WeirFoulds LLP

LITIGATION UPDATE

OCTOBER 2011

DEVELOPMENTS OF INTEREST IN CASE LAW

(a) Construction Liens – Value of a Claim for Lien – s 35 of the *Construction Lien Act*

***Landmark II Inc v 1535709 Ontario Limited*, 2011 ONCA 567 (Released August 31, 2011)**

In 2004, the plaintiff Landmark II Inc. ("**Landmark**") entered into a written contract with the defendant 1535709 Ontario Limited ("**1535709**") to expand a truck parking lot on 1535709's property. The entire contract price was $58,850, to be paid in four equal instalments based on the construction milestones set out in the contract. When 1535709 refused to pay the second instalment when due, Landmark abandoned the job, filed a lien for the unpaid balance of the contract and commenced a claim of *quantum meruit* for the same amount. 1535709 counterclaimed for damages suffered as a result of Landmark's failure to complete the contract.

The trial judge found that 1535709 had breached the contract by failing to pay and that Landmark was not obligated to continue its work without payment. The trial judge found that Landmark's work as of the date of abandonment was valued at $16,000 and, after deducting the amount of the first payment, she determined that 1535709 owed Landmark $1,287.50. 1535709's counterclaim was dismissed. On appeal, the Divisional Court upheld the trial judge's decision in brief written reasons.

Landmark subsequently appealed to the Court of Appeal. Of importance, Landmark contested the trial judge's finding of liability for having registered a lien in an amount that was grossly excessive to the amount owed to it, pursuant to s. 35 of the *Construction Lien Act* ("***CLA***"). Landmark argued that it was able to lien for the unpaid balance of the contract. The Court disagreed.

Typically, the amount claimed in a construction lien relates to the value of work or materials supplied for which payment has not been received and not the value of work or materials not yet supplied. In this case, the Court found that it is not necessarily improper for a lien claimant to lien for the entire amount of a contract. Although a lien claimant is only secured for the actual value of the work or materials supplied (usually determined at trial) through a lien, if a lien claimant demonstrates an intention to stay on the job and finish the contract, the lien claimant can avoid liability under s. 35 of the *CLA* and effectively secure the value of future work to complete the contract.

The Court held that a lien claimant cannot lien for the value of the contract when it has left the job and does not intend to finish it. In other words, the Court held that a lien claimant cannot use a lien to secure a claim for breach of contract should it walk off the job.

In this case, the Court found that Landmark had improperly claimed a lien for the full contract value as it placed the lien two months after it had abandoned the job and had no intention of completing the contract. Landmark was therefore found liable under s. 35 of the *CLA* to 1535709 for the borrowing costs to vacate the lien.

The Court's expanded view of liens being used to secure future work or materials supplied to a project where a lien claimant intends to complete its work is especially problematic for project owners as the costs to vacate liens could rise to an insurmountable level.

On a second ground of appeal, the Court's decision followed existing jurisprudence setting out the election that a lien claimant must make between a claim for *quantum meruit* and a claim for breach of contract. In a construction lien action, a claimant must elect between these alternative remedies, at the latest by the time of judgment. Landmark argued that it was entitled to an election from the court.

In this case, the Court found that Landmark had not indicated it was pursuing alternative remedies with the intention of making an election. Further, there was no obligation on the trial judge to provide an election. If Landmark was seeking damages for breach of contract as an alternative to its claim for *quantum meruit*, it was required to so elect. Without the election, Landmark was not entitled to damages for the breach of contract as an alternative to the trial judge's assessment of damages under the claim for *quantum meruit*.

Landmark's results may have been significantly different if it had acted to preserve its right to an election for breach of contract. The decision highlights the importance of maintaining a lien claimant's right to an election between alternative remedies in order to ensure that the best recovery is obtained.

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(b) Insurance liability coverage – Notice of action – Who may give notice – s 129 of the *Insurance Act* – Relief from forfeiture

***The Sovereign General Insurance Company v Walker*, 2011 ONCA 597 (Released September 19, 2011)**

The respondent Marie Walker slipped and fell at the Power Centre in Burlington, Ontario, and sustained serious and permanent injuries. The Walkers sued Emshih Developments Inc. ("**Emshih**"), the owner, and Sun Shelters, the maintenance company retained to clear the property of snow and ice. Sun Shelters was bankrupt and did not defend the action but Emshih notified its insurer, The Sovereign General Insurance Company ("**Sovereign**"), of the claim. Sovereign declined to participate.

The Walkers settled the action with Emshih and obtained a judgment against Sun Shelters for $100,000 in damages and related relief. The Walkers then brought an action against Sovereign under s. 132 of the *Insurance Act*, which allows a third party to recover against an insurer where the insured has failed to satisfy a judgment for damages. Alternatively, they relied on s. 129 of the Act, which gives a court jurisdiction to grant relief from forfeiture where there has been imperfect compliance with a condition in an insurance policy. The Walkers moved for summary judgment on their claim. Sovereign brought a cross-motion to dismiss the action, claiming that Sun Shelters did not give effective notice of the action as required by the policy, thereby breaching the policy and relieving Sovereign from liability coverage.

On appeal from the motion judge's decision granting summary judgment to the Walkers, the Court upheld the motion judge's decision that the notice given by Emshih was effective under s. 3(a) of the policy. Notice was required "by or for the insured". On a plain reading of the provision, notice may be given by a person other than the insured. Section 3(a) must be interpreted in light of its purpose, which is to make Sovereign aware of a claim against its insured so that it has the opportunity to deal with it. The Court held that if the notice is to be given on an insured's behalf, the party giving it should have sufficient proximity to the claim to have knowledge of the information required by s. 3(a). The Court held that Emshih was such a party and its notice to Sovereign constituted effective notice under the policy. Sovereign was aware of the action but made no effort to contact its insured or seek its assistance. It cannot now complain that Sun Shelters breached its duty to cooperate.

The Court also upheld the motion judge's decision that the Walkers would be entitled to relief from forfeiture under s. 129 of the Act. The law has treated the failure to give timely notice of a claim as imperfect compliance rather than non-compliance. Even if this was not the state of the law, Sovereign had actual notice of the claim and it made a conscious decision not to participate in it. This was clearly a case of imperfect compliance. The only remaining question under s. 129 is whether forfeiture of the insurance proceeds would be inequitable. The motion judge made two key findings of fact: first, there was no bad faith by Sun Shelters, Emshih or the Walkers; and second, although Emshih gave Sovereign notice of the Walkers' claim over five years after the accident occurred, Sovereign suffered no prejudice from the late delivery of the notice. The Court upheld these findings of fact.

The appeal was dismissed. Sovereign was given effective notice in accordance with the policy conditions for liability coverage, and the Walkers were entitled to relief from forfeiture.

(c) Shoreline Dispute – Public Highway – Summary Judgment – *Registry Act*

***The Corporation of the Municipality of Meaford v Grist*, 2011 ONSC 5195 (Released September 21, 2011)**

The Superior Court granted summary judgment dismissing the Township's action for declaratory relief against its residents in a dispute over the ownership of a strip of land running along the Georgian Bay shoreline. Although the motions for summary judgment were brought by only some of the defendants, the Court dismissed the plaintiff's action as against all defendants.

The defendants owned cottage lots located on Georgian Bay. The disputed road, which the Township asserted had been established by a pre-Confederation by-law in 1854 ("**By-law 11**") ran through the defendants' properties immediately adjacent to the water's edge. By-law 11 was not registered on title in respect of any land until after 2004, when it was discovered by the Township in the basement of the municipal offices. Upon discovery of By-law 11, the Township passed By-law 80-2007 which purported to accept the location of the public road as determined by a partial survey of the By-law 11 lands.

The Township asserted that the public road was established over the defendants' properties on several grounds: (1) the enactment of By-law 11; (2) as a result of the doctrine of dedication and acceptance of road, as evidenced by the expenditure of public funds on the road and the historic use of the road by members of the public; and (3) that the Township had acquired title to the land along the waterfront by virtue of a public highway that existed in the location prior to the enactment of By-law 11 in 1854. In the alternative, the Township asserted that By-law 11 gave it title to the disputed lands despite it not being registered on title until 2007. Moreover, the Township argued that it had acquired title in modern times by a presumption of dedication and acceptance.

The Court rejected all of the Township's arguments. The Court found no evidence to suggest that there was a shoreline road in existence prior to the enactment of By-law 11 in 1854. The Township also produced no records referring to the By-law 11 lands in the years following the passage of the by-law. The Court found that the Township had not met the test required to establish dedication and acceptance in the modern era. At its highest, the Township's evidence only suggested that persons who were using the disputed road were predominantly friends, visitors and invitees.

As By-law 11 had not been registered on title before the defendants took title to their properties, By-law 11 was unenforceable as against them. Prior to the 1865 amendments of the *Registry Act*, there was no requirement to register a by-law. While the Township was not required to register By-law 11 on title at the time of its enactment, actual notice of a prior interest in title was still required by the law of equity in order for any ownership interest created by the by-law to prevail over a subsequent registered transfer. In this case, the property owners occupying the disputed lands were only required to search title to their properties back 40 years prior to the date of purchase to identify any encumbrances on the title they were acquiring.

In passing By-law 80-2007, the Township preferred "the wishes of a small group of citizens to the concerns raised by its town planner" (para 177). It failed to carry out all proper inquiries and to give timely and adequate notice to affected property owners before the enactment of the by-law. By-law 80-2007 was void as it was not passed for a proper municipal purpose.

Finally, the Court noted that the Township had "slept on their rights for over 150 years" (para 184). The defendants acted in reliance on their justifiable belief the disputed lands were part of their private property. Given that the Township was not acting for the purpose of enforcing any legislation but rather was seeking to take away property rights, laches and acquiescence should apply in favour of the defendants.

(d) Franchise – *Arthur Wishart Act* – Disclosure Document – One-year Term – Franchise Fee

***TA & K Enterprises Inc v Suncor Energy Products Inc*, 2011 ONCA 613 (Released September 27, 2011)**

In this decision, the Court of Appeal for Ontario concluded (1) that the franchise disclosure requirements in the *Arthur*

Wishart Act (Franchise Disclosure), 2000, SO 2000 ("**Act**") do not apply to franchise agreements where the term of the franchise rights and obligations is one year or less and (2) that "franchise fees" do not include ongoing payments such as royalties.

The case came to the Court from Perell J.'s decision which granted the defendant Suncor's motion to dismiss a proposed class action brought by TA & K Enterprises Inc. ("**TAK**") on behalf of a class of over 200 former Sunoco retailers. The claim arose from Suncor's merger with Petro-Canada and Suncor's subsequent decision to cull some franchisees and re-brand the remainder. In asserting that Suncor had not met an obligation to provide disclosure, TAK hoped to recover some of its set-up and wind-down costs. In response, Suncor relied on s. 5(7)(g)(ii) of the Act which provides an exemption from disclosure where "the franchise agreement is not valid for longer than one year and does not involve the payment of a non-refundable franchise fee".

Justice Goudge (MacFarland and Watt JJ.A. concurring) rejected all of TAK's arguments. He held that although the franchise agreement was signed on November 11, 2008 and due to expire on November 14, 2009, it was not valid for longer than one year. Rather, the "time frame during which the franchisee is bound to certain rights and obligations" was only one year. The franchisee's ability to repudiate the agreement for franchisor non-performance in the period between the signing of the agreement and the commencement of its performance did not tip the term length over the one year.

Further, the existence of obligations such as indemnity and confidentiality which survive the termination of the agreement did not extend the agreement past one year. By definition those obligations only arise after the termination of the agreement and so after the agreement can be considered valid. The existence of a clause within the franchise agreement which provided for a monthly tenancy in the event the franchisee remained in possession and continued to pay rent at the conclusion of the agreement did not extend the term. Because the term came into force at the expiration of the agreement, it did not extend it. Finally, a letter from Suncor extending the franchise relationship on a month-to-month basis did not stretch the franchise agreement beyond a year.

The Court also dismissed TAK's claim that its payments to Suncor were franchise fees and that as a result Suncor did not satisfy the second branch of the disclosure exemption. Goudge J.A. relied on the relevant regulation and the law reform report which led to the Act to hold that a franchise fee is paid to become a franchisee, and does not include royalties or other payments for goods or services. The Court's decision makes sense as a plain interpretation of the Act. However, it leaves potential franchisees faced with one-year agreements – which will surely now become more popular with franchisors – to bargain for longer agreements or more complete disclosure. The decision thereby does not live up to the Act's broad goal of rebalancing power between potential franchisees and franchisors.

(e) Constitutional Division of Powers – Interjurisdictional Immunity – *Canadian Charter of Rights and Freedoms* – Life, Liberty and Security of the Person – Principles of Fundamental Justice – Ministerial Discretion

***Canada (Attorney General) v PHS Community Services*, 2011 SCC 44 (Released September 30, 2011)**

The Supreme Court of Canada unanimously ordered that the federal Minister of Health (the "**Minister**") must exempt Insite, a safe drug injection facility in Vancouver's Downtown Eastside, from provisions of the *Controlled Drugs and Substances Act* ("***CDSA***").

Insite has provided various medical services, including supervised injections of controlled substances, to intravenous drug users since 2003. The Insite facility was able to operate legally between 2003 and 2008 under a discretionary exemption by the Minister pursuant to s. 56 of the *CDSA*, which allows for targeted ministerial exemptions necessitated by medical, scientific, or other public interest purposes. In 2008, the Minister indicated that he did not intend to grant a continued exemption. The Supreme Court considered the legislative scheme and the Minister's decision in light of the *Canadian Charter of Rights and Freedoms* and the constitutional division of powers.

The Court rejected an argument that the application of the *CDSA* to Insite ran afoul of the constitutional division of powers. The Court concluded that the *CDSA* was a valid exercise of the federal criminal law power, and that the doctrine of interjurisdictional immunity did not render the *CDSA* inapplicable to Insite as an impermissible federal intrusion into the core of a provincial thing or undertaking. In so deciding, the Court noted that no other cases had recognized a protected core of provincial power over health; that the claimants had failed to delineate any meaningful core; and that recognizing a protected core of provincial power over health may give rise to legal vacuums with respect to such issues as human cloning or euthanasia.

The Court further held that the legislative scheme created by the *CDSA* complied with s. 7 of the *Charter*. Although the life, liberty, and security of the person interests of Insite staff and clients were engaged by the *CDSA* prohibitions against possession of narcotics, the s. 56 ministerial exemption served as a "safety valve" to prevent arbitrary, overbroad, or disproportionate application of the law.

The Court found that the Minister's decision not to continue Insite's exemption pursuant to s. 56 of the *CDSA* did breach s. 7 of the *Charter*. The life, liberty, and security of the person interests of Insite staff and clients were engaged by the application of the prohibition against possession of narcotics to the Insite facility because of both the possibility of imprisonment for contravention of the *CDSA* and the serious health and safety interests at stake for Insite clients. The Court further found that the Minister's failure to grant an exemption to Insite was contrary to the principles of fundamental justice since it was both arbitrary and grossly disproportionate with reference to the *CDSA*'s dual purposes of protecting health and public safety. The Court relied on the trial judge's factual findings that the life-saving benefits of Insite had been proven, and that there was no discernable negative impact to public health and safety objectives.

The Court emphasized that the decision was not "an invitation for anyone who so chooses to open a facility for drug use under the banner of a 'safe injection facility'" (at para 140), and that the holdings in this case were dependent on the specific factual findings that the Insite facility reduced death and disease while having no negative impact on legitimate criminal law objectives.

(f) Civil Procedure – Appeals – Jurisdiction

***Canadian Broadcasting Corporation v Ontario*, 2011 ONCA 624 (Released October 5, 2011)**

The CBC applied to the Superior Court for an order granting it access to a video that was an exhibit in the appellant's bail hearing. The application judge granted the order and released the video to the CBC on the condition the appellant's face would be obscured. The appellant appealed the order.

The CBC brought a motion seeking to quash the appeal on the basis that the correct avenue to appeal was to the Supreme Court, with leave. The determinative issue was whether the appeal was a "criminal appeal" or a "civil appeal". The Court of Appeal would only have jurisdiction over a civil appeal.

The Court rejected the CBC's arguments, which were supported by the Crown, that this was a criminal appeal. The Court noted that the criminal proceedings had concluded (the appellant was ultimately acquitted). Therefore, the appellant's trial rights were not in play, the application

would not impact a criminal proceeding, and the application was not made in the course of a criminal proceeding. Given these circumstances, the Court held the proceeding should not be characterized as criminal.

The Court noted that this motion appeared to be the first time an appellate court had expressly considered the characterization of this sort of appeal. The Court's holding appears to turn in part on two policy reasons:

1. There is a functional benefit of enhanced access to appellate review allowed by characterizing this as a civil appeal. If it were characterized as a criminal appeal, an appeal would be available only to the Supreme Court with leave; and
2. The characterization of the appeal as a civil appeal enhances the overall effectiveness of the administration of justice as it enables appeals to go through the entire judicial hierarchy, allowing these intermediate appeal courts to serve their function as well as the development of effective and cohesive jurisprudence.

(g) Environmental Contamination – Nuisance – Strict Liability – Application of Limitation Period in Class Actions

***Smith v Inco Limited*, 2011 ONCA 628 (Released October 7, 2011)**

This appeal reversed a 2010 trial judgment awarding $36 million against Inco Limited ("Inco") in a class action stemming from particle emissions from the operation of Inco's Port Colborne nickel refinery from 1918 to 1984.

It is undisputed that the refinery emitted nickel oxide into the air and, as a result, nickel has been found in the soil on many nearby properties. In 2001, 7,000 surrounding property owners brought a class action against Inco and others alleging a variety of claims, although by trial the case had been reduced to one claim against Inco.

On appeal, the Court emphasized the importance of recognizing the exact nature of the claim advanced at trial. Rather than allege that the emissions violated environmental regulations, posed a threat to human health, or interfered with the claimants' use of their property, the claimants alleged the emissions were ultimately to blame for their property values in the early 2000s not appreciating at the same rate as comparable property values in similar nearby cities.

According to the claimants, reports released by the Ministry of the Environment ("MOE") in the early 2000s regarding nickel contamination in the soil led to widespread public health concerns about their properties, which in turn negatively affected the increase in their property values. The health concerns turned out to be unfounded.

Although claims for trespass, public nuisance and punitive damages were dismissed, the trial judge found that the property values were diminished because of the public concern, and that Inco was liable for this loss under the theories of private nuisance and strict liability imposed under the rule in Rylands v Fletcher.

The Court of Appeal reversed this decision, finding that the claimants had failed to establish liability under either private nuisance or the rule in Rylands v Fletcher, and, in any event, had not proved damages.

First, the Court disagreed with the trial judge's reasoning that the emissions constituted "material physical damage" to the claimants' properties sufficient to constitute a private nuisance. The Court held that a mere change in the chemical composition of the land, absent evidence of a detrimental effect on the land or its use by its owners, does not constitute physical damage. Moreover, the Court was unwilling to accept the disconnect between the time of the emissions and the alleged materiality of the harm arising in the early 2000s. Public concerns about potential health risks alone did not amount to evidence that the nickel in the soil constituted actual, substantial, physical damage to their properties; therefore, the claim for nuisance failed.

The Court of Appeal also rejected the trial judge's finding of strict liability under the rule in Rylands v Fletcher. This rule imposes strict liability for damages caused to property by the escape from the defendant's property of a substance "likely to cause mischief".

Specifically, the Court disagreed with the trial judge's findings regarding the two main elements of the rule: a "non-natural" use of the property and the "escape" component. Because the refinery was operated in a heavily industrialized area in a usual and ordinary manner, it did not constitute a "non-natural" use of the property. Moreover, the emissions were not an "escape" because they were the intended result of an activity reasonably and lawfully conducted on Inco's property and not the type of mishap or accident contemplated by the rule.

Although declining to decide the "important jurisprudential question" of whether foreseeability of damages is a requirement for liability under Rylands v Fletcher, the Court warned against imposing a requirement of foreseeability of escape as this would effectively merge the rule in Rylands v Fletcher with liability in negligence.

The Court also expressly rejected any expansion of the rule that would impose strict liability based solely on the "extra hazardous" nature of the defendant's conduct, stating that to do so was a policy decision "best introduced by legislative action and not judicial fiat". In any event, the Court found no evidence that Inco's operation of the refinery constituted an extra hazardous activity.

Finally, the Court held that the claimants had failed to prove damages. Specifically, the claimants had not demonstrated that their properties failed to appreciate in value as they otherwise would have but for the adverse publicity arising from the MOE reports on the nickel contamination.

The Court found that the market comparison data presented by the claimants' experts and accepted by the trial judge was flawed in several ways, including, among others: (1) the data compared "apples to oranges" in the types of properties included in the analysis and when this was corrected, any difference in appreciation rates disappeared; and (2) the experts had merely assumed that any difference in property values was attributable to the nickel contamination without making any efforts to see what other factors may have contributed. The trial judge also erred in focusing his attention on certain data and not others. According to the Court of Appeal, when the data was considered "fully and fairly" it demonstrated no loss to the claimants' property appreciation rates.

Although the Court of Appeal had disposed of any basis for liability, thereby allowing the appeal and dismissing the action, it went on to address the trial judge's treatment of the applicability of the limitation period to class actions.

The trial judge had found that, because an "overwhelming majority" of the class members did not known and ought not to have known about the material facts giving rise to their claim until February 2000, the claim on behalf of the class members was not statute-barred.

The Court of Appeal held that the trial judge erred in treating the discoverability question as a common issue in this case. The Court explained if the evidence did not establish that all class members did not discover the claim until February 2000, then the application of the limitation period is an individual, and not a common issue. "A class action is a procedural vehicle. Its use does not have the effect of changing the substantive law applicable to individual actions."

Suggested content for next month's newsletter can be forwarded to either Richard Ogden or Jessica Eisen.