Legality and Formalities of a Contract

4

LEARNING OUTCOMES

After completing this chapter, you should be able to:

- List at least three illegal purposes that can affect the validity of a contract.
- Explain the difference between an unlawful and an illegal contract, and describe the impact on the remedy available to the parties in the event of a breach.
- Describe the difference between a simple contract and a formal contract.
- Describe at least two contract "formalities" and understand how to comply with a requirement for formalities.

Introduction

consideration
the price, which must be something of value, paid in return for a promise

In Chapter 3, you learned that the validity of a contract requires that the parties had an intention to be legally bound, that one party made an offer that the other accepted in its entirety without any changes, and that there was an exchange of **consideration**.

In this chapter, we examine two additional contract elements: legality and formalities. A contract's legality is essential to its validity.

As you will learn in this chapter, the requirement of writing applies only to certain well-defined categories of contracts.

Legality

In order to be binding and enforceable on the parties, a contract must have a legal purpose; it cannot violate any statute or violate public policy. If the contract is found to have an unlawful purpose because it violates a statute or public policy, the courts will not enforce it. The courts will declare it to be void or illegal, or both. Accordingly, you cannot take out a contract with an assassin to kill someone and then sue the assassin in court if that person fails to fulfill the contract.

The distinction between a contract that is merely void for having an unlawful purpose and one that has an unlawful purpose and is also illegal is important. If the contract is merely void for being unlawful, the court may grant some remedies to the parties who entered into it by attempting to restore them to their original positions. For example, if money and goods have changed hands but the contract is unlawful, the court may order the goods and the money returned.

However, if the contract is not only unlawful but also illegal, the court will not grant any remedies to any party who knowingly entered into it. Remedies are discussed in more detail in Chapter 9, Breach of Contract and Legal Remedies for Breach of Contract.

Example of Effects of Illegality

In the case of *Archbolds (Freightage) Ltd v S Spanglett Ltd*,[1] the court stated:

> The effect of illegality upon a contract may be threefold. If at the time of making the contract there is an intent to perform it in an unlawful way, the contract, although it remains alive, is unenforceable at the suit of the party having that intent; if the intent is held in common, it is not enforceable at all. Another effect of illegality is to prevent a plaintiff from recovering under a contract if in order to prove his rights under it he has to rely upon his own illegal act … . The third effect of illegality is to avoid the contract ***ab initio*** [void from the time it is made] and that arises if the making of the contract is expressly or impliedly prohibited by statute or is otherwise contrary to public policy. [Emphasis added.]

ab initio
from the beginning; void *ab initio*—invalid from the beginning (no rights can arise from a contract that is void *ab initio*)

1 [1961] 1 QB 374 at 388 (CA).

The principles enunciated in this case have been applied to many cases since the 1960s. The courts have also affirmed the principle that a contract cannot be saved from illegality even if it has not been pleaded by a party.[2]

Simply put, the courts will not protect a party that enters into a contract knowing that the contract is illegal and a contract cannot be saved from illegality even if it has not been pleaded by a party.

Contracts That Violate Statute Law

It is important to look closely at the wording of the statute in question to determine whether a contract that violates the statute is void or void and illegal.

- Some statutes expressly prohibit certain activities; may describe contracts that provide for such activities, and the activities themselves, as "unlawful" and "illegal"; and may impose criminal penalties, such as a fine or imprisonment. Such contracts have an unlawful purpose and may be illegal as well.
- Some statutes prohibit certain kinds of agreements; only a few will be discussed here.
- Some statutes impose requirements on certain activities. A contract that provides for activities that do not comply with those requirements has an unlawful purpose by implication.

The *Criminal Code*[3] is federal legislation that governs the conduct within society by imposing sanctions on people who act in certain specifically prohibited ways. Accordingly, a contract to commit any act prohibited by the *Criminal Code* is both void and illegal. This includes, for example, any agreement to commit murder, rob, assault, or kidnap. The courts will not enforce such a contract and will not provide any remedies to parties who enter into it. Conspiring to commit a crime is a criminal offence, and thus entering into a contract to commit a crime is a form of conspiracy and a crime in itself. Even if the crime is not carried out, the parties to the illegal contract can be charged with conspiracy. The *Customs Act*[4] prohibits contracts to smuggle, and such contracts are both void and illegal.

Some contracts prohibit activities that are contrary to the public interest. The *Competition Act*[5] prohibits business practices that unduly restrict business, such as an agreement to fix prices, eliminate competition, allocate markets, or create monopolies. Such business practices represent forms of **restraint of trade**. The Act renders illegal any contract entered into whose purpose is to engage in the prohibited

restraint of trade practices that are designed to artificially maintain prices, eliminate competition, create a monopoly, or otherwise obstruct the course of trade and commerce

2 *Song's International Holding Inc v Franchise Review Services Corp*, [2005] OJ No 1231 (QL) (Sup Ct J); *Kotello v Dimerman*, 2006 MBCA 77, 205 Man R (2d) 264; *Edwards Dean & Co v University of King's College*, 2007 NSSM 61, 260 NSR (2d) 355; *Spyglass v McCabe*, 2010 SKPC 164, 364 Sask R 240; *Stevens Pools Ltd v Carlsen*, 2015 BCPC 23.

3 RSC 1985, c C-46.

4 RSC 1985, c 1 (2nd Supp).

5 RSC 1985, c C-34.

practices. It is possible to obtain governmental approval to enter into contracts to engage in such practices, such as for mergers, to avoid violating the Act. However, without approval, such contracts are void and illegal.

The *Workplace Safety and Insurance Act, 1997*[6] prohibits any agreement between employers and employees that attempts to deprive employees of the protection of the Act. For example, a contract in which an employee agrees not to make any workplace injury claims if he or she is injured on the job is void, although it is not illegal. Contracts to sell land that violate the provisions of the *Planning Act*,[7] and in which the parties do not obtain approval from the government, are void but not illegal. The *Bankruptcy and Insolvency Act*[8] renders void, but not illegal, any contract a person enters into in which that person transfers property either as a gift or for inadequate compensation within one year before declaring bankruptcy.

Various statutes and bylaws require tradespeople and professionals to be licensed before they can offer services to the public. If an unlicensed tradesperson or professional enters into a contract for services that he or she is not licensed to provide, such a contract is void but not illegal. However, this law generally applies only to the services provided, not to any goods provided. An unlicensed plumber, then, could not enforce that part of the contract for payment for the work he or she did, but could enforce that part of the contract that provided for the supply of goods, such as pipes and fittings. However, this issue cannot be raised as a defence by the unlicensed tradesperson to the enforcement of the contract by the other party. If the unlicensed plumber did shoddy work and caused damage, the plumber could be sued for **breach of contract** by the customer. The plumber could not then claim that he or she incurred no liability under the contract because he or she was unlicensed. This is an application of the general principle that a party may not rely on his or her own wrongdoing to gain an advantage in court.

breach of contract
failure, without legal excuse, to perform any promise that forms part of a contract

Table 4.1 summarizes the kinds of contracts that violate statute law and their legal status.

TABLE 4.1 Some Contracts That Violate Statute Law

Category	Legal Status	Type of Contract	Examples
Prohibited Activities	Void but illegal	Agreements to commit any act prohibited by the *Criminal Code,* the *Customs Act*	• Murder, robbery, assault, kidnapping, smuggling
Prohibited Agreements	Void but not necessarily illegal	Agreements not in the public interest and without governmental approval (e.g., *Competition Act*)	• Agreements to fix prices, eliminate competition, allocate markets, create monopolies

(*Continued on the next page.*)

6 SO 1997, c 16, Sched A.

7 RSO 1990, c P.13.

8 RSC 1985, c B-3.

TABLE 4.1 Some Contracts That Violate Statute Law (*continued*)

Category	Legal Status	Type of Contract	Examples
Activities with Statutory Requirements	Void but not illegal	Agreements for service between unlicensed professionals and consumers, where the professional is required to be licensed to deliver services to the public (e.g., *Workplace Safety and Insurance Act, Planning Act, Bankruptcy and Insolvency Act*)	• Contract in which an employee agrees not to make any workplace injury claims if injured on the job • Contracts to sell land that violate the provisions of the *Planning Act* without government approval • Property transfer as a gift or for inadequate compensation within one year before declaring bankruptcy

Contracts That Violate Public Policy

Public policy refers to the principles and standards regarded by the legislature or by the courts as being of fundamental concern to the state and the whole of society.[9] Accordingly, contracts that violate public policy are void and may be illegal as well.

Such contracts include those designed to interfere with the administration of justice (e.g., paying a witness to give a certain kind of evidence in court), injure the public service (e.g., giving "kickbacks" to a public official), promote unnecessary litigation (e.g., paying someone to start a lawsuit to generate publicity), or suppress evidence of a crime (e.g., entering into an agreement not to report a theft if the wrongdoer pays back the money).

Other contracts may be void because they involve an agreement to commit a dishonest or an immoral act. For instance, contracts for loans that charge an unconscionably high rate of interest are void. Contracts for loans that charge an interest rate higher than 60 percent are also illegal. Contracts that involve prostitution are void. Some contracts that involve gambling are void. However, societal mores change, and some acts that may once have been considered immoral by the courts are no longer illegal.

In Canada there have been significant changes to what is considered moral versus immoral over the past few decades. Changes to societal mores regarding unmarried couples residing together, attitudes toward same-sex relationships, and, potentially, the legalization of marijuana are a few examples of how society in general has changed its perspective on the rights of people to live their lives without interference from the government.

9 *Black's Law Dictionary*, 8th ed, *sub verbo* "public policy."

The 2017 changes to the *Criminal Code* with respect to removing so called "zombie laws," which refers to outdated laws set out in the *Criminal Code* that are no longer enforced, are also examples of the change in societal mores. For example, it is no longer a criminal offence to spread false news about great men of the realm[10] because of the introduction of the *Canadian Charter of Rights and Freedoms*[11] and criminal and civil case law on defamation.

Examples of Change in Societal Mores

In the case of *Prokop v Kohut*,[12] the court stated that it would not enforce an agreement made between a man and a woman that granted the woman a half-interest in the man's estate based on the couple's commitment to live together as a married couple, although they were not married. Despite the fact that the couple lived together for 16 years, the court dismissed the woman's claim, stating that any such contract would be "void as having been made for an illegal consideration and the plaintiff can recover nothing." However, the more recent case of *Chrispen v Topham*[13] dismissed the traditional approach, with the judge stating, "In my opinion, it cannot be argued that the [cohabitation agreement] between the plaintiff and the defendant was made for an immoral purpose, and therefore, [is] illegal and unenforceable. Present day social acceptance of common law living counters that argument."

A more recent example of the change in societal mores is the case of *KK v KWG*.[14] The Court of Appeal upheld the trial court decision that the mother had breached her fiduciary duty to her daughter by not protecting her from being sexually assaulted by the child's father in the 1950s.

The trial court rejected the mother's defence argument of laches, referring to unreasonable delay in proceeding with a claim, which was upheld on appeal.

The mother argued that the daughter had lacked diligence in making her claim against the mother. The court rejected this argument, finding that the "applicable jurisprudence and policy considerations underlying it pointed strongly against a rigorous application of the doctrine of laches in an incest case."

The finding of negligence against the mother with respect to protecting her daughter from the sexual abuse of her father, and rejecting the argument that children of sexual abuse must act more promptly in commencing an action against the abuser or the parent who is a bystander, or both, is a departure from the societal mores according to which the state does not interfere with the family.

10 *R v Zundel*, [1992] 2 SCR 731, 1992 CanLII 75.

11 Part I of the *Constitution Act 1982*, being Schedule B to the *Canada Act 1982* (UK) 1982 c 11.

12 (1965), 54 DLR (2d) 717 (BCSC).

13 1986 CanLII 3568, 28 DLR (4th) 754 (Sask QB), aff'd 1987 CanLII 4616, 39 DLR (4th) 637 (Sask CA).

14 2008 ONCA 489, 90 OR (3d) 481.

In addition, it further opens the door to litigants of historical abuse to commence court proceedings with decreasing fear of losing their case because they did not act quickly enough.[15]

Business contracts can be challenged as void for containing **restrictive covenants** that constitute a restraint of trade. Non-competition covenants are often included in contracts to protect goodwill in the sale of a company, but the courts will generally not uphold them beyond the duration of the business relationship if they place restraints on trade. Provisions that continue to apply restraints after the business relationship has ended must be reasonable in scope, time, and territory.[16]

restrictive covenants
a provision in a contract that prohibits certain activities or uses of property

While these contracts may not violate the *Competition Act*, discussed above, they nonetheless may be void for violating public policy. There is a presumption at law that all restrictive covenants that constitute a restraint of trade are void. This presumption can be rebutted if the party wishing to enforce the contract can show that the restrictive covenant did not generally restrain trade.

When a business is sold, the purchasers usually want to ensure that the vendors do not engage in a business that would compete with them. The parties often include a restrictive covenant in the sale agreement that the vendors will not open a competing business for a certain period of time within a certain geographical area. If the time period and the geographical area of restriction are reasonable, the courts will uphold the contract. However, if they are unreasonable, the courts will find that the restrictive covenant is a restraint of trade and will not enforce it. What is "reasonable" depends on the circumstances of each case and the standards of the industry or business in question.

Example of a Restrictive Covenant

Newco Ltd buys a dry-cleaning business in Toronto from Oldco Ltd. In the sale agreement, Newco states that it does not want Oldco opening a dry-cleaning business anywhere in the province of Ontario for a period of 25 years. The courts would likely find that such a restrictive covenant is contrary to public policy and is therefore void. However, if the covenant stated that the restricted area was within a 10-kilometre radius from the business site and for a period of four years, the courts would likely uphold it.

Contracts between employers and employees that unreasonably restrict the employee's right to compete with the employer or to work for a competitor after the employment agreement terminates can also be void for restraint of trade. However, if the time period and geographical area are reasonable, the courts may enforce the contract. It is harder to enforce a contract of this nature than a contract for the sale

15 See Christine Adams, "Mothers Who Fail to Protect Their Children from Sexual Abuse: Addressing the Problem of Denial" (1994) 12:2 Yale L & Pol'y Rev, Art 7, for a more in-depth discussion about the development and changes around this societal more.

16 *Black's Law Dictionary*, 8th ed, *sub verbo* "restrictive covenants."

of a business because the courts are reluctant to restrict an individual from earning a living. However, it will not offend the public interest and will be enforced if the restraint is reasonable and necessary.

Restitution: A More Modern Approach to Legality Issues

Modern commentators have been highly critical of the courts' refusal to soften the impact resulting from a contract found to be void because it is illegal. There is a tendency in some recent court decisions to look beyond an automatic and rigid response to a finding that a contract is illegal and to mitigate the impact of such a finding in circumstances where the illegality is a technicality or one of the parties was innocent of illegal intent. In such cases, the courts have severed illegal parts of a contract, or introduced a concept of notional severance, in effect rewriting the parts of a contract that had made it illegal so that the contract is legal and enforceable.[17] A more recent trend has been to develop the law of restitution to put a party back in the position he or she should have been in had the contract not been illegal. The cases so far, as the example that follows illustrates, may permit restitution in cases where

- a contract is illegal and granting relief is clearly not contrary to public policy, or
- a party acted in good faith or in justifiable ignorance of whether the contract was legal or illegal.

PRACTICE TIP

Where the subject matter involves a regulated activity, such as a consumer transaction, an extension of credit, or an activity requiring licensing, it may be wise to obtain legal advice about legal limits on the activity prior to entering into a contract. While the court may forgive an unwitting innocent straying into an area of illegality (as in the Case in Point feature below), it will still impose a "reasonable person" test, and a reasonable person might well be expected to obtain legal advice, particularly in commercial transactions subject to regulation.

17 *Transport North American Express Inc v New Solutions Financial Corp*, 2004 SCC 7, [2004] 1 SCR 249; *William E Thomson Associates Inc v Carpenter*, 1989 CanLII 185, 69 OR (2d) 545 (CA). More recent decisions on the issue of notional severance include *Shafron v KRG Insurance Brokers (Western) Inc*, 2009 SCC 6, [2009] 1 SCR 157; *Schnarr v Blue Mountain Resorts Ltd*, 2017 ONSC 114.

CASE IN POINT

Can a Party Obtain Relief When a Contract Is Held to Be Illegal?

From: *Still v MNR*, [1998] 1 FCR 549, 1997 CanLII 6379 (FCA).

In this case, Still had married a Canadian citizen and immigrated to Canada to join her husband. Having applied for permanent resident status, she was provided with a document that stated she would be granted permanent resident status and that the document declared her eligible to apply for employment and/or student status. Still assumed this meant that she could work without needing to do anything further, and she did so from May to October 1993, when she was laid off. In September, she received her permanent resident status. In October, after she was laid off, she applied for employment insurance. Her claim was denied on the ground that her employment contract was void because she was not technically a permanent resident until September. Although her employment contract from September to its termination was valid, it was not a long enough period to support a claim for employment insurance.

Still appealed this decision to the Tax Court, and then to the Federal Court of Appeal. The latter court noted that the classic model, in which the contract is strictly unenforceable, was no longer persuasive as it was far too rigid and ill-suited for solving the problem at hand. The court favoured the following principle, to be applied on a case-by-case basis: "where a contract is expressly or impliedly prohibited by statute, a court may refuse to grant relief to a party when, in all of the circumstances of the case, including regard to the object and purposes of the statutory prohibition, it would be contrary to public policy, reflected in the relief claimed, to do so." Consequently, the court should look to those "policy considerations which outweigh the applicant's *prima facie* right to unemployment insurance benefits." The court then went on to find that Still had acted in good faith without stealth or deception. Nor was there a penalty for her breach of the *Immigration Act*. Lastly, the court found that the deprivation of employment insurance benefits was disproportionate to the breach of statute and ordered restitution in the form of payment of employment insurance benefits.

Form and Writing Requirements

Formal and Simple Contracts

Contracts can be classified as either **formal contracts** or **simple contracts**. Formal contracts, also called deeds, are in writing and sealed by the promisor.[18]

Deeds were the first type of contract to be recognized as valid, enforceable contracts. A deed is a legal document that is an official record of an agreement or official proof that someone owns land or a building. The early common law did not recognize most promises, in whatever form, for the purpose of enforcement. However, if a contract was written and sealed by the promisor, the formal act of applying a seal to the document was seen as evidence of a serious intention to make and keep a promise. Contracts under seal were the first to be enforced by the courts.

formal contract
a contract that is in writing and sealed by any party who is a promisor; also called a "deed," and in English law sometimes referred to as a "covenant"

simple contract
a contract that can be oral or in writing and that is not a formal contract

18 For cases examining a simple contract, see *Pollier v Laushway*, 2006 NSSC 165, 244 NSR (2d) 386; *Jack v Canada (Attorney General)*, 2004 CanLII 6217, [2004] OTC 706 (Sup Ct J).

Law in Practice

Types of Contracts

Formal contracts (*deeds*) must be in writing and under seal. As discussed in Chapter 3, Formation of a Contract, a seal is required to enforce a promise made if there is no consideration, also known as a **gratuitous promise**. For example, if I promise to give you my car as a gift, there is no consideration because you are not required to do anything to obtain the car. For this gift to be enforceable by you, I must make the gift in writing and under seal, or you must successfully argue the principle of **promissory estoppel**, meaning that I cannot unfairly retract or deny my promise to you if you have relied on it. Accordingly, I can change my mind about giving you my car, but, if I do, you may be successful suing me for it if I put the promise in writing and under seal, or you can convince the court to stop me from reneging on my promise under the doctrine of promissory estoppel. This type of contract is enforceable because of its form, regardless of its contents.

Simple contracts

- *may* be oral agreements;
- *may* be in writing; and
- if required by the *Statute of Frauds* or other legislation, *must* be in writing and signed by the parties who have made promises that are meant to be enforced if breached.

gratuitous promise
a promise made in exchange for nothing; a promise not supported by consideration

promissory estoppel
a rule whereby a person is prevented from denying the truth of a statement of fact made by him or her where another person has relied on that statement and acted accordingly

Contracts that are not formal contracts are called simple contracts. "Simple" does not refer to the complexity of the contract. A simple contract can be very complicated and may go on for pages. It may be oral or in writing. In the medieval period, the common law courts would not recognize simple contracts as worthy of enforcement.

However, by the end of the 17th century, the law was well on its way to enforcing all simple contracts and abandoning prescribed formality requirements altogether. Today, simple contracts do not depend on any particular ceremony or prescribed form to be enforceable. However, there are some areas of contract law where enforceability depends on meeting some formality requirements.

As you will learn in this chapter and Chapter 5, Capacity to Contract, contracts of certain types that cover certain subject matter must be in writing and signed by the party or parties to be bound to be valid and enforceable. In addition, when a contractual promise is made by one party to another without any valuable consideration, a seal is required. In the absence of consideration, the seal is still seen as evidence of a serious intention to create legal relations.

FACT SCENARIO

From: *2316796 Ontario Inc v Chetti*, 2016 ONSC 5216.

Two parties came to an Agreement of Purchase of Sale of a restaurant. The applicant, Dusan Varga, and respondent, John Chetti, operated restaurants in the same building, one leased and one owned. The agreement was that Chetti would lease Varga's establishment and buy the assets of the business for $125,000. The Agreement of Purchase of Sale was signed after the closing date and was conditional on the landlord's consent to an assignment of lease.

Varga alleged that Chetti had agreed to pay rent pending the landlord's consent to the deal but did not do so, and that Chetti did not proceed with the agreement after the consent was given. Chetti argued that Varga had failed to deliver an assignment of lease by closing day, and therefore Chetti was not in breach.

1. Was the agreement binding on the parties?
2. Can Chetti rely on a claim that the assignment was conditional on rent being paid if he and Varga were the ones responsible for the rent?
3. Does it matter that the Agreement of Purchase and Sale was signed after the closing date?

The Statute of Frauds

The *Statute of Frauds (An Act for the Prevention of Frauds and Perjuries)*[19] was enacted in England in 1677 and adopted during the colonial period in Canada and the United States. Initially designed to introduce order and stability to the law regarding long-term leases and other land rights, it has long been regarded as an anachronism and has been repealed in England. Sections 1–4 are still relevant to the law of contract today in most parts of Canada, except for British Columbia, Quebec, and Manitoba.

The *Statute of Frauds* requires that certain types of contracts be in writing and be signed by the parties who are to be bound by their promises. Such contracts do not necessarily have to be made under seal unless there is an absence of consideration. The *Statute of Frauds* also covered certain situations that are now dealt with by simple contracts. Because of the Statute, these contracts must be in writing. The specific types of contracts that must be in writing to comply with the *Statute of Frauds* are discussed in different chapters in the book according to the particulars of that type of contract—for example, contracting with minors.

Technical Requirements for Written Contracts

The *Statute of Frauds* requires that an agreement be in writing. Whether required by the Statute or generally, the following considerations apply. A formal document drafted by lawyers is not necessarily required. The contract can consist of written

19 (1677), 29 Car II, c 3.

notes on the back of a menu or on a restaurant tablecloth, or an exchange of letters, faxes, or emails. Whatever the form, a written agreement, whether it is one document or several letters between the parties, should

- identify the parties to the contract by name or by description;
- identify the terms of the contract, including the offer that has been accepted and the consideration to be given;
- be signed by the party whose promise is being enforced—it is not necessary to have other parties' signatures if the agreement is not being enforced against them; and
- include a printed or stamped signature, which may suffice in place of an actual signature. An actual signature is preferable if there is an issue about whether a party actually "signed" an agreement.

PRACTICE TIP

If you have to draft or review written contracts, keep a checklist like the one above but customize it to your own specific requirements. Use it to see that all necessary elements are present.

Formal contracts (deeds) must be in writing and under seal, which means that the document should be signed by the persons being bound with a gummed paper seal or a wax impression attached next to the signature. Drawing a circle next to the signature and labelling it "LS," Latin for *locus sigilli*, which means "the place of the seal," is sufficient evidence that the document is meant to be under seal. It is also usual for the document to be signed by the person who witnessed the promisor signing and affixing the seal to the document.

FIGURE 4.1 ***Locus Sigilli***

Signatures are not legally required in theory but are invariably present because seals are usually gummed and do not by themselves identify the person to be bound. When contract law was developing, seals were usually made by impressing a signet ring with a person's identifying sign or coat of arms into hot wax applied to the document. This is obviously no longer done because most people do not have coats of arms, signet rings, or seals, or carry around hot wax.

PRACTICE TIP

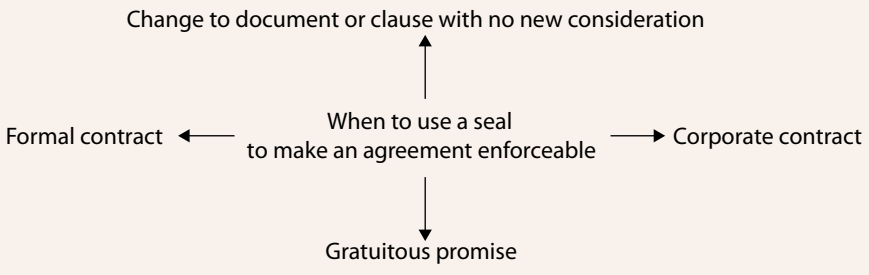
Don't have a seal? Draw a circle on the page where the seal would be affixed, and write "LS" inside the circle. This may be evidence that the document was intended to be under seal. As an alternative, you can also write, where the seal would be affixed, "This document is, and is intended to be, under seal."

The existence of the seal indicates that the party signing the document intends to be bound by the agreement even when he or she receives no consideration from other parties, as in cases where the promisor is promising a gift to someone. This can be important if, as in tax cases, it matters that a conveyance of something is meant to be seen as a gift and not something else.

Must the seal be affixed for the contract to be enforceable? The fact that a person has gone to the trouble of affixing a seal is, in theory, evidence of serious intent, so that validity and enforceability arise from the solemn form of the agreement itself. In most cases, evidence that the document was intended to be sealed will suffice to make it a deed and have it enforced as if it were a deed. However, a person may not have used a pre-written or prepared form with the word "seal" on it, as it defeats the purpose of a seal being used to demonstrate that the person has put his or her mind specifically to that clause. However, there are still cases where some evidence that seals were affixed, even if they later fell off, is required.

If a corporation or other legal "person" who is not an individual, such as a government department, is a signatory to a contract, it usually will execute an agreement using a corporate seal that identifies the corporation by name. Some statutes require that a signing officer of the corporation sign his or her name next to the seal. Often, the seal alone or the signature of a corporate officer is sufficient. Legislation governing business corporations in many jurisdictions no longer requires a corporation to have and use a seal.

FIGURE 4.2 When to Use a Seal



Generally, most contracts need not be witnessed unless there is some statutory requirement. However, it is a good idea to have the signatures witnessed so that proof of a signature on the contract can be more readily obtained if required. For some deeds, witnesses are required, and an **affidavit of execution** by the witness may also be required in which the witness swears that he or she was present and saw the party sign the document. This is the case with Wills. In this situation, the affidavit of execution itself becomes evidence that a party to the contract signed it.

affidavit of execution a sworn statement in writing, signed by the witness to a contract, stating that the witness was present and saw the person signing the contract actually sign it; the affidavit can be used to provide that a party to a contract actually signed it

Protecting Weaker Parties

From the 17th century on, the development of modern contract law was driven by the needs of an expanding trading, manufacturing, and banking economy. These needs included a legal system that would enforce commercial agreements without interfering with the bargaining process that led to them. The common law met these needs by interpreting commercial agreements and enforcing them. The courts rarely inquired into the process that led to forming a contract; they assumed that in commercial agreements business people were roughly equal in bargaining power and could look after themselves. The presumption is that business parties who are strangers to one another and enter into a business arrangement intended to create a legally binding relationship that would be enforced by the courts. If a party made a bad bargain because he or she was not as sharp or clever as the other party, that was his or her misfortune. This is contrasted to parties who are family, and some situations involving friends, where the rebuttable presumption is that they did not intend to create a legally enforceable relationship.

Although this "hands-off" approach is the one usually taken in contract law, the courts do sometimes intervene where parties are clearly unable to protect themselves in the bargaining process. This can occur because one party lacks the intellectual capacity to protect himself or herself; the other party acts dishonestly during the bargaining process or takes advantage of a position of trust; or the other party takes unfair advantage of expert knowledge of the subject matter of the contract that the weaker party does not have. Another situation in which the courts may interfere in a contractual relationship occurs when failure to do so would lead to an unconscionable result. Often there is interplay between these considerations. Some of the circumstances in which the courts protect weaker parties where the capacity of a party to enter into a contract is at issue are discussed in Chapter 5, Capacity to Contract.

CHAPTER SUMMARY

This chapter discussed two issues that can affect the validity of contracts: legality and the presence, or absence, of contract formalities.

Legality

In order for a contract to be valid, it must not have an unlawful or illegal purpose. A contract with an unlawful or illegal purpose is void (unenforceable) at law.

Although courts will not enforce an unlawful contract, they will in some cases order that the parties be returned to their original positions—for example, by ordering money paid to be returned. If the contract is illegal, however, the courts will not make any attempt to "undo" the breached contract. Apart from contracts that have a purpose that is criminal or obviously immoral, which are illegal, the distinction between an unlawful and an illegal contract is not always obvious. Where a contract is prohibited by statute, the statute will sometimes identify the contract as illegal and void, or as merely void.

The two main ways in which a contract can be unlawful or illegal are (1) by violating the provisions of a statute, or (2) by being contrary to public policy. An example of a contract that is unlawful because it violates statute law is a contract between an employer and employee through which the employee promises not to exercise his or her rights under the Ontario *Workplace Safety and Insurance Act, 1997*. An example of a contract that is illegal because it is contrary to public policy is a contract offering a bribe to a public official in exchange for a special privilege that would not otherwise be granted.

Formalities

Contracts can be grouped into two categories: simple contracts and formal contracts. Formal contracts, also called deeds, are in writing and under seal. Simple contracts may be oral or in writing, but they are not formal contracts, usually because they are not under seal. Although many oral contracts are enforceable, some contracts must be in writing and, in some cases, under seal as well.

An example of a contract that must be under seal is a contract that promises a benefit without requiring consideration in return. If not under seal, such a contract is not enforceable; however, the contract can be enforced, despite lacking what is normally an essential requirement of consideration, if made under seal.

The Ontario *Statute of Frauds* requires that certain contracts be in writing. Those particular contracts are discussed in various chapters throughout this book. To prevent rigid and unfair application of this rule, which requires written contracts, the courts have developed some exceptions where there has been part performance by one party.

REVIEW QUESTIONS

1. What is the difference between a contract that has an unlawful purpose and a contract that is illegal?
2. Describe two instances where a contract would be void for violating a statute.
3. Describe two instances where a contract would be void for violating public policy.
4. What is a restrictive covenant?
5. What are the formality requirements for a contract that is a deed?
6. Is it a good idea to have a signed contract witnessed? Why or why not?
7. What does the phrase "inequality of bargaining power" mean?

EXERCISE

1. Viktor owns a movie theatre that shows unusual and little-known movies. He wants to generate publicity to attract audiences to a movie he is showing that is particularly violent and frightening. He enters into a contract with Louise whereby Louise will come to his theatre and pretend to faint during the movie. She is then to sue him, claiming damages for nervous shock and stress. Viktor agrees to pay her expenses for the lawsuit and an additional $5,000. Louise fulfills her part of the contract. The lawsuit is well publicized, and even though Louise loses her lawsuit, people flock to see the movie in droves. Viktor never pays Louise the $5,000. Can she enforce this contract? Explain.