

Rectification on the Basis of Implied Terms and Business Efficacy

May 15, 2020

The Ontario Court of Appeal recently reviewed the law applicable to rectification claims and the interpretation of contracts in *2484234 Ontario Inc. v Hanley Park Developments Inc.*^[1] After applying contractual interpretation principles to the parties' prior agreement and implying a term in that agreement, the Court allowed the appeal, and ordered that the formal agreement be rectified and specifically performed as rectified.

Factual Background

The appellant brought a claim for rectification of a "Transfer Agreement". Under the Transfer Agreement, the respondent was to transfer, and provide an easement over, certain lands, i.e. Parts 1 to 4 of a property. The Transfer Agreement was entered into because the appellant required the transfer and easement to construct an access road to a proposed subdivision that the appellant had acquired. After the execution of the Transfer Agreement, the appellant discovered that Part 5 of the property was also required for the access road. The appellant's application for rectification was for the addition of Part 5 to the lands specified in the Transfer Agreement because the latter were insufficient to build the access road.

In the course of the litigation, the respondent's representative conceded on cross-examination that he had always been aware that, without Part 5, Parts 1 to 4 were not sufficient for the access road.

Rectification Remedy

The purpose of the rectification remedy is to correct a document to accord with what was agreed. However, it cannot be used to change an agreement to make it achieve a party's desired result. In other words, while rectification corrects mistakes in the recording of a prior agreement, it is not available to correct mistakes in the prior agreement itself.^[2]

The rectification of an agreement is available upon the court being satisfied that:

- (i) the parties had reached a prior agreement, the terms of which are definite and ascertainable;
- (ii) the agreement was still effective when the instrument was executed;
- (iii) the instrument fails to record accurately that prior agreement; and
- (iv) if rectified as proposed, the instrument would carry out the agreement.

In the case of a unilateral mistake, the court must also be satisfied that:

- (v) the party resisting rectification knew or ought to have known about the mistake; and
- (vi) permitting that party to take advantage of the mistake would amount to fraud or the equivalent of fraud. [\[3\]](#)

Decision of the Application Judge

The application judge dismissed the appellant's application for rectification. She held that the appellant failed to meet factors (iii) and (vi) above. She found that the Transfer Agreement accurately recorded the parties' prior agreement because Part 5 was never discussed and never made the subject of a prior agreement. She also found that permitting the respondent to take advantage of the appellant's mistake did not amount to fraud or its equivalent because: (a) there was no clause requiring the respondent to convey all lands necessary for the development of the access road; (b) the respondent did not intentionally deceive the appellant; and (c) the appellant should have verified the boundaries pursuant to the due diligence condition.[\[4\]](#)

Decision of the Court of Appeal

The Court of Appeal identified the central question in this case as being the following: did the parties have an agreement that preceded the document sought to be rectified, and if so, what were the terms of that prior agreement and what did they mean? According to the Court, it was only by answering this question that one could determine whether the appellant was seeking to correct an error in the recording of the parties' true agreement or, instead, was seeking to insert something that was never the subject of a prior agreement.[\[5\]](#)

The Court of Appeal noted that while the application judge had found that there was a prior agreement, she had not expressly identified where the terms of the antecedent agreement were found, nor comprehensively described their content. The Court stated that there was only one document that the application judge could have been referring to as containing the terms of the prior agreement, which was a letter dated March 7, 2017 written by the respondent's lawyer ("**March 7 Letter**"). According to the Court, the fact that the March 7 Letter was sent on a without prejudice basis did not prevent it from constituting a prior agreement for the purposes of rectification.[\[6\]](#)

The Court of Appeal found that the application judge erred in her interpretation of the antecedent agreement. She failed to apply contractual interpretive principles, and instead of determining the meaning of the antecedent agreement objectively, she relied on the respondent's evidence about its subjective intention not to transfer more than the Parts mentioned in the Transfer Agreement. The application judge also failed to analyze the words in the antecedent agreement in light of the factual matrix, as is required to interpret an agreement.[\[7\]](#)

The Court of Appeal reviewed and analyzed the surrounding circumstances and the language of the March 7 Letter, including language about facilitating the development of the proposed subdivision and about the sufficiency of Parts 1 to 4 for the access road. The Court concluded that the factual matrix supported an interpretation that the risk with respect to the sufficiency of Parts 1 to 4 was on the respondent.[\[8\]](#) Ultimately, the Court of Appeal found that the transfer of Part 5 was an implied term in the antecedent agreement. It stated:

Here, the respondent having promised to convey Parts 1 to 4 on the basis that they were sufficient, was obligated to do what was necessary to make them sufficient and which was in its power to do, namely, to include Part 5. The circumstances for implying a term about Part 5 were undoubtedly present. With Part 5, the agreement has business efficacy; without it, the agreement does not. It cannot seriously be disputed that if parties who had contracted in good faith for the terms found in the antecedent agreement had been asked, by an officious bystander, about whether Part 5 would be included if the Parts specified as sufficient were not in fact sufficient, they would have answered: "obviously". The inclusion of Part 5 is an implied term of the parties' true agreement.[\[9\]](#)

As a result of the implied term including Part 5 in the antecedent agreement, the Court of Appeal concluded that the Transfer Agreement did not accurately record the parties' prior agreement because it did not fully record it.^[10] The Court also concluded that the appropriate correction was to add Part 5 to the Transfer Agreement.

Finally, the Court of Appeal held that permitting the respondent to take advantage of the appellant's mistake would amount to fraud or the equivalent of fraud. It stated:

The respondent's principal was aware that the Access Road was the reason why the appellant wanted the transfer and easement. He was aware of the terms of the antecedent agreement and that it referred to advice received by the respondent regarding the sufficiency of the lands for the Access Road. [...] He was aware that the lands could only be sufficient with Part 5; Parts 1 to 4 were insufficient if Part 5 was not included. And he was aware that the formal Transfer Agreement only referred to Parts 1 to 4. In my view, the respondent's explanation for its behaviour, a concern that the appellant might not close the purchase of the Development Lands unless it thought it was getting what it needed for the Access Road, accentuates rather than attenuates the unfair and unconscionable nature of the respondent's conduct, which was to lead, or knowingly allow, the appellant to think that it was getting what it needed. In my view, element (vi) of the rectification test was met in these circumstances.

Conclusion

In its reasons, the Court of Appeal focused only on the elements of the test for rectification that the application judge had found were not met. One element that was not discussed in any detail is the requirement that the terms of the prior agreement reached by the parties be "definite and ascertainable". Based on the decision of the Court, however, it appears that terms can be "definite and ascertainable" for the purposes of rectification even if they have to be implied in the prior agreement after an extensive and lengthy contractual interpretation exercise. When an agreement is rectified based on a term that is implied in the prior agreement to achieve business efficacy, the Court is coming close to do what rectification is not supposed to do, i.e. to correct mistakes in the prior agreement itself. The bad conduct of the respondent in this case may have been a factor that influenced the Court's decision.

^[1] 2484234 Ontario Inc. v Hanley Park Developments Inc., 2020 ONCA 273.

^[2] *Ibid.* at paras. 34-35.

^[3] Canada (Attorney General) v Fairmont Hotels Inc., 2016 SCC 56 at paras. 14-15.

^[4] 2484234 Ontario Inc. v Hanley Park Developments Inc., 2020 ONCA 273 at para. 27.

^[5] *Ibid.* at para. 41.

^[6] *Ibid.* at para. 46.

^[7] *Ibid.* at paras. 49-55.

^[8] *Ibid.* at para. 65.

^[9] *Ibid.* at para. 72.

[10] *ibid.* at para. 73.

The information and comments herein are for the general information and are not intended as advice or opinion to be relied upon in relation to any particular circumstances. For particular application of the law to specific situations, please contact any of our lawyers for further guidance.

WeirFoulds^{LLP}

www.weirfoulds.com

Toronto Office

4100 – 66 Wellington Street West
PO Box 35, TD Bank Tower
Toronto, ON M5K 1B7

Tel: 416.365.1110
Fax: 416.365.1876

Oakville Office

1320 Cornwall Rd., Suite 201
Oakville, ON L6J 7W5

Tel: 416.365.1110
Fax: 905.829.2035