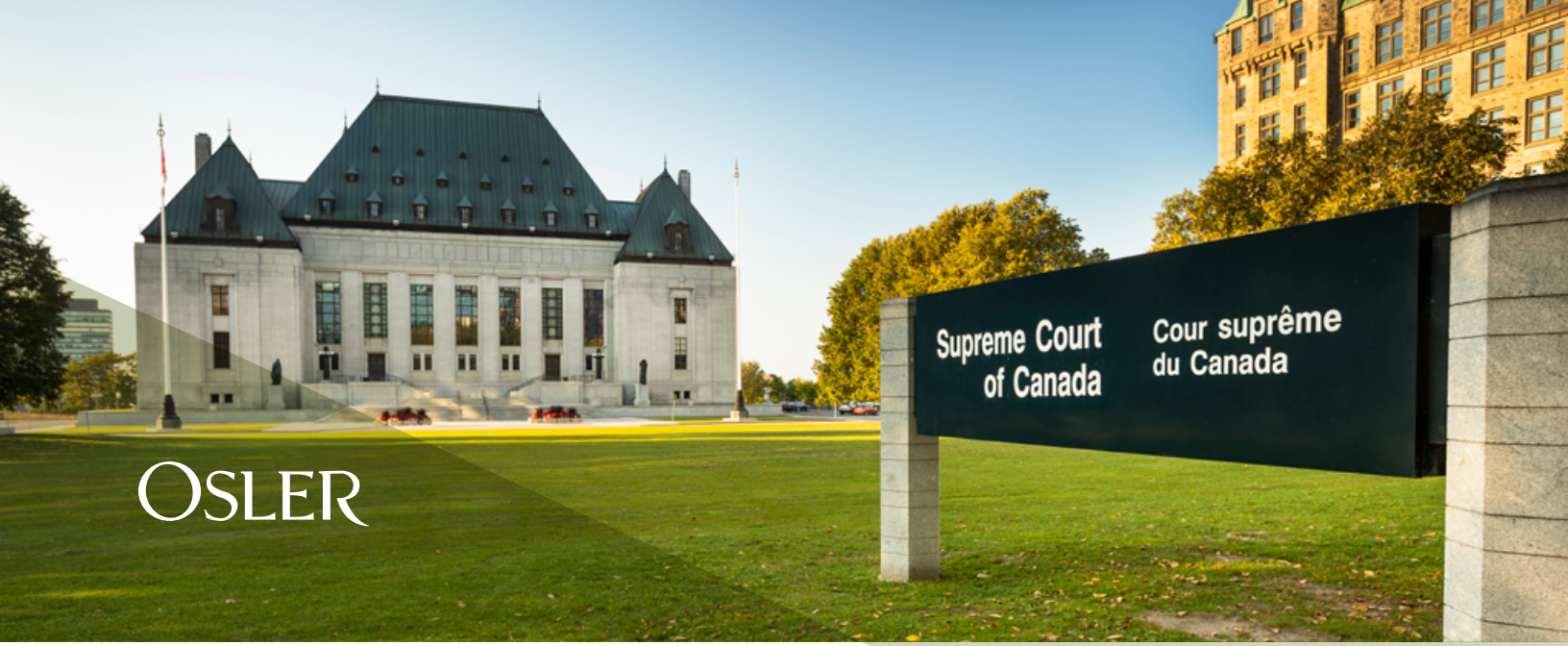

OSLER

KEY CASES

What businesses should watch for from the SCC in 2020

In 2019, the Supreme Court of Canada (SCC) heard and/or granted leave to appeal in a number of cases that could have a significant impact on Canadian business. Three such cases will address the developing doctrine of good faith performance in contract. Other cases deal with arbitration clauses, insolvency restructurings, the application of the *Canadian Charter of Rights and Freedoms* to corporations and the enforceability of provisions that impose penalties on the insolvency of a contracting counterparty.

Good faith trilogy

The SCC's 2014 decision in *Bhasin v. Hrynew,* 2014 SCC 71 (*Bhasin*) recognized a duty of honest contractual performance, which was presented as an incremental change to the common law. The decision left considerable scope for further development in this area of law. The SCC has clearly determined that the time is ripe to advance the doctrine, as evidenced by the fact that no fewer than three cases are pending before the Court.

In these three cases, the Court will consider several key aspects of the contractual duty of good faith. The guidance in these three cases could profoundly impact the standards of contractual performance for contracting parties.

i) *David Matthews v. Ocean Nutrition Canada Limited* (NS)

Status: Heard on October 8, 2019; under reserve.

Mr. Matthews worked for the respondent from 1997 to 2011. In 2011, he resigned and sued Ocean Nutrition for wrongful dismissal, seeking damages for breach of his employment contract and the loss of a Long Term Incentive Plan (LTIP). Under the LTIP, Matthews would have been entitled to a portion of the proceeds of the sale of the company if a sale occurred during Mr. Matthews' employment. Ocean Nutrition was sold in 2012, after his employment ended.

The trial judge agreed that Mr. Matthews had been constructively dismissed and awarded him substantial damages. Most of the damages were related to the loss of the LTIP because the rights under the LTIP would have crystallized if Mr. Matthews had remained employed throughout the 15-month notice period. The Court of Appeal upheld the finding of constructive dismissal but held that the trial judge erred in awarding damages pursuant to the LTIP where that plan, by its plain wording, precluded any such payment.

Avoidance of contractual limitations: The SCC is considering whether the doctrine of good faith precludes an employer from constructively dismissing an employee and then escaping its obligations under the LTIP during the required notice period. This case may have broader significance if the SCC accepts that the doctrine of good faith limits the ability of an employer to rely on the express terms of the employment contract or related agreements governing the employment relationship.

ii) *Wastech Services Ltd. v. Greater Vancouver Sewerage and Drainage District* (BC)

Status: Heard on December 6, 2019, under reserve.

Wastech Services Ltd. and Greater Vancouver Sewerage and Drainage District (Metro) were parties to a 20-year contract for the disposal of solid waste. Allocation of waste was at Metro's sole discretion. Metro's allocation negatively impacted Wastech's contractual profit margin. An arbitrator found Metro did not exercise its discretion capriciously or arbitrarily and Metro was honest and reasonable from its own perspective; however, Metro breached its duty of good faith because it lacked appropriate regard for Wastech's legitimate expectations.

On appeal, the Supreme Court of British Columbia determined that a contracting party has no free-standing obligation to exercise its discretionary power in good faith. The British Columbia Court of Appeal dismissed the subsequent appeal, holding that because the arbitrator did not find an implied term in the agreement, the duty of good faith did not apply.

Contractual discretion: Before *Bhasin*, a line of lower court and appellate cases held that the doctrine of good faith precluded a contracting party from exercising contractual discretion in a way that effectively deprives the other party of the benefit of the bargain and/or is contrary to the other party's reasonable expectations. The SCC now has the opportunity to determine whether, even though a party is exercising express rights under the contract, the doctrine of good faith limits that party's freedom to act solely in its own commercial interest.

iii) *C.M. Callow Inc. v. Tammy Zollinger, et al.* (Ontario)

Status: Heard on December 6, 2019, under reserve.

Callow provided maintenance services to condominium corporations managed by a Joint Use Committee (JUC). The JUC entered into two separate two-year maintenance contracts with Callow. The winter contract, which ran from November 2012 to April 2014, allowed the JUC to terminate it on 10 days' notice. In March or April of 2013, the JUC decided to terminate the winter contract, but did not disclose its decision. The JUC gave Callow the impression that the renewal was not yet decided. During the summer of 2013, Mr. Callow performed extra "freebie" landscaping work, hoping to convince the JUC to renew the contracts. In September 2013, the JUC gave notice of termination. Mr. Callow sued for breach of contract.

The trial judge held that the JUC breached its contractual duty of honest performance and acted in bad faith. The Court of Appeal disagreed, holding that the trial judge improperly expanded the duty of honest performance established in *Bhasin*. The duty of good faith does not impose a unilateral duty to disclose. The JUC owed Mr. Callow nothing beyond the 10-day formal notice period.

Duty of disclosure: The SCC will consider the circumstances in which the deliberate silence of a contracting party can constitute bad faith. Although the SCC in *Bhasin* held that the doctrine of good faith does not impose fiduciary-like obligations of disclosure, this case may lead the Court to conclude that there are some circumstances where disclosure of material facts is required.

The Supreme Court's guidance in the good faith trilogy could profoundly impact standards of contractual performance for contracting parties.

Other cases of interest

A number of other cases will provide the SCC with the opportunity to consider disparate themes with potentially significant implications for commercial contracting, corporate restructurings and the regulation of corporations.

i) *Uber Technologies Inc., et al. v. David Heller* (Ontario)

Status: Heard on November 6, 2019; under reserve.

At issue in this case is the enforceability of an arbitration clause in a standard-form licence agreement that mandated that disputes connected to the agreement be resolved by arbitration in Amsterdam, upon payment of a $14,000 non-refundable fee. The motion judge stayed a proposed Ontario class action alleging violations of the Ontario *Employment Standards Act* in favour of arbitration pursuant to this clause. The Ontario Court of Appeal held that the arbitration clause was unconscionable at common law and invalid as an illegal contracting-out of the basic employment entitlements established under the *Employment Standards Act*.

Enforceability of arbitration clauses: In *Seidel* (2011) and *Wellman* (2019), the SCC considered the enforceability of arbitration clauses in light of provincial consumer protection legislation and arbitration legislation. Here, the SCC has the opportunity to consider how arbitration clauses interact with provincial employment legislation, as well as the enforceability of standard form contracts with arguably onerous terms. If Uber can require disputes with its Canadian drivers to be resolved in the Netherlands, the plaintiff (who works for minimum wage) will likely have no effective remedy.

Moreover, this case could have broader significance for companies who conduct business in multiple jurisdictions and who seek to avoid the implications of local laws through carefully crafted arbitration provisions.

ii) *9354-9186 Québec inc., et al. v. Callidus Capital Corporation, et al.* (Québec)

Status: Tentatively scheduled to be heard in January 2020.

The applicants obtained protection under the *Companies' Creditors Arrangement Act* (CCAA). They sold all their assets, which were bought by Callidus, their secured lender. The purchase extinguished Callidus' secured claim against the applicants; however, it did not extinguish the applicants' litigation claims for damages against Callidus for its predatory lending practices that were alleged to have contributed to the applicants' demise, nor did it extinguish the unsecured portion of Callidus' claim.

The applicants sought court approval for a litigation funding agreement to allow them to sue Callidus. In response, Callidus sought to convene a creditors' meeting to vote on a plan of arrangement. Certain creditors, whose legal fees were to be paid by Callidus, requested that Callidus be entitled to vote the unsecured portion of its claim. This would allow it to achieve the necessary voting thresholds for plan approval, which would release Callidus from the litigation.

The Superior Court refused to order a creditors' meeting. Callidus had acted in bad faith and it should not be entitled to use its vote for an improper purpose. The Court of Appeal allowed the appeal, disagreeing that the lower court had the jurisdiction to deprive Callidus of its vote.

Creditor classification and voting in restructuring: The SCC only rarely considers cases under the CCAA. The Court has not recently considered principles of creditor classification, which arise in both CCAA plans and plans of arrangement under other statutes such as the *Canada Business Corporations Act*. A number of recent cases have raised the question of whether a creditor with specific economic or self-interested motives should be allowed to vote in the same class as other creditors, and to potentially determine the outcome of a restructuring.

The Court will also consider when a CCAA court can disallow a vote by a creditor with alleged ulterior or bad faith motives. The SCC's guidance on this point may be particularly valuable in light of the recent amendments to the CCAA imposing an express duty of good faith on any interested party in a CCAA proceeding (CCAA, s. 18.6).

iii) *Attorney General of Québec, et al. v. 9147-0732 Québec inc.* (Québec)

Status: Tentatively scheduled to be heard in January 2020.

The respondent, a private company, was charged under the Québec *Building Act* for carrying out construction work as a contractor without a licence. Under the Act, the penalty for such an offence is a mandatory minimum fine. The respondent argued that the fine violated its right to be protected against "any cruel and unusual treatment or punishment" under s. 12 of the *Canadian Charter of Rights and Freedoms*.

The Court of Québec held that it was not necessary to rule on whether s. 12 of the *Charter* applies to legal persons because the mandatory minimum fine was not cruel and unusual. The Québec Superior Court held that legal persons such as the respondent could not benefit from the protection of s. 12 of the *Charter*. A majority of the Québec Court of Appeal disagreed.

Corporate "cruel and unusual punishment": A decision by the SCC that s. 12 of the *Charter* is available to corporations could open the door to challenges under other regulatory statutes, particularly those that impose mandatory minimum fines. The application of mandatory minimum fines can give rise to large total fines that are arguably "grossly disproportionate" relative to the offender's conduct and the fine that would be imposed in the absence of the mandatory minimum.

iv) *Chandos Construction Ltd. v. Deloitte Restructuring Inc. in its capacity as Trustee in Bankruptcy of Capital Steel Inc., a bankrupt* (Alberta)

Status: Tentatively scheduled to be heard in January 2020.

A construction contract between Capital Steel Inc. and Chandos Construction Ltd. provided that Capital Steel was to forfeit 10% of the total contract price if Capital Steel became insolvent. Capital Steel became bankrupt prior to completing its contract. The issue was whether this clause was enforceable and capable of giving rise to a set-off.

At trial, the provision was held to be enforceable as a genuine pre-estimate of damages, rather than a penalty. As such, it was a bona fide commercial transaction and it was not invalid as an impermissible attempt to deprive Capital Steel of property on bankruptcy. The majority of the Alberta Court of Appeal disagreed, and held that the clause was invalid.

Penalties vs. liquidated damages; anti-deprivation rule: Provisions similar to the one at issue in this case exist in many construction and other commercial contracts. The SCC has not considered whether provisions that impose payment requirements triggered by insolvency are unenforceable because they deprive the debtor of property that should be available to creditors.

Moreover, the general common law doctrine invalidating so-called "penalty" clauses is also ripe for consideration by the SCC. A number of lower court cases have suggested that courts should no longer invalidate so-called penalty clauses that are entered into between sophisticated contracting parties. Guidance from the SCC on this point may be of considerable value to commercial contracting parties across industries.

A decision by the SCC that s. 12 of the Charter is available to corporations could open the door to challenges under other regulatory statutes, particularly those that impose mandatory minimum fines.

More to come

Also watch for the reasons of the SCC in *Nevsun Resources Ltd v. Gize Yebeyo Araya, et al.* (currently under reserve), and for the *BC Pipeline Reference* and the Carbon Tax cases (likely to be heard in 2020), discussed in more detail in our articles Chevron: High threshold for piercing corporate veil affirmed and Legislative powers, division and discontent: The provinces jostle to lead.

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