



DRAFTING EFFECTIVE COMMERCIAL CONTRACTS POST COVID-19

FIVE ISSUES AND HOW TO ADDRESS THEM

Presented by:

Heather Devine, Partner

Mike Furyk, Associate

Toronto Chapter of Fleet Safety Council

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BACKGROUND

- COVID-19 has had an unprecedented effect on local, national, and international commerce, disrupting business relationships, and undermining supply chains.
- The way we draft contracts must respond to this changing reality.

AGENDA

- 1 Force Majeure Clauses
- 2 Termination Clauses
- 3 Entire Agreement Clauses
- 4 Limitations of Liability Clauses
- 5 Notice Requirements



FORCE MAJEURE CLAUSES

FORCE MAJEURE CLAUSES

What are they?

“Act of God” or Force Majeure clauses generally operate to “discharge a contracting party when a supervening, sometimes supernatural, event makes performance impossible. The common thread is that of the unexpected, something beyond reasonable human foresight and skill”

Atlantic Paper Stock Ltd. v. St. Anne-Nackawic Pulp & Paper Company, [1976] 1 SCR 580 at page 583

FORCE MAJEURE CLAUSES

- What do they cover?
 - A properly-worded *force majeure* clause operates to relieve a party from liability which may arise from non-performance or delayed performance as a result of a *force majeure* event.
 - What constitutes a force majeure event is governed and limited by the language of the clause itself.

FORCE MAJEURE CLAUSE: SAMPLE (1/2)

*No party shall be liable or responsible to the other party, nor be deemed to have defaulted under or breached this Agreement, for any failure or delay in fulfilling or performing any term of this Agreement [(except for any obligations to make payments to the other party hereunder)], ...when and to the extent such failure or delay is caused by or results from acts beyond the impacted party's ("**Impacted Party**") [reasonable] control, including, without limitation, the following force majeure events ("**Force Majeure Event(s)**"):*....

FORCE MAJEURE CLAUSE: SAMPLE (2/2)

(a) acts of God;

(b) flood, fire, earthquake, tsunami, epidemics, pandemics [including the 2019 novel coronavirus pandemic (COVID-19),][other potential disaster(s) or catastrophe(s),] or explosion;

(c) war, invasion, hostilities (whether war is declared or not), terrorist threats or acts, riot, or other civil unrest;

(d) government order or law;

(e) actions, embargoes, or blockades in effect on or after the date of this Agreement;

(f) action by any governmental authority;

(g) national or regional emergency;

(h) strikes, labour stoppages or slowdowns, or other industrial disturbances;

(i) shortage of adequate power or transportation facilities; and

(j) other [similar] events beyond the [reasonable] control of the Impacted Party.

FORCE MAJEURE CLAUSES: CASE LAW EXAMPLES

- Courts have offered diverse opinions on how strictly these clauses should be construed.
- In one case called *Durham Sports Barn Inc. Bankruptcy Proposal*, the Ontario Supreme Court narrowly read a *force majeure* clause, finding it only operated to exclude the landlord in this case from its obligations to provide quiet enjoyment as a result of a *force majeure* event.
- Durham had argued it was relieved from its obligation to pay rent on the basis it was prohibited from operating its store from March to May 2020 due to the pandemic. The Court disagreed, however, finding the clause did not cover Durham's obligation to pay rent.



FORCE MAJEURE CLAUSES: CASE LAW EXAMPLES

- On the other hand, in the case of *Hudson's Bay Company U.L.C. v. Pensionfund Investment Ltd.*, the BC Supreme Court considered a provision in Hudson's Bay's lease agreement which listed *force majeure* events that included, among other things, any failed performance as a result of an "act of God...and any condition or cause beyond the reasonable control of the party obligated to perform."
- The Court held that "it appears uncontroverted that the events listed in that clause would include the COVID-19 pandemic".

HUDSON'S BAY

TAKEAWAYS FROM THE CASE LAW

- While *force majeure* clauses operate generally to relieve parties from liability as a result of their non-performance or delayed performance, precisely what is considered a *force majeure* event, and precisely the obligations from which the parties are freed, are governed by the terms of the clause.
- A party cannot rely on a clear, unambiguous *force majeure* clause to relieve themselves of liability for a breach of their obligations where the events causing the breach, or the obligation breached, is not found in the language of the clause itself.

CONSEQUENCES OF A POORLY-DRAFTED OR ABSENT *FORCE MAJEURE* CLAUSE OR UNCLEAR CONTRACT



- Where your contract does not contain a *force majeure* clause, or it is unenforceable or poorly-drafted, parties may still rely on the **doctrine of frustration**.
- However, there are risks to relying on this doctrine to address the effects of COVID-19, particularly as the effects of the Pandemic become more foreseeable over time.

CONSEQUENCES OF A POORLY-DRAFTED OR ABSENT FORCE MAJEURE CLAUSE OR UNCLEAR CONTRACT

- The doctrine of frustration may apply to relieve parties from their obligations under a contract “when a situation has arisen for which parties made no provision in the contract and performance of the contract becomes a thing radically different from that which was undertaken by the contract”
 - *Naylor Group Inc. v. Ellis-Don Construction Ltd.*, 2001 SCC 58
- There are two main risks on relying on the doctrine of frustration, especially as the long-term effects of the Pandemic become more well known:
 1. The unpredictability of the judicial process as liability for failed performance caused by supervening events is left to the courts; and
 2. Common law courts have already held that not every effect of the Pandemic, including economic downturn, will be covered by this doctrine

FORCE MAJEURE CLAUSES: KEY TAKEAWAYS

1

Force majeure clauses operate to relieve a party from liability that may arise from delayed or failed performance of a contract which is due to a *force majeure* event.

2

Precisely what constitutes a *force majeure* event, and the breached obligations from which a party may be relieved of liability, are governed by the precise language of the *force majeure* clause.

3

Parties whose *force majeure* clauses cover only unforeseeable events may run into arguments that, due to previous widespread medical emergencies and the length of the Pandemic, a party cannot escape liability for delayed or non-performance as a result of COVID-19.

FORCE MAJEURE CLAUSES: KEY TAKEAWAYS

4

Foreseeability is not your friend. Depending on the specific wording of the contract, the operation of *force majeure* clauses is premised on the notion that the event is unforeseeable, unexpected, or “beyond reasonable foresight and skill”.

5

Parties who use *force majeure* clauses which exclude foreseeable events may be unable to rely on them for protection as the Pandemic progresses and its effects become foreseeable, or in light of past widespread medical emergencies (Avian flu, SARS, and/or the Ebola virus)

6

Unless your *force majeure* clause expressly includes COVID-19 and its effects, the longer we live with the Pandemic, the stronger the argument becomes that the effects of the Pandemic itself were foreseeable and not covered by the clause or by the doctrine of frustration.



TERMINATION CLAUSES

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Termination clauses govern the ability of one or all of the parties to an agreement to prematurely end their obligations under the contract.



TERMINATION CLAUSES

Properly-drafted termination clauses should be certain and unambiguous in their terms, particularly with respect to the **Who**, the **When**, and the **Why**.

WHO?

Which party or parties can exercise the right to terminate?

WHEN?

Under what circumstances can a party exercise its right to termination?

- Termination “**for cause**” – one or all parties have the right to terminate the contract upon another party’s actual or threatened breach, or upon another party’s insolvency.
- Termination “**for convenience**” – one or all of the parties have the right to terminate the contract in the form and manner prescribed by the contract, even without a reason to do so.

HOW?

If a party decides it wishes to exercise its right under a termination clause, what method and timing must be used to give notice of termination?

SAMPLE OF TERMINATION FOR A *FORCE MAJEURE* EVENT

The Impacted Party shall give notice within [NUMBER IN WORDS] ([NUMBER]) days of the Force Majeure Event to the other party, stating the period of time the occurrence is expected to continue. The Impacted Party shall use diligent efforts to end the failure or delay and ensure the effects of such Force Majeure Event are minimized. The Impacted Party shall resume the performance of its obligations as soon as reasonably practicable after the removal of the cause. In the event that the Impacted Party's failure or delay remains uncured for a period of [NUMBER IN WORDS] ([NUMBER]) [consecutive] days following written notice given by it under this Section [X], [either party/the other party] may thereafter terminate this Agreement upon [NUMBER IN WORDS] ([NUMBER]) days' written notice.

SAMPLE OF “FOR CONVENIENCE” TERMINATION CLAUSE

For Convenience. [Vendor/Customer/Either Party], in its sole discretion, may terminate this Agreement at any time [after [DATE]], without cause, by providing at least [NUMBER] days' prior written notice to the [Customer/Vendor/other Party]. [As consideration for the right to terminate this Agreement under this Section 1.3(a), the terminating party shall, upon [termination/providing notice of termination], pay to the non-terminating party a termination fee in an amount equal to [\$(AMOUNT)]/[TERMINATION FEE FORMULA]] (“Termination Fee”). The parties intend the Termination Fee to be liquidated damages constituting compensation, and not a penalty. The terminating party's payment of the Termination Fee is the terminating party's sole liability and entire obligation and the non-terminating party's exclusive remedy for any termination by the terminating party under this Section 1.3(a).]

TERMINATION CLAUSES: KEY TAKEAWAYS

1

Properly-drafted termination clauses can operate to alleviate some of the future risk and uncertainty associated with COVID-19, as parties have a defined process for ending their contractual obligations in light of changing circumstances.

2

Without a termination clause, parties may have to rely on the courts to decide whether a contract has been terminated, and on what terms. This introduces a significant amount of uncertainty into commercial dealings. To avoid this uncertainty, a well-drafted termination clause is advisable.

3

Termination Clauses should be drafted clearly and unambiguously, particularly with respect to the **Who**, the **When**, and the **How**



ENTIRE AGREEMENT CLAUSES

ENTIRE AGREEMENT CLAUSES

- Entire agreement clauses operate essentially to codify what is known in law as the **parol evidence rule**.
- These clauses aim to prevent parties relying on the clause from being contractually liable for any representations or statements (including those made prior to execution of the contract), unless they are expressly set out in the contract itself.
- “An entire agreement clause is generally intended to lift and distill the parties’ bargain from the muck of negotiations. In limiting the expression of the parties’ intention to the written form, the clause attempts to provide certainty and clarity”

Sobocynski v. Beauchamp, 2015 ONCA 282 [*Sobocynski*] at para 43

ENTIRE AGREEMENT CLAUSES: EXAMPLE

5.13 *Entire Agreement.* The [Contract] constitute[s] the entire agreement between the parties to this Agreement with respect to the subject matter thereof and supersede all prior negotiations, proposals and agreements, whether oral or written, with respect to the subject matter thereof.

ENTIRE AGREEMENT CLAUSES

- For many, the COVID-19 Pandemic has interrupted, complicated, or otherwise hindered, clear negotiation. It has also introduced a host of new topics and concerns for parties to address.
- It is important that parties not only ensure that their negotiations are distilled clearly into the language of their contract, but also that the content of their prior negotiations are not used to thwart or alter their written terms.



ENTIRE AGREEMENT CLAUSES



Balfour v. Tarasenko,
2015 BCSC 1232

- This was a case in which a creditor sought to enforce a loan guarantee against two individuals.
- The respondents argued their guarantee was contingent on the existence of a collateral second contract, which provided that the creditor would facilitate their receipt of a further \$300,000.

BALFOUR V. TARASENKO

- The Court disagreed with the respondents and gave effect to a properly-drafted entire agreement clause contained in the initial loan agreement, which provided:

15. Entire agreement

There are no representations, conditions, promises, agreements or understandings with respect to this Guarantee or affecting the liability of the Guarantors other than as set forth or referred to in this Guarantee. Possession of this Guarantee by the Creditor shall be conclusive evidence against the Guarantors that the Guarantee was not delivered in escrow or pursuant to any agreement that it should not be effective until any condition precedent or subsequent has been complied with and this Guarantee shall be operative and binding notwithstanding the non-execution thereof by any proposed signatory.

- The Court therefore concluded that a collateral contract, whatever its terms, would be in contradictory to the entire agreement clause, and that, as a general rule, it should not be given effect.

ENTIRE AGREEMENT CLAUSES: KEY TAKEAWAYS

1

Entire agreement clauses operate to codify the parol evidence rule and exclude its exceptions. They confine the party's obligations to the words in the contract, and limit parties' liability for pre-contractual representations and statements which do not ultimately end up in the contract.

2

Clearly-drafted entire agreement clauses are instrumental to ensuring that contracts are clear and certain in their terms by reducing the risk that parties will be held liable for their pre-contractual representations or statements, where they do not end up in the executed agreement.

3

In light of the myriad of novel circumstances and issues which have arisen due to COVID-19, and which must be negotiated by parties, the certainty provided by entire agreement clauses is invaluable.



LIMITATIONS OF LIABILITY CLAUSES

LIMITATIONS OF LIABILITY



Limitations of liability clauses operate to limit one or both parties' remedies for damages which may arise upon a breach of an agreement, either by limiting the amount of potential damages or by excluding a particular type of damages entirely.

LIMITATIONS OF LIABILITY: EXAMPLE

No Consequential Damages — In no event will CIBC WM or any affiliate or its or their respective shareholders, employees, officers, directors, or agents be liable to the Client for any indirect, incidental, special or consequential losses or damages (including, but not limited to, loss of profits or revenue or failure to realize expected profits or savings, or the avoidance of any losses) arising out of or related to this Agreement, the Systems Interconnect or use of the Trading System, including the provision of or failure to provide access to the Trading System, regardless of whether such damages could have been foreseen or prevented.

- *Montrose Hammond & Co. v. CIBC World Markets Inc., 2019 ONSC 2870*

MONTROSE HAMMOND & CO. v. CIBC WORLD MARKETS INC.

- The plaintiff, a start-up hedge fund, sued for breach of contract and negligence. It claimed that it had made a number of error trades due to the malfunctioning of a direct market access services system provided by CIBC.
- In addition to damages for direct losses related to the unwinding of those trades, the plaintiffs also claimed for lost profits.



CIBC
World Markets

MONTROSE HAMMOND & CO. v. CIBC WORLD MARKETS INC.

- The Court agreed with CIBC's submissions, reasoning that the plaintiffs had unambiguously claimed for lost profits, which were, on a plain reading of the limited liability clause, excluded.
- The limitation of liability clause in this case therefore operated to relieve CIBC from a particular type of damages, namely for loss of profits.



CIBC
World Markets

LIMITATIONS OF LIABILITY CLAUSES: KEY TAKEAWAYS

1

Limitations of liability clauses can operate to limit a party or parties' remedies under a contract, either by excluding a particular type of damages or limiting damages to a prescribed amount.

2

COVID-19 and related governmental actions have introduced substantial uncertainty to commercial dealings as well as the potential for unforeseen circumstances to hinder performance.

3

Limitations of liability operate as a means of managing and allocating those risks.



NOTICE REQUIREMENTS

NOTICE REQUIREMENTS

- Various contracts require parties provide their contracting partner with notice upon the happening of certain events such as termination or a *force majeure* event.
- With restrictions on personal contact, travel restrictions, the temporary closing of business locations, and staff working remotely, it is important to consider how and when to serve notice, particularly if a contract requires hand delivery



NOTICE REQUIREMENTS: EXAMPLE

The Impacted Party shall give notice within ten (10) days of the Force Majeure Event to the other party, stating the period of time the occurrence is expected to continue. The Impacted Party shall use diligent efforts to end the failure or delay and ensure the effects of such Force Majeure Event are minimized. The Impacted Party shall resume the performance of its obligations as soon as reasonably practicable after the removal of the cause. In the event that the Impacted Party's failure or delay remains uncured for a period of sixty (60) consecutive days following written notice given by it under this Section, either party may thereafter terminate this Agreement upon ten (10) days' written notice.

NOTICE REQUIREMENTS: KEY TAKEAWAYS

In your contract, consider including:

- a) alternate methods of service to hand-delivery – for example, by electronic mail.
- b) provisions governing the negotiation and amendment of a contract for temporary methods or addresses for service, in the event of business closure or a change in commercial locations.



CLOSING THOUGHTS

CLOSING THOUGHTS

1. **Alternative dispute resolution** (“ADR”) mechanisms, such as mediation and arbitration, are operating remotely and are effective during COVID-19, but it is important that parties remain mindful of the risks associated with including ADR mechanisms and clauses in their contracts which require in-person appearance.
2. COVID-19 has, above all, required each of us be **resilient and adaptable** in the face of rapidly changing circumstances. Our approach to contract drafting should be no different. Now is the time to assess our contracts in light of the novel challenges associated with the Pandemic, and to tailor their drafting to our client’s particular operational requirements. This will involve being sensitive not only to our own client’s local needs, but also to more remote issues, such as disruptions in supply chains and manufacturing across the globe.

*The sample clauses provided during this presentation were based on precedents found on Thompson Reuters *Practical Law Canada* and the cited case law, with changes made where appropriate.

QUESTIONS?



Heather Devine
Partner
hdevine@ahbl.ca
905-531-2902



Mike Furyk
Associate
mfuryk@ahbl.ca
416 639 9050

OFFICES

Vancouver

TD Tower
2700 – 700 West Georgia Street
Vancouver, BC V7Y 1B8
Canada

T: 604 484 1700

Toronto

TD Canada Trust Tower
2700 – 161 Bay Street, PO Box 508
Toronto, ON M5J 2S1
Canada

T: 416 639 9060

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