



Written in Stone? The Supreme Court of Canada Solidifies the Use of the Factual Matrix in Contract Interpretation Cases

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The goal of contract interpretation is to determine the intention of the parties at the time that they entered into the contract. The intention is to be determined on an objective basis (what the written contract means to reasonable people reading it), not a subjective basis (what each party individually thought they were agreeing to). There has been much ink spilled in the Commonwealth on the issue of whether or not factual circumstances surrounding the formation of a contract (often referred to as the “factual matrix”) ought to be considered by a court when there is a dispute about the meaning of a written agreement. A recent decision of the Supreme Court has provided courts guidance on how to go about determining the parties’ objective intention.

Background

This past summer, the Supreme Court of Canada released a unanimous decision in *Sattva Capital Corp v. Creston Moly Corp.* (“*Sattva*”), which solidified the use of the factual matrix in contract interpretation cases in Canada, and will ultimately limit the number of appeals from most arbitral awards. In the process, the Supreme Court of Canada has changed how trial and appellate courts across Canada will approach contract interpretation cases generally.

At issue in *Sattva* was the amount of a finder’s fee owing to Sattva Capital Corp. by the defendant, Creston Moly Corp, in relation to the acquisition of a mining property. The *Sattva* decision was made in the context of an appeal from the decision of an arbitrator in British Columbia, but will have broad implications on contract disputes throughout Canada, whether being tried in arbitration hearings or before the courts.

Contract Interpretation and the Factual Matrix

In *Sattva*, the Supreme Court re-affirmed (from its previous decisions in *Eli Lilly v. Novapharm* and *Consolidated-Bathurst v. Mutual Boiler*), that the goal of contractual interpretation is to ascertain the intent of the parties at the time when the contract is entered into. *Sattva* added a new element to this exercise, requiring the trial judge to consider the circumstances surrounding the formation of the contract - such as the purpose of the contract, the background to the agreement and the relationship between the contracting parties.

The Supreme Court provided some guidance to courts on how to go about determining intention, and stated that the “factual matrix” is comprised of “objective evidence of the background facts at the time of the execution of the contract, that is, knowledge that was or reasonably ought to have been within the knowledge of both parties...” This “factual matrix” cannot be used to re-write the contract but a trial judge must consider it when interpreting a contract to ensure consistency between the written words of the contract and the intentions of the parties.

In the case of written agreements, evidence which purports to modify the meaning of a written contract cannot be considered by a trial judge hearing the case - this is known as the “parole evidence rule.”

Previously, the Supreme Court had allowed evidence of the factual matrix to be heard as an exception to the parole evidence rule, but limited the use of such evidence to cases where some ambiguity existed in the written words of the contract. The Ontario Court of Appeal had previously released several decisions modifying this approach and requiring that the factual matrix always be considered when interpreting a contract.

The Supreme Court in *Sattva* implicitly accepted the Ontario Court of Appeal's approach by adopting the factual matrix as an essential tool in contract interpretation, even in cases where there is not necessarily an ambiguity in the written contract. The result will be that trial judges will have a greater discretion to determine the true meaning of the contracts before them in the context of the relationship between the parties and the facts that existed at the time the parties signed the agreement. This may assist parties in obtaining relief from overly harsh contract provisions in certain agreements, but for the reasons set out below, will also make it more difficult for parties to appeal from arbitration and lower court decisions on issues of contract interpretation.



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Standard of Review and Contract Interpretation

Generally speaking, commercial actors enter into arbitration to avoid the cost and delay associated with the traditional civil justice system, as well as to maintain a certain level of privacy – since unlike court proceedings, the information disclosed in arbitrations may be kept confidential. However, in recent years, more and more parties have been appealing arbitration decisions to traditional courts. This has the effect of diminishing the efficiencies of the arbitration process. The Supreme Court of Canada in *Sattva* seems intent on reversing this trend – and limiting the number of appeals from contract cases more generally.

The Supreme Court has done this by bonding the factual matrix to contract interpretation. Put simply: when any appellate court receives an appeal from either a lower court or an arbitration alleging that there was an improper factual finding, it will now defer to the decision maker (i.e. the lower court or arbitrator). This is because the Supreme Court has reclassified contract interpretation not as an issue of law, but as an issue of mixed fact and law. Whereas there is no deference given by an appeal court to a lower court on issues of law, deference is given on issues of mixed fact and law. This is because the decision maker has access to the best factual evidence – usually having seen witnesses give live testimony. Therefore, by stating that a court can and should interpret contracts within the factual matrix in every case, the court turned the exercise of interpreting a contract (an issue traditionally seen as a legal one), to a factual one (making findings relating to the factual matrix).

Traditionally, appeals involving contract interpretation were thought to be based on errors of law. The Honourable Justice Rothstein in *Sattva* sets out the historical rationale for this:

“This rule originated in England at time when there were frequent civil jury trials and widespread illiteracy. Under those circumstances, the interpretation of written documents had to be considered questions of law because only the judge could be assured to be literate and therefore capable of reading the contract.”

The Supreme Court went on to state that this rationale no longer applies and that given that the overriding concern in contract interpretation cases is to determine the intent of parties to individual contracts, including a consideration of the factual matrix – contract interpretation as a rule is highly fact-specific. Accordingly, after *Sattva* most cases of contract interpretation will be treated as being issues of mixed fact and law. The result is that it will be much more difficult to appeal from contract cases generally. Appeals will likely only be allowed in the context of a clear error of law, where the principal at issue has wider application to the law in general rather than only application to the particular parties involved in the case being decided.

Conclusion

As a result of the *Sattva* decision, cases involving contractual interpretation will become less predictable (due to the inclusion of the factual matrix) and also more difficult to appeal. The benefit is hopefully fewer appeals, resulting in cases being brought to finality more quickly and at less cost. The decision re-enforces the importance of the trial and the oral evidence provided by the contracting parties. As a result, commercial parties are well advised to refer their contract interpretation cases to experienced and well prepared trial counsel. ■