Contract Law Update

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Mechantaf Law

The Court of Appeal for Ontario (CA) and the Superior Court of Justice (SCJ) have issued a few decisions addressing key considerations on contract law, including contract formation, breach of contract and damages. Both the Court of Appeal and the Superior Court of Justice are one of the main Ontarian Courts for consideration of binding precedent in the province of Ontario.

Reported cases:

1. *Frye v. Sylvestre*, 2023 ONCA 796;
2. *Southwell v. Carlgate Development Inc.* 2024 ONSC 822;
3. *The Rosseau Group Inc. v. 2528061 Ontario Inc.*, 2023 ONCA 814

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CONTRACT FORMATION

Frye v. Sylvestre, 2023 ONCA 796

On 4 December 2023, the Court of Appeal dismissed the appeal in *Frye v. Sylvestre*, deciding that there was no concluded agreement for the sale of shares for two reasons. First, the manner in which the transaction would be structured was an essential term of the proposed purchase. Second, the e-mails exchanged between the parties did not record an agreement to that structure or the method of payment.

The underlying action was to enforce an agreement for the acquisition of shares by the respondent in a family corporation. On a motion for summary judgment, the motion judge declared that the respondent *"did not make a binding agreement to sell her shares . . . to [the appellant]"*. The purported agreement was contained in an exchange of emails between the parties' respective lawyers, the first requesting a confirmation of an agreement to sell shares, followed by a suggestion to prepare *"the documents necessary to give effect to these sale transactions"*; the second confirming such agreement, and further suggesting that an accounting firm confirms or updates the payable amounts and structure thereof to determine the net amount of taxes. In appeal, the appellants argued that the structure of the transaction was not an essential term but a matter of implementation.

"No valid agreement exists unless essential terms intending to govern the contractual relationship have been agreed upon between the Parties"

In relying on its prior decision in *Bawitko Investments Ltd. v. Kernels Popcorn Ltd.*, [1991] O.J. No. 495, 79 D.L.R. (4th) 97, the Court of Appeal rejected these allegations, explaining that an exchange of correspondence agreeing on terms to be incorporated into a more formal document will not amount to an enforceable contract in certain circumstances, including where *"essential provisions intended to govern the contractual relationship have not been settled or agreed upon"*. Although the subsequent conduct of the parties can be relevant to ascertain whether, objectively, a binding and

enforceable contract has been made, the fact that the accounting firm did not guarantee that the structure and method they proposed would be acceptable to Canada Revenue Agency in calculating the taxes owed from the sale, made the structure and method of payment of critical importance and, therefore, an essential term. Absent any such agreement there was no concluded agreement for the sale of shares. The appeal was dismissed.

Southwell v. Carlgate Development Inc. 2024 ONSC 822

On 8 December 2023, the Superior Court of Justice issued its decision in *Southwell v. Carlgate Development Inc.*, in which it addressed the very point of the conduct of the parties in *Frye v. Sylvestre*.

Just before his passing, a father undertook to restructure his corporation, with the applicant and the other two respondents, his mother and sister, names as joint executors of the estate. The mother had dementia and was removed as an executor, leaving the applicant and his sister as the sole executors. Amongst what was left of the corporate documents relating to the restructuring, most of which were corrupted and unrecoverable, was an unsigned share purchase agreement and resolution naming the mother and sister as directors. The applicant claimed that there was no evidence that the mother paid for the shares purportedly transferred to her, that the share purchase agreement and resolution naming the sister and mother as directors were not signed, and that the proper processes for appointing directors and transferring shares were not followed.

In considering the applicant's allegations, the SCJ considered the parties' conduct over the years, specifically whether there was a clear understanding that an agreement was concluded such that a finding of a de facto contract was justified. In doing so, the Court looked as to whether there was unambiguous evidence of a meeting of the minds for a contract to have been formed. It is not sufficient that the parties demonstrate an intent to be bound together.

"Absence any agreement to the contrary, signature of the sale purchase agreement was a mere formality and not an essential term of contract"

The SCJ dismissed the application, holding that there was a valid agreement to sell the shares to the mother and a valid resolution to appoint the mother and sister as directors. While there were some irregularities in the documentation of the corporate reorganization (which, according to *Trezzi v. Trezzi,* [2018] O.J. No. 4620, 2018 ONSC 5180, may have rendered the transaction invalid) there were other evidence demonstrating that the father sold 30 Class A common shares to the mother for fair market value. Such evidence can be summarized as follows: (a) there is a clear intent to restructure the corporation; (b) witness evidence confirming an intent to update the corporate minute book; (c) contemporaneous record confirming the sale of 30 Class A common shares. Despite the absence of a signed version of the sale purchase agreement, the Court stated that the provisions of the said 'unsigned' agreement do not require the execution of the documents for the share purchase agreement to be valid. 'Signature' was, therefore, a mere formality [*Kernwood Ltd. v. Renegade Capital Corp.*, [1997]

O.J. No. 179, 97 O.A.C. 3 (C.A.)] and not an essential term of the SPA. Hence, the parties were bound by a de facto contract for sale of shares.

The SCJ further held that the parties' conduct after the reorganization also confirmed that there was a valid agreement to transfer the shares, as various documents portrayed the mother as a shareholder and the applicant had never objected.

Finally, the decision noted that the applicant's allegation that *"for the sale of the shares to be valid, share certificates had to be properly registered in a securities register"*, lacked authority on the matter. In fact, according to *Romexim Canada Inc. v. Morrison*, [2022] O.J. No. 2375, 2022 ONSC 2889 (S.C.J.), even the absence of a share certificate does not negate a shareholder's status as such. The application was dismissed.

MEASURE OF DAMAGES

The Rosseau Group Inc. v. 2528061 Ontario Inc., 2023 ONCA 814

On 8 December 2023, the Ontario Court of Appeal issued its decision in *The Rosseau Group Inc. v. 2528061 Ontario Inc.,* addressing a claim for specific performance and, alternatively, damages arising from a breach of contract for sale of land.

In the facts, the plaintiff agreed to purchase from the defendant undeveloped land zoned for agricultural and conservation uses. The agreement initially provided for an initial deposit of $50,000, conditional for 90 days to allow the plaintiff to satisfy itself of the feasibility of development of the site and other issues. On waiver of the conditions, a further deposit of $400,000 was payable, with closing to be 60 days after removal of all specified conditions. The parties then discussed changes to the payment terms, one of which was that the plaintiff would agree to assume the first mortgage on the property in exchange for a deletion of the requirement to pay the further deposit of $400,000. Accordingly, the agreement of purchase and sale was later amended to reduce the purchase price, however the amending document did not expressly refer to the $400,000 further deposit, nor did it delete the schedule providing for the further deposit. The plaintiff did not provide a $400,000 deposit, which the defendant treated as a repudiation of their agreement. There was no closing. Importantly, the plaintiff intended to resell rather than develop the land. The plaintiff commenced an action for specific performance and, in the alternative, damages, before later abandoning its claim for specific performance. The trial judge found that there was no provision for the further deposit in the amended agreement of purchase and sale, and that the defendant had breached the agreement by refusing to complete. The judge considered it a proper case to depart from the normal measure of damages of the difference between the market value at the closing date and the contractual purchase price as the plaintiff was ready, willing, and able to close and was prepared to assume the mortgage. She then awarded the plaintiff over $11 million based on the estimated profit it would have earned had the transaction closed. The defendant appealed liability and damages. The Court of Appeal dismissed the liability appeal and allowed the appeal for the damages.

The liability appeal

The Court of Appeal stated that the further deposit of $400,000 was an issue of contractual interpretation. It continued that "it was significant that the amendment did not refer to the further deposit as a component of the purchase price at all, let alone state how, or against what component of the purchase price, the further deposit was to be credited". Absent an extricable legal error by the trial judge, the Court considered that she is entitled to deference on appeal [*Sattva Capital Corp. v. Creston Moly Corp.*, [2014] 2 S.C.R. 633]. The Court added that the trial judge was required to construe the agreement as a whole, post-amendment, including reconciling apparently inconsistent terms.

Accordingly, the Court upheld the decision, which concluded that the parties deleted the requirement for the further deposit by the language of the amendment, i.e. by performing a contextual and factual analysis of the parties' intent rather than what was embedded in the four corners of their amending document.

The damages appeal

Regarding the awarded damages, the Court considered that a trial judge's assessment of damages attracts considerable deference on appeal. However, an assessment made based on an error of principle or law may be interfered with on appeal [*SFC Litigation Trust (Trustee of) v. Chan (2019)*, 147 O.R. (3d) 145, [2019].

The Court decided that the trial judge erred in not using the normal measure of damages for a real estate purchase, which is the difference between the contract price and the market value of the land on the "assessment date", usually being the closing date. This is specifically the case in the absence of anything suggesting that such measure would not address the plaintiff's recoverable loss. That being said, the court may set a later date if the party seeking damages satisfies certain criteria, however the presumption is that damages are to be assessed as of the date of the breach [*100 Main Street Ltd. v. W.B. Sullivan Construction Ltd.* (1978), 20 O.R. (2d) 401, [1978].

"The difference between the purchase price and the land's market value on the closing date, cannot be departed from unless the party seeking damages shows that the normal measure does not address the type of loss sought"

Based on the foregoing, the Court decided that the trial judge erred in relying solely on the parties' contemplation of future development of the property into service lots as a reason for departing from the normal measure of damages. In summarizing, the Court stated that, first, the judge did not use the closing date as the assessment date, nor did it appear that she used a later specific date, which was problematic because the expected profit was inherent in the value of the land at the date of closing: *"Damages are awarded on the principle that the innocent party, as nearly as possible, should*

be put in the position it would have been in if the contract had been performed. Using, as the measure of damages, the difference between the purchase price and the land's market value on the closing date puts this principle into effect". Despite the fact the parties contemplated that the property would be developed into serviced lots, such contemplation does not warrant a departure from the normal measure of damages, unless the party seeking damages shows that that normal measure does not address that type of loss, i.e. loss of development value: *"The trial judge made no such finding that Rosseau Group could extract a special value from developing the land that other market participants could not because, for example, it owned adjacent land and could combine it in a unique way with the land to be acquired, or because it had special development techniques not known generally to the market. In those types of situations, the normal measure of damages may not be adequate"*. Second, the trial judge erred in using contingencies as she did, i.e. whether a discount is appropriate to reflect the contingency that the opportunity may not be realized, perfectly or at all [*Eastwalsh Homes Ltd. v. Anatal Developments Ltd.* (1993), 12 O.R. (3d) 675].

The appeal on damages was allowed and a new hearing was ordered on damages, to be assessed on the normal measure, namely the difference between the purchase price and the market value of the lands on the date set for closing.

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