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ENFORCEABILITY OF IGAMING DEBTS IN ONTARIO

by Michael D. Lipton, Q.C. and Kevin J. Weber

As previously reported in *Gaming Legal News*, in October 2010 the Ontario Superior Court of Justice (Divisional Court) ruled in the case of *Bérubé v. Rational Entertainment Limited*[1] that an Ontario resident who incurred debts while betting and gaming online on a website operated and regulated from outside Canada ("offshore iGaming") was responsible for those debts as a matter of contract. In that case, the agreement which the Ontario resident assented to in order to use PokerStars' website was held to require the Ontario resident to verify the legality of the use of that website in her jurisdiction. This was held to be "a complete answer to…submissions concerning the enforceability of an illegal contract."[2]

In Canada, there has been no attempt to prosecute the operators of offshore iGaming websites under the *Criminal Code* (the "Code") where the only real connection between the website and Canada is that some of its customers are located in Canada. Similarly, Canadian businesses that have provided goods or services to such operators have not been subject to prosecution.

Canadian authorities nonetheless take the view that offshore iGaming operators are acting unlawfully when they accept persons in Canada as customers. In that environment, could the issue of "enforceability of an illegal contract" be used to prevent a Canadian company from enforcing its agreement against an offshore iGaming operator in a Canadian court?

Some guidance on this issue emerged last year in the decision of the British Columbia Supreme Court in *Tsoi v. Lai*.[3] Lai operated a land-based operation relating to the playing of mah-jong for money. Tsoi lent Lai $50,000 in connection with that operation, which Lai used to provide credit to players, on the basis of an oral loan agreement.[4]

The parties agreed that mah-jong is a "game" as that word is defined by section 197 of the Code. On that basis, the court held that Lai "therefore appears to have admitted to being involved in an illegal business, namely, keeping a common gaming house or betting house under s. 201" of the Code.[5]

Based on recordings of conversations between the parties after the loan was made, the court further found that Tsoi knew of Lai's intended unlawful use of the proceeds of the loan at the time the agreement was entered into.[6]

Because the oral loan agreement was not illegal "on its face," but instead was rendered unlawful by Tsoi's knowledge that the proceeds of the loan were to be put to unlawful use, the court analyzed the agreement

on the basis of "common law illegality."[7] This led the court to find that the loan agreement was unenforceable as against Lai on the basis of the maxim of *ex turpi causa non oritur actio* ("an action does not arise from a dishonorable cause").[8]

However, the court noted that the *ex turpi* doctrine is not applied mechanically. While one of the consequences of such illegality is that the court will not order the return of property transferred under the illegal contract, there are at least three exceptions that can apply to relieve a party of such consequences:

1. Where the party claiming for return of property is less at fault;

2. Where the claimant "repents" before the illegal contract is performed; and

3. Where the claimant has an independent right to recover (e.g., where recovery in tort might be possible despite an illegal contract).[9]

The British Columbia Supreme Court held that Tsoi, the lender, was "less at fault" than Lai, the keeper of the common gaming house. In making that determination, the court drew a contrast between Lai's direct benefit from the illegal activity as against Tsoi's indirect benefit by way of the interest he made on the loan.[10]

The court went on to state that even if both parties were equally at fault, it would find in favour of Tsoi on the basis that to do otherwise would create an "unjust windfall" in the hands of Lai (also commonly referred to as "unjust enrichment").[11] Finding that Tsoi's conduct did not rise to the level of being "egregious" as compared to earlier cases in which enforcement of agreements had been denied, the court stated that it had greater concern about unjustified windfall or unjust enrichment than it did about the nature of the illegality.[12] The court relied upon precedents which held that concerns about unjustified windfalls may override a court's concern about illegality,[13] and it held in favour of the plaintiff and ordered that Lai repay the outstanding amount of the loan and interest owing to Tsoi.[14]

The decision in *Tsoi v. Lai* tells us that a very subjective standard would apply where a Canadian company asks a Canadian court to enforce its agreement with an offshore iGaming operator. While it would seem at first blush that the Canadian company would be "less at fault" than the offshore iGaming operator from the perspective of the Code, depending upon the nature of the goods or services provided by the Canadian company and the terms of the agreement between the two entities, a particular judge may see them as being "equally at fault." For example, where the Canadian entity provides software to the offshore iGaming operator in the knowledge that the software will likely be used to accept bets from Canada, a court may see the two entities as being equally at fault. If that software provider also provides customer support to the operator's Canadian customers, such a finding is more likely still.

However, following the rationale expressed by the Ontario Superior Court in *Bérubé v. Rational Entertainment Limited*,[15] if the contract between the Canadian service provider and the offshore iGaming operator expressly states that the goods or services are being provided on the understanding that the offshore gaming operator does not accept Canadian customers, that contractual provision may be held to be "a complete answer to…submissions concerning the enforceability of an illegal contract."

Even where a court finds the Canadian company and the offshore iGaming operator to be "equally at fault" from the perspective of the Code, an agreement between the two may be enforceable by way of the application of another subjective standard: where the court is more concerned about "unjustified windfall" or "unjust enrichment" than it is about the nature of the illegality. To a large extent, this may depend upon how seriously a particular judge views the gaming and betting offences in the Code. The court's assessment on this issue could also be influenced against the Canadian company if it is compensated by the offshore iGaming operator on the basis of a formula tied to the offshore iGaming operator's revenue (including revenue earned by Canadian customers), as might be the case where a Canadian software company provides games to be played on the offshore website.

The subjective nature of this analysis makes it difficult to provide a "one-size-fits-all" answer as to how Canadian companies that provide goods and services to offshore iGaming operators can structure their contractual relationships with those operators so as to make "illegal contract" arguments less likely to succeed. This makes it all the more important that Canadian companies entering into these relationships obtain legal advice from counsel experienced in the field, tailored to the specific circumstances that exist between the Canadian company and the offshore iGaming operator in question.

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[1] 2010 ONSC 5545.
[2] *Ibid*., paras. 14–15.
[3] 2012 CarswellBC 2138.
[4] *Ibid*., para. 4.
[5] *Ibid*., para. 2.
[6] *Ibid*., paras. 7–9.
[7] *Ibid*., para. 9.
[8] *Ibid*., paras. 10, 13.
[9] *Ibid*. at para. 13. See also *Still v. Minister of National Revenue* (1997), 154 D.L.R. (4th) 229 (Fed. C.A.) at para. 24.
[10] *Ibid*., paras. 14–17.
[11] *Ibid*., para. 18.
[12] *Ibid*., para. 22.
[13] *Ibid*., para. 20.
[14] *Ibid*., para. 23.
[15] *Supra* note 1.