ISSUE #2 – NOVEMBER 2024

On the Docket: Cases to Watch

Lenczner Slaght

Contents

Introduction

On the Docket: Cases to Watch features a collection of decisions, identified by our expert Research & Advisory team, that are important to keep top of mind as they offer significant legal insights and shape the evolving landscape of Canadian law.

- *Auer v Auer*: The Supreme Court of Canada confirmed that the *Vavilov* reasonableness standard applies to the review of subordinate legislation and rejected the highly deferential approach from *Katz Group*.
- *TransAlta Generation Partnership v Alberta*: The Supreme Court of Canada applied the reasonableness standard to the review of subordinate legislation in the context of a challenge alleging administrative discrimination.
- *R v Sullivan*: In a case several years old but worth highlighting, the Supreme Court of Canada addressed the principles of horizontal *stare decisis* and tightened its requirements.
- *Buduchnist Credit Union Limited v 2321197 Ontario Inc*: The Ontario Court of Appeal confirmed its broad jurisdiction to enforce court orders, including *Mareva* injunctions.
- *660 Sunningdale GP Inc v First Source Mortgage Corp*: The Ontario Court of Appeal examined three often confused areas of law—penalty clauses, relief from forfeiture, and unconscionability—clarifying that the law of penalty clauses applies only to clauses triggered by a breach of contract.
- *Algarawi v Berger*: The Ontario Superior Court of Justice reaffirmed the law concerning the quality assurance privilege, providing clarity on its scope and application.

AUER V AUER

SCC Rejects Part of the *Katz Group* Approach to Assessing *Vires* of Subordinate Legislation

KEY TAKEAWAYS

The Supreme Court of Canada has rejected its earlier highly deferential approach to determining the *vires* of subordinate legislation and confirmed that the reasonableness standard set out in *Canada (Minister of Citizenship and Immigration) v Vavilov* is the presumptive standard.

Auer v Auer is significant in removing any doubt about the standard of review that applies to subordinate legislation and affirming the *Vavilov* reasonableness standard as appropriate. This reaffirmation and extension of *Vavilov* will likely further *Vavilov*'s objective of providing simplicity, predictability and coherence in judicial reviews. In this way, it may advance the SCC's previously stated goal of allowing both practitioners and courts to focus on the merits of administrative decisions instead of endlessly debating the standard of review.

There will, of course, still be issues to litigate regarding the standard of review. As in *Vavilov*, the Court in *Auer* recognized exceptions to the presumptive reasonableness standard where the legislature intends a different standard to apply or where the rule of law requires a different standard. The SCC recognized in *Vavilov* that these categories are not closed. In that vein, in *Auer*, the SCC specifically acknowledged a particular exception to the reasonableness standard that applies to subordinate legislation — when it is alleged that subordinate legislation did not respect the division of powers between Parliament and the provincial legislatures. While the scope for debate regarding the standard of review is far more limited than previously, there are still narrow avenues for counsel and courts to consider.

In addition to determining the standard of review, as in *Vavilov*, the SCC in *Auer* took the opportunity to provide useful guidance regarding how the reasonableness standard ought to be applied. The guidance provided in *Auer* may be particularly useful given that the review of subordinate legislation is somewhat different from other types of judicial review. In an important statement regarding the proper inquiry for the review of subordinate legislation, the SCC noted that the reasonableness standard does not assess the reasonableness of the rules promulgated by the regulation-making authority but rather the reasonableness of the regulation-making authority's interpretation of its statutory regulation-making power. Parties challenging the *vires* of subordinate legislation or responding to such challenges should be careful to focus on precisely that — the regulation-maker's interpretation of its regulation-making power.

While the Court has clearly disavowed the highly deferential approach of *Katz Group Canada Inc v Ontario (Health and Long-Term Care)*, it retained some of the *Katz Group* principles, including the presumption in favour of the validity of the impugned subordinate legislation. Thus, despite the change to the *Vavilov* reasonableness standard, it may remain challenging for those seeking to establish that subordinate legislation is *ultra vires*. Of note in this regard, even with the less deferential standard of review, in both *Auer* and the companion case *TransAlta Generation Partnership v Alberta*, the challenge to the *vires* of the subordinate legislation was unsuccessful.

CASE COMMENTARY

In *Auer v Auer*, the appellant sought to challenge the *vires* of the Federal Child Support Guidelines which were enacted pursuant to the *Divorce Act*. The appellant argued that the Governor in Council exceeded its authority in various ways in enacting the Guidelines. In rejecting the appellant's arguments regarding the Guidelines, the SCC had to consider whether the approach to assessing the *vires* of subordinate legislation set out in *Katz Group Canada Inc v Ontario (Health and Long-Term Care)* remained appropriate in the aftermath of *Canada (Minister of Citizenship and Immigration) v Vavilov*.

In *Katz Group*, the SCC considered a challenge to regulations made under two Ontario statutes which prevented private label drug products from being listed in the provincial Formulary or designated as "interchangeable". Two separate pharmacy chains, including one represented by now Justice Jamal, argued

unsuccessfully for the Court to overturn the regulations as *ultra vires*. In upholding the regulations, the SCC concluded that regulations could only be found *ultra vires* if they were determined to be "irrelevant", "extraneous" or "completely unrelated" to the purpose of the governing statute. The Court's approach was highly deferential with Justice Abella noting that it would take an "egregious" case for the Court to intervene.

In its later decision in *Vavilov*, the SCC considered a judicial review of a decision by the Canadian Registrar of Citizenship who determined that Mr. Vavilov was not a Canadian citizen based on an interpretation of a provision in the *Citizenship Act*. In reviewing this decision, the SCC broke with past jurisprudence regarding the standard of review. In an effort to improve clarity and certainty in the area, the Court in *Vavilov* concluded that the presumptive standard for administrative decision-making is reasonableness. The Court noted that there were only limited exceptions to this reasonableness standard where the legislature intends a different standard to apply or where the rule of law requires a correctness standard.

While *Vavilov* brought a sweeping change in the law of judicial review, one of the questions that was left unanswered was whether its default reasonableness standard applied to assessing the *vires* of subordinate legislation which was not specifically addressed in the decision.

The *Auer* Decision

Ultimately, while the SCC in *Auer* reaffirmed various principles from *Katz Group*, it rejected the highly deferential "irrelevant", "extraneous" or "completely unrelated" approach. Instead, the Court in *Auer* confirmed the extension of *Vavilov*'s "robust reasonableness" to the review of the *vires* of subordinate legislation.

In terms of the principles from *Katz Group* which remain, the Court in *Auer* reaffirmed that:

- A successful challenge to the *vires* of regulations requires that they be shown to be inconsistent with the objective of the enabling statute or the scope of the statutory mandate;
- Regulations benefit from a presumption of validity which has two aspects: (1) it places the burden on challengers to demonstrate the invalidity of regulations, and (2) it favours an interpretive approach that reconciles the regulation with its enabling statute so that, where possible, the regulation is construed in a manner which renders it *intra vires*;
- Both the challenged regulation and the enabling statute should be interpreted using a broad and purposive approach consistent with the Court's approach to statutory interpretation generally; and
- The Court's inquiry does not involve assessing the policy merits of the regulations to determine whether they are necessary, wise, or effective in practice.

While affirming these principles, the SCC went on to clearly depart from its earlier decision in *Katz Group* regarding the threshold for court intervention. Following *Vavilov*, the SCC in *Auer* concluded that the default standard of review for assessing the *vires* of all subordinate legislation is reasonableness. The Court noted that the reasonableness standard applies regardless of the delegate who enacted the regulations, their proximity to the legislative branch or the process by which the subordinate legislation was enacted.

As in *Vavilov*, the SCC in *Auer* then provided helpful guidance on how the reasonableness review is to be carried out, noting that such reviews can proceed even in the absence of formal reasons from the decision-maker — a critical point given that there often are not formal reasons associated with the enactment of subordinate legislation.

The Court emphasized, as it had in *Katz Group*, that conducting a reasonableness review is not an examination of policy merits. Instead, it addresses the reasonableness of the regulation-making authority's interpretation of its statutory regulation-making power. The Court's role is to review the legality or validity of subordinate legislation, not to review whether it is necessary, wise, or effective in practice.

Turning to the case at hand, the Court analyzed the Guidelines having regard to the *Divorce Act* under which they were enacted, and concluded that the Guidelines were *intra vires*.

TRANSALTA GENERATION PARTNERSHIP V ALBERTA

SCC Explains Reasonableness Review of Subordinate Legislation When Administrative Discrimination is Alleged

KEY TAKEAWAYS

TransAlta Generation Partnership v Alberta provides a useful guide to the application of the reasonableness standard set out in *Canada (Minister of Citizenship and Immigration) v Vavilov* in the context of a challenge based on an allegation of administrative discrimination.

Quite apart from its contribution to the caselaw concerning *Vavilov* and reasonableness review, *TransAlta* is also a useful reconsideration of the common law concerning administrative discrimination. This relatively infrequently litigated aspect of administrative law has been touched on by the SCC only a handful of times since its leading decision in *Montreal v Arcade Amusements Inc*.

As in the companion case *Auer v Auer*, the failure of the challenge in *TransAlta* may reflect the fact that certain aspects of the *Katz Group Canada Inc v Ontario (Health and Long-Term Care)* framework, including the presumption of validity, remain. Despite the rejection of the highly deferential *Katz Group* approach, disputing the *vires* of subordinate legislation may continue to be challenging.

CASE COMMENTARY

TransAlta Generation Partnership v Alberta is a companion case to *Auer v Auer*. In *TransAlta*, the SCC considered the *Vavilov* reasonableness standard applied to a challenge to subordinate legislation on the basis of alleged administrative discrimination.

The appellants, TransAlta Generation Partnership and TransAlta Generation (Keephills 3) (together, "TransAlta") owned coal-fired electric power generation facilities in Alberta. In 2016, TransAlta entered into an agreement with the provincial Crown pursuant to which it agreed to cease coal-fired emissions in exchange for transition payments from the province. TransAlta challenged the *vires* of certain guidelines (the "Linear Guidelines") issued under the *Municipal Government Act* which address municipal taxation. The Linear Guidelines provide that TransAlta and other parties to off-coal agreements are ineligible to claim additional depreciation to account for the reduced life of their coal-fired facilities.

The appellants challenged the validity of the Linear Guidelines on two bases. First, they invoked the common law principle that a statutory delegate has no authority to make discriminatory distinctions unless the statute either expressly, or by necessary implication, grants them such authority. Second, the appellants argued that the Linear Guidelines are inconsistent with the overarching purpose of the assessment and taxation regime under the *Municipal Government Act*.

> *TransAlta* provides a useful guide to the application of the reasonableness standard set out in *Vavilov* in the context of a challenge based on an allegation of administrative discrimination.

With respect to the first challenge, the Court noted that administrative discrimination arises when subordinate legislation expressly distinguishes among the persons to whom its enabling legislation applies. It is different from the discrimination addressed in the *Charter* and human rights legislation. It relates to the drawing of distinctions between persons or classes that are discriminatory in the non-pejorative sense in that they simply do not

apply equally to all those engaged in the activity that are subject of the enactment. Subordinate legislation that discriminates is invalid unless the discrimination is authorized by the enabling statute.

Applying the law to the Linear Guidelines at issue, the SCC disagreed with the lower courts and concluded that the Linear Guidelines did actually discriminate against the appellants. The SCC noted that TransAlta was discriminated against because owners of linear property who are not parties to off-coal agreements are eligible to make claims for additional depreciation, while the parties to the off-coal agreements cannot. The Court noted that the fact that all parties to off-coal agreements are treated equally in this respect does not mean they are not discriminated against.

The Court, however, went on to uphold the validity of the Linear Guidelines after analyzing the *Municipal Government Act* and concluding that the discrimination was authorized by statute. The Court noted that the question of statutory authorization to discriminate falls within the reasonableness review called for by *Vavilov*. The Court further noted the grant of authority in the *Municipal Government Act* is broad — "without limitation" — and that, pursuant to this authority, the Minister has authority to draw distinctions on the basis of the specifications and characteristics of properties, including whether the property is subject to an off-coal agreement.

Regarding the second issue, the Court then considered whether the Linear Guidelines are consistent with the scheme and purpose of the *Municipal Government Act*. Given that the Court had concluded that the Minister had authority to discriminate between different types of property, the next question was whether the Minister exercised that authority in a manner that is consistent with the scheme and purpose of the *Municipal Government Act*. After analyzing the purpose of the Act — (1) to establish a property assessment system that fairly and equitably distributes taxes and promotes transparency, predictability and stability, and (2) to ensure that assessments are current, correct, fair and equitable — the SCC concluded that the Linear Guidelines, and the discrimination against owners with off-coal agreements, were in accordance with it.

The Court concluded that TransAlta had not met its burden of proving that the Linear Guidelines were *ultra vires* the Minister, with the result that the guidelines were upheld.

R V SULLIVAN

SCC Reiterates Importance of – and Tightens Test for – Horizontal *Stare Decisis*

KEY TAKEAWAYS

Though not a new decision, *R v Sullivan* is a helpful reminder of the importance of decisions from judges of concurrent jurisdiction. They are not merely persuasive; unless the *Spruce Mills* criteria are met, they must be followed.

Counsel should familiarize themselves with the essential features of horizontal *stare decisis* set out in *Sullivan*. Not only did the SCC reiterate the importance of its principles, but the Court also tightened its application by explicitly rejecting any notion that the decision of a judge of concurrent jurisdiction may be departed from simply based on a judicial difference of opinion.

Counsel faced with an unfavourable decision of a judge of concurrent jurisdiction should be prepared to argue why the *Spruce Mills* test means that the earlier decision may be departed from. Meanwhile, counsel with a favorable decision should make use of *Sullivan* in arguing that, absent one of the *Spruce Mills* criteria applying, the earlier decision must be followed.

Notably, horizontal *stare decisis* applies differently at different levels of court. Both *R v Sullivan* and *Spruce Mills* address horizontal *stare decisis* at the trial level. *R v Kirkpatrick* discusses horizontal *stare decisis* at the Supreme Court of Canada. Though not specifically referenced, the discussion in *Kirkpatrick* is interesting in light of the Court's treatment of its prior decisions in *Auer*.

With respect to vertical *stare decisis*, the Court in *Sullivan* reiterated the approach set out earlier by the SCC in *Bedford v Canada*.

CASE COMMENTARY

Although counsel routinely have regard for the principles of vertical *stare decisis* (that a decision of a higher court is binding on a lower court), less attention is generally paid to the related doctrine of horizontal *stare decisis* (which applies with respect to decisions from courts of concurrent jurisdiction). In a decision that is not new but is notable, the Supreme Court of Canada in *R v Sullivan* redefined the principle of horizontal *stare decisis* and emphasized its importance.

The Supreme Court of Canada in *R v Sullivan* redefined the principle of horizontal *stare decisis* and emphasized its importance.

R v Sullivan was a criminal appeal which considered the constitutionality of section 33.1 of the Criminal Code. The issue of *stare decisis* arose because there had been other cases in which superior courts of Ontario had declared the provision unconstitutional. In this case, the accused argued that the trial judge was bound by these decisions. The accused also argued that a section 52(1) declaration of unconstitutionality by one superior court judge effectively removes the provision from the Criminal Code.

The SCC explicitly rejected the argument that a court may depart from a prior judgment of a court of concurrent jurisdiction if the earlier decision is considered "plainly wrong", for "good reason", or due to "extraordinary circumstances". As the Court noted:

> "[t]he institutional consistency and predictability rationales of *stare decisis* are undermined by standards that enable difference in a single judge's opinion to determine whether precedent should be followed".

In terms of the limited situations in which a decision of a judge of concurrent jurisdiction need not be followed, the Supreme Court approved of the framework in *Hansard Spruce Mills Ltd (Re)* in which the Court noted that another judgment may be departed from if:

> (1) the rationale of an earlier decision has been undermined by subsequent appellate decisions;
>
> (2) the earlier decision was reached *per incuriam* ("through carelessness" or "by inadvertence"); or
>
> (3) the earlier decision was not fully considered (e.g., taken in exigent circumstances).

With respect to the first element, a decision can be departed from where it has been overruled by, or is necessarily inconsistent, with a decision of a higher court. Second, a judge may depart from a decision where it was reached without considering a relevant statute or binding authority – *per incuriam* or by inadvertence. The Court noted that this circumstance is likely to be "rare". In order to apply, it is not enough that there was an authority not mentioned in the decision; it must be that the missing authority affected the judgment. Third, a judge may depart from a prior authority where the exigencies of a trial required an immediate decision without the opportunity to consult authority fully and thus the decision was not fully considered.

Where, as in *Sullivan*, a judge is faced with conflicting authority, the judge must follow the most recent authority unless the *Spruce Mills* criteria are met.

The Court noted that where, as in *Sullivan*, a judge is faced with conflicting authority, the judge must follow the most recent authority unless the *Spruce Mills* criteria are met.

In addressing the effect of a section 52 declaration of invalidity, the Court noted that, in issuing a declaration that a law is inconsistent with the Constitution and thus of no force and effect, a judge is exercising an ordinary judicial power to determine a question of law. The law is not "struck from the books" as a result of a section 52 declaration. The SCC noted, in this regard, that it is legislatures that have the power to remove laws from the statute books, not judges.

The Court turned to consider the legal nature and effect of a section 52(1) declaration beyond the parties to the litigation. The Court noted that a section 52 determination is binding *erga omnes* (towards all) as a matter of precedent, according to the ordinary rule of *stare decisis*, and not because the law has been truly removed from the statute books. The Court noted the difference between a section 52(1) declaration and a section 24 remedy: section 52(1) operates *erga omnes* and not on a case-by-case basis. The doctrine of *stare decisis* extends the effect of the judgment declaring a provision unconstitutional beyond the parties to the case, *erga omnes* within the province at least.

The Court noted the impact of federalism with respect to declarations of unconstitutionality under section 52(1). Federalism prevents a section 52(1) declaration issued within one province from binding courts throughout the country. A declaration made in one province may be followed in another because it is persuasive, but a declaration issued by a superior court in BC does not bind a superior court in Quebec or Alberta.

BUDUCHNIST CREDIT UNION LIMITED V 2321197 ONTARIO INC

Court of Appeal Affirms Broad Jurisdiction to Respond to Breach of a *Mareva* Order

KEY TAKEAWAYS

Buduchnist Credit Union Limited v 2321197 Ontario Inc confirms the Court's broad remedial powers to address breaches of court orders, in this case a breach of a *Mareva* Order.

Parties with notice of *Mareva* orders should be assiduous in ensuring that they respect them. If they do not, their options may be limited if they subsequently come to court seeking the court's assistance.

CASE COMMENTARY

In *Buduchnist Credit Union Limited v 2321197 Ontario Inc*, the Court of Appeal considered its jurisdiction to respond to a breach of a *Mareva* order.

In *Buduchnist*, the appellant, Trade Capital, was the victim of an elaborate fraud in which it paid for accounts receivable which were entirely fraudulent. Trade Capital took various steps to trace and recover the monies lost through the fraudulent scheme including obtaining a *Mareva* order which froze assets owned directly or indirectly by the *Mareva* defendants. The *Mareva* order also restrained all persons with notice of it from encumbering any assets of the relevant parties. On the *Mareva* motion, the judge was satisfied Trade Capital had made out a strong *prima facie* claim of fraud. Trade Capital served the *Mareva* order on Buduchnist Credit Union ("BCU") which held mortgages over properties owned by one of the alleged fraudsters. Following receipt of the *Mareva* order, BCU made advances to the alleged fraudster and his related corporations on various mortgages. The mortgages went into default.

BCU brought an action and obtained judgment against the fraudsters. BCU then obtained the appointment of a receiver and sought an order directing the receiver to distribute to it the net proceeds of sale after payment of the receiver's fees and expenses.

The parties agreed that BCU should retain its priority for all pre-*Mareva* advances. However, Trade Capital argued that BCU should not be paid any amounts that it advanced following its receipt of the *Mareva* order in priority to the amounts owing to Trade Capital.

The motion judge found that BCU had breached the *Mareva* order and that, as a result, it could not claim priority payment as a secured creditor for the advances made in breach of that order. However, he determined that BCU, in its capacity as a judgment creditor, was still entitled to immediately enforce its judgment against the fraudster and therefore varied the application of the *Mareva* order for that limited purpose. The effect of the motion judge's order was that BCU could execute on its judgment and recover amounts owed, including the funds advanced contrary to the *Mareva* order. If Trade Capital was ultimately successful in its action against the fraudster, those funds advanced contrary to the *Mareva* order would no longer be available.

> The deliberate breach of court orders strikes at the very heart of the administration of justice and can never be tolerated.

On appeal, the Court confirmed that BCU had breached the *Mareva* order in advancing the funds. It noted that the key issue was whether the Court should exercise its discretion and vary the *Mareva* order for the purpose of allowing BCU to enforce its judgment and recover funds advanced in breach of the *Mareva* order.

The Court noted that its broad jurisdiction to craft an appropriate order in response to a breach of a court order arises from its well-established inherent jurisdiction to prevent an abuse of the court's process. The Court noted that the deliberate breach of court orders strikes at the very heart of the administration of justice and can never be tolerated. The Court noted that BCU's creditor protection argument ignored the

consideration, in light of the motion judge's finding of a breach, that its claim to the post-*Mareva* advances would never have arisen but for its breach of a clear court order.

The Court noted its broad jurisdiction in the face of a breach of a court order includes the power to dismiss or refuse to entertain a proceeding. The jurisdiction clearly encompasses the jurisdiction to postpone the enforcement of a creditor's claim arising solely from a breach of a court order. BCU did not have a judgment for debt arising in the normal course; rather the debt owed to BCU only arose because of BCU's breach of a clear court order. The Court of Appeal concluded that the motion judge had mistakenly determined that he lacked jurisdiction to order that the receiver hold proceeds pending the resolution of Trade Capital's claims.

The Court's broad jurisdiction in the face of a breach of a court order includes the power to dismiss or refuse to entertain a proceeding.

The Court concluded that the justice of the case did not warrant the variance of the *Mareva* order in favour of BCU to permit the distribution of the post-*Mareva* advances. It noted that, given the breach of the *Mareva* order, BCU did not come to court with clean hands. There would be no unfairness to BCU if the *Mareva* order is not varied because, but for BCU's breach of the *Mareva* order, the indebtedness in issue would not exist. There would, however, be tremendous unfairness to Trade Capital. It is the victim of an elaborate fraud and has expended considerable time and expense. Allowing BCU to reap the fruits of its improper actions would undermine the administration of justice and offend the rule of law.

The Court concluded that removing BCU's secured creditor priority was a reasonable exercise of the motion judge's discretion, but it did not go far enough. In light of BCU's breach and in response to its motion for distribution, the appropriate and proportionate order was to delay the enforcement of BCU's judgment while the *Mareva* order remained in place until Trade Capital's proceeding against the fraudster was determined.

The Court ordered that enforcement of BCU's judgment be delayed until Trade Capital obtains judgment or its action is otherwise determined. If Trade Capital obtains judgment, Trade Capital and BCU should collect on their respective judgments which would rank equally.

660 SUNNINGDALE GP INC V FIRST SOURCE MORTGAGE CORP

Court of Appeal Affirms No Penalty Clause or Relief from Forfeiture Without a Contractual Breach

KEY TAKEAWAYS

660 Sunningdale GP Inc v First Source Mortgage Corporation provides a useful clarification of the law concerning three related, and often confused, areas of the law: penalty clauses, relief from forfeiture, and the doctrine of unconscionability.

In this decision, the Court of Appeal confirmed that the law of penalty clauses and relief from forfeiture only has application with respect to provisions that apply in relation to a breach of contract. While there may be broader scope for the doctrine of unconscionability, it too has specific requirements including an inequality of bargaining power and an improvident bargain.

CASE COMMENTARY

In *660 Sunningdale GP Inc v First Source Mortgage Corporation*, the Court of Appeal overturned a motion decision which refused to enforce a contractual term on the grounds that it was a penalty clause and also granted relief from forfeiture in regard to the provision. In overturning the lower court decision, the Court of Appeal confirmed that the law regarding penalty clauses and relief from forfeiture has no application absent a contractual breach.

660 Sunningdale agreed, as part of a loan agreement, to pay a "Lender Fee" equal to 2.75% of the loan amount. The Lender Fee was due upon acceptance and execution of the commitment. $100,000 of the Lender Fee was to be paid upon execution of the loan agreement, with the remainder paid in accordance with the terms of the loan agreement.

660 Sunningdale decided not to proceed with the loan and ultimately brought a proceeding seeking the refund of the $100,000 it had paid upon the acceptance and execution of the commitment, and the balance of the $326,5000 of the Lender Fee which had been held in trust given the dispute between the parties. 660 Sunningdale alleged that the termination of the loan arrangement was the fault of the lender.

On a summary judgment motion, the lower court judge was unable to determine that the termination of the loan was the fault of the lender which would have permitted 660 Sunningdale to avoid the Lender Fee under the terms of the contact. The motion judge concluded that the $100,000 was a "pre-estimate of damages" and not a penalty clause which the lender was permitted to retain. The motion judge did, however, conclude that the balance of the Lender Fee was unenforceable as a penalty clause and that relief from forfeiture should be granted under section 98 of the *Courts of Justice Act*. The motion judge concluded that the Lender Fee was a "stipulated remedy clause" which was:

> (1) an unenforceable penalty clause if it is "extravagant and unconscionable in amount in comparison with the greatest loss that could conceivably be proved to have followed from the breach"; or
>
> (2) a forfeiture, that is eligible for relief from forfeiture because it would be unconscionable for the party seeking the forfeiture to retain the right, property or money forfeited (citing *Peachtree II Associates – Dallas LP v 857486 Ontario Ltd*).

In overturning the lower court decision, the Court of Appeal confirmed that the law regarding penalty clauses and relief from forfeiture has no application absent a contractual breach.

The Court of Appeal overturned the motion decision.

The Court of Appeal rejected the argument that the law relating to unenforceable penalty clauses applied at all. The Court noted that the Lender Fee is not payable as a stipulated remedy for breach but rather as consideration for First Source obtaining the loan commitment. By its terms, the Lender Fee was payable as consideration whether or not the contract was ultimately breached by 660 Sunningdale. Put otherwise, the obligation to pay the Lender Fee did not arise because of conduct by 660 Sunningdale, as a remedy for that conduct. The Lender Fee was, therefore, not a stipulated remedy clause and could not be an unenforceable penalty clause. The Court noted in this regard that, unless a term of a contract stipulates a purported remedy for a breach, it cannot be a penalty clause.

The Court also concluded that the motion judge had erred in applying the law of relief from forfeiture. Relief from forfeiture may be available to relieve a party of the consequences of its non-observance or breach of the terms of a contract. The balance of the Lender Fee was payable under the terms of the Loan Agreement regardless of any breach or non-observance of its terms. The Court noted that, by granting relief against forfeiture from a contractual payment obligation that did not arise from any breach of the loan agreement, the motion judge in effect applied the independent doctrine of unconscionability incorrectly in the circumstance given that there was no finding of inequality of bargaining power. With respect to relief from forfeiture, the Court noted that the paradigm circumstance in which it is available is where the enforcement of a clause inserted to secure some aspect of the bargain would result in overcompensation for a breach of contract by the party seeking relief. The doctrine may also be applied where there has been fraud, accident, mistake or surprise. As the Court noted:

> "[i]t is not the role of relief against forfeiture to relieve parties from terms of a contract they agreed to, on the grounds of the improvidence of that term. That is the function of the independent doctrine of unconscionability".

Unless a term of a contract stipulates a purported remedy for a breach, it cannot be a penalty clause.

The Court noted that the penalty clause doctrine and relief against forfeiture are available in a relatively narrow set of circumstances while the doctrine of unconscionability has a wider ambit. The Court noted, however, that the doctrine of unconscionability is limited to unfair agreements that have resulted from inequality of bargaining power, a circumstance that had no application in the instant case.

The Court of Appeal concluded that the motion judge had erred in granting summary judgment to 660 Sunningdale with respect to the balance of the Lender Fee.

ALGARAWI V BERGER

Court Confirms Quality Assurance Privilege

KEY TAKEAWAYS

Algarawi v Berger serves as a helpful reminder of the quality assurance privilege, which can be used to protect communications aimed at improving health care following negative outcomes. While it is not a categorical privilege and must be established on a case-by-case basis, courts have given it clear recognition.

It should also be noted that a quality assurance privilege can exist in situations other than the health care context. In *Lipson v Cassels Brock & Blackwell* for instance, Justice Perell considered it in relation to communications involving memoranda from a law firm's Ethics and Standards Committee. The memoranda related to tax advice which had been provided by one of the firm's partners. Justice Perell noted that the committee was playing the same role as played by in-house counsel for a business entity like a corporation with the law firm, in effect, acting as the client of the committee. The Court concluded that the documents were solicitor-client privileged, but also irrelevant. Though it was unnecessary given his finding of irrelevance, Justice Perell went on to consider the possible application of quality assurance privilege given that it had been fully argued before him. He noted that, to apply, the Court must be satisfied that the communications were genuinely made as a quality assurance measure with a view to improving the quality of legal services and to ensure that the firm's clients are safeguarded from mistakes in the firm's provision of legal services. After applying the *Wigmore* criteria, Justice Perell concluded that the quality assurance privilege can be available to law firms and that it was available in the immediate case.

It is not difficult to imagine other contexts in which similar claims to quality assurance privilege may be appropriate.

CASE COMMENTARY

In *Algarawi v Berger*, the Court confirmed that quality assurance privilege exists to protect documents created in connection with steps aimed at improving the quality of patient care. In this case, the Court considered material generated by doctors regarding the care provided in order to inform a discussion of what, if anything, could be learned from the events at issue in the litigation. While the material was deemed relevant to the proceeding, it was also determined to be privileged.

The Court found that the defendants could not bring themselves within the protection of the *Quality of Care Information Protection Act* ("QCIPA") which provides a statutory privilege over certain quality assurance communications in specific circumstances. The QCIPA provides robust, categorical protection for activities that fall within the process created by the QCIPA. The Court noted that the legislature is presumed not to alter the common law unless the language of the statute demonstrates clearly and unambiguously that it intended to do so. The Court also noted that there was nothing in the statute that limit any common law privilege that would otherwise apply to material that does not fall within the privilege protection under the QCIPA.

> Quality assurance privilege exists to protect documents created in connection with steps aimed at improving the quality of patient care.

The Court then went on to consider the *Wigmore* case-by-case privilege and assessed whether it applied in the circumstances. The four conditions necessary to establish common law privilege were first articulated by Wigmore and subsequently adopted by the Supreme Court of Canada in *Slavutych v Baker* as follows:

- The communications must originate in a confidence that they will not be disclosed;
- This element of confidentiality must be essential to the full and satisfactory maintenance of the relation between the parties;

- The relation must be one which in the opinion of the community ought to be sedulously fostered; and
- The injury that would be caused to the relation by the disclosure of the communications must be greater than the benefit thereby gained for the correct disposal of litigation.

Applying these criteria to the documents in question, the Court concluded that:

- The communications had originated in confidence in that they were labelled confidential and the uncontradicted evidence was that there was an expectation of confidentiality;
- Confidentiality was essential to the quality assurance program. While such programs would exist regardless of confidentiality, confidentiality is essential in their success. Knowing that the discussions are not off the record would create a powerful disincentive to full and frank participation;
- The relationship should be diligently fostered. Society desires to improve the quality of health care, quality of care reviews contribute significantly to that goal and confidentiality is essential for quality-of-care reviews to achieve that purpose; and
- The injury caused by disclosure is greater than the benefit gained for the correct disposal of litigation. The Court agreed with the associate judge's determination that there was minimal benefit to disclosure because the medical records had already been produced which contained the relevant facts, the individual defendants had been examined for discovery and the quality assurance process did not result in any policy or systemic changes. On the other hand, disclosure would cause damage to the effectiveness of quality assurance processes going forward.

The appeal was dismissed, and the privilege claim was upheld.

About the Author

Lynne's practice is focused on legal research, written advocacy, and advice. She uses her thorough understanding of the law to help our clients analyze their complex legal problems and execute the best litigation strategy.

Prior to joining Lenczner Slaght and after starting her career practicing litigation at a large full-service firm, Lynne spent 20+ years practicing litigation for the provincial Crown.

During her career, Lynne has acted for clients in a wide variety of proceedings including oppression and dissent claims, commercial disputes, various class actions and injunctions, an aggregate claim for the recovery of health care costs caused by smoking, judicial reviews, and the defence of Crown attorneys and police officers.

Lynne has appeared at all levels of court including the Supreme Court of Canada.

Lynne McArdle

RESEARCH COUNSEL
416-238-1860
lmcardle@litigate.com