties may not be the only ones affected by the transaction. For example, when individuals or firms suffer losses under a contract, the externalities or third-party effects may be so extensive and scattered that they are difficult to measure. Besides its mechanical limits, this efficiency criterion has also been criticized on moral grounds. For example, equity considerations rather than efficiency may carry greater weight from society's point of view. Kaldor-Hicks efficiency accepts all existing preferences, or initial distributions of wealth as given, and without ethical criteria for disqualifying certain preferences the concept can be applied to absurd ends. See, for example, Posner's discussion of the efficiency of baby markets and slave contracts in E.M. Landes and R.A. Posner, "The Economics of the Baby Shortage" (1978), J. Leg. Stud. 323; and Posner, *Economic Analysis of Law* (Boston, Little, Brown and Company, 1986) at p. 16.

114 Trebilcock, *supra*, footnote 104.

(a) Certainty

Economists gain important insights about legal rules by appraising them as incentives or disincentives to certainty in private exchanges. The compulsory terms imposed by the majority in *Atlas Supply* may be similarly viewed. With respect to the implied warranty deemed to have been given by Atlas, the court provided mixed signals by the imposition of the term. If excluded warranties are nevertheless reintroduced by judicial construction, then an element of uncertainty is introduced into business relations. There are costs attached to this uncertainty. Franchisors may have to spend money and time to review past contracts to determine the status of projections. Given their inherent unreliability, many franchisors may simply refuse to provide projections in the future if their accuracy has to be warranted. Franchisees may be encouraged to spend resources to challenge those projections previously considered immune from judicial attack under exclusion clauses. On the other hand, positive incentives may flow from the imposed warranty. Franchisors, unable to avoid projections, will be encouraged by the decision to be more diligent in the preparation of profit forecasts and this may lead to new methods of presenting projections.

The investigation and disclosure terms imposed by the majority in *Atlas Supply* may be viewed from a similar perspective. In not enforcing the "investigation" and "entire agreement" clauses, the court imposed an obligation on Atlas to investigate Yarmouth Equipment's financial status, to establish Yarmouth's ability and resources to conduct an independent investigation, and disclose the original projections. These compulsory terms also send mixed signals. On the one hand, franchisors are encouraged, during pre-contractual negotiations, to fully investigate the financial status of prospective franchisees and to disclose profit and sale projections in their entirety. On the other hand, the non-enforcement of the exclusion clauses creates uncertainty in commercial relations. This uncertainty may encourage franchisors to renegotiate previous agreements with similar clauses, and franchisees to challenge the legal status of the clauses. These are just some of the incentives and disincentives to contractual certainty under compulsory terms.

(b) Reducing Transaction Costs

Besides promoting certainty, another economic function of contract law is the minimization of transaction costs by providing

and encouraging the use of standard terms (which the parties are nevertheless free to bargain around). The standard form exemption clauses used in *Atlas Supply* provide an example. These standard terms are frequently joint welfare maximizing and save the parties the transaction costs involved in fully specifying a complete contingent claims contract.[115]

As noted above, the judicial setting of compulsory terms over standard form exclusion clauses has the potential of affecting the certainty and therefore the transaction costs of a commercial agreement. Transaction costs include legal fees, negotiation costs, the costs of researching the effects and probability of a contingency, and the costs to the parties and the courts of verifying whether a contingency occurred.[116] For economists, the closer the judicially set compulsory terms reflect the likely negotiated terms of the parties, the lower the transaction costs should be. The disclosure requirement set in *Atlas Supply* provides a good example. Had the original projections been fully disclosed, the legal costs necessary to obtain this information would have been avoided. Thus, the compulsory disclosure term set by the court, despite being in direct conflict with the "entire agreement" clause, has the effect of minimizing transaction costs by compelling the full disclosure of relevant information.

Conversely, new or compulsory terms set by the court which do not reflect what the parties would have wanted will involve higher transaction costs. These may include higher priced contracts, timely renegotiations and expensive litigation. For example, the compulsory warranty term set in *Atlas Supply* has the potential of augmenting transaction costs. Warranted information is more costly. This raises the contract price of future franchises to offset the increased costs imposed by a new warranty requirement. The forced price adjustment also raises the prospect of re-opening and renegotiating franchise agreements which had been agreed upon and finalized by the parties. The new warranty requirement and the uncertain status of the exclusion clauses also raises the possibility of future court challenges to determine the status of potentially "warranted" projections made during pre-contractual negotiations.

---

115 Shavell, "Damage Measures for Breach of Contract" (1980), 11 Bell Journal of Economics 466; Harris and Veljanovski, "The Use of Economics to Elucidate Legal Concepts: The Law of Contract", in Daintith and Teuber, eds., *Law and the Social Sciences* (Florence, European University Institute, 1984), p. 110.

116 Harris and Veljanovski, *ibid.*

These renegotiation, legal and court costs are just some of the transaction costs that may be associated with the imposition of a compulsory warranty term.

(c) Risk Sharing

Another important economic function of contract law relates to the allocation of risks. Economists identify different reactions to risk, such as risk-neutrality, risk-aversion and risk-taking. In many contracts, including the Atlas franchise agreement, there is a reciprocal allocation of specified risks to each party. Because the future is uncertain, parties may attempt to reduce that uncertainty by allocating risk *via* binding promises, for example, through the use of exemption clauses. If one party is risk averse to a future event, whereas the other party is not (being either a risk-taker or risk-neutral), there is a mutually beneficial opportunity for the risk to be borne by the latter. The party assuming this risk can almost be considered an insurer, in the sense of being better able to bear it, either by spreading its cost among other parties or by controlling its occurrence. The reward for the risk-taker is a lower contract price or better counter-promise from the other party.

Risk allocation has received particular attention in the law and economics literature. Posner has argued that in allocating liability for future contingencies, the risk should be borne "according to who can obtain the relevant information at lower cost".[117] More specifically, Priest has examined the content of various warranties to demonstrate that they are consistent with allocating liability to least cost considerations. He advances a comparative measurement as a way of determining the cheaper insurer based on which party has the most knowledge, control and information with regard to the risk in question.[118] Shavell has added to this comparative approach the idea that some parties have a "natural advantage" over some information as a result of engaging in particular activities.[119] Kronman has similarly argued that legal rules should be designed and interpreted to impose liability on the party who can more cheaply

---

[117] Posner, *Economic Analysis of Law*, *supra*, footnote 113, p. 50.

[118] Priest, "A Theory of the Consumer Product Warranty" (1981), 90 Yale L.J. 1297 at p. 1328.

[119] Shavell, *Economic Analysis of Accident Law* (Cambridge, Mass., Harvard University Press, 1987).

gather or produce the relevant information.[120] He adds an important qualification, however: information that is too costly or prohibitive to gather or produce should not have to be warranted or to be disclosed.[121]

The literature offers important insight to the risk allocations set by the court in *Atlas Supply* under the disclosure, investigation and warranty terms. Economic analysis involves determining the comparative and natural advantages that existed between Atlas and Murphy with regard to these obligations. For example, which party was the cheaper insurer of the warranted information? Which had more knowledge, information or control to meet the disclosure and investigation obligations? Was some of the information simply too costly to be gathered, disclosed or warranted? A related way to determine the efficiency of these compulsory terms is to consider the consequences of their enforcement. This aspect was discussed in the two previous sections of this paper in relation to incentives and transaction costs. A related consideration is what economists refer to as the "moral hazard" problem.[122] Will franchisees with warranted profit and sale projections become less motivated or concerned about losses because of the warranty? For economists, if a seller insures a purchaser against risks that the purchaser can more effectively control himself, the purchaser may not take the proper precautions to reduce those risks. Moral hazard is typically invoked to explain why the seller's liability for the purchaser's misuse of a product is usually excluded from contractual protection. While the moral hazard problem may be of limited value in this context because the franchisee has other incentives to make a profit and avoid loss, it nonetheless illustrates the effect judicial modifications of risk allocation can have on incentives and transaction costs.

Applying the foregoing analysis to the majority decision in *Atlas Supply* leads to the following conclusion. The disclosure requirement imposed by the court can be defended, the investigation obligation is open to challenge, and the warranty is debatable. Starting with the challenge, it seems problematic not to enforce the "investigation" clause and instead to impose an obligation on Atlas to investigate the corporate franchisee's financial stability

---

120 Kronman, "Mistake, Disclosure, Information and the Law of Contract" (1978), 7 J. Leg. Stud. 1.

121 *Ibid.*, p. 8.

122 See, for example, Ehrlich and Becker, "Market Insurance, Self-Insurance and Self-Protection" (1972), 80 Pol. Econ. 623, at pp. 641-43.

and to confirm its ability and resources to conduct an independent investigation. Murphy clearly had the comparative and natural advantage to determine whether Yarmouth Equipment could conduct an independent investigation. He owned Yarmouth Equipment and ownership suggests superior information and knowledge concerning the investigative capacity of the company. It would be much more expensive for Atlas to gather the information and determine whether Yarmouth Equipment had this capacity. Following Kronman's suggestion about costly information, Atlas should not be forced under a compulsory investigative term to acquire and process this information. The costs of the information-producing obligation would exceed the benefits under the "investigation" clause.

On the other hand, the court's imposition of a disclosure requirement on Atlas, with regard to the original projections, can be defended from an economic perspective. While the disclosure requirement was in direct conflict with the "entire agreement" clause, it nevertheless reflects the natural and comparative advantage Atlas enjoyed over the original projected information. Murphy would have had to expend considerably more resources to obtain the information on his own. The benefits of this information-producing obligation therefore exceeded its cost to Atlas.

More contentious is the court making Atlas a guarantor of its sale and profit projections. From an economic perspective this assumes that it had a comparative and natural advantage over Murphy. Given the circumstances, it probably did. Its access to Imperial Oil suggests that it had far more resources, skill and personnel than did Murphy to obtain this market information at a lower cost. This access to Imperial's pool of resources, including its larger customer base, also meant that Atlas was the cheaper insurer of the risk of the projections not materializing and the franchise suffering losses. It could more easily bear the risk by spreading the cost of the losses among other parties (*i.e.*, customers). The debatable aspect of Atlas' comparative advantage arises from the fact that Murphy had some control over the occurrence of the risk. Murphy, as franchisee, also had a degree of control over the risk of future profits and sales. The profitability of the franchise would also depend on Murphy's business abilities. Despite this shared control over the projected information, however, Atlas still had the comparative advantage in warranting the projections.

(d) Identifying Pareto Superior Exchanges and Market Failures

The preceding analysis is premised on the existence of market failure. Within a Pareto framework, the main failures justifying intervention include lack of voluntariness (*i.e.*, fraud, duress and incapacity), asymmetric or imperfect information (*i.e.*, collateral warranty, misrepresentation, unconscionability) and externalities (*i.e.*, unequal bargaining power in a monopoly situation). Judicial or legislative intervention to correct these market failures may follow. From an economic perspective, whether these corrective measures are necessary depends upon their costs in proportion to the market improvement. Arguments against such intervention frequently rest on the assumption that the costs of market imperfections are less than the costs of judicial or legislative remedies. These economic considerations related to non-intervention and intervention, whether judicial or legislative, are helpful to understanding *Atlas Supply.*

A Coasian world of no transaction costs,[123] market failures and information barriers, would support Hallett J.A.'s non-interventionist approach and strict enforcement of the parol evidence rule and exclusion clauses. The non-interventionist approach preserves the concept of freedom of contract, which is fundamental to the economist's notion of a voluntary bargain enhancing the utility of the parties, moving resources to a higher valued use, and promoting efficiency in general. Also, in respecting the risk allocation found under the exclusion clauses, the non-interventionist approach avoids the problems of uncertainty, inefficient risk allocation and negative incentives (*i.e.*, moral hazard).

In Murphy's world, however, there were serious market failures stemming from the undisclosed and exaggerated projections. Of the three market failures, the court's intervention was based primarily on asymmetric information. It did not fully consider lack of voluntariness or fraud as a grounds of intervention but, as suggested above, it should have. Nor did it address inequality of

---

[123] Much of the economic analysis is based on the seminal work of Ronald Coase, "The Problem of Social Cost" (1960), 3 J. L. & Ec. 1. The Coase Theorem asserts that, in a world of zero transaction costs, irrespective of the legal allocation of risks, the mutual interests of the parties will tend to lead them to bargain their way to the most efficient allocation of risks; that is, the risk allocation that maximizes the joint value of their respective resources, in which state, in a Pareto-optimal sense, both parties are better off.

bargaining power under the unconscionability doctrine as a problem of monopoly or lack of competition from an antitrust perspective.[124] Rather, it dealt with bargaining inequality as an information problem. Trebilcock defends this more limited inquiry. He views the antitrust inquiry as complex and beyond the institutional capacity of the judiciary.[125] On the other hand, a court is better equipped to identify and cure asymmetric information, given that it need only examine the circumstances surrounding the transaction, the characteristics of the parties and the nature of the relationship between them.[126] Given this advantage, it is not clear why the court in *Atlas Supply* did not tailor more specific legal remedies, such as breach of collateral warranty or negligent misrepresentation, to the information problem between the parties.

Despite the ability to identify information problems, the reference to institutional limitations still raises the question whether the judiciary is the most efficient mechanism for correcting the information asymmetries identified in *Atlas Supply*, and this in turn raises Kaldor-Hicks considerations. The legislative method shifts the control of informationally impaired markets from an *ex post* to an *ex ante* approach. For example, in Alberta the Franchises Act[127] provides *ex ante* protection to the public. The Act is a disclosure-registration statute requiring that the franchisor provide full, plain and true disclosure of all material facts, including projections, relating to the franchise being offered. The regulation of franchises within the ambit of securities regulation is novel in Canada and emphasizes the "public interest" mandate of the Franchises Act. Such protection is advantageous to franchisees given the expense and uncertainty associated with *ex post* civil remedies. However,

---

124 While the court in *Atlas Supply* did not explicitly adopt an antitrust test to determine inequality of bargaining power between the parties, it did make some implicit references to the market which may have influenced its reasoning. For example, the failed franchise in Yarmouth was not an isolated event, and other similar Imperial Oil franchises across the Maritimes had also failed. The court may have attributed these failed franchises to an unequal bargaining position between the parties, in a market that left each franchisee in a vulnerable position, with few alternative franchise opportunities and generally in a "take it or leave it" position. Again, the court did not explicitly refer to these antitrust considerations to determine the bargaining power of the parties.

125 Trebilcock, "An Economic Approach to the Doctrine of Unconscionability", in Reiter and Swan, eds., *Studies in Contract Law* (Toronto, Butterworths, 1980), p. 391. For Trebilcock, the courts simply lack the resources, sophistication and remedies to identify and cure structurally impaired, as opposed to informationally impaired, markets.

126 *Ibid.*

127 R.S.A. 1980, c. F-17, as amended by the Franchise Amendment Act, 1983, S.A. 1983, c. 30.

there are costs and this may explain the reason why Alberta is the only Canadian jurisdiction with franchise legislation. These include the legal costs of compliance to the franchisor and the administrative costs of the Act to the public.[128]

The non-intervention, legislative and judicial approaches each involve costs and benefits. Which is the most efficient in regulating the asymmetric information in *Atlas Supply* is debatable. It is a question of determining how the costs and benefits of each approach would operate in the particular circumstances.

However, there are more concrete conclusions to be derived from consideration of the economic perspective, and they are useful in assessing *Atlas Supply.* Was the court's intervention "efficient"? Although its imposition of a compulsory investigation term on Atlas did not, the disclosure requirement promoted efficiency. The imposed warranty term is more debatable. On one hand, Atlas had the comparative advantage to warrant the projected revenues. On the other hand, there are negative consequences to the imposed warranty, such as higher priced franchise agreements and increased transaction costs (*i.e.*, renegotiations, legal challenges). Was the non-intervention "efficient"? Market failures and corrective measures deserved closer attention. Hallett J.A. underestimated the significance of the original projections as a source of asymmetric information and therefore the importance of their full disclosure as a corrective measure. The oversight is particularly problematic in light of Alberta's franchise legislation, which suggests that public policy supports disclosure to non-disclosure in franchise situations. While the majority of the court intervened on the basis of asymmetric information, it underestimated the significance of fraud, collateral warranty and negligent misrepresentation as corrective measures.

III. CONCLUSION

The court's implicit invitation in *Atlas Supply* to other courts, and particularly the Supreme Court of Canada, to resort more often in the future to unconscionability in commercial contracts, should

---

128 These costs may explain the recent changes to Alberta's franchise legislation. Significant amendments were made to the legislation under the new Franchises Act, S.A. 1995, c. F-17.1 (Bill 33). For example, Bill 33 eliminates the registration requirements, provides *ex post* civil remedies and introduces the concept of self-government in franchising. See Zaid, *supra*, footnote 99, pp. 2-118cc to 118mm for a review of Bill 33.

be rejected. While the decision was the first at the appellate level to apply the unconscionability doctrine to a franchise agreement, it is unlikely to become a leading case.[129] Instead, it should stand alone, as an undesirable precedent. This conclusion is supported by legal, economic and public policy considerations that the court failed to consider. As a result of this oversight, important legal principles (*i.e.*, collateral warranty, misrepresentation, and the parol evidence rule) and economic principles (*i.e.*, efficiency and market failures) and public policy (*i.e.*, disclosure regulation) were either missed completely or not given sufficient weight. Until the Supreme Court of Canada has adopted and clarified the unconscionability doctrine in a commercial setting, therefore, the Court of Appeal's decision to use the doctrine as a "catch-all" leaves *Atlas* unchartered.

[129] This critical assessment may be contrasted with Frank Zaid's view of the decision. In the *Canadian Franchise Guide, supra*, footnote 99, he concludes at p. 2-620C (May):

> The *Atlas Supply Co.* case is very important in the development of the Canadian law of franchising. It represents the first case in Canada in which a higher court has applied the law of unconscionability to franchise agreements and franchise relationships, and reviewed the application of the entire agreement or exclusionary clause in light of such conduct. Quite clearly, in a well-written and well-reasoned decision, the court determined that a court has the power to, and will, in fact, intervene when a party attempting to enforce an exclusionary clause has engaged in unconscionable conduct.

tab 5

Annual Review of Insolvency Law 2003

Janis P. Sarra

THOMSON
CARSWELL

Preface

Insolvency law and litigation have now been generally recognized as being at the cutting edge. Indeed, litigation in this field involves the original concept of a class proceeding. This is so particularly when one appreciates that insolvency is an inherently chaotic condition. In large part, business decisions and legal approaches must be accomplished in "real time" for two vital reasons. First, value to all stakeholders tends to evaporate with the effluxion of time. Second, the resolution of matters in many instances is required instantly so that the salvageable parts of the operation may carry on. This may be contrasted with "autopsy" litigation where it matters little whether the issue or case generally is dealt with today, a month, or a year from now. Insolvency practitioners were also pioneers in the aspect of resolving on a timely basis many issues by immediate negotiation, the oldest (and perhaps best) form of ADR, with such negotiations taking place "in the shadow of the law". The concept of "in the shadow of the law" requires that the participants have a high degree of comfort as to the predictable outcome of a matter, whether it be based on statute or judge-made law.

Practitioners and other participants (including the judiciary) in the insolvency field have a fundamental need to be up to date with the jurisprudence, both on a theoretical and practical basis. The *Annual Review of Insolvency Law* is an important contribution in this field. As will be seen from the contributions to this first issue, current topics of significant importance are analyzed by well and justly respected practitioners and academics in a manner that will, I respectfully submit, bring a keen insight to the problems this area is presently encountering or will have to be dealt with in the near future. I believe that it will be readily apparent that the various contributions will be seen as giving a balanced view of their subject matter. This approach should be most helpful to the reader who truly wishes to gain a firm understanding and foundation of any particular issue. While some problems may be dissected under the microscope, it is very helpful that all problems are kept in perspective of an overall view of the world. That is, such things as social issues and balancing of interests are dealt with on a realistic basis and not in isolation.

Insolvency law and practice are not exercises in mere word games. Indeed this sector is one in which people are affected in very fundamental ways. Without a viable insolvency regime, a country's economic base will not be able

to reach anywhere near its full potential. It is an area in which there is constant change, both in the factors affecting economic activity and the rules engaged to ensure that the enterprise economy works smoothly. Domestic and international relations and concerns must be accommodated. The Senate Committee on Bankruptcy and Insolvency has issued its report (and recommendations) on changes to the regime in November 2003. Change is again imminent in Canadian insolvency statute law.

While having to make the disclaimer that I am a member of the editorial advisory board for this Review, I most enthusiastically recommend it to the interested reader in this area who wants to understand what the pressing problems are, the factors and considerations, pro and con, affecting these issues, and how they may play out in an integrated analysis scenario.

J. M. Farley
Justice of the Superior Court of Justice
Toronto, Ontario

IN THE MATTER OF A PLAN OF COMPROMISE OR ARRANGEMENT OF URBANCORP (WOODBINE) INC. AND URBANCORP (BRIDLEPATH) INC., THE TOWNHOUSES OF HOGG'S HOLLOW INC., KING TOWNS INC., NEWTOWNS AT KINGTOWNS INC., AND DEAJA PARTNER (BAY) INC. (COLLECTIVELY, THE "APPLICANTS") AND IN THE MATTER OF TCC/URBANCORP (BAY) LIMITED PARTNERSHIP

Court File No. CV-16-11549-00CL

ONTARIO
SUPERIOR COURT OF JUSTICE
(Commercial List)

PROCEEDINGS COMMENCED AT TORONTO

RESPONDING BOOK OF AUTHORITIES OF STEFANO SERPA AND ADRIAN SERPA

FOGLER, RUBINOFF LLP
Lawyers
77 King Street West, TD Centre
Suite 3000, North Tower
Toronto, ON M5K 1G8

Vern W. DaRe (32591E)
Tel: 416.941-8842
Fax: 416.941-8852
Email: vdare@foglers.com

Lawyers for Stefano Serpa and Adrian Serpa