

1 Introduction

I. Introduction to Commercial Contracts 2

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Agreements keep the world in motion, and nowhere is this more true than in business. In Canada, no one dares manufacture a product or provide a service for a customer, or pay for either, without first having made an agreement. But not just any kind of agreement: a contract.

A contract is a special agreement, for just one reason. The Canadian legal system will enforce a contract. If one party to a contract will not carry out its obligations under the contract, the other party has the right to commence legal action and, if successful, will have the full force and majesty of the law behind it to require performance of those obligations or payment of damages to compensate for non-performance.

That's the good news. The bad news is that the Canadian legal system is fussy about exactly what constitutes a "contract," and about how it will interpret the wording of a contract once made.

Imagine that you have made an agreement with another person to provide a service in exchange for payment; you provide the service and then lo and behold the other person refuses to keep its end of the bargain. Off you trot to court in righteous indignation ... only to be told that no court will enforce your agreement. It has failed in some way to meet the necessary standards. And there are many necessary standards! Here are just some of the reasons you will not be able to enforce an agreement in court:

- One of the parties did not provide "valuable" consideration;
- One of the parties did not have the legal capacity to enter into a contract;
- The agreement was illegal;
- The agreement's provisions were uncertain.

Now imagine something different: that you have an enforceable contract, but you can no longer perform it for certain reasons. You tell the other party you're quitting. The other party says it will sue the pants off you. Can it do that? It depends.

- The other party has no right to sue you if the contract gave you the right to terminate before it was completed.
- The other party also has no rights against you if forces beyond your control, such as a hurricane flattening your factory, have deprived you of the ability to carry out the contract.
- However the other party can sue you and get an award of damages against you if the contract gave you no right of termination before it was completed, or if you had to close your factory simply because you couldn't get the bank loan you needed to keep it running.

Or imagine this. You have an enforceable contract that says that in the event of litigation between the parties, the party that loses the litigation will pay the full

legal costs of the party that wins, in addition to whatever damages the court awards. Somehow this did not seem unfair or unreasonable when you signed the contract, and you've signed contracts with similar language before and there was never a lawsuit ... but *this time* there *is* a lawsuit, and you lose the court case. The judge awards damages to the other party. But then the judge says that you, the losing party, do not have to pay any legal costs incurred by the winning party because of the winning party's reprehensible behaviour related to the lawsuit. Nevertheless, the contract is still enforceable. You have to do what you promised in the contract. The winning party grins at you and brandishes its legal bill in the tens of thousands of dollars.

We could play this game for hundreds of pages. In fact, that's what ordinary contracts textbooks do. They set up all the things that can go wrong with a contract—and frankly there is no limit to the things that can go wrong with a contract—and the horrendous consequences for at least one of the parties (and not infrequently both of them).

But even this short exercise in using your imagination should be warning you that *whatever is written in a contract is extremely important and has real-world consequences*.

The message? That anyone who reviews and negotiates a contract must (1) know the principles of Canadian contract law; (2) understand the meaning of the language in a contract; and (3) fully understand the relationship between contract language and contract law.

A. A Standard Law of Contracts

Discussion of the “fundamental” principles of common law has often been very difficult. In part, this difficulty is caused by the fact that the principles of the common law are constructed out of a backwards look at what has been done in the individual cases that have been identified as the “raw material” for the principle, i.e. the cases whose results and reasons for decision are considered—especially the “leading cases”—in developing the principle. ... Perhaps the principal source of the difficulty is the fact that the form of any statement of a “fundamental” principle can differ depending on the theoretical and philosophical views of the judges.¹

You can say that again!²

1 Angela Swan & Jakob Adamski, *Canadian Contract Law*, 3rd ed (Toronto: LexisNexis Canada, 2012) at 27.

2 And in fact Swan and Adamski do say that again, at 29: “The common law seldom starts from a statement of principle: its principles, such as they are, are constructed out of a backward look at what has been done to see what, if any, generalizations, can be made from the ‘wilderness of single instances.’”

Most contracts professionals, if asked, will probably confess that they are essentially self-taught. Out of the welter of leading cases they read in a contracts law course (if indeed they took a contracts course; many individuals working as contracts professionals have not—and you the reader may even be a business owner acting as your own, untaught, contracts professional) and what they’ve picked up afterwards along the wayside, they have constructed their own personal law of contracts. The result is that when contracts professionals negotiate a contract, they are often in conflict about what the law actually says about any given issue. A negotiation about a principle of law frequently has to precede negotiation of a particular provision in a contract.³

There *are* standard principles of the law of contracts, and they are the same for everyone, just like family law or bankruptcy law is the same for everyone. If you are not familiar with the fundamental principles of tort law, that doesn’t give you the right to make up new torts whenever you feel like it. (Anyone for the tort of cellphone snubbing?) And if you do not understand the principles of contract law you cannot draft contracts on your own principles. The only reason contracts professionals sometimes get away with doing just that is the ignorance of other contracts professionals.

If You Want to Know the Law, Don’t Ask a Lawyer, Ask a Bank Teller

Not many years ago I received from my client a contract in which the named Counterparty was an unincorporated association. (If this does not seem like a problem to you yet, please go to Chapter 4, Section III, “Who Does and Who Does not Have the Legal Capacity to Enter into a Contract?”) I called up the contracts professional acting for Counterparty and told him that Counterparty had no legal capacity to enter into a contract. Strongly (verging on rudely) questioning my objection to Counterparty, he replied that mine was the 12th of 12 contracts relating to the same project that Counterparty had already entered into with different parties, and every one of them had accepted Counterparty as a proper party and had executed the agreement.

3 Nevertheless, the courts demonstrate a rather touching trust in the work of contracts professionals, often treating the wording of a contract as though it had been carefully considered from every possible angle and altitude by the parties—when in reality there is a good chance that neither party noticed the language at all, or each party thought it meant something different. A not-atypical comment from the bench (in interpreting a provision) is “[It] would have been a simple matter for the draftsman to have used the word ‘exclusive’ if that was what the parties had intended.” See *Old North State Brewing Co Inc v Newlands Services Inc*, 1998 CanLII 6512 (BCCA).

Well, I responded diplomatically, perhaps none of those parties had a lawyer reviewing the contract. They all had lawyers, he answered. Later in the course of our conversation he admitted that a humble bank teller had made the call months ago, refusing to open a bank account for the unincorporated association. Yet Counterparty had gone ahead regardless. I think it was at the end of that phone call that this book became a twinkle in my eye.

B. A Prudent Law of Contracts

Although there are identifiable standard principles of contract law, contracts textbooks are awash in Hail Mary Pass case law generated by litigators clutching at the hope of winning a dismal case. It's not always easy to tell the difference between the two. This book will almost entirely ignore controversial and last-chance case law. (If you need it, look in *other* contracts textbooks.) This book will instead set out the straight and narrow path, a conservative and safe statement of Canadian contract law in the commercial context, suitable for contracts professionals praying that the contracts they are reviewing will never be dragged into court and thence into case law or a contracts textbook.

C. A Realistic View of Contract Language

Besides the differing views of judges in contract law cases, there is another problem facing the contracts professional, as opposed to the litigator. Contracts law textbooks are written and contracts law courses are taught (whether author, teacher, and students realize that or not) from the point of view of litigation—not from the point of view of a contracts professional sitting down to review a contract.

Contracts case law almost never contains an actual contract. In fact, apart from small snatches of contract provisions quoted in a case here and there, students of contract law can easily complete a course—or read a textbook cover to cover—without having a clue what a contract looks like. There is a *huge* difference between reading case law about contracts and reading wild contracts in their natural habitat.

Contracts case law tells a story (usually dramatic). The law often seems to emerge from the plot rather than from a contract. You may remember affectionately that:

- If you advertise your product, a carbolic smoke ball the inhalation of which is intended to prevent influenza, not merely by saying, “Buy it, it works,” but by offering 100 pounds to anyone who (1) buys the product (2) uses it as specified and (3) contracts influenza, you have crossed the line from advertising to making an offer—and you can end up with a contract

that is enforceable against you. It was thus that you learned about offer and acceptance.⁴

- If at the request of your uncle you refrained from smoking, drinking, swearing, and playing cards or billiards until age 21 on his promise that he would pay you 5,000 pounds, you ended up with an enforceable contract against your uncle.⁵ It was thus that you learned that consideration does not have to be positive but can take the form of a detriment. You may even have pressed further on into consideration and discovered that if you take care of a shipwrecked man who washes up on your beach and nurse him back to health at your own expense, you have no right of action on the recovered man's promise to repay you because such a promise is a moral obligation, insufficient consideration to support a contract.⁶
- If as a strip mining company you agreed to restore the landowner's land to its original form after you destroyed it by strip mining, when you refused to restore it you only had to pay in damages the difference between the value of the land in its present state and in its restored state—not the cost of restoring it. It was thus that you learned about measure of damages in contract.⁷
- If you rented out your ideally located flat to someone whose sole purpose was to watch a coronation parade from it, but the coronation was cancelled because the new king had an attack of appendicitis, you could not collect the agreed amount of rental. Thus it was that you learned about frustration of contracts.⁸

And so, educated and prepared you sallied forth to review your first contract. But the whole thing looked like this:

The waiver or acquiescence by any party or the failure of any party to claim a breach of any provision of this Agreement will not be deemed to constitute a waiver with respect to any subsequent breach of any provisions hereof. No condoning, excusing, or overlooking by any party of any default, breach, or non-observance by any other party at any time or times in respect of any covenants, provisos, or conditions of this Agreement shall operate as a waiver of such party's rights under this Agreement in respect of any continuing or subsequent default, breach or non-observance, so as to defeat in any way the rights of such party in respect of any such continuing or subsequent default or breach and no waiver shall be

4 *Carlill v Carbolic Smoke Ball Co*, [1893] 1 QB 256.

5 *Hamer v Sidway* (1891), 124 NY 538, 27 NE 256.

6 *Mills v Wyman* (1825), 3 Pick [20 Mass] 207.

7 *Peeryhouse v Garland Coal & Mining Co* (1962), 382 P.2d 109 (Okla.).

8 *Krell v Henry*, [1903] 2 KB 740.

inferred from or implied by anything done or omitted by such party, save only an express waiver in writing.

This didn't look like any of the cases you read about in your contracts course! Where was the narrative drama—the ships delayed in port or sunk in a storm, the accidents on the ski slopes, the crankshafts careening about the country in search of repair? Where was the charmingly quirky cast of characters—the pathetic father mistreated by a hard-hearted bank, the rogue posing as a TV actor, the businessmen at each other's throats, the minor in debt up to his ears to his tailor and bootmaker (and possibly also his bookmaker)? On top of that, the language was completely incomprehensible! You felt like someone had first stuffed a carbolic smoke ball into your brain and then strip-mined it.

Whether you come to the review and negotiation of contracts with or without a legal education background, you will come unprepared for your initial experience of commercial contracts.

Your first challenge will be to stay awake to read more than two consecutive paragraphs. The ritualized language of a commercial contract is actually intended to induce deep drowsiness, or preferably coma, with the result that Party presented with Counterparty's contract mutters, "Give me a pen, I'll sign, don't make me read any more," and then immediately after forming the signature passes out on the desk.

It *is* possible to learn to read a contract without falling asleep, and eventually without losing focus and rational thought. Understanding what the individual parts and paragraphs actually mean is a big step in the direction of staying awake. But even so, reading a contract requires a high level of concentration and focus. One single small word—or even punctuation mark—buried inside a big chunk of text can change the entire meaning of a provision and if you miss that one word or comma, heaven help you.

The Misplaced Comma

In a famous Canadian case, usually referred to in news reports as "The Million Dollar Comma" case, the placement of a comma had major financial consequences for the parties. Rogers Communications had an agreement with Aliant Telecom that contained the following paragraph:

[This Agreement] shall be effective from the date it is made and shall continue in force for a period of five (5) years from the date it is made, and thereafter for successive five (5) year terms, unless and until terminated by one year prior notice in writing by either party.

Rogers took the position that the agreement could be cancelled only at the end of the five-year term, on one year's notice. Aliant Telecom argued that

the agreement could be terminated at any time on one year's notice. The Canadian Radio-television and Telecommunications Commission (CRTC) initially ruled in favour of Aliant on the basis of grammar, but then overturned its decision, agreeing with Rogers (citing the language of the French version of the contract, which had "only one possible interpretation").⁹

This book includes many standard contract provisions, so the reader will have the opportunity to become familiar with (and immunized against) the appearance of contract language, and at the same time learn what the language means, how to revise it to take the sting out of it if necessary, and when to delete it. There are also appendices containing sample contracts such as an indemnity agreement, an amendment, and an assignment—contracts that tend not to be very mutable in nature. Note that these are sample contracts and not "model" contracts. They may be useful as a framework for drafting an agreement or as a checklist to review an agreement provided by Counterparty. I have not made any attempt to provide templates of contracts that contain more individualized content, such as a purchase agreement, a lease, a licence, or an agreement for services. This book is intended to cover the middle ground where most contracts meet, not to branch out into particular business transactions.

The default position in this book for contract language is fairness between the parties. On your own you can be as one-sided as you like or can get away with. Nevertheless, I encourage fairness on the part of everyone. A fair contract is less likely to end in tears and litigation.

D. The Map and the Territory

You've probably heard the expression "the map is not the territory." A contract is a kind of a map to a relationship between the parties. The contract is not the relationship, but it should reflect and structure the relationship. It should be the servant, not the master, of the relationship.

A contract is at least as much about practical matters as it is about legal ones. The contracts professional should be in appropriate communication with his/her client to ensure that the contract reflects what the client wants, and that the contract is not imposing something unexpected, undesired, or even impossible on the client.

If you are a contracts professional in a specialized field you will need to explore for yourself the applicable law, become thoroughly familiar with it, and be prepared to deal with it in contracts.

9 Telecom Decision CRTC 2007-75, 20 August 2007—Rogers Communications Inc—Application to review and vary Telecom Decision 2006-45 regarding the termination and assignment of a support structure agreement. Reference: 8662-R28-200612326.

E. I'll See You in Court! On Second Thought ... Let's Not Go There

In the quotation earlier in this Introduction, Swan and Adamski speak of case decisions that differ depending on the “theoretical and philosophical views of the judges.” This is an academic way of saying that going to court is essentially a gamble. You don’t want to gamble with your contract. A good way not to gamble is to stay out of court.

Some court decisions can only be described as whimsical. For example in *Barnett v Harrison*,¹⁰ where the Supreme Court of Canada was asked to overturn the rule in *Turney v Zhilka*, Dickson J gave five reasons why not. Number 4 was that “application of the rule in *Turney v Zhilka* may avoid determination of two questions which can give rise to difficulty”; and Number 5 was “the rule in *Turney v Zhilka* has been in effect since 1959, and has been applied many times.” Other court decisions may be characterized as just plain wrong; the losing party may not have had the cash and energy to appeal, seeking wiser judges. Or the losing party sought but never found wiser judges.

Therefore, this book takes the approach that it’s best to negotiate a contract with the intention of avoiding trouble in the first place, rather than expect a court to be your knight in shining armour and rescue you later on.

F. Structure of This Book

Contracts textbooks—*other* contracts textbooks, that is—are set up to reflect the order in which a contract is created, with offer and acceptance getting the ball rolling, and a great deal of attention being paid to consideration. Offer and acceptance and consideration are, with a few exceptions, of little concern to a commercial contracts professional. Finding valuable consideration is not normally a problem in a business deal, and by convention offer and acceptance are superseded by execution of the contract. Many other aspects of contract law that are treated as highly significant in other contracts textbooks are of limited importance in day-to-day commercial contracts work. And numerous aspects of contract law that *are* significant in commercial contracts never find their way into other contracts textbooks.

This book is instead set up to follow the outlines of a commercial contract itself, which typically begins with the language “This agreement, effective as of DDMMYYYY, is made between the parties. In consideration of the mutual promises contained herein, the parties agree as follows....” The first few chapters therefore consider What is an Agreement, When does an Agreement come into

10 [1976] 2 SCR 531. See Chapter 8, Section III.B, “Whose Performance?”

Effect, Who (or What) are the Parties, What is Consideration? And so forth. The intention is that a reader who is reviewing a contract can turn from the contract to this book and conveniently find the law related to a puzzling or annoying contract provision.

G. Terms Used in This Book

Case law always and standard contracts textbooks often refer to the parties to a contract as “the plaintiff” and “the defendant.” That isn’t very useful or encouraging nomenclature when you’re still at the stage of negotiating an agreement! For ease and standardization of reference, parties in this book will be referred to as “Party” and “Counterparty,” with the assumption generally being that the reader is acting on behalf of Party.

The words “obligor” and “obligee” will generally be used in reference to parties with rights and obligations—the obligor having the obligation and the obligee having the right—and will be taken to include in the case of obligor, a promisor and a debtor; and in the case of obligee, a promisee and a creditor.

H. Bibliography/References

Case law cited in this book is as often as possible obtained through the Canadian Legal Information Institute (CanLII). The CanLII website is <<https://www.canlii.org/en/>>. Standard Canadian reference texts were also consulted in the writing of this book.

If you need or want to consult a standard reference on Canadian contract law, go to:

Fridman, GHL, *The Law of Contract in Canada*, 6th ed (Toronto: Carswell, 2011).

McCamus, John D, *The Law of Contracts*, 2nd ed (Toronto: Irwin Law, 2012).

Swan, Angela & Jakub Adamski, *Canadian Contract Law*, 3rd ed (Toronto: LexisNexis Canada, 2012).

Waddams, Stephen M, *The Law of Contracts*, 7th ed (Aurora, ON: Canada Law Book, 2017).

I. No Need to Keep Your Thoughts to Yourself! (As Long as They Are Pure)

This book is a new enterprise in the way of looking at commercial contract law. Your constructive comments are welcome and may inform future editions. If you have something to say, please contact the publisher, Emond.