

CLIENT ALERT

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THE SUPREME COURT CONFIRMS THE COMMON LAW APPROACH TO CONTRACT ENFORCEABILITY APPLIES TO POST-INCORPORATION CONTRACTS

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Background

On October 23, 2020, the Supreme Court of Canada (“**SCC**”) released its decision in *The Owners, Strata Plan LMS 3905 v. Crystal Square Parking Corporation* (“**Crystal Square**”), an appeal about whether a pre-incorporation agreement was binding on the owner of an office tower.¹ The SCC’s ruling in *Crystal Square* clarifies the requirements for finding pre-incorporation contracts binding on corporations following incorporation, i.e. the enforceability of post-incorporation contracts.

The Supreme Court held that the applicable test for finding that a post-incorporation contract is enforceable is the same as the one for finding that any other agreement exists at common law. Namely, the test is objective, and that offer, acceptance, consideration, and terms may be inferred from the parties’ conduct, and from the surrounding circumstances.

Factual History

Crystal Square involves a large development by Crystal Square Development Corporation (the “**Developer**”) in Burnaby, British Columbia. The development includes office and residential towers, hotel and retail complexes, and, central to this dispute, a parking facility.

In March 1999, the Developer and the City of Burnaby (the “**City**”) entered into an air space parcel agreement (the “**ASP Agreement**”). The ASP Agreement contained certain provisions regarding the parking facility, including parking and access rights, parking fees, and capital costs.

In 2002, the Developer sold the parking facility to Crystal Square Parking Corporation (“**CSPC**”), the respondent, and assigned the ASP Agreement to CSPC. Strata Plan LMS 3905 (“**Strata**”), the appellant and a strata corporation, is the owner of the office tower. Strata only came into existence in May 1999.²

Until 2012, Strata’s members used the parking facility, and Strata paid parking fees at the ASP Agreement’s prescribed rate. A dispute then arose between Strata and CSPC, and CSPC demanded capital reserve payments from Strata, alleging it was owed such payments under the ASP Agreement. When Strata refused to pay any more than its existing fees, CSPC revoked Strata’s parking privileges.

Strata launched a civil claim against CSPC, seeking to either invalidate the ASP Agreement’s provisions regarding the parking facility, or a declaration that the ASP Agreement was unenforceable. Strata also argued that, in any event, it was not a party to the ASP Agreement since it pre-dated Strata’s incorporation, and was therefore not bound by the ASP Agreement’s terms.

Procedural History

The British Columbia Supreme Court (the “**BCSC**”) agreed with Strata that it was not bound by the ASP Agreement. The BCSC found that Strata had not demonstrated an intention to enter into a post-incorporation contract on the same terms as the ASP Agreement.³

On appeal, the British Columbia Court of Appeal (“**BCCA**”) overturned the BCSC’s decision.⁴ According to the BCCA, the trial judge had erred in relying on the fact that Strata was not a party to the ASP Agreement and that Strata had not ratified it.

The SCC’s Decision

The majority in *Crystal Square* held that the payment obligations stipulated in the ASP Agreement are enforceable against Strata on the basis that Strata demonstrated an objective intention to be bound by terms that replicated the ASP Agreement’s terms regarding the parking facility.⁵

The test for determining whether a pre-incorporation contract is binding following incorporation is the same for finding that any other agreement exists at common law.

According to the majority in *Crystal Square*, the test for finding that a binding post-incorporation contract exists is an “outward manifestation of assent by each party such as to induce a reasonable expectation in the other.” This test is objective and rooted in the common law’s general approach to contract formation.⁶

¹ *The Owners, Strata Plan LMS 3905 v. Crystal Square Parking Corporation*, 2020 SCC 29

² A strata corporation is a legal entity with all of the powers of a natural person who has full capacity. In other jurisdictions, such as Ontario, strata are known as condominiums.

³ *Ibid* at para 12.

⁴ *Ibid* at para 13.

⁵ *Ibid* at para 53.

⁶ *Ibid* at para 33.

Therefore, whether pre-incorporation contracts are binding following incorporation requires determining:

- (1) whether a reasonable person in the position of one party would consider that the other party's conduct constituted an offer; and
- (2) whether a reasonable person in the position of the other party would consider the former's conduct constituted an acceptance.⁷

Strata objectively demonstrated an intention to be bound by a post-incorporation contract on the relevant terms of the ASP Agreement.

According to the majority in *Crystal Square*, Strata objectively manifested an intention to be bound by a post-incorporation contract with CSPC after CSPC purchased the parking lot from the Developer. It did so by virtue of the strong evidence regarding offer and acceptance of a post-incorporation contract between Strata and CSPC.⁸

Specifically, *CSPC actively demonstrated an intention to offer Strata a contract on the terms of the ASP Agreement.*⁹ For example, CSPC made parking passes available to Strata members in a quantity that corresponded to their share of parking spaces under the ASP Agreement. In addition, the ASP Agreement provided for maintenance and operation costs of the parking facility in its definition of "Operating Costs." These costs, as per the ASP Agreement, were factored into the fee CSPC charged Strata for parking passes.¹⁰

In turn, *Strata objectively demonstrated an intention to accept CSPC's offer.*¹¹ Strata paid for the parking passes on the ASP Agreement's terms, and its members exercised their parking rights as per the ASP Agreement, which corresponded to those payments. Thus, viewed from the reasonable person's perspective, he or she would view Strata's conduct as demonstrating agreement to the terms regarding the parking facility in the ASP Agreement.

In concluding that Strata was bound by ASP Agreement's terms regarding the parking facility, the majority also noted that the ASP Agreement's existence was only one aspect of the objective circumstances that could be used to interpret the parties' conduct following Strata's incorporation.¹² Whether the ASP Agreement was invalid or not, the surrounding circumstances would lead a reasonable person to understand CSPC and Strata as acting in a manner implying offer and acceptance of terms replicating those found in the ASP Agreement regarding the parking facility.¹³

Conclusion

The key takeaway from *Crystal Square* is that the traditional approach to contract formation applies to post-incorporation contracts. This means that a contract's elements – offer, acceptance, consideration, and terms – can be inferred from the conduct and circumstances surrounding two or more parties' business arrangements.

It is therefore important for any business operating in Canada, to consider how their informal or ad-hoc business arrangements and conduct when dealing with one or more other parties, could reasonably be perceived. Even if the business *subjectively* perceives some of their own business activities and arrangements as non-legally binding, a court could consider some or all aspects of them enforceable in the event of a legal dispute.

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⁷ *Ibid.*

⁸ *Ibid* at para 47.

⁹ *Ibid* at para 49.

¹⁰ *Ibid.*

¹¹ *Ibid* at para 50.

¹² *Ibid* at para 52.

¹³ *Ibid.*