TAB 2

What's So Good About Good Faith?

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Safeguarding Real Estate Transactions –
Protecting Your Clients from the Dangers of Litigation
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THE DUTY - WHAT'S IT ALL ABOUT?

In the past few years the duty to act in good faith has been finding broad application across various fields of law. Contract law generally has always contemplated the idea of good faith but specific practice areas such as franchise, construction, employment, and insurance are finding particular and increasing application of the principal. Real estate transactions is another area where the duty to act in good faith is oft-contemplated. Parties to a transaction and their counsel are well advised that acting in "good faith", however defined, is certain to work to their benefit should contractual problems arise.

What is less certain is what, exactly "good faith" entails and the breadth of its parameters. "Good faith" tends to exist in specific relation to the terms of the contract in question and the particular circumstances at hand. Even still, litigation seems to focus on establishing the existence of "bad faith" as evidence of a lack of "good faith". The Ontario Court of Appeal affirmed in *Shelanu Inc. v. Print Three Franchising Corp* that the standard of good faith is breached when a party "*acts in a bad faith manner*".[1]

[1] *Shelanu Inc. v. Print Three Franchising Corp.* (2003), 64 O.R. (3d) 533

In Shelanu, Justice Weiler found that the duty of good faith allows a party to act in its own self-interest, while having regard to the legitimate interests of the other party. Justice Weiler stated:

> "Unconscionability" accepts that one party is entitled as of course to act self-interestedly in his actions towards the other. Yet in deference to that other's interests, it then proscribes excessively self-interested or exploitative conduct. *"Good faith," while permitting a party to act self-interestedly, nonetheless qualifies this by positively requiring that party, in his decision and action, to have regard to the legitimate interests therein of the other.* The "fiduciary" standard for its part enjoins one party to act in the interests of the other — to act selflessly and with undivided loyalty. There is, in other words, a progression from the first to the third: from selfish behaviour to selfless behaviour. Much the most contentious of the trio is the second, "good faith." It often goes unacknowledged. It does embody characteristics to be found in the other two [emphasis added].[2]

Justice Weiler continued that the duty of good faith *"requires that parties to a contract exercise their rights under that agreement honestly, fairly and in good faith."* "Good faith" conduct is the *"guide to the manner in which the parties should pursue their mutual contractual objectives. Such conduct is breached when a party acts in "bad faith" — a conduct that is contrary to community standards of honesty, reasonableness or fairness."*

As "good faith" is somewhat of an amorphous term, its application attracts evaluation on a case-by-case basis. From the litigation perspective this is helpful as there is a healthy body of jurisprudence addressing the various aspects of real estate transactions where the duty to act in good faith appears. Below are various situations where the real estate solicitor will benefit from a keen awareness.

WHEN DO VENDORS OR PURCHASERS HAVE TO ACT IN GOOD FAITH?

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[2] *Ibid* at para. 68

Pre-Contractual Negotiations

Ontario courts have not yet recognized a duty to negotiate a contract in good faith. In *International Corona Resources Ltd. v. Lac Minerals Ltd.*, the possibility of such a pre-contractual duty seemed to be emerging. Justice LaForest stated:

> [T]he institution of bargaining in good faith is one that is worthy of legal protection in those circumstances where that protection accords with the expectation of the parties.[3]

Subsequent decisions, however, did not pick up on Justice LaForest's comment and have avoided the application of good faith principles in a pre-contractual setting. In *Martel Building Ltd. v. Canada*[4], the Supreme Court of Canada considered whether the tort of negligence included a duty of care on parties during contractual negotiations for a leased premises.

The Supreme Court recognized that the bilateral nature of most negotiations means that gains of one party are sometimes obtained at the expense of the other party. The court noted that the prospect of causing deprivation by economic loss is implicit in the negotiating environment and found a *prima facie* duty of care. Despite this, the court held that there were policy reasons to negate that duty or as they put it: "*compelling policy reasons to conclude that one commercial party should not have to be mindful of another commercial party's legitimate interests in an arm's length negotiation*."[5] These policy reasons include:

- the primary goal of commercial negotiations is to achieve the most advantageous financial bargain. In the context of bilateral negotiation, such gains are realized at the expense of the other negotiating party;

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[3] [1989] 2 S.C.R. 574
[4] [2000] 2 S. C.R. 860
[5] *Ibid* at para. 55

- Second, there is a risk of deterring socially and economically useful conduct. It would defeat the essence of negotiation and hobble the market place to extend a duty of care to the conduct of negotiations and to label as negligent a party's failure to disclose its bottom line, its motives or its final position. This would force the disclosure of privately acquired information and the dissipation of any competitive advantage derived from it. This would be incompatible with the activity of negotiating and bargaining;

- Third, to impose a duty could interject tort law as after-the-fact insurance against failures to act with due diligence or to hedge the risk of failed negotiations through the pursuit of alternative strategies or opportunities;

- Fourth, the courts would assume a significant regulatory function, scrutinizing the minutiae of pre-contractual conduct, when other causes of action already provide remedies; and,

- Fifth, needless litigation should be discouraged – extending a duty of care to negotiations would encourage a multiplicity of proceedings.[6]

In *Peel Condominium Corporation No. 505 v. Cam-Valley Homes Ltd.*[7] The Ontario Court of Appeal used *Martel* for the authority that there is no duty to bargain or negotiate in good faith in Canadian contract law. Here, a condominium corporation was suing the developer for building neighbouring townhouses when it was their expectation that a park was going to be constructed. At the trial level, Justice Epstein found for the condominium corporation. In reaching her conclusions, Justice Epstein relied on the principle that contracting parties owe one another a duty to act reasonably and in good faith.

At the Court of Appeal, the ruling was overturned by a split decision. Speaking for the majority, Justice Finlayson was careful to separate contract formation from contract performance and citing Martel he confirmed that It is only after the contract is negotiated and signed that the

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[6] *Ibid* at paras. 63-71
[7] 2001 CarswellOnt 579

purchaser is entitled to rely on the developer to carry out the agreement honestly and in good faith. With regard to Justice Epstein's reasons he stated:

> I think that the weakness of the trial judge's analysis is that she fails to draw a bright line between the status of the respective developer and purchaser prior to executing a binding agreement of purchase and sale and the obligation of the contracting parties to complete the closing of the sale in good faith.[8]

In *978011 Ontario Ltd. v. Cornell Engineering Co.* the Ontario Court of Appeal again addressed the good faith issue. Here, the trial judge ruled that the plaintiff had an obligation to bring a termination clause to the defendant's attention and struck out the clause from the contract in question. The plaintiff had drafted the contract which contained the termination clause providing for certain compensation to the plaintiff. The defendant did not read the termination clause before signing the contract and the provision had not formed a part of the negotiations. On appeal, the Court of Appeal again confirmed that there is no duty of good faith in pre-contractual negotiations and reinstated the termination provision which heavily favoured the plaintiff.

In *Martel*, the court had left open the particular question of "good faith" as separate from the question of a duty of care during pre-contractual negotiations:

> As a final note, we recognize that Martel's claim resembles the assertion of a duty to bargain in good faith. The breach of such a duty was alleged in the Federal Court, but not before this Court. As noted by the courts below, a duty to bargain in good faith has not been recognized to date in Canadian law. These reasons are restricted to whether or not the tort of negligence should be extended to include negotiation. Whether or not negotiations are to be governed by a duty of good faith is a question for another time.[9]

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[8] *Ibid* at para 38

[9] *Supra* Note 3 at para 73

Despite this, the courts have yet to find any duty of good faith in pre-contractual negotiations and have left parties to make whatever agreement they wish. Generally, no duty of care arises in conducting negotiations. The duty to bargain in good faith has not been recognized in Canadian law. The duty, it would seem, comes into existence when a contract is signed.

During the Life of a Contract

Once a contract is in place, traditionally, there has been an overarching obligation of the part of both sides to the transaction to act in good faith in respect of the completion of the transaction. In *Amaren Corp v. Cara Operations Ltd.*[10] Justice Farley stated:

> *There is no independent duty of good faith and fair dealing in Ontario. There is of course a duty to fulfil the contractual obligations of a contract in good faith.*

Generally, the Court will not countenance a party to a transaction's bad faith, or surreptitious attempts to free themselves of contractual responsibilities by whatever means. The vendor, and the purchaser, must to do everything necessary to perform the contract:

> the court will readily imply a promise on the part of each party to do all that is necessary to secure performance of the contract[11]
>
> The court will also imply that each party is under an obligation to do all that is necessary on his part to secure performance of the contract[12]

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[10] [1999] O.J. No. 365 (Gen. Div.)
[11] 9 *Hals.* (4th ed.), p. 234, para. 350
[12] *Chitty on Contracts*, "General Principles", (23rd ed.) p. 316, para. 698

The decision of *Leung v. Leung*,[13] demonstrates that *"a vendor is under a duty to act in good faith and to take all reasonable steps to complete the contract."* Further, the case provides some useful rules by which parties to a real estate transaction must play:

- Where a vendor acted contrary to good faith in his performance of the contract, the law precludes him from relying on the "time of the essence" provision to terminate the contract...
- The duty to act in good faith to complete the contract extends to cases involving minor omissions or defects...
- No requirements of precision should be imposed on a party whose tendered performance include minor but easily corrected errors.[14]

Where minor problems exist at the time of tender there is a clear authority in Ontario for the proposition that good faith behavior may avail parties to a transaction to appropriate remedies. As one commentator notes:

> the doctrine of "good faith bargaining" or "fair dealing" has been utilized by the judiciary to address minor technical breaches and to prevent strict reliance on non-essential terms of the Contract, in an effort to alleviate hardship to one of the contracting parties, particularly in those circumstances where the party insistent upon strict adherence is not significantly prejudiced, or where there has been a lack of good faith or bona fides on the part of the non-defaulting party who is purporting to rescind the Contract as a consequence of the other party's breach or default[15]

As is outlined below, there may be little leeway in avoiding a transaction in "good faith", short of the options available when the innocent party attempts to satisfy all contractual requirements and is ready to tender.

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[13] [1990] O.J. No. 2276 (Ont. Gen. Div.)
[14] Barry J. Reiter, R.C.B. Risk and Bradley N. McLellan, Real Estate Law, 3rd ed., p. 790, cited in *Leung v. Leung*:
[15] *Supra* note 2 at page 3

In *DeFranco v. Khatri*[16] the vendors had expressed their interest in repudiating the agreement and a willingness to pay damages. The vendor showed up at the home of the purchaser and pleaded with the purchaser to accept damages in lieu of performance of the contract. Nonetheless, the purchasers sold their previous home and did everything to be ready to close.

The vendors refused to close and the purchasers did not tender on closing. After the failed closing date the purchasers looked at other homes but could not find something with a similar design, location and price. The purchaser sought specific performance of an agreement for the sale of a home and was found to have been acting in good faith despite his stern unwillingness to discuss the breaking of the contract in exchange for damages with the vendor who came pleading to his door.

WHEN DOES BAD FAITH (OR A LACK OF GOOD FAITH) CONTRIBUTE TO A BREACH?

Anticipatory breaches are a bad faith hallmark. An anticipatory breach as defined by Fridman, "*occurs when a party, by express language or conduct, or as a matter of implication from what he has said or done, repudiates his contractual obligations before they fall due.*"[17] While acting in good faith can mean as little as getting to the point of tender willing to complete the contract, an anticipatory breach is clearly a step of bad faith.

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[16] [2005] O.J. No. 1890 (Sup. Crt. Jus.)
[17] G.H.L. Fridman, The Law of Contract in Canada, 4th ed. (Toronto: Carswell, 1999) at 638

The case law is replete with parties trying to avoid contracts for minor defects, through unilateral action, or inaction, or by refusing to extend a closing, sometimes in a rising market. Generally, the avoidance constitutes breach of contract, and bad faith. As Middleton J. put it in *Hurley v. Roy*[18]*: "The policy of the Court ought to be in favour of the enforcement of honest bargains".*

Further, a party under an obligation to bring about an event on which a contract is conditional, who tries to repudiate the contract relying on the condition, must prove it used reasonable efforts to fulfill the obligation. Failing this, the party cannot rely on the condition to repudiate the contract. In his Annual Review of Civil Litigation, 2003, Archibald J. stated as follows:

> The impetus behind implying good faith principles in these conditional agreement cases is to prevent parties from short-circuiting contracts through their own misconduct. If parties cannot fulfil a condition based on circumstances beyond their control, that is understandable. However, the law will not countenance the conduct of a party which creates the very basis on which he or she seeks to rely to subvert a bargain. For the conditional clause to have any meaning, it must be under-girded by good faith notions. Otherwise, one party has virtually unfettered power to frustrate the objective of the contract - a result that is manifestly against the intention of the parties at the time of contracting.[19]

In Morgan (In Trust) v. Lucky Dog Ltd.[20]*,* bad faith came into play in a failed agreement. In awarding specific performance, the Court found that the vendor had acted in bad faith by manufacturing a situation in which closing the sale at the agreed date would be an unattractive option for the purchaser.

> [T]he vendor, by the conduct of its representatives, was disentitled from relying on the failure to close on July 31st, 1981 and, in refusing to close on August 4th, 1981, wrongfully repudiated its

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[18] *50 O.L.R. 281 at p. 285, 64 D.L.R. 375 at p. 377*

[19] Annual Review of Civil Litigation 2003,Chapter G - Good Faith in Contracts: A Continuing Evolution F. Paul Morrison and Hovsep Afarian

[20] [1987] O.J. No. 647 (H.C.J.)

> obligations under the agreement. It is my assessment on all of the evidence that the failure to close the transaction on July 31st, 1981 was the effectuation of the very result which the vendor's representatives deliberately orchestrated and strove to accomplish... and was the successful implementation of a stratagem which they intended and expected would throw the purchaser into disarray and--to use Mr. Yarmon's phrase (Ex. 86)--would make it "quite likely" that the purchaser would either wish to delay closing beyond July 31st (a request which they were expressly instructed to refuse) or to ask for its deposit back and terminate the sale (a request which would accomplish the objective they knew their principal desired). In these circumstances, the law precludes the vendor from relying on the provision making time of the essence of the agreement and from taking advantage of the existence of a state of affairs which it itself produced particularly where, as here, it is acting contrary to good faith in its performance of the contract.

In *Doherty v. Southgate Township*[21] the Ontario Court of Appeal pronounced the importance of good faith in relation to conditions precedent. Here, the vendor municipality tried to have the sale of a former fire hall voided by its own failure to give public notice of the proposed sale.

Part of the agreement in *Doherty* was that the township was obliged to pursue a zoning by-law amendment and obtain the requisite municipal approvals thereto which would allow the fire hall to be rezoned as a housing complex. The town did nothing to advance the by-law amendment and the purchaser agreed to extend the closing date. The town again failed to do anything in regard to the zoning by-law and the transaction did not close. Upon a suit by the purchaser for specific performance, the municipality took the position that public notice, which was never given, is required for this kind of sale. The issue of public notice had not been raised before this point.

The Court of Appeal looked at the actions of each party within the rubric of good faith and sided with the purchaser despite there being a by-law requiring that public notice be given. The Court stated:

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[21] (2006) 46 R.P.R. (4th) 30

> Southgate's position in this litigation with respect to the public notice is a disingenuous attempt to take advantage of its own failure. Significantly, Southgate's decision not to complete the sale on March 5, 2004, was based on its unwillingness to proceed with the zoning amendment called for in the agreement of purchase and sale and not on the fact that it had not given the public notice required by s. 268(3)(c)... Southgate did not raise the notice issue as a reason for not closing and first raised it in its statement of defence in an attempt to extricate itself from an action for breach of contract.
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> While it may be said that Doherty should have been aware of Southgate's obligation to give notice and its failure to do so, there is no evidence to suggest that he did not act in good faith throughout. Doherty, through his lawyer, took steps necessary to prepare for a closing of the sale and Southgate's actions would have led him to believe that Southgate had fulfilled all of the statutory requirements necessary to complete the transaction.[22]

In *St. Thomas Subdividers* Ltd. V. 639373 Ontario Ltd.[23], a vendor failed to use its best efforts to secure registration of a plan of subdivision. The Court of Appeal held as follows:

> In any case, we think that it would be a gross injustice in these circumstances to permit the vendor to rely on the August 31, 1987 termination provision in the agreement. As noted, the trial judge found that the vendor failed to use its best efforts to register the plan of subdivision by either August 31 or December 31, 1987. The parties contemplated that the agreement might continue past the intermediate August 31st date if the plan of subdivision were not registered by then. After August 31st, it remained within the vendor's control to use its best efforts to register the plan. It was only after the passing of the December 31, 1987 date that the parties contemplated the agreement could not be continued if the plan were not registered.
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> We acknowledge that the vendor was not wholly responsible for failing to register the plan of subdivision by either of the two deadlines. The vendor was, however, wholly responsible for reducing the purchaser's chance of buying the land by its failure to act in good faith and to use its best efforts to register the plan. Preventing the vendor from invoking the August 31, 1987 termination date seems to us to be justified because of the vendor's representations as to when the plan of subdivision would be registered and because it remained within the vendor's control to attempt to have the plan registered through the exercise of its best efforts up to the final deadline of December 31, 1987.[24]

In *LeMesurier v. Andrus*[25], a purchaser sought to terminate an agreement of purchase and sale, relying on a title clause in the agreement to claim that a minor title defect that the vendor had

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[22] *Ibid* at paragraph 43
[23] 1996 CarswellOnt 1899
[24] 1996 CarswellOnt 1899 at para. 24
[25] *(1986) 54 O.R. (2d) 1 (C.A.)*

remedied, entitled him to terminate the contract. Grange J., citing the Supreme Court of Canada decision in *Mason v Freedman*, stated:

> Quite apart from the fact that the clause appears to be inserted for the benefit of the vendor only, I do not think the purchaser can rely upon that clause to repudiate the contract in the circumstances of this case. .....The clause is very similar to that in Mason v. Freedman, [1958] S.C.R. 483, 14 D.L.R. (2d) 529. There the vendor sought to use the clause to enable him to repudiate the contract when the purchaser required a bar of dower. Judson J. rejected that defence at p. 486 S.C.R., pp. 532-3 D.L.R. as follows:
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> > "This proviso does not apply to enable a person to repudiate a contract for a cause which he himself has brought about . . . Nor does it justify a capricious or arbitrary repudiation. I am content to adopt the words of Middleton J. in Hurley v. Roy [(1921), 50 O.L.R. 281 at p. 285, 64 D.L.R. 375 at p. 377] that the provision, "was not intended to make the contract one which the vendor can repudiate at his sweet will"."

Where an agreement stipulates that time is of the essence, good faith will be a factor interpreting that provision. A party cannot rely on a time is of the essence provision where it is in default. The same can be said for conditions precedent. Justice Perell, quoting from his text Remedies and the Sale of Land (2d ed) stated as follows:

> The case law recognizes three main qualifications before a party may rely on a time of the essence provision. The commonly recited rule that outlines all the qualifications states that time may be insisted upon as of the essence of the agreement only by a litigant who has shown him or herself ready, desirous, prompt and eager to carry out the agreement, who has not been the cause of the delay or default; and who has not subsequently recognized the agreement as still existing. Recent case law puts the rule perhaps more simply by asserting that a party must be acting in good faith to rely on time of the essence.
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> A similar rule exists for conditions precedent. A party cannot rely on the deadline for the satisfaction of a condition precedent when the failure to meet the deadline is a consequence of the party (a) not having proceeded diligently or in good faith to satisfy the condition or (b) having acted in bad faith by interfering with the other party's ability to satisfy the condition precedent. Here, the unavailability or time of the essence reflects, in part, the general contract law principles that a party may not rely on the non-satisfaction of a condition precedent that

> arises as a result of the party's misconduct, and a party cannot take advantage of its own default as a basis for alleging that it is relieved of its contractual obligations[26].

In *Leung v. Leung*,[27] a vendor acting unreasonably and in bad faith was unable to rely on a "time of the essence" clause where the vendor had a minor technical problem with tender that could be easily remedied while closing was in escrow. *"It is clear that the exercise of the power of rescission by a vendor of land must not be arbitrary, capricious or unreasonable. Much less can he act in bad faith."*

The solicitors for the parties met at the Toronto Registry Office an hour before it was set to close. The plaintiff's solicitors provided a cheque for the closing funds and a copy of a second mortgage that was required under the agreement. When the second mortgage was presented for registration, it was rejected as not in registrable form because of a minor mistake. The plaintiff's solicitor advised that the second mortgage could be corrected within a few hours and suggested that the transaction be closed in escrow with registration the following day. After obtaining instructions, the vendors' solicitor rejected the suggestion and terminated the contract. The second mortgage was in registrable form by 18:00. The plaintiff was successful in a suit for specific performance of the agreement.

In *Borthwick v St. James Square Associates Inc.*[28], a vendor of a condominium to be constructed sought to resile from the sale of the units to more than 30 purchasers. In finding that the vendor had not acted reasonably or in good faith when entering into the agreement and

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[26] P.M. Perell and B.H. Engel, *Remedies and the Sale of Land* (2d ed) (Toronto) Butterworths, (1998) at pp. 44-45, cited in Shapiro (c.o.b. ISR Ent. in Trust) v. 1086891 Ontario Inc. [2006] O.J. No. 302; 2006 ON.C. LEXIS 337.
[27] [1990] O.J. No. 2276 (Ont. Gen. Div.)
[28] 1989 CarswellOnt 2148

purchase and sale, and thereafter, Justice Van Camp adopted the reasoning in *Selkirk v Roman*[29]

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> a vendor, in seeking to rescind, must not act arbitrarily, or capriciously, or unreasonably.
>
> Much less can he act in bad faith. He may not use the power of rescission to get out of a
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> sale "brevi manu", since by so doing he makes a nullity of the whole elaborate and protracted transaction. Above all, perhaps, he must not be guilty of "recklessness" in entering into his contract, a term frequently resorted to in discussions of the legal principle and which their lordships understand to connote an unacceptable indifference to the situation of a purchaser who is allowed to enter into a contract with the expectation of obtaining a title which the vendor has no reasonable anticipation of being able to deliver. A vendor who has so acted is not allowed to call off the whole transaction by resorting to the contractual right of rescission.

The result was that the vendor, who claimed to be unable to construct a condominium building within the time contemplated by the agreements of purchase and sale, was not permitted to terminate the transactions. In a pre- *Semalhago* decision, specific performance was ordered.

In the recent decision of *2054476 Ontario Inc. v. 514052 Ontario Ltd.*[30] the plaintiff purchaser claimed specific performance of certain property transactions. Here, the vendor encountered several problems affecting numerous delays in its ability to close. The vendor made "valiant efforts" to be ready for closing but problems always impeded such and time extensions were necessary. Because of the delayed closing, the purchaser asked for abatements of the purchase prices (which was contemplated in the contracts).

Closing was eventually set for December 10, 2004 and the frustrated vendor wanted to finally complete the transaction on this date or abort the sale. The performance of the vendor's

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[29] 3 All E.R. 994

[30] 2009 CarswellOnt 296

obligations under the contracts in question was costly and time consuming and the closing dates had been delayed time and time again. Moreover, evidence at trial indicated that the value of the property had greatly increased.

In the days just prior to closing the vendor declined to communicate with the purchaser's solicitor. At closing the vendor's solicitor delivered a statement of adjustments with various miscalculations all to the benefit of the vendors. Further, the vendor refused to negotiate the request for abatements, contrary to its contractual obligation to do so. The clear message was sent to the purchasers that they must close on the vendor's terms or the transaction would be aborted. Not being able to close, the vendor's solicitor then declared the transaction as at an end.

The court decided that the vendors had not been acting in good faith and its actions amounted to an anticipatory breach. Two properties were involved and in one case specific performance was ordered and in the other a postponed closing date was set.

The above cases speak to the common law duty of good faith. In the recent decision of *Southcott Estates Inc. v. Toronto Catholic District School Board*[31] the impugned agreement of purchase and sale contained an explicit provision whereby the defendant school board was under an obligation to act in good faith and use its best efforts to obtain a severance from the city. While such a good fait h provision may be superfluous given the common law duty

[31] 2009 CarswellOnt 494

discussed above, the inclusion of this clause in the agreement made things easier for the Plaintiff as there could be no debate about the duty's existence.

It was conceded that the duty existed. The defendant school board, however, arguing causation, took the position that the plaintiff did not satisfy the burden of proving that had the defendant not breached its obligation to use its best efforts, the severance would have been granted in time for the transaction to be completed by January 31, 2005.

The issue was whether the city planning department would have opposed the severance as premature to the committee of adjustments. The defendant argued that regardless of their obligation, the deal could not have closed because of the planning department issue. Indeed evidence was given in support of this position. Despite this, with the underlying evidence that the defendant had breached its duty of good faith, the court favoured the plaintiff. Justice Spiegel found on a balance of probabilities that:

> there was a reasonable probability that [the planning department] would have achieved the required level of comfort with the plaintiff's development application within ten weeks of the date of filing the application. Based on my finding that the application could have been filed by September 13, 2004, this means that by November 22, 2004 the Planning Department would not have considered the severance premature. I also find that there was a reasonable probability that had this occurred, [the city counselor] would have taken the same position.
>
> I find that had the defendant not breached the obligation to use its best efforts, it could have obtained a hearing before the COA much earlier than it did. However, even if the hearing was held as late as December 16, 2004, I find that in the absence of an objection from the Planning Department and [the city counselor], the severance would likely have been granted and the transaction would have been completed by January 31, 2005.[32][33]

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[32] *Ibid* para 22

[33] This case is presently under appeal.

AVOIDING AN AGREEMENT IN GOOD FAITH

There are times when it is in a client's best interest to avoid a closing. The market or financing options may have changed and going through with a transaction may be a far more difficult option. Actions frequently arise with regard to an Agreement of Purchase and Sale where one party wishes to escape their obligation. *"It is typical of the situation that has occurred frequently in a falling market where the purchaser attempts to avoid closing a transaction that has become uneconomic."*[34]

The principle set out by Judson J. in *Mason v. Freedman,*[35] has application in these circumstances:

> *A vendor who seeks to take advantage of the [rescission] clause must exercise his right reasonably and in good faith and not in a capricious or arbitrary manner.*

The fact that a defaulting party cannot rely on a time of the essence provision was discussed above. Conversely, the innocent party acting in good faith, may so rely and a time is of the essence provision is one of the best ways for an innocent party to capitalize on a situation. In *Domicile Developments v. MacTavish*[36] the Ontario Court of appeal stated:

> *A time is of the essence provision means that on the closing date an innocent party may treat the contract as ended and sue the defaulting party for damages or it may keep the contract alive and sue for specific performance or damages.*

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[34] *Victorian Homes (Ontario) Inc. v. DeFreitas* (Ont. Ct. (Gen. Div.)) [1991] O.J. No. 324
[35] 1958 *CanLII 7 (S.C.C.), [1958] S.C.R. 483*
[36] (1999) 45 O.R. (3d) 302 (C.A.) at para. 11

So long as the innocent party carries through with its obligations under the agreement to the time of tender (In order to take advantage of a time of the essence provision the innocent party must itself be "*ready, desirous, prompt and eager*" to carry out the agreement) its good faith will allow it the upper hand with regard to the best means to benefit from a potentially botched transaction.

In the *Domicile Development* case, the defendant purchaser, prior to closing, stated his intention to avoid the contract. The vendor accepted the contract as repudiated, took no further actions and sold to a third party at a reduced price. On appeal, the action was unsuccessful as the vendor had failed to carry on with its obligations after the purchasers stated intention to repudiate. Here, "good faith" is expressed as the innocent party's willingness to complete the transaction. Had the vendor been "*ready, desirous, prompt and eager*" recourse to the above remedies would have been available. In this case the property was not ready on time but given the purchaser's repudiation, it was available to the vendor to reinstate time of the essence by setting a new date for closing and providing reasonable notice to the purchaser.

In *1473587 Ontario Inc. et al. v. Jackson et al.*[37] by an inadvertence, the purchaser was seven days late in delivering the deposit. Within those seven days the vendor had found a new purchaser and entered into second agreement, treating the first as repudiated as time was of the essence.

[37] 74 O.R. (3d) 539 (Sup. Crt. Jus.)

The issue went to Court to determine whether the parties would be held strictly to their bargain or whether there was room to accommodate the plaintiffs' inadvertent error. The plaintiff was of the mind that the purchaser was acting in bad faith by not accepting the late deposit.

In reaching his decision which was affirmed on appeal, Rutherford J. looked at the seminal Privy Council decision in *Union Eagle Ltd. v. Golden Achievement Ltd.*[38] where, he stated, "*the holding of parties to their bargain in this respect perhaps met its zenith.*" In *Union Eagle*, the purchase of a Hong Kong flat was to close at 5:00 p.m. on the closing date. Due to rush hour traffic, the cheque for tender arrived at 5:10 p.m. and the vendor treated the agreement as terminated under the time is of the essence clause. There was no intentional delay by the purchaser, there was no specific deadline for registration and the vendor did not suffer any damages as a result of the 10 minute delay. Regardless, the Privy Council held that the parties should be bound to the agreement they had made.

Following the Privy Council's reasoning, Rutherford J. held that the plaintiff was late to tender which entitled the vendor to treat it the agreement as repudiated. The fact that the vendor was not sympathetic to the inadvertence did not operate to diminish any good faith on the part of the vendor:

> Mr. Horst suggested that perhaps the Vendors were not acting in good faith in not immediately asserting their right to treat the contract as discharged and then discussing the possibility of a sale of the entire property with Forecast. While it may seem unfair, or perhaps more accurately, unfortunate to Loblaw that another purchaser with an inclination to do business came along precisely at the time Loblaw fell into breach of the deposit provision, it was through no fault,

[38] [1997] A.C. 514

> guile, deception or subterfuge on the part of the Vendors. The Vendors' solicitor returned the six-day overdue cheque the same day he received it, telling Loblaw that the Vendors did not agree to accept the late deposit. That the Vendors discussed and subsequently came to an agreement with Forecast based on the early advice received that the first agreement was no longer binding does not, in my view, come anywhere near using their position unfairly or playing fast and loose with Loblaw. Loblaw was told that its cheque would not be accepted the same day two of the defendant Vendors first met with Forecast and the cheque was actually sent back to Loblaw several days before Forecast and the Vendors executed the second agreement.[39]

In a recent 2009 Superior Court decision, Justice Kelly endorses the decision of Rutherford stating that *"any waiver of the time is of the essence provision would have to be explicitly and fully proven"*. In this case, entitled *Mutual Apartments Inc. v. Lam,*[40] the purchaser gave the deposit cheque to its solicitor but the solicitor by inadvertence neglected to deposit the cheque into the trust account. The vendor did not realize this at the time and continued to work towards closing the transaction. The vendor later wished to avoid the transaction for other reasons and upon discovery that the deposit had not been made, used this as an excuse. As time was of the essence, the vendor was able to avoid the transaction and was not seen as straying from its duty to act in good faith:

> When Mutual, through inadvertence, failed to deposit the cheque within the time specified, it breached a fundamental term of the contract. Mutual cannot rely upon the fact that the defendants continued to attempt to close the transaction after the default of the payment on April 18, 2001 thereby waiving such right. As I have stated above, they did not know that Mutual had breached such a term of the APS so that they could not have waived such a right. They presumed that such a condition was complied with and therefore continued to work towards the closing of the transaction.
>
> I am of the view that even though Mutual provided the second deposit cheque to its lawyer, it had the money to cover the cheque and it was not deposited through inadvertence, it is a breach of a fundamental term of the APS and as such, the APS is null and void for that reason.[41]

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[39] 74 O.R. (3d) 539 (Sup. Crt. Jus.) at para. 22
[40] 2009 CarswellOnt 3768
[41] *Ibid* at para 35

GOOD FAITH AT THE TIME OF TENDER

Tender constitutes evidence that the tendering party is capable of and prepared to close a transaction and entitled to pursue its remedy against a defaulting party. One commentator describes it as follows:

> Tender is the act of offering to perform one's contract obligations. By tendering, the innocent party shows his or her readiness and willingness to carry out the contract, that he or she is not the cause of the delay or default and that there has been no waiver. By tendering, the innocent party shows that it is acting in good faith.[42]

In their text (Justice) Paul Perell and Bruce Engell address the interplay between good faith and the timing of tender.

> Where tender is made, the details of the particular contract will define what is required. Modern cases seem to be accepting less than perfect tender and recognize that apparent difficulties can be sorted out if the parties act in good faith. There is a line of authority holding that absent specific language, tender may be made up to midnight on the day set for closing that is even after the close of the registry office.[43]

Tender further relates to good faith in the question of how far a party must go to discharge its duty of good faith in an agreement where the other side is seeking to repudiate. Where one party has performed an anticipatory breach of an agreement the Courts have held that the formality of tendering would be futile or meaningless in such a situation. "The law does not require a nugatory and meaningless ritual to be carried out."[44] (Justice) Paul Perell states:

> Tender... is not itself a prerequisite. Despite the absence of any tender, the court may be satisfied that the innocent party is entitled to invoke time of the essence. Tender is also not

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[42] Perell, Paul and Engell, Bruce. Remedies and the Sale of Land, (Butterworths, Markhan: 1998) at page 48
[43] *Supra* note 1 at 48
[44] *Stewart v. Ambrosino* (1977) 16 O.R. (2d) 221 (C.A.)

> required from a party when the other party has clearly repudiated the agreement; numerous cases have held that the law does not require what would be a meaningless or futile gesture.[45]

In *Lawrie v. Gentry Developments Inc*[46] an anticipatory breach was found where the vendor stated that he would refuse to accept tender after 4:30 p.m. on the day of closing. Although the purchaser's ability to tender was in question, the Court held that his tendering between 4:30 and midnight was not necessary for a remedy as any such tendering would be futile. The purchaser was awarded the return of his deposit as well as much larger sum representing the value that the house had increased since the day of closing.

Lawrie v. Gentry Developments Inc. isn't explicitly influenced by the existence of good or bad faith though the undertones are impossible to miss. The judge makes clear that the lawyer for the vendor left his office prior to 3:45 p.m. the day of closing, was unreachable by telephone and had nobody in his office that could be of any assistance to the purchaser's solicitor. The judge also suggests the vendor was unreasonable for not extending the closing by a few days to allow the purchaser to travel to California for his mother's funeral:

> With full knowledge the purchasers could close the transaction on the next business day, without bothering to check to see if it had been lied to about Lawrie having gone to California to bury his mother, without concern for the fact -- indeed, perhaps because of the fact it held the purchasers' deposit of $17,500 and that the house had increased in value by $10,000 since the purchasers had agreed to buy it, the vendor refused to close the transaction at any time after May 30th. The vendor took the position the deal was at an end and that it was entitled to keep the deposit. The purchasers began an action for specific performance. They were, in my view, entitled to that relief.[47]

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[45] *Supra* note 1 at page 48
[46] [1989] O.J. No. 3230 (H.C.J.)
[47] *Ibid* at paragraph 36

In *DeFranco v. Khatri,* discussed above, the Court awarded specific performance on the basis of the vendor's anticipatory breach despite the vendors' argument that the purchasers were not ready to close as they had not tendered. S.E. Pepall J. stated:

> Here, the plaintiffs were ready willing and able to [complete the transaction] and, in my view, were acting in good faith. In the face of the defendants' repudiation there was no need to tender. The fact that the solicitor was not in funds is not determinative.[48]

CONCLUSION

While we have set out our review of the cases and the principals to be derived from them, an overarching theme tends to emerge. That theme is simply that the Court will favour the party who has acted in good faith, in compliance and with his or her contractual obligations. When advising the client we recommend being "up front". Courts today look for the justice of the case, rather than for strict formality.

Where there is a concern that a transaction may become problematic, or that the opposing party may be acting in a manner that hints at the possibility of a last minute failure to close, counsel are advised to start considering the evidentiary record well in advance of the closing. Letters or emails confirming conversations will be of great assistance at a trial that is going to take place a year or more down the road. Similarly, correspondence setting out the opposing party's failure to respond to phone calls is helpful. The better the record is documented, the easier it is for counsel at trial.

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[48] *Ibid*. at paragraph 27