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THE USE OF EXTRINSIC EVIDENCE IN THE INTERPRETATION OF WRITTEN AGREEMENTS IN ALBERTA

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The main objective of the court when attempting to interpret a written agreement is to give effect to the true intention of the parties to that agreement. To do this, the court first looks to the words compiling the agreement to attempt to give a fair and plain meaning to it. However, when the agreement after considering the plain and ordinary meaning of the words therein is still not clear, the court may feel justified in using extrinsic evidence, such as the circumstances surrounding the parties when coming to the agreement, to find and give effect to their true intentions.

The use of extrinsic evidence to interpret a written agreement must be limited to situations where the intentions of the parties are unclear after looking at the written agreement on its own. Various rules and principles complicate this basic underlying statement. They exist to ensure the court does not simply transpose its "view" of what is fair and reasonable in lieu of contractual interpretation. This article attempts to outline these various rules and principles as they exist in the law of extrinsic evidence when interpreting contracts in Alberta.

En tentant d'interpréter une entente écrite, le principal objectif de la cour consiste à traduire en pratique la véritable intention des parties liées par l'entente en question. Pour ce faire, la cour examine d'abord les mots qui forment l'entente dans le but d'y donner un sens juste et clair. Cependant, si après avoir considéré le sens juste et clair des mots utilisés, l'entente n'est toujours pas claire, la cour peut pencher vers le recours à la preuve extrinsèque comme les circonstances qui entouraient les parties lorsqu'elles ont contracté l'entente, dans le but de trouver et d'en appliquer les véritables intentions.

Le recours à la preuve extrinsèque pour interpréter une entente écrite doit être limité aux situations où les intentions des parties ne sont toujours pas claires même après avoir examiné l'entente en soi. Divers principes et règles compliquent cette déclaration sous-jacente fondamentale. Ces règles et principes existent pour que la cour ne transpose pas simplement sa « vue » de ce qui est juste et raisonnable à l'interprétation contractuelle. Cet article essaie de brosser les grandes lignes de ces règles et principes tels qu'ils existent dans le droit de la preuve extrinsèque dans l'interprétation des contrats en Alberta.

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I. INTRODUCTION

The purpose of this article is to provide a summary of the present state of the law in the Province of Alberta relating to the rules of contractual interpretation and in particular the use of extrinsic evidence in that process. This article will restate the basic principles of contractual interpretation that have been established in Alberta by the Supreme Court of Canada (Supreme Court), the Alberta Court of Appeal (Court of Appeal — which term includes the Alberta Supreme Court sitting *en banc* and the Alberta Supreme Court, Appellant Division) and the other courts established in the Province. Recent trends in contractual interpretation will also be reviewed. The article will focus less on what the law "should be" and will focus more on what the law is as of this writing. It is hoped that this article will serve as a research tool for those reviewing the law in this area.

The law relating to contractual interpretation in Alberta has developed from the same common law principles as has the law in other jurisdictions in Canada and the Commonwealth. However, there are areas where the courts in Alberta have taken a different approach than those in the other provinces, particularly in relation to the use of extrinsic evidence. Where these differences arise, the writer will discuss the case law from the other jurisdictions. However, for the most part, the cases referred to will either be decisions of the Supreme Court or decisions arising from the Province of Alberta. It is often helpful to know the views held by particular judges. Therefore, the names of the judges who decided the Alberta cases will be included in the citations. Where Supreme Court or Court of Appeal cases are being referenced, only the page numbers will be given unless the reference does not necessarily reflect the views of the majority of the Court. In that case, the name of the judge will be given.

II. PURPOSE OF CONTRACTUAL INTERPRETATION

A. DETERMINING THE INTENTION OF THE PARTIES

The purpose of contractual interpretation would initially appear self-evident. Common sense would suggest that the purpose is to determine "what the contract says." Accordingly, the process of contractual interpretation could be viewed as being similar to the process of translating ancient writings into English. As part of that process each word or hieroglyphic would be given an English translation. Using this method, the content of the ancient text would eventually be revealed. Determining the meaning of the words used is, in fact, a major part of the process of interpreting a written contract. However, a contract is more than just a piece of prose. A written contract is, among other things, a statement of the intended rights and obligations of the contracting parties in a given set of circumstances. The object of the interpretation process is therefore to learn the nature of those intended rights and obligations. The mechanical process of defining each of the words used in the contract is often ill-suited

to this task. The interpretation of a contract therefore bears similarities to the "interpretation" of a painting or sculpture. During that process the work is looked at in its entirety with the objective of understanding the meaning its creator intended to convey. For example, the Court of Appeal and Supreme Court of Canada, in discussing contractual interpretation, said that

> The objective is to discover and give effect to the real intention of the parties. That intention must be found, in the first instance, in the operative words of the documents, read as a whole, giving meaning to every provision if that is possible.[1]
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> ...
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> [t]he normal rules of construction lead a court to search for an interpretation which, from the whole of the contract, would appear to promote or advance the true intent of the parties at the time of entry into the contract.[2]

These principles have been widely applied by the Alberta courts[3] and they have generally applied the principle that the ultimate purpose of the process of contractual interpretation is to ascertain the intention of the parties from the language they have used in the contract.[4]

B. PROPER INTERPRETATION NEED NOT ACHIEVE A FAIR RESULT

Given the equitable jurisdiction of the court and its role in dispensing justice, one might expect that the interpretation of any given contract would be governed by the court's view of what is "fair and reasonable" as between the parties. In fact, the concept of "fairness" has a rather limited application in the process of contractual interpretation. The Alberta courts have been very clear in stating that they are not at liberty to read a contract so as to achieve a "fair" result when the words used do not support such a result. The governing rule in Alberta is that the court is to find the initial meaning of a contract from the words that have been used. The court does not have a right to make a contract for the parties. These principles have been stated in a variety of ways:

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1 *Scurry-Rainbow Oil Ltd. v. Kasha* (1996), 39 Alta. L.R. (3d) 153 at 168 (C.A.), leave to appeal to S.C.C. refused [1996] S.C.C.A. No. 391 [*Kasha*].

2 *Consolidated Bathurst Export Ltd. v. Mutual Boiler and Machinery Insurance*, [1980] 1 S.C.R. 888 at 901 [*Bathurst*]; see also *Hillis Oil & Sales Limited v. Wynn's Canada Ltd.*, [1986] 1 S.C.R. 57 at 66 [*Hillis Oil*]; *Manulife Bank of Canada v. Conlin*, [1996] 3 S.C.R. 415 at para. 79, Iacobucci J. (Gonthier J. concurring) [*Manulife*].

3 *Guaranty Trust Co. of Canada v. Hetherington* (1987), 50 Alta. L.R. (2d) 193 (Q.B.), O'Leary J., aff'd (1989), 67 Alta. L.R. (2d) 290 (C.A.) [*Hetherington*]; *Delta Hotels Ltd. v. Okabe Canada Investments Ltd.* (1991), 81 Alta. L.R. (2d) 338 at 370 (Q.B.), Power J. [*Delta Hotels*]; *Scurry-Rainbow Oil Ltd. v. Galloway Estate* (1993), 8 Alta. L.R. (3d) 225 at 226 (Q.B.), Hunt J., aff'd (1994), 23 Alta. L.R. (3d) 193 (C.A.), leave to S.C.C. refused (1995), 26 Alta. L.R. (3d) 1 [*Galloway*].

4 *Bank of Nova Scotia v. Siler* (1999), 253 A.R. 333 at 335 (Q.B.), Coutu J. [*Siler*]; *Morrison Petroleums Ltd. v. Phoenix Canada Oil* (1997), 198 A.R. 81 at 99 (Q.B.), Moshansky J. [*Phoenix*]; *Edmonton (City of) v. Protection Mutual Insurance* (1997), 197 A.R. 81 at 109 (Q.B.), Lee J. [*Protection*]; *Dornan Petroleum v. Petro-Canada* (1996), 189 A.R. 241 at 275 (Q.B.), Murray J. [*Dornan*]; see also *Bank of British Columbia v. Turbo Resources Ltd.* (1983), 27 Alta. L.R. (2d) 17 at 30 (C.A.) [*Turbo Resources*]; *L&W Moving Ltd. v. Royal Bank of Canada* (1985), 40 Alta. L.R. (2d) 94 at 96 (C.A.) [*L&W Moving*].

> [t]he function of the court is limited to construing the words employed; it is not justified in forcing into them a meaning which they cannot reasonably admit of. Its duty is to interpret, not to enact.[5]
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> ...
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> I do not want to lose sight of the fact that it is the Court's obligation to interpret a contract according to the used words. It is not the Court's duty to remake a contract or to give it a fair result.[6]
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> ...
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> The court does not make contracts for the parties. A court is not to impose its idea of fairness and interpret the plain wording of a contract to give it a meaning other than that which the language can bear because a court thinks that this would be a fair method of handling the matter.[7]
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> ...
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> Nothing is more dangerous than to allow oneself liberty to construct for the parties contracts which they have not in terms made by importing implications which would appear to make the contract more businesslike or more just.[8]

A court is not normally entitled to read words into a contract that do not appear in the written agreement.[9] Likewise, a court is not normally entitled to ignore or strike out express provisions in a contract.[10] This is so even if the words used create a hardship for one party. The fact that a contract has become very difficult for one party to perform on its express terms is not sufficient grounds for the court to amend its wording.[11] Generally, the court must enforce the imposition of a clearly expressed contractual liability even if the imposition of that liability offends the court's ideas of fairness.[12] Liability under a contract is not a matter

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5 *Toronto Railway v. Toronto* (1906), 37 S.C.R. 430 at 434-35; applied in *Calgary (City of) v. Canadian Western Natural Gas* (1916), 33 D.L.R. 385 at 389 (Alta. S.C. (A.D.)), Stuart J., aff'd (1917), 40 D.L.R. 201 (S.C.C.) [*Cdn. Western Gas*]; *Galloway, supra* note 3.

6 *Prenor Trust Co. of Canada v. Kerkhoff Properties* (1994), 21 Alta. L.R. (3d) 122 at 131 (Q.B.), Fruman J. [*Kerkhoff*].

7 *Alex Duff Realty Ltd. v. Eaglecrest Holdings Ltd.* (1983), 44 A.R. 67 at 75 (C.A.), McGillvray C.J.A. [*Alex Duff*].

8 *Canadian Delhi Oil Ltd. v. Aliminex Ltd.* (1967), 62 W.W.R. 513 at 525 (Alta. SC. (A.D.)), aff'd [1968] S.C.R. 775 [*Delhi Oil*], quoting Lord Atkins' statement from *Bell v. Lever Bros. Ltd.*, [1932] A.C. 161 at 226 (H.L.).

9 *Alberta Energy Co. v. Canadian Western Natural Gas Co.* (1992), 5 Alta. L.R. (3d) 250 at 255 (C.A.) [*Alberta Energy*]: subject to the Court's somewhat limited power to imply terms that were obviously intended but not included in the text of the agreement.

10 *J. G. Collins Insurance Agency Ltd. v. Elsley Estate*, [1978] 2 S.C.R. 916; *Edmonton (City of) v. Triple Five Corp.* (1994), 22 Alta. L.R. (3d) 289 at 303 (Q.B.), Bielby J.; subject to the court's power to do so where the words either (a) directly conflict with the overall contractual intent; (b) destroy altogether an obligation created in an earlier provision; (c) are meaningless; or (d) contain an inaccurate description of a person or thing that is properly described elsewhere in the document: *Continental Insurance v. Law Society of Alberta* (1984), 34 Alta. L.R. (2d) 214 at 220-21 (C.A.) [*Continental Insurance*]; *Brown v. Norbury*, [1931] 4 D.L.R. 507 at 518-19 (Alta. S.C. (A.D.)) [*Norbury*]; *Bucke (Township of) v. MacRae Mining Co.*, [1927] S.C.R. 403 at 411 [*Bucke*].

11 *Catre Industries Ltd. v. Alberta* (1989), 99 A.R. 321 at 332 (C.A.) [*Catre Industries*]; *Homes by Jayman Ltd. v. Kellam Berg Engineering & Surveys Ltd.* (1995), 29 Alta. L.R. (3d) 1 at 31 (Q.B.), Hunt J., varied (1997) 54 Alta. L.R. (3d) 272 (C.A.); *Steel Co. of Canada* v. *Willand Management Ltd.*, [1966] S.C.R. 746 at 753-54.

12 *Alex Duff, supra* note 7 at 72; *Bryan v. Canadian Home Assurance* (1982), 19 Alta. L.R. (2d) 188 at 190 (Q.B.), Legg J.; *Zotzman v. Mutual Life Assurance Co. of Can.* (1991), 114 A.R. 330 at 333 (Q.B.), Miller J. [*Zotzman*].

of discretion or fairness.[13] The courts take the view that contractual provisions, which may seem to be unfair, may have been the product of hard bargaining between the parties and therefore deserve to be enforced in accordance with their terms.[14] The result is that, when the words of the contract are clear, they will normally be given effect. As was stated by the Supreme Court of Canada: "Certainly where the parties have capacity in law to enter into the contract, where the terms of the contract are clear and unambiguous, where there is valid consideration passing between the parties, and where there is no evidence of oppression or operative misrepresentation, the law recognizes no principle which fails to enforce the validity of such a contract."[15]

III. BASIC RULES OF CONTRACTUAL INTERPRETATION

A. INTERPRETATION IS A QUESTION OF LAW

The interpretation of a written agreement drafted in ordinary English is a question of law. Accordingly, the interpretation of such an agreement is not a fit subject to introduce evidence and the court will normally not accept evidence, expert or otherwise, to aid in that process.[16] The court is charged with reviewing the agreement and applying the rules of interpretation to determine its legal effect. Therefore the evidence of English professors or other such experts is considered to be of no assistance to the court.[17]

Consistent with this position is the well-established rule that direct evidence of a contracting party's intention is inadmissible,[18] since the meaning that a party subjectively intended to convey is irrelevant to the legal meaning of the words used.[19]

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13 *Manufacturers Life Insurance v. Toronto-Dominion Bank* (1988), 92 A.R. 92 at 95 (C.A.), followed by Master Funduk in *Wye Gardens Inc. v. Edmonton Equipment Sales Ltd.* (1991), 85 Alta. L.R. (2d) 104 at 111 (M.C.) [*Wye Gardens*]; *Steeplejack Services (Canada) Ltd. v. Access Scaffold & Ladder* (1989), 98 A.R. 311 at 314 (M.C.) [*Steeplejack*].

14 *Hunter Engineering v. Syncrude Canada Ltd.*, [1989] 1 S.C.R. 426 at 488, Wilson J.

15 *Ronald Elwyn Lister Ltd. v. Dunlop Canada*, [1982] 1 S.C.R. 726 at 745, see also *MLH&A v. Shepp* (1997), 201 A.R. 112 at 118 (Q.B.), Clarke J.; to the same effect is *Brewery, Beverage and Soft Drink Workers Local 250 v. Labatt's Alberta Brewery* (1996), 38 Alta. L.R. (3d) 308 at 316 (C.A.).

16 *Morguard Trust v. Royal Bank* (1989), 70 Alta. L.R. (2d) 242 at 244 (C.A.) [*Morguard Trust*]; followed in the decisions of Master Funduk in *Imperial Oil Limited v. Whissell Enterpirses Ltd.* (1985), 62 A.R. 321 at 325 (M.C.) [*Whissell*]; *Nelson (Trustee of) v. Nelson* (1989), 75 C.B.R. (N.S.) 47 at 50 (Alta. Reg); and *Alberta (Treasury Branches) v. Bate* (1996), 180 A.R. 161 at 165 (M.C.) [*Bate*]; see also *Tokarek v. Davison* (1991), 85 Alta. L.R. (2d) 300 at 304 (M.C.); *852819 Alberta Ltd. v. Louie's Submarine*, [2000] A.J. No. 1493 at para. 31 (Q.B.) (QL) [*Louie's Submarine*]; *Re Bohnet (Bankruptcy)* (2002), 310 A.R. 53 at 58 (M.C.), cases in which Master Funduk, cites J.E. Côté, *An Introduction to the Law of Contract* (Edmonton: Juriliber, 1974) at 147-48 to the same effect. For the purposes of review by the Court of Appeal the interpretation of a contract is a question of law: *Alberta v. Western Irrigation District* (2002), 312 A.R. 358 at 362 (C.A.) [*Western Irrigation*].

17 *Canadian National Railway v. Volker Stevin Contracting Ltd.* (1991), 1 Alta. L.R. (3d) 167 at 170 (C.A.) [*Volker*]; *United Canso Oil & Gas Ltd. v. Washoe Northern Inc.* (1990), 78 Alta. L.R. (2d) 79 at 87-88 (Q.B.), Hutchinson J. [*United Canso*]; see also *Avco Delta Corp. Canada Ltd. v. MacKay*, [1977] 5 W.W.R. 4 at 8 (Alta. S.C. (A.D.)) [*Avco*].

18 *Turbo Resources, supra* note 4 at 30.

19 *Anderson and Anderson v. Chaba and Chaba*, [1978] 1 W.W.R. 631 at 637 (Alta. S.C. (A.D.)) [*Chaba*]; *Marthaller v. Lansdowne Equity Venture* (1997), 200 A.R. 226 at 230 (C.A.) and Master Funduk's decisions in *Bate, supra* note 16 at 165; *Capital Underwriters Corp. v. Kruger* (1996), 194 A.R. 63 at 74 (M.C.) [*Underwriters*]; *Louie's Submarine, supra* note 16 at para. 30.

However, this does not mean that the interpretation of a written agreement is to be done without reference to extraneous material. The court may consider submissions of counsel regarding the meaning of the words used and may make reference to dictionaries.[20] Further, as will be discussed below, the court may accept evidence regarding the circumstances surrounding the making of the agreement so as to put the agreement in context,[21] and extrinsic evidence may be admitted to resolve ambiguities.[22]

However, as will also be discussed below,[23] where the ordinary meaning of the words used is clear and unambiguous that meaning will be applied, and there will be little, if any, need for the court to look beyond the words used.

B. RELIANCE ON PLAIN AND ORDINARY MEANING

A written agreement is to be construed and interpreted using the "plain," "ordinary," "common" and "literal" meaning of the words used provided that the words are not ambiguous in themselves or the application of the words in the circumstances does not create ambiguity or an absurdity.[24] This approach is sometimes referred to in the case law as the "golden rule of interpretation."[25] Under this approach, where the language used is, in its primary meaning, unambiguous, and such primary meaning is not excluded by the context and is sensible with reference to the extrinsic circumstances, such primary meaning will be conclusively adopted. However, where the literal construction leads to an absurdity, repugnancy or inconsistency that reasonable people would not have contemplated under the circumstances, then the construction ought to be modified so as to avoid such a result.[26] The court has a duty in the latter circumstances to avoid an interpretation that would result in a commercial absurdity.[27]

Cases involving a latent ambiguity or absurdity are the exception rather than the rule. Unless the circumstances are such as to exclude the plain and ordinary meaning of any

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20 See *e.g. Volker, supra* note 17 at 172; *Continental Insurance, supra* note 10 at 219; *Prism Petroleum Ltd. v. Omega Hydrocarbons Ltd.* (1992), 4 Alta. L.R. (3d) 332 at 348 (Q.B.), Egbert J. [*Prism*]; *McDonald's Restaurants of Canada Ltd. v. West Edmonton Mall Ltd.* (1994), 22 Alta. L.R. (3d) 402 at 413 (Q.B.), Mason J.; see generally Côté, *supra* note 16 at 156-57.

21 *Turbo Resources, supra* note 4 at 170.

22 *Cooke v. Anderson and Anderson*, [1945] 1 W.W.R. 657 at 668 (Alta. S.C. (A.D.)) [*Cooke*].

23 See *infra* notes 24-29.

24 *Great Plains Development Co. of Canada v. Hidrogas Ltd.* (1979), 17 Alta. L.R. (2d) 17 at 25-26 (C.A.); *Brinkerhoff International v. Numac Energy* (1997), 53 Alta. L.R. (3d) 4 at 9-10 (C.A.); *Merrill Petroleums Limited v. Seaboard Oil* (1957), 22 W.W.R. (N.S.) 529 at 550 (Alta. S.C. (T.D.)), Egbert J., aff'd (1958), 25 W.W.R. (N.S.) 236 (Alta. S.C. (A.D.)); *Gordon v. Wyatt Co.* (1998), 57 Alta. L.R. (3d) 182 at 187 (Q.B.), Hutchinson J. [*Wyatt*]; *Suncor Inc. v. Norcen International Ltd.* (1988), 89 A.R. 200 at 223 (Q.B.), Power J. [*Suncor*]; *Phoenix, supra* note 4 at 99.

25 *Toronto (City of) v. W.H. Hotel Ltd.*, [1966] S.C.R. 434 at 440 [*W.H. Hotel*]; *Suncor, ibid.* at 223; *Bilawchuk v. Blomberg* (2000), 279 A.R. 269 at 275 (Q.B.), Lee J. [*Bilawchuk*].

26 *Delhi Oil, supra* note 8 at 518-19; *Reddy v. Strople* (1911), 44 S.C.R. 246 at 257, Duff J.; *Bar-Don Holdings Ltd. v. Reed Stenhouse Limited* (1983), 44 A.R. 246 at 249 (Q.B.) [*Bar-Don*].

27 *W. H. Hotel, supra* note 25; *Begro Construction Ltd. v. St. Mary River Irrigation District* (1994), 154 A.R. 1 at 27-28 (Q.B.), Power J. [*Begro*]; *Suncor, supra* note 24 at 223.

reasonable application, the plain and ordinary meaning must be applied.[28] This result flows from the presumption that the parties intended the ordinary meaning of the words used to apply. Likewise where the words in question have, through judicial consideration, come to have an accepted legal meaning, the court will assume that the parties intended that such meaning would apply.[29]

C. INTERPRETATION IS IN CONTEXT OF ENTIRE AGREEMENT

The court will often be called upon to interpret only a portion of the agreement in question. In some cases the result will turn on the interpretation of only one phrase or clause. It is clear that in such a case the court must determine the intention of the parties from looking at the agreement as a whole, thereby putting the disputed words into context. The court must try to give effect to every part of that agreement.[30] The best interpretation of a contract is one that will harmonize and reconcile all portions of the agreement.[31] However, if the words of a particular clause are clear and unambiguous, they cannot be modified by reference to other clauses in the agreement.[32]

D. USE OF RECITALS

Commercial agreements often contain recitals as well as operative portions. The common law rule regarding the use of recitals has been described in a number of ways. Justice O'Leary applied the following rule in *Hetherington*: "When the words in the operative part of an instrument are ambiguous, the recitals and other parts of the instrument may be used to discover the intention of the parties and to fix the true meaning of those words. But clear words in the operative part of an instrument cannot be controlled by recitals."[33]

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28 *Delhi Oil*, *supra* note 8 at 519-20; *Alberta Energy*, *supra* note 9 at 254-55; *Predator Corp. v. Ricks Nova Scotia Co.* (2001), 318 A.R. 1 (Q.B.), Wilkins J., aff'd (2002), 317 A.R. 322 (C.A.); *Sinclaire v. South Trail Shell* (1987) (2002), 1 Alta. L.R. (4th) 135 at 142 (Q.B.), Watson J. [*Sinclaire*]; *Liquor Depot at Riverbend Square Ltd. v. Time for Wine Ltd.* (1997), 203 A.R. 382 at 387-88 (Q.B.), Fraser J.; *Herron v. Chase Manufacturing* (2003), 330 A.R. 52 at 61 (C.A.): "the plain and ordinary meaning of each contract must be assessed in its own context with a focus on the intention of the parties."

29 *Prism*, *supra* note 20 at 236.

30 *Western Irrigation*, *supra* note 16 at 363; *Kasha*, *supra* note 1 at 168; *Edmonton Northlands v. Edmonton Oilers Hockey Club* (1994), 149 A.R. 92 at 95 (C.A.) [*Edmonton Northlands*]; *Canada Deposit Insurance Corp. (CDIC) v. Canadian Commercial Bank* (1991), 113 A.R. 371 at 374 (C.A.), aff'd [1992] 2 S.C.R. 3 [*Canada Deposit*]; *Hillis Oil*, *supra* note 2 at 66; *L.&W. Moving*, *supra* note 4 at 96; *Continental Insurance*, *supra* note 10 at 220; *Hetherington*, *supra* note 3 at 209; *Delta Hotels*, *supra* note 3 at 370; *Canadian Foundry Co. Ltd. v. Edmonton Portland Cement Co. Ltd.* (1915), 10 Alta. L.R. 232 at 236 (S.C. (T.D.) and S.C. (A.D.)), Walsh J.; *Winnipeg (George) Canada Limited v. Groveridge Imperial Properties Ltd.* (1985), 40 Alta. L.R. (2d) 339 at 345 (Q.B.), Purvis J.; *Qualico Developments Ltd. v. Calgary (City of)* (1987), 53 Alta. L.R. (2d) 129 at 138 (Q.B.), Virtue J. [*Qualico*]; *Opron Construction Ltd. v. Alberta* (1994), 151 A.R. 241 at 342 (Q.B.), Feehan J. [*Opron*]; see also *Rustin v. Fairchild & Co.* (1907), 39 S.C.R. 274 at 277.

31 *Cooke*, *supra* note 22 at 668; *Alberta Power Ltd. v. McIntyre Porcupine Mines Ltd.*, [1975] 5 W.W.R. 632 at 639 (Alta. S.C. (A.D.)) [*Alberta Power*]; *Northwestern Metal & Salvage Ltd. v. Alltar Roofing Ltd.* (1994), 19 Alta. L.R. (3d) 439 at 440 (C.A.); *Canada Deposit*, *ibid.* at 375; *Galloway*, *supra* note 3 at 234; *Beller Carreau Lucyshyn Inc. v. Cenalta Oilwell Servicing Ltd.* (1997), 211 A.R. 1 at 6 (Q.B.), Lewis J.

32 *Kasha*, *supra* note 1 at 168.

33 *Supra* note 3 at 209-1, citing A.G. Guest, ed., *Chitty on Contracts*, 24th ed. (London: Sweet & Maxwell, 1977) at para. 713.

The following rule has been referred to in several cases: "(1) If the recitals are clear and the operative part is ambiguous, the recitals govern the construction; (2) If the recitals are ambiguous and the operative part is clear, the operative part must prevail; (3) If both the recitals and operative part are clear, but they are inconsistent with each other, the operative part is to be preferred."[34]

These passages appear to be consistent in stating that the operative portion of an agreement has priority over the recitals and the operative portion must apply if it is clear.[35] They suggest that recitals must always be referred to. However, the Court of Appeal has subsequently stated that "The recitals may only be referred to if the operative part of the agreement does not clearly disclose the intention of the parties."[36] It is not clear whether the Court of Appeal simply meant that recitals will only govern where the operative portion is ambiguous. The authority cited in support of the statement suggests that this is what was meant.[37] If so, the passage is uncontroversial. However, if the Court of Appeal was stating that recitals should not even be considered and are inadmissible in interpreting the commercial context of the operative portion of an agreement, this would seem to work a change in the common law. The common law has traditionally been that the court is always entitled to examine the surrounding facts and circumstances known to and affecting the parties at the time of contracting, including the genesis and background of the transaction.[38] This type of information is often contained in recitals and would seem to have been admissible at common law to explain the commercial context of the operative portions of the agreement.[39]

E. INTERPRETATION OF CONFLICTING OR CONTRADICTORY CLAUSES

Courts are often faced with the problem of interpreting a written agreement whose clauses appear inconsistent or contradictory. There are a number of techniques that have been used by the courts to deal with such problems. In some cases these techniques merely employ basic principles. However, there are a number of techniques that are specific to the interpretation of apparently contradictory clauses. These techniques, listed in roughly descending order from the more general, widely accepted rules to the more specific, and, perhaps more controversial, rules are as follows:

(a) determine the general intention evidenced by the contract as a whole and by the surrounding circumstances and interpret both clauses in harmony with that intention and to give effect to that intention;
(b) interpret the more general clauses as being limited or qualified by more specific clauses;

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34 *McLeay v. Burns*, [1920] 2 W.W.R. 815 at 822 (Alta. S.C. (A.D.)) [*McLeay*]; *Delta Hotels*, *supra* note 3 at 370; *Galloway*, *supra* note 3 at 234.

35 See *Skov Lumber v. Clark*, [1932] 3 D.L.R. 780 at 783 (Alta. S.C. (A.D.)).

36 *Kasha*, *supra* note 1 at 168; referred to in *Western Irrigation*, *supra* note 16 at 363.

37 *Kasha*, *ibid.*

38 *Turbo Resources*, *supra* note 4 at 30; *A.R. Williams Machinery Co. Ltd. v. Moore*, [1926] S.C.R. 692 at 705 [*A.R. Williams*]; *Canada Law Book v. Boston Book* (1922), 64 S.C.R. 182 at 185-86, Duff J. [*Canada Law Book*]; *Deserres v. Brault* (1906), 37 S.C.R. 613 at 617 [*Deserres*].

39 *Underwriters*, *supra* note 19 at 75.

(c) give priority to clauses depending on where they appear in the document and if a clause that appears later in a contract destroys all together the obligation created by an earlier clause, the later clause is to be rejected as repugnant and the earlier clause prevails; but if they can be read together, the later clause limits or qualifies the earlier;

(d) interpret the contract to give effect only to those clauses that carry out the general intention expressed in the document as a whole; and

(e) ignore and sever those clauses that are meaningless or incorrect subsidiary terms.

The first principle is simply an application of a primary rule of contractual interpretation. It is illustrated by the decision of the Court of Appeal in *Alberta Power*,[40] which in turn relied on the decision of Cartwright J. in *Cotter v. General Petroleums Ltd.*[41] — a decision of the Supreme Court that reversed the decision of the Court of Appeal[42] and restored the trial judgment of McLaurin J.[43] In both cases, apparently conflicting clauses were read in light of the overall intention evidenced by the contract. In *Alberta Power*, a clause in the agreement provided that all questions raising differences between the parties would be dealt with by way of arbitration. A later clause provided that in the event of a breach of contract either party could bring an action in the courts. A further clause indicated that all remedies afforded by the agreement were cumulative. In *Cotter*, an option agreement relating to petroleum and natural gas rights provided that the option was exercisable in a certain manner within a certain time period. A later clause provided that the optionee was required to exercise the option within a specific time period, failing which they would be liable for breach of covenant. It was argued that the two clauses were inconsistent in that one granted an option and the other made the "option" mandatory.

In both cases the Court resolved the apparent conflict by reading the conflicting clauses together. In *Alberta Power* it was held that both the arbitration and litigation remedies were available, and in *Cotter* effect was given to both terms of the "option" and the right of the optioner to sue for damages in the event the option was not exercised. The principle of law applied in both cases is: "The general rule of construction is, that the Courts, in construing the deeds of parties, look much more to the intent to be collected from the whole deed, than from the language of any particular portion of it."[44]

The Court in *Alberta Power* applied the following passage from *Cooke*: "The best construction of all written instruments is to make all parts agree. The instrument must be construed as a whole and the words of each clause must be so interpreted as to bring it into harmony with the other provisions of the document."[45]

With regard to any rule of interpretation that would strike out a clause on account of repugnancy, Cartwright J. in *Cotter* referred to a passage from the dissenting judgment of

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40 *Supra* note 31.

41 [1951] S.C.R. 154 [*Cotter*].

42 [1949] 2 W.W.R. 146 (Alta. S.C. (A.D.)).

43 [1949] 1 W.W.R. 193 (Alta. S.C. (T.D.)).

44 *Alberta Power*, *supra* note 31 at 638, quoting *Cotter*, *supra* note 41 at 171, citing *Mill v. Mill* (1852), 3 H.L. Cas. 828 at 847.

45 *Supra* note 22 at 669.

Duff J. in *Forbes v. Git*, in which he stated: "The rule as to repugnancy, therefore, is obviously a rule to be applied only in the last resort and when there is no reasonable way of reconciling the two passages and bringing them into harmony with some intention to be collected from the deed as a whole."[46]

The second principle that the courts have applied if the first general principle of harmonious interpretation cannot be used, is that specific clauses operate to limit or qualify general clauses. In *Two Forty Engineering Ltd. v. Platte River Resources Ltd.*,[47] Mason J. applied the following passage from the decision of the Supreme Court in *BG Checo International Ltd. v. British Columbia Hydro & Power Authority*:

> It is a cardinal rule of the construction of contracts that the various parts of the contract are to be interpreted in the context of the intentions of the parties as evident from the contract as a whole.... Where there are apparent inconsistencies between different terms of a contract, the court should attempt to find an interpretation which can reasonably give meaning to each of the terms in question. Only if an interpretation giving reasonable consistency to the terms in question cannot be found will the court rule one clause or the other ineffective.... In this process, the terms will, if reasonably possible, be reconciled by construing one term as a qualification of the other term.... A frequent result of this kind of analysis will be that the general terms of a contract will be seen to be qualified by specific terms — or, to put it another way, where there is apparent conflict between a general term and a specific term, the terms may be reconciled by taking the parties to have intended the scope of the general term to not extend to the subject-matter of the specific term.[48]

This type of analysis would ensure that a general clause would be given effect only so far as is allowed by specific clauses dealing with the same subject matter. It is submitted that this is a technique that has a basis in logic and is consistent with the more general principles of contractual interpretation in that it gives some effect to all parts of the document.

The third approach that has been applied is to establish a priority of the clauses depending on where they appear in the document. If two clauses are completely inconsistent, the later clause will be rejected. If they are only partially inconsistent, the earlier clause may be limited or qualified by a later term. This approach may be found in two propositions advanced by Lord Wrenbury in *Forbes*, where he stated:

> If in a deed an earlier clause is followed by a later clause which destroys altogether the obligation created by the earlier clause, the later clause is to be rejected as repugnant and the earlier clause prevails.... But if the later clause does not destroy but only qualifies the earlier, then the two are to be read together and effect is to be given to the intention of the parties as disclosed by the deed as a whole.[49]

An example of the application of the first part of this passage is to be found in *Ottawa Electric v. St. Jacques*.[50] It is submitted that this method of interpretation is arbitrary. It flows from an ancient maxim of interpretation that gives primacy to clauses depending on where they are located in the text of the document. The technique was not actually employed by

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46 [1921] 62 S.C.R. 1, rev'd [1922] 1 W.W.R. 250 (P.C.) [*Forbes*].
47 (1995), 26 Alta. L.R. (3d) 183 at 190-91 (Q.B.).
48 [1993] 1 S.C.R. 12 at 23-24.
49 [1922] 1 W.W.R. 250 at 253 (P.C.).
50 (1901), 31 S.C.R. 636 at 638-39.

Lord Wrenbury, who found that the clauses in question could be reconciled. As was noted by Duff J. in the same case, this technique should only be applied as a last resort.

The second part of the passage from Lord Wrenbury's speech was applied by the Court of Appeal in *Cooke*,[51] where the earlier clause in a purchase and sale agreement called for payment of a purchase price of $5,000 in cash. A later clause called for payment by way of delivery of crops at a "guaranteed price." It was held that the first clause was qualified by the later clause so that it only set out the minimum payment that could be made and did not fully describe the purchase price.

The fourth principle would direct the court to enforce only those terms which accord with the general intention expressed in the documents. This approach allows the court to pick and choose those parts of the document to which it will give effect. In *Hassard v. Peace River Co-Operative Seed Growers Association Ltd.*, the Supreme Court first noted the existence of the ancient maxim: "If there be two clauses or parts of the deed repugnant the one to the other the first part shall be received and the latter rejected except there be some special reason to the contrary."[52] The Court found that the requirement of a "special reason to the contrary" is met where the general intention of the parties is disclosed by the document, read as a whole and in light of the surrounding circumstances. The Court held that where there are inconsistent parts of a document, effect should be given to the part that denotes the real intentions of the parties, regardless of their relative order in the document. In that case the Supreme Court refused to give effect to an early part of the document that described a transfer of property as a "sale."[53] Rather, it gave effect to later portions of the document, which described the transfer as a form of "deposit" or "advance."[54]

This technique tends to sterilize portions of the document in question and would only appear appropriate where portions of the document are wholly inconsistent. This approach appears to have been employed by the Supreme Court in *Ginter v. Sawley Agency Ltd.*[55] to reject a description of an option period that did not accord with the general intention expressed in the contract. The Court applied another description of the option period, which it considered to be consistent with the contractual intention.

A final technique goes somewhat further and relies on the proposition that a court may ignore and sever a term if it is a meaningless subsidiary term. This proposition was stated by the Court of Appeal in *Continental Insurance* as follows:

> If a contract contains a meaningless phrase it can be ignored and in effect severed from the contract so long as it is a subsidiary term: Chitty on Contracts, 25th ed. (1983), para. 122, at pp. 69-70; *Nicolene Ltd. v. Simmonds*, [1953] 1 Q.B. 543, 2 W.L.R. 717, [1953] 1 All E.R. 822 (C.A.). In the case at bar the second portion of section 4 is, in the face of the clear words of the first portion of that section, meaningless. It purports to refer to a further condition or qualification of the limit of liability and is in these circumstances a "subsidiary term" within the meaning of that phrase as it is used in Halsbury's Laws of England, 9 Hals (4th) 150, para.

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51 *Supra* note 22.
52 [1954] 2 D.L.R. 50 at para. 22 (S.C.C.), aff'g (1952), 7 W.W.R. (N.S.) 118 (Alta. S.C. (A.D.)).
53 *Ibid.* at para. 20.
54 *Ibid.* at para. 19
55 [1967] S.C.R. 451 at 454 [*Ginter*].

268, where the principle is stated in these words: "Where there is agreement on all substantial terms, the court may disregard a subsidiary term on the grounds that it is meaningless."[56]

This proposition was applied in earlier Alberta cases[57] and was arguably a factor in the Supreme Court's decision in *Ginter*.[58]

A related doctrine is found in the maxim of interpretation *falsa demonstratio non nocet*, which directs that where an adequate and sufficient description of a person or thing is made in a contract, but there is also an incorrect and conflicting description, the incorrect description may be struck out. The correct description will then govern.

This maxim was applied by the Court of Appeal in *Norbury*,[59] a case in which an easement grant contained two conflicting land descriptions. As Harvey C.J.A. pointed out, the interpretation maxim is "useless unless and until the Court has made up its mind as to which of two or more conflicting descriptions ought under the circumstances to be considered the true description. When this is done, the false description may, of course, be disregarded, and the maxim merely calls attention to this obvious result."[60]

The Supreme Court came to the same result in *Bucke* and pointed out that it is not material where the *falsa* exists so long as what remains is an accurate and sufficient description.[61]

Justice Beck placed reliance on the maxim in his concurring judgment in *McLeay*[62] to remove words that would have improperly limited the cattle that were subject to a purchase and sale agreement to those feeding in a particular pasture. It appears that any meaningless or clearly incorrect term or description may be severed from a contract so as to remove any conflict in the document.

F. USE OF THE MOST REASONABLE INTERPRETATION

Where a contract is ambiguous the court may, to some extent, take into account the question of whether any particular interpretation would give rise to a "reasonable" result. If there are two possible interpretations available, the court is entitled to consider the consequences of each interpretation. If one interpretation would lead to an absurd result, the court is entitled to conclude that the contract was not intended to produce such a result and, indeed, the court may be under a duty to avoid an interpretation that gives rise to such a result.[63] Likewise, the court will avoid an interpretation that gives rise to a result that would

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56 *Supra* note 10 at 220-21.

57 *Risvold v. Scott*, [1938] 1 W.W.R. 682 at 687 (Alta. S.C.), Ewing J.; *Fetherston v. Bice*, [1917] 1 W.W.R. 224 at 226 (Alta. S.C.), Walsh J.; *Shorb v. Public Trustee* (1953), 8 W.W.R. (N.S.) 657 at 674 (Alta. S.C.), Egbert J., aff'd (1954), 11 W.W.R. (N.S.) 132 (Alta. S.C. (A.D.)) [*Shorb*]; see also *Bilawchuk*, *supra* note 25 at 276.

58 *Supra* note 55 at 454.

59 *Supra* note 10 at 518-20.

60 *Ibid.* at 516.

61 *Supra* note 10 at 411.

62 *Supra* note 34 at 820.

63 *W.H. Hotel*, *supra* note 25 at 440; *Delhi Oil*, *supra* note 8 at 518-19; *Begro*, *supra* note 27 at 27-28; *Suncor*, *supra* note 24 at 223.

be "totally unreasonable" from the practical perspective of the parties at the time of contracting.[64] The law in Alberta on this point appears to be that

> Where words may bear two constructions, the more reasonable one, that which produces a fair result, must certainly be taken as the interpretation which would promote the intention of the parties. Similarly, an interpretation which defeats the intentions for the parties and their objective in entering into the commercial transaction in the first place should be discarded in favour of an interpretation of the policy which promotes a sensible commercial result.[65]

This principle is often applied in cases involving contracts of insurance to ensure that ambiguous provisions in such contracts are not interpreted in a way that would defeat an attempt of the insured to obtain coverage. Insurance policies are normally interpreted in favour of the insured by interpreting the provisions allowing coverage broadly and those provisions that limit coverage strictly or narrowly against the insurer.[66] These rules of interpretation are often used in conjunction with the doctrine *contra proferentum*.

In recent cases the Supreme Court has reviewed these principles. The Supreme Court has said:

> In interpreting an insurance contract the rules of construction relating to contracts are to be applied as follows:
>
> (1) The court must search for an interpretation from the whole of the contract which promotes the true intent of the parties at the time of entry into the contract.
> (2) Where the words are capable of two or more meanings, the meaning that is more reasonable in promoting the intention of the parties will be selected.
> (3) Ambiguities will be construed against the insurer.
> (4) An interpretation which will result in either a windfall to the insurer or an unanticipated recovery to the insured is to be avoided.[67]
>
> ...
>
> In each case, the courts must interpret the provisions of the policy at issue in light of general principles of interpretation of insurance policies, including, but not limited to:
>
> (1) the *contra proferentum* rule;

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64 *Field v. Bachynski* (1976), 1 A.R. 491 at 506 (S.C. (A.D.)), McGillivray C.J.A.

65 *Bathurst, supra* note 2 at 901; *W.R. Scott Equipment Ltd. v. Guardian Insurance Co. of Canada* (1998), 58 Alta. L.R. (3d) 45 at 50 (C.A.); *SCS Western Corp. v. Dominion of Canada General Insurance Co. of Canada* (1998), 218 A.R. 344 (Q.B.), McIntyre J. [*SCS Western*]; *Pro-Man Construction v. Toronto-Dominion Bank* (1997), 215 A.R. 358 at 363-64 (Q.B.), Andrekson J. [*Pro-Man*]; *Galloway, supra* note 3 at 235; *Duxbury v. Training Inc.* (2002), 308 A.R. 265 at para. 15 (Prov. Ct.), LaGrandeur J.

66 *Aetna Insurance v. Canadian Surety* (1994), 19 Alta. L.R. (3d) 317 at 356 (C.A.) [*Aetna*]; *Amos v. ICBC*, [1995] 3 S.C.R. 405 at 414; *Indemnity Insurance Co. of North America v. Excel Cleaning Service*, [1954] S.C.R. 169 at 179-80 [*Excel*]; *SCS Western, ibid.* at paras. 17-18; *ESA Holdings Ltd. v. Royal Insurance Co. of Canada* (1997), 199 A.R. 394 at 397 (Q.B.), Paperny J. [*ESA Holdings*]; *Zotzman, supra* note 12 at 332-33; *Armenco Ltd. v. Continental Insurance* (1988), 84 A.R. 121 at 126 (Q.B.), Crossley J., rev'd on other grounds (1989), 96 A.R. 299 (C.A.) [*Armenco*]; *Bar-Don, supra* note 26 at 250.

67 *Brissette Estate v. Westbury Life Insurance*, [1992] 3 S.C.R. 87 at 92-93 [*Brissette*].

(2) the principle that coverage provisions should be construed broadly and exclusion clauses narrowly; and

(3) the desirability, at least where the policy is ambiguous, of giving effect to the reasonable expectations of the parties.[68]

G. *CONTRA PROFERENTUM*

The doctrine of interpretation known as *verba-fortis accipiuntur contra proferentum* only applies in cases where the language used is ambiguous[69] and all other rules of contractual interpretation have failed.[70] The basic principle is that an ambiguous provision will be construed against the party who drafted the provision.[71]

The doctrine is often used in situations where a party seeks to impose exceptions or limitations on its liability. The rationale of the rule in those cases is that if a party wishes to limit, by some qualification, a risk it would otherwise appear to assume in plain terms, then that party should make it perfectly clear what the qualification is, particularly since the party drafting the agreement has control over the contents of the document.[72] This is true whether or not the contractual stipulation was made in favour of the person against whom the doctrine is sought to be used. An ambiguous clause will be interpreted against the party who drafted it, no matter whom it was intended to benefit.[73]

This is a rule widely applied in respect to contracts of insurance where the exclusionary language drafted by the insurer is ambiguous or unclear,[74] but it also has been relied on in Alberta in respect to commercial contracts.[75] However, the rule generally applies only to complicated contracts and standardized business documents and does not normally extend to informal agreements such as those formed from correspondence, since the same care in

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[68] *Reid Crowther & Partners Ltd. v. Simcoe & Erie General Insurance*, [1993] 1 S.C.R. 252 at 269; see also *Yang v. Canadian Lawyers Insurance Association* (1997), 196 A.R. 276 at 280-81 (C.A.).

[69] *Viswalingham v. Sun Life Assurance Co. of Canada* (1996), 193 A.R. 42 at 43 (C.A.); *Sherritt Gordon Ltd. v. Dresser Canada* (1994), 156 A.R. 257 at 265 (Q.B.), McDonald J., aff'd (1996), A.R. 234 (C.A.); *Hongkong Bank of Canada v. Caproco Prevention Corrosion Ltd.* (1991), 85 Alta. L.R. (2d) 306 at 312 (C.A.) [*Hongkong*]; *Kissinger Petroleums Ltd. v. Keith McLean Oil Properties Ltd.* (1984), 33 Alta. L.R. (2d) 1 at 16 (C.A.), McDermid J.A.; see also *Loyer v. Capital Jeep Eagle Ltd.* (1996), 40 Alta. L.R. (3d) 186 at 187 (C.A.) [*Loyer*]; *Bilawchuk*, *supra* note 25 at 276.

[70] *Alex Duff*, *supra* note 7 at 74; *Cooke*, *supra* note 22 at 672; *Stevenson v. Reliance Petroleum Limited*, [1956] S.C.R. 936 at 953; *Bathurst*, *supra* note 2 at 899-900; *Pro-Man*, *supra* note 65 at 364; *Sinclaire*, *supra* note 28 at 146.

[71] *Loyer*, *supra* note 69 at 187; *Hillis Oil*, *supra* note 2 at 68-69; *Bathurst*, *ibid.*; *Manulife*, *supra* note 2 at 425; *Harris v. Robert Simpson Co.* (1984), 34 Alta. L.R. (2d) 64 at 72-73 (Q.B.), Foisy J. [*Harris*]; *Protection*, *supra* note 4 at 109.

[72] *Excel*, *supra* note 66 at 179-80.

[73] *Ironside v. Smith* (1998), 70 Alta. L.R. (3d) 393 at 411 (C.A.) [*Ironside*]; *Manulife*, *supra* note 2 at 425.

[74] *Fletcher v. Manitoba Public Insurance*, [1990] 3 S.C.R. 191 at 224-25; *Aetna*, *supra* note 66 at 356; *Zurich Life Insurance. Co. of Canada v. Davies*, [1981] 2 S.C.R. 670 at 674; *Wawanesa Mutual Insurance v. Shoemaker* (1994), 155 A.R. 2 at 3 (C.A.); *Bar-Don*, *supra* note 26 at 250; *Armenco*, *supra* note 66 at 126; *Zotzman*, *supra* note 12 at 332-33; *ESA Holdings*, *supra* note 66 at 397; *Protection*, *supra* note 4 at 110.

[75] *Blue Label Beverages (1971) Ltd. v. Centennial Packers Ltd.* (1986), 44 Alta. L.R. (2d) 68 at 79 (Q.B.), Gallant J.; *Sign-o-Lite Signs Ltd. v. Windsor Plywood (Kelowna) Ltd.* (1988), 61 Alta. L.R. (2d) 21 at 24 (Q.B.), MacCallum J.; *Atlas Signs (1995) Ltd. v. Atlas Signs Ltd.*, Action No. 9501-18593, 5 November 1997 (Q.B.), Clark J.

drafting is not expected in such informal documents.[76] The rule also has no application to an exclusion clause relied on by an insurer where the exclusion clause was drafted by the insured, and, in this respect, insurance contracts are similar to any other type of contract.[77]

The concept of *contra proferentum* has been taken a step further in some jurisdictions by classifying certain contracts as being "contract of adhesion," which will be interpreted in a manner that honours the reasonable expectation of the weaker party to the contract.[78] This concept has been discussed in Alberta case law.[79]

In other jurisdictions, the courts have ruled that any unusual or onerous provisions in contracts, particularly "contracts of adhesion," must be brought to the attention of the adherent. If this is not done, the clauses will not be enforceable against the adherent.[80] This approach has not been adopted in Alberta and in fact was drawn in part from the dissenting judgment of Beck J.A. in *Gray-Campbell Ltd. v. Flynn*.[81] The decisions of Hyndman and Clarke JJ.A. are directly contrary and state that if a party signs a contract without reading its contents he is normally bound by its terms.[82] There are also more recent cases that affirm view.[83] The presumption in Alberta is that, subject to cases involving fraud or misrepresentation, a party, by signing the document, becomes bound by its terms even if the document was not read.[84] In the writer's view it is not clear that there are any special rules of interpretation for "contracts of adhesion" in Alberta beyond the general applicability of the doctrine of *contra proferentum*.

IV. USE OF EXTRINSIC EVIDENCE

A. INTRODUCTION

There is perhaps no topic that creates more difficulty in relation to the interpretation of written agreements than the extent to which a court is entitled to rely on evidence outside the "four corners" of the document. The law in this area appears to be a tangled mass of contradictions. The courts have stated that the purpose of contractual interpretation is to

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76 *Harris*, *supra* note 71 at 73; *Watson v. Jamieson* (1910), 3 Alta. L.R. 230 at 232-33 (S.C. (A.D.)), Stuart J.A.

77 *Triple Five Corp. v. Simcoe & Erie Group* (1997), 196 A.R. 29 at 40 (C.A.).

78 See *Brissette*, *supra* note 67.

79 *S.R. Petroleum Sales Ltd. v. Canadian Turbo Ltd.* (1995), 175 A.R. 52 at 57 (Q.B.), Veit J. and *421489 Alberta v. Nesbitt Burns* (2003), 336 A.R. 201 at paras. 65-72 (Q.B.), Moore J.

80 *Tilden Rent-A-Car v. Clendenning Ltd.*, [1978] 18 O.R. (2d) 601 (C.A.); *Trigg v. M.I. Movers Int. Transport Services Ltd.*, [1991] 4 O.R. (3d) 562 (C.A.); *Beer v. Townsgate I Ltd.*, [1997] 36 O.R. (3d) 136 (C.A.); *Zippy Print Enterprises Ltd. v. Pawliuk* (1994), 100 B.C.L.R. (2d) 55 (C.A.); Shannon Kathleen O'Byrne, "Good Faith in Contractual Performance: Recent Developments" (1995) 74 Can. Bar Rev. 70 at 91; Paul M. Perell, "A Riddle Inside an Enigma: The Entire Agreement Clause" (1998) 20 Adv. Q. 287.

81 (1922), 18 Alta. L.R. 547 (S.C. (A.D.)) [*Flynn*].

82 *Ibid.* at 567, 570.

83 *Budget Rent-A-Car of Edmonton v. University of Toronto* (1995), 165 A.R. 236 at 237 (C.A.); *American Express Canada Inc. v. International Warranty*, [1994] A.J. No. 101 at para. 2 (C.A.); *Steeplejack*, *supra* note 13 at 314; *Stetor v. Schamaus* (1989), 96 A.R. 19 at 27 (Q.B.), Murray J.; *Whissell*, *supra* note 16 at 336-38.

84 *W.C. Fast Enterprises Ltd. v. All-Power Sports (1973) Ltd.* (1981), 16 Alta. L.R. (2d) 47 at 61 (C.A.) [*All-Power*]; see also *Union Steamships Ltd. v. Barnes*, [1956] S.C.R. 842 at 856 [*Union Steamships*].

determine the intention of the parties,[85] and yet they have also ruled that direct evidence of the intention of the parties is inadmissible.[86] The courts have ruled that they are always entitled to, and should, review the "commercial context" when interpreting the document,[87] but have also established the Parol Evidence Rule, which states that extrinsic evidence cannot be received to contradict, vary, add to or subtract from, a written agreement.[88]

The courts have held that they are always entitled to review the "genesis" and "background" of the making of the contract but, at the same time, refuse to admit evidence of the negotiations between the parties that led to the contract.[89] In recent cases the courts have indicated that extrinsic evidence need not be resorted to at all where the contract is clear and unambiguous.[90]

Notwithstanding these apparent contradictions, the case law applying in Alberta does reveal some coherent themes that may be employed to produce fairly predictable results in any given case. These themes are examined below.

B. "COMMERCIAL CONTEXT," "SURROUNDING CIRCUMSTANCES" AND "MATRIX OF FACTS" EVIDENCE

The traditional rules relating to the use of extrinsic evidence to establish the "commercial context" of, or the "matrix of facts" surrounding, the execution of a written agreement are of long standing. In 1906 the Supreme Court said: "The intention of the parties must be sought in interpreting any document, and as an aid thereto the surrounding facts and circumstances can and, in doubtful cases when ambiguous words are used, must always be looked at."[91]

Sixteen years later the Supreme Court affirmed the use of such evidence when members of the Court relied on the following statements of law:

> [E]xtrinsic evidence is always admissible not to contradict or vary the contract but to apply it to the facts which the parties had in their minds and were negotiating about.
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> ...
>
> Extraneous evidence is admissible (even in the case of a memorandum required to satisfy the Statutes of Frauds) [of every material fact which will enable the Court to ascertain the nature and qualities of the subject matter of the instrument], or, in other words, to understand the subject-matter of the contract.[92]

Shortly after that, the view was again confirmed by the Supreme Court:

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85 *Kasha, supra* note 1 at 168.

86 *Turbo Resources, supra* note 4 at 30.

87 *Amerada Minerals Corp. of Canada Ltd. v. Mesa Petroleum (N.A.) Co.* (1986), 47 Alta. L.R. (2d) 289 at 296-97 (C.A.) [*Amerada*].

88 *Northwestern Mechanical Installations Ltd. v. Yukon Construction Co. Ltd.* (1982), 20 Alta. L.R. (2d) 156 at 162 (C.A.) [*NW Mechanical*].

89 *Qualico, supra* note 30 at 138-39.

90 *Eli Lilly & Co. v. Novopharm Ltd.*, [1998] 2 S.C.R. 129 at 166-67 [*Eli Lilly*]; *Guaranty Properties Ltd. v. Edmonton (City of)* (2000), 261 A.R. 376 at 383 (C.A.) [*Guaranty Properties*].

91 *Deserres, supra* note 38 at 617.

92 *Canada Law Book, supra* note 38 at 185, 193, citing *Bank of New Zealand v. Simpson*, [1900] A.C. 182 at 187-88 (P.C.).

In order to interpret the correspondence we must look to the state of the facts and circumstances as known to and affecting the parties at the time. As was said by Blackburn J. in *Fowkes v. Manchester and London Life Assurance and Loan Association*,

> the language used by one party is to be construed in the sense in which it would be reasonably understood by the other

And Lord Watson said in *Birrell v. Dryer*:

> I apprehend that it is perfectly legitimate to take into account such extrinsic facts as the parties themselves either had, or must be held to have had, in view, when they entered into the contract.[93]

The Court of Appeal came to a similar result in subsequent cases, following rules established by the House of Lords. The Court of Appeal has approved the following statements:

> The time has long passed when agreements, even those under seal, were isolated from the matrix of facts in which they were set and interpreted purely on internal linguistic considerations. There is no need to appeal here to any modern, anti-literal, tendencies, for Lord Blackburn's well-known judgment in *River Wear Comrs v. Adamson* [(1877) 2 App. Cas. 743] provides ample warrant for a liberal approach. We must, as he said, enquire beyond the language and see what the circumstances were with reference to which the words were used, and the object, appearing from those circumstances, which the person using them had in view.[94]
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> ...
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> No contracts are made in a vacuum: there is always a setting in which they have to be placed. The nature of which is legitimate to have regard to is usually described as "the surrounding circumstances" but this phase is imprecise: it can be illustrated but hardly defined. In a commercial contract it is certainly right that the court should know the commercial purpose of the contract and this in turn presupposes knowledge of the genesis of the transaction, the background, the context, the market in which the parties are operating.[95]
>
> ...
>
> It is apparent that the court, when interpreting a contract in its commercial context, cannot simply ignore the words, phrases and definitions which are used in the agreement. Where there is no conflict between the wording and the commercial purpose, it is then quite acceptable to review the commercial context in which the words are used, in order to ascertain the purpose of the agreement.[96]

These principles have subsequently been applied by the Alberta courts on numerous occasions.[97]

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93 *A.R. Williams*, *supra* note 38 at 705.

94 *Re Ulster Petroleums Ltd. and Pan-Alberta Gas Ltd.* (1975), 53 D.L.R. (3d) 459 at 467-68 (Alta. S.C. (A.D.)) [*Re Ulster*] citing *Prenn v. Simmonds*, [1971] 3 All E.R. 237 at 239-40 (H.L.), Lord Wilberforce [*Prenn*]; see also *Bank of British Columbia v. Hayes* (1980), 26 A.R. 504 at 506 (Q.B.), MacDonald J.

95 *Turbo Resources*, *supra* note 4 at 30, citing *Reardon Smith Line Ltd. v. Hanson-Tangin*, [1976] 1 W.L.R. 989 at 995-96 (H.L.), Lord Wilberforce.

96 *Amerada*, *supra* note 87 at 297, approving the words of the Trial Judge, Moshansky J. at [1985] 4 W.W.R. 607 at 621-22 (Alta. Q.B.).

97 *First City Trust v. Triple Five Corp.* (1989), 65 Alta. L.R. (2d) 193 at 208 (C.A.); *Edmonton Northlands*, *supra* note 30 at 95; *Paddon Hughes Development v. Pancontinental Oil Ltd.* (1998), 223 A.R. 180 at 188-89 (C.A.) [*Paddon Hughes*]; *Hetherington*, *supra* note 3 at 210-11; *Qualico*, *supra* note 30 at 132; *Alpine Resources Ltd. v. Bowtex Resources Ltd.* (1989), 66 Alta. L.R. (2d) 144 at 147-48 (Q.B.), Virtue J. [*Alpine*]; *United Canso*, *supra* note 17 at 84-86; *Keles Production v. Husky Oil Ltd.* (1991), 80 Alta. L.R. (2d) 5 at 22 (Q.B.), McBain J.; *Delta Hotels*, *supra* note 3 at 345; *Paddon-*

Even when these very broad formulations were applied there were limits upon the type of evidence the court would consider when reviewing the commercial context of an agreement and upon the use that may be made of such evidence once it was received.

As discussed below,[98] the type of "commercial context" evidence that is admissible normally does not include statements made by the parties during negotiations, earlier drafts of the contract in question and other parol evidence of the intentions of the parties. Such evidence is generally inadmissible as "commercial context" evidence and may only be referred to, if at all, to resolve ambiguities.

The use to which evidence of "commercial context" or "surrounding circumstances" may be put is also limited. This type of extrinsic evidence may not be used to advocate a particular meaning to particular words. The Court of Appeal has adopted the rule "that all facts are admissible which tend to shew the sense the words bear with reference to the surrounding circumstances of and concerning which the words were used, but that such facts as only tend to shew that the writer intended to use words bearing a particular sense are to be rejected."[99] Further, the Parol Evidence Rule applies to such evidence so that it may not be used to add to, subtract from or in any manner vary or qualify the written agreement.[100]

It may seem that these restrictions greatly limit the types of "commercial context" evidence that may be used and the use to which it may be put. However, it is submitted that these restrictions on the traditional formulation of the "commercial context" rule were not as severe as they appear.

Dealing first with the type of evidence to be used, the parties were entitled to present evidence relating to the "history of the transaction and the commercial setting in which they were used,"[101] as well the "business objective of the transaction,"[102] the "purpose for which the particular clause was inserted"[103] and the "market in which the parties were operating."[104] While earlier draft agreements were generally inadmissible, other more informal documents and discussions predating the agreement have been used to establish the background of the transaction.[105] It appears that the traditional approach was that any such evidence had to be objective rather than subjective in nature. This would exclude statements of intention made

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Hughes Development v. Chiles Estate (1991), 1 Alta. L.R. (3d) 76 at 78 (Q.B.), Montgomery J. [*Chiles Estate*]; *Galloway, supra* note 3 at 234-35; *Kerkhoff, supra* note 6 at 130-31; *Unryn v. Melcor Developments* (1994), 22 Alta. L.R. (3d) 355 at 360-61 (Q.B.), Power J. [*Unryn*]; *Dilcon Construction Ltd. v. ANC Developments Ltd.* (1996), 42 Alta. L.R. (3d) 32 at 70 (Q.B.), McMahon J. [*Dilcon*]; *Protection, supra* note 4 at 137.

98 See *infra* notes 175-83.

99 *NW Mechanical, supra* note 88 at 162; see also *Indian Molybdenum v. The King*, [1951] 3 D.L.R. 497 at 503 (S.C.C.), Estey J. [*Molybdenum*].

100 See *infra* notes 145, 147.

101 *Alpine, supra* note 97 at 147.

102 *United Canso, supra* note 17 at 84-85, 88, 91.

103 *Opron, supra* note 30 at 343; *Kerkhoff, supra* note 6 at 130.

104 *Turbo Resources, supra* note 4 at 30.

105 *Clarke's-Gamble of Canada Ltd. v. Grant Park Plaza Ltd.*, [1967] S.C.R. 614 at 616-17 [*Clarke's-Gamble*]; *Turbo Resources, supra* note 4 at 22-27; *Dilcon, supra* note 97 at 57-63.

by the parties during negotiations, both in draft documents and through evidence of intention given by the parties at trial.[106]

While evidence of the "surrounding circumstances" may not be used to advocate any particular meaning for any particular words, this use of the evidence would only be important if the words used were ambiguous. Traditionally, "commercial context" evidence was not admitted for the purpose of resolving ambiguities. The resolution of ambiguities was a separate ground for the admission of extrinsic evidence.[107] As will be discussed below, it is not entirely clear whether this has been changed by recent cases.

"Commercial context" evidence was normally used to provide the background and setting in which the contract was made and, notwithstanding some authority to the contrary,[108] the traditional view was that evidence of "commercial context" could be referred to whether the contract was ambiguous or not.[109] For example, the Supreme Court ruled in an early case that the surrounding facts and circumstances "may always" be referred to, and in cases of "doubt or ambiguity," such evidence "must" be referred to.[110] Likewise, the Court of Appeal has said that "[a]lthough parol evidence is not admissible to vary a contract in writing, evidence of the surrounding circumstances is always admissible to assist the court in determining the true agreement of the parties."[111]

Under the traditional rule it was said that such evidence may not be used to advocate a particular meaning to particular words, however it was recognized that it could have a significant impact on the way the words are interpreted. In the traditional view, "commercial context" evidence "assists in ascertaining the intentions of the parties from the language they have used,"[112] that it may be reviewed to "ascertain the purpose of the agreement[113] and "to show the purpose for which the various contractual provisions were included."[114] It seems apparent that such purposes are fundamental to the interpretation process.[115] Therefore, the admission of evidence relating to the "commercial context" or "surrounding circumstances" could, in fact, affect the way individual words and phrases in the agreement were interpreted. This was recognized by Virtue J. who noted: "While the court cannot change the words of the contract, it can, if the circumstances require, give those words a broad or loose interpretation (rather than a strict or narrow one) so as to achieve, if possible, the commercial aim and purpose of the parties."[116] The result was that, while this type of extrinsic evidence was not to be used to advocate any particular meaning to individual words or phrases, such

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106 *Qualico*, *supra* note 30 at 138-39; *Hetherington*, *supra* note 3 at 210; *United Canso*, *supra* note 17 at 90-91.

107 See *infra* notes 160-68.

108 *Whissell*, *supra* note 16 at 325-26.

109 *Hetherington*, *supra* note 3 at 210; *Alpine*, *supra* note 97 at 147; *United Canso*, *supra* note 17 at 84; *Kerkhoff*, *supra* note 6 at 130-31; *Lakewood 1986 Development Limited Partnership v. Fletcher Challenge Petroleum* (1994), 163 A.R. 96 at 120 (Q.B.), Rawlins J. [*Lakewood*].

110 *Deserres*, *supra* note 38 at 617; see also *Nathu v. Imbrook Properties Ltd.* (1990), 75 Alta. L.R. (2d) 126 at 133 (Q.B.), Brennan J., aff'd (1992), 2 Alta. L.R. (3d) 48 (C.A.).

111 *Thiel v. Perepelitza* (1982), 19 Alta. L.R. (2d) 293 at 295 (C.A.) [*Thiel*].

112 *Turbo Resources*, *supra* note 4 at 30; *Hetherington*, *supra* note 3 at 211; *Alpine*, *supra* note 97 at 147.

113 *Amerada*, *supra* note 87 at 297.

114 *Kerkhoff*, *supra* note 6 at 130; *Opron*, *supra* note 30 at 343.

115 See *supra* notes 1-5.

116 *Alpine*, *supra* note 97 at 147.

evidence could be submitted by a party to support a particular interpretative approach to the contract, be that "broad" or "narrow." Likewise, the effect of a breach may be determined by such evidence. For example, in *Turbo Resources*,[117] the issue of whether a particular term was a warranty whose breach would only give use to an action for damages, or a condition the breach of which could bring the contract to an end, was resolved using "commercial context" evidence.

However, all of that said, the rule remained that clear and unambiguous words in a particular clause could not be modified by context evidence, whether that evidence was contained in other clauses in the agreement[118] or found outside of the agreement. These rules have been summarized by the proposition that "clear and unambiguous words prevail over any intention, but if the words used are not clear and unambiguous, the intention will prevail."[119] This passage may initially seem confusing in that it appears to contemplate a conflict between the words used in a contract and the contractual intention. In fact the words used indicate such intention. As the Court of Appeal has said, "That intention must be found, in the first instance, in the operative words of the document, read as a whole, giving meaning to every provision if that is possible.... However, if the words of a particular clause are clear and unambiguous, they cannot be modified by reference to the other clauses in the agreement."[120] Therefore clear and unambiguous words used in a particular clause would indicate the specific intention in relation to their subject matter and would have priority over any *general* intention to be gathered from the document as a whole or the surrounding circumstances. If the words used in the clause were clear and unambiguous those words would be applied according to their ordinary meaning. If the words in the clause were not clear and unambiguous then the general intention could be relied upon to determine their meaning. Thus evidence of "surrounding circumstances" or "commercial context" was of little or no practical value when the relevant clauses of the contract were drawn in clear, precise and unambiguous language. The tension between the concept that "commercial context" evidence was always admissible to assist the court in interpreting contracts and the fact that it is of little or no practical value in the case of clear and unambiguous contracts appears to have been a source of considerable confusion and controversy.

The law relating to "commercial context" evidence may be changing in recognition of this reality. Both the Supreme Court[121] and the Court of Appeal[122] have recently stated that it is "unnecessary" to consider extrinsic evidence at all when the contract under consideration is clear and unambiguous. These rulings may have the effect of greatly restricting the use of "commercial context" evidence where the agreement under consideration is clear on its face. It is not yet clear whether these cases will displace the large body of authority which states

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117 *Supra* note 4.

118 *Kasha, supra* note 1 at 168.

119 *McDonald's Restaurants of Canada Ltd. v. West Edmonton Mall Ltd.* (1994), 22 Alta. L.R. (3d) 402 at 413 (Q.B.), Mason J., citing Gerald Dworkin, *Odgers' Construction of Deeds and Statutes* 5th ed. (London: Sweet & Maxwell, 1967) at 31.

120 *Kasha, supra* note 1 at 168, citing partly Sir William R. Anson, *Law of Contracts*, 2d ed. (Chicago: Callaghan & Co., 1877) at 149; see also *Protection, supra* note 4 at 138-39.

121 *Eli Lilly, supra* note 90 at 166-67.

122 *Guaranty Properties, supra* note 90 at 383; see also *Bilawchuk, supra* note 25 at 273; *Louie's Submarine, supra* note 16 at para. 32.

that "commercial context" evidence is "always admissible."[123] What seems clear is that these recent cases provide a trial court with good grounds for refusing to consider such evidence. While it is probably not a reversible error for a trial court to review such evidence, it may be a reversible error for the trial court to rely on "commercial context" evidence to interpret a clear and unambiguous contract.[124] If there is a finding that the contract is clear and unambiguous on its face, recent cases suggest that a trial court is justified in refusing to admit this evidence.[125] While it is true that in *Guaranty Properties* the Court of Appeal said that parol evidence is admissible to establish the factual matrix, it went on to say that parol evidence should not be used in the case of a clear and unambiguous contract and in fact ruled the evidence inadmissible on that ground.[126]

In *Eli Lilly*, the Supreme Court ruled that the trial judge erred in admitting such evidence, although it did so in part because the evidence contained statements of the subjective intentions of the parties.[127] As such, a trial court is entitled to be skeptical when dealing with an argument that such evidence is always admissible.[128] Under the earlier rulings a trial court would be at risk of being in error if it excluded such evidence. It is clear that a refusal to admit relevant and otherwise admissible evidence can amount to a reversible error.[129] However, the Court of Appeal has also held that a trial court has the discretion in a civil case to exclude evidence and factual assertions when they do not have sufficient probative force to justify the expenditure of the time necessary to prove, test and weigh them.[130] This latter proposition would seem to apply to evidence that is "unnecessary."

While the facts in any particular case may vary, it is not at all clear why a trial court would be required to spend much, if any, time dealing with "commercial context" evidence in circumstances where that court has already found that the contract is clear and unambiguous.

C. DIRECT EVIDENCE OF THE INTENTION OF THE PARTIES

The rule in this area is long standing and has been consistently applied. In 1906 the Supreme Court ruled that the surrounding facts and circumstances may be looked at to interpret a contract but added: "I must not be understood as including in that, evidence of actual intention or agreement."[131]

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123 *Canada Law Book*, *supra* note 38; *A.R. Williams*, *supra* note 38; *Re Ulster*, *supra* note 94; *Thiel*, *supra* note 111; *Turbo Resources*, *supra* note 4; *Amerada*, *supra* note 87.

124 *Eli Lilly*, *supra* note 90 at 167-68.

125 *Eli Lilly*, *ibid.*; *Guaranty Properties*, *supra* note 90; *Bilawchuk*, *supra* note 25; *Louie's Submarine*, *supra* note 16.

126 *Guaranty Properties*, *ibid.*

127 *Supra* note 90 at 167-68.

128 See the process employed in *Mount Calvary Evangelical Lutheran Church of Calgary v. Abraham*, (2000), 78 Alta. L.R. (3d) 120 at para. 63 (Q.B.).

129 *Trusz v. Witzke* (1990), 111 A.R. 349 at 351-52 (C.A.).

130 *Babcock v. C.P.R. Co. Ltd.* (1916), 9 Alta. L.R. 270 at 283 (S.C. (A.D.)); see also John Sopinka, Sidney N. Lederman & Alan W. Bryant, *The Law of Evidence in Canada*, 2d ed.(Toronto: Butterworths, 1999) at paras. 2.43, 2.50.

131 *Deserres*, *supra* note 38 at 617.

In a leading decision, *Turbo Resources Ltd.*, the Court of Appeal said, "Consideration of the commercial setting in which a contract is made is not, of course, to be confused with parol evidence of the intention of the parties. That is not admissible."[132] This statement of principle has been widely relied on and quoted in subsequent cases.[133] The Court of Appeal's statement is consistent with the position taken in a number of House of Lords' decisions, which have also been relied on by the Alberta courts.[134]

It appears that the primary rationale for the rule is relevance. Determination of the intention of the parties is the primary objective of the court in interpreting the contract.[135] The interpretation of a contract drafted in ordinary English is a question of law and not a fit subject for evidence.[136] That being so, the actual subjective understandings or intentions of the parties is irrelevant. As the Court of Appeal has stated: "What the parties respectively understood is not relevant — it is what they said which binds them."[137]

Another rationale offered for the rule is that it creates certainty. As the Supreme Court stated in *V.K. Mason Const. v. Bank of Nova Scotia*: "much of the value of commercial contracts lies in their ability to produce certainty. Parties are enabled to regulate their relationship by means of words rather than by means of their understanding of what each other's actions are intended to imply. I think this is one reason why the common law imposes an objective rather than a subjective test for the creation of an agreement."[138]

Finally, such subjective evidence is, by its very nature, difficult to assess and not conclusive.[139] The admission of such evidence would almost never resolve the questions before the court. The fact that the court is being called upon to interpret the agreement means that the parties do not agree on how it is to be interpreted. It is very unlikely that either litigant would testify that his intention was the same as the opposing party. If that were so,

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132 *Supra* note 4 at 30.

133 *Amerada*, *supra* note 87 at 296; *Qualico*, *supra* note 30 at 139; *Alpine*, *supra* note 97 at 147; *United Canso*, *supra* note 17 at 84; *Keles*, *supra* note 97 at 24; *Delta Hotels*, *supra* note 3 at 346; *Kerkhoff*, *supra* note 6 at 130; *Unryn*, *supra* note 97 at 361; *PTI Group v. BOT Québec Ltée* (1995), 166 A.R. 104 at 118, para. 41(Q.B.), Fraser J.; see also *Eli Lilly*, *supra* note 90 at 166.

134 See discussion of English cases in *Philip F. Levine Marketing Ltd. v. 3 SM Tours Ltd.*, [1983] 4 W.W.R. 149 at 154 (Alta. Q.B.), Power J.; *Qualico*, *ibid.* at 138.

135 *Kasha*, *supra* note 1 at 168. See also *supra* notes 1-5.

136 *Morguard Trust*, *supra* note 16 at 244; *Volker*, *supra* note 17 at 170; see also *Avco*, *supra* note 17 at 8; *United Canso*, *supra* note 17 at 87-88.

137 *Chaba*, *supra* note 19 at 637, applied in *Marthaller v. Landsdowne Equity Venture* (1997), 52 Alta. L.R. (3d) 329 at 333 (C.A.); also applied by Master Funduk in *Whissel*, *supra* note 16 at 325; *Marwood Cedar Homes Ltd. v. Hanson Food Processing Ltd.* (1988), 86 A.R. 207 at para. 29 (M.C.) [*Marwood Cedar*]; *Steeplejack*, *supra* note 13 at 314; *Bate*, *supra* note 16 at 165; *Paskaluk v. Plawiuk* (1992), 128 A.R. 284 at paras. 27-35 (M.C.); *Chrysler Credit Canada Ltd. v. Adorable Pacific Rim Boarding Kennels for Dogs and Cats Ltd.* (1992), 130 A.R. 273 at para. 81(M.C.) [*Chrysler Credit*]; *Cedar Village Building Materials Ltd. v. Janary Construction Inc.* (1994), 153 A.R. 310 at para. 23 (M.C.) [*Marwood*]; *Underwriters*, *supra* note 19 at 74; *Louie's Submarine*, *supra* note 16 at para. 30; *Bohnet*, *supra* note 16 at 58; see also *Canada Deposit*, *supra* note 30 at 374; *All-Power*, *supra* note 84 at 51; and *Royal Bank v. Lane* (1991), 81 Alta. L.R. (2d) 289 at para. 8 (C.A.).

138 [1985] 1 S.C.R. 271 at 282-83, followed by Master Funduk in *Chrysler Credit*, *ibid.* at 292; *Underwriters*, *ibid.* at 74.

139 *NW Mechanical*, *supra* note 88 at 162; *Whissel*, *supra* note 16 at 324.

the only issues before the court would relate to the application of the contract rather than its interpretation.

The rule excluding direct evidence of the intention of the parties is not identical to the Parol Evidence Rule. As will be seen below, the Parol Evidence Rule excludes evidence that would have the effect of adding to, subtracting from or varying the written agreement. The rule excluding direct evidence of intention renders such evidence inadmissible, regardless of its effect.

D. PAROL EVIDENCE RULE

The Parol Evidence Rule is the best known and arguably the most sweeping restriction on the use of extrinsic evidence. The Court of Appeal has accepted the following 19th century statement of the English common law as continuing to reflect the law in Alberta:

> By the general rules of the common law, if there be a contract which has been reduced into writing, verbal evidence is not allowed to be given of what passed between the two parties, either before the written instrument was made, or during the time that it was in a state of preparation, so as to add to or subtract from, or in any manner to vary or qualify the written contract.[140]

The Parol Evidence Rule has been accepted in a long line of cases in both the Court of Appeal[141] and the Supreme Court,[142] and its existence as an operative rule in Alberta seems beyond doubt. Indeed, the rule is sufficiently well-established that it has been relied on in Alberta as a basis for summary judgments.[143]

The more interesting issues arise out of the so-called "exceptions" to the Parol Evidence Rule, which are often just fact situations beyond the scope of the rule or situations where the

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140 *NW Mechanical, ibid.* at 162 quoting *Goss v. Lord Nugent* (1833), 110 E.R. 713 (K.B.). See also *Dassen Gold Resources Ltd. v. Royal Bank* (1994), 23 Alta. L.R. (3d) 261 at 344 (Q.B.), O'Leary J., aff'd (1997), 52 Alta. L.R. (3d) 193 (C.A.); *King v. Major Oil Investments Ltd.*, [1943] 2 W.W.R. 541 at 543 (Alta. S.C. (T.D.)), W.A. Macdonald J., aff'd [1944] 3 W.W.R. 233 (Alta. S.C. (A.D.)); *Wyatt, supra* note 24 at 186.

141 *Eaton v. Crook* (1910), 3 Alta. L.R. 1 at 7 (S.C. (A.D.)) [*Eaton*]; *Bible v. Croasdale* (1915), 9 Alta. L.R. 133 at 136 (S.C. (A.D.)); *Kaster v. Cowan*, [1925] 1 W.W.R. 186 at 187-88 (Alta. S.C. (A.D.)); *Whitney v. MacLean* (1931), 26 Alta. L.R. 209 at 222, 236-237 (S.C. (A.D.)), Harvey C.J.A., McGillivray J.A.; *Chaba, supra* note 19 at 634-35; *Catre Industries, supra* note 11 at 328-3; *Doolaege v. Solid Resources Ltd.* (1992), 127 A.R. 1 at 2 (C.A.) [*Doolaege*].

142 *Case Threshing Machine v. Mitten* (1919), 59 S.C.R. 118 at 119-20, Duff and Anglin JJ. [*Case Threshing Machine*]; *Forman v. Union Trust Company*, [1927] S.C.R. 1 at 7 [*Forman*]; *Hawrish v. Bank of Montreal*, [1969] S.C.R. 515 at 518-21 [*Hawrish*]; *Bauer v. Bank of Montreal*, [1980] 2 S.C.R. 100 at 112-13 [*Bauer*]; *Carman Construction Ltd. v. Canadian Pacific Railway*, [1982] 1 S.C.R. 958 at 969 [*Carman Construction*].

143 *Doolaege, supra* note 141 at 2; see also *Westmount Shopping Centre v. Fraser Valley Work Clothing Ltd.* (1993), 13 Alta. L.R. (3d) 274 at 277 (M.C.), Master Quinn [*Westmount*]; and the decisions of Master Funduk in *Whissel, supra* note 16; *Re/Max Real Estate (Edmonton) Ltd. v. Edmonton Wholesale Auctions* (1986), 46 Alta. L.R. (2d) 205 at 218-20 (M.C.) [*Re/Max Real Estate*]; *Marwood Cedar, supra* note 137 at 211-15; *Equity Capital Corp. v. Mouwen* (1992), 136 A.R. 53 at 58 (M.C.) [*Mouwen*]; *Toronto Dominion Leasing Ltd. v. Szantech Machine Tools Inc.*, [1992] A.J. No. 1057 (M.C.) (QL) [*Szantech*]; *Steeplejack, supra* note 13 at 313-14, 318; *Bate, supra* note 16 at 165; *Underwriters, supra* note 19 at 73-74.

underlying rationale for the rule do not apply.[144] To understand the "exceptions" to the rule, it is necessary to first examine the scope of, and rationale for, the rule.

There are two primary elements that limit the scope of the rule. These can be identified in the following statement by the Supreme Court: "it has been established as a rule of law that extrinsic evidence is not, in general, admissible to contradict, vary or explain written instruments."[145]

First, the evidence must be "extrinsic" or outside the "four corners" of the contract. In this sense, the rule is similar to the rule against the admission of evidence of the subjective intention of the parties.[146] Second, the evidence in question must be offered to "contradict, vary or explain" the document. Words and phrases such as "add to, or subtract from ... or qualify" the contract are also used to describe this parameter of the rule.[147] Therefore the purpose for which the evidence is to be used is fundamental to whether the rule applies in any particular case. A primary rationale behind the prohibition of extrinsic evidence that may "contradict, vary or explain" written instruments has been described as follows:

> when parties have deliberately put their engagements in writing in such language as imports a legal obligation it is only reasonable to presume that they have introduced into it every material term and circumstance;[148]
>
> ...
>
> The general presumption is that the parties have expressed every material term which they intended should govern their agreement, whether oral or in writing.[149]
>
> ...
>
> The rule I think is clear that where parties have deliberately put their agreement into formal terms so that the court can infer an intention, that it should contain the whole agreement then parole [sic] testimony to contradict directly an express term of the written agreement is not admissible unless some question of a mistake is raised.[150]
>
> ...
>
> It is presumed that the parties intended what they have said and therefore their intention is found in the document itself.[151]

There is also a related legal presumption that the written agreement was intended to comprise the final arrangement arrived at by the parties[152] and that all prior discussions are superseded

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144 *Eaton*, *supra* note 141 at 7.

145 *Forman*, *supra* note 142 at 7.

146 See *supra* notes 131-39.

147 *NW Mechanical*, *supra* note 88 at 162, quoting *Goss v. Lord Nugent* (1833), 110 E.R. 713 (K.B.).

148 *NW Mechanical*, *ibid.*, quoting *Ellis v. Abell* (1882), 10 O.A.R. 226 (Ont. C.A.); see also *Evans v. Evans* (1911), 19 W.L.R. 237 at 241 (Alta. S.C. (A.D.)), aff'd (1912), 50 S.C.R. 262 [*Evans*].

149 *Catre Industries*, *supra* note 11 at 328, quoting *Luxor v. Cooper*, [1941] 1 All E.R. 33 at 52 (H.L.).

150 *Chaba*, *supra* note 19 at 635, quoting *Bible v. Croasdale*, *supra* note 141 at 136.

151 *Hetherington*, *supra* note 3 at 209; see also *Canada Deposit*, *supra* note 30 at 511.

152 *Knight Sugar v. Webster*, [1930] S.C.R. 518 at 523, rev'g [1929] 2 W.W.R. 505 (Alta. S.C. (A.D.)) [*Knight Sugar*].

by[153] or merged into[154] the written agreement. This same presumption would also apply to a signed preliminary agreement that later led to a more detailed, formal agreement.[155]

These presumptions are supplemented by a legal presumption that, by signing an agreement, a party intended that they would be bound by its terms, even if they are different than pre-contractual discussions. This presumption exists even if one party did not read the agreement before it was signed.[156]

With all of these presumptions operating, it may seem that virtually every form of extrinsic evidence offered to assist in the interpretation of a contract could have the effect of "varying, contradicting, explaining, adding to or subtracting from" the contract, since the written document is presumed to be absolutely final and complete. In fact, there are situations in which these presumptions are not valid. What follows is a discussion of situations in which these presumptions do not operate; that is, the "exceptions" to the Parol Evidence Rule.

E. EXCEPTIONS TO PAROL EVIDENCE RULE

1. INTRODUCTION

The following discussion relating to exceptions to the Parol Evidence Rule has been relied on in the Alberta case law:

> So the rule does not extend to cases where the document may not embody all the terms of the agreement. And even in cases where the document seems to embody all the terms of the agreement, there is a myriad of exceptions to the rule. I will set out some of them. Evidence of an oral statement is relevant and may be admitted, even where its effect may be to add to, subtract from, vary or contradict the document:
>
> (a) to show that the contract was invalid because of fraud, misrepresentation, mistake, incapacity, lack of consideration, or lack of contracting intention;
>
> (b) to dispel ambiguities, to establish a term implied by custom, or to demonstrate the factual matrix of the agreement;
>
> (c) in support of a claim for rectification;
>
> (d) to establish a condition precedent to the agreement;
>
> (e) to establish a collateral agreement;
>
> (f) in support of an allegation that the document itself was not intended by the parties to constitute the whole agreement;

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153 *Molybdenum, supra* note 99 at 502-503; see also *United Grain Growers Ltd. v. Genesis* (2002), 324 A.R. 229 at 234-36 (Q.B.), Verville J.

154 *The Provident Savings Life Assurance Society of New York v. Mowat* (1902), 32 S.C.R. 147 at 155 [*Mowat*]; *Color Your World v. Robert F. Avery Holdings Ltd.* (1988), 88 A.R. 163 at 164 (Q.B.), Matheson J. [*Color Your World*].

155 *Home Oil Ltd. v. Page Petroleum Ltd.*, [1976] 4 W.W.R. 598 at 604 (Alta. S.C. (T.D.)), Laycraft J. [*Home Oil*]; *Resman Holdings Ltd. v. Huntex Limited* (1983), 28 Alta. L.R. (2d) 396 at 397 (Q.B.), Power J.; *Monashee Petroleums Ltd. v. PanCana Resources Ltd.* (1986), 70 A.R. 277 at 290-91 (Q.B.), Egbert J.; *B.P. Resources Canada Ltd. v. General American Oils Ltd.* (1989), 66 Alta. L.R. (2d) 82 at 95 (Q.B.), Dixon J.

156 *Flynn, supra* note 81 at 570; see also *All-Power, supra* note 84 at 51; the presumption may apply to unsigned documents if they have been acted on, *Union Steamships, supra* note 84 at 856.

(g) in support of a claim for an equitable remedy, such as specific performance or rescission, on any ground that supports such a claim in equity, including misrepresentation of any kind, innocent, negligent or fraudulent; and

(h) in support of a claim in tort that the oral statement was in breach of duty of care.[157]

The exceptions referred to in paragraphs (a), (g) and (h) of the above quote deal with topics not directly related to the interpretation of written contracts and will not be dealt with here. The "exception" relating to the "factual matrix" referred to in paragraph (b) was discussed above.[158] The balance of the exceptions will be discussed below.

2. AMBIGUOUS AGREEMENTS

As discussed above,[159] a primary rationale for the exclusion of parol evidence that may vary a written agreement is that the parties are presumed to have expressed their entire and final intention in the written agreement. That rationale has little force if the document does not express the intentions of the parties in any clear fashion. It does not make sense to presume that the parties intended to be ambiguous. It would seem unreasonable for the court to take the position that the parties meant what they said, in circumstances where the court is not clear what the parties have in fact said. The courts, recognizing the failure of the rationale for the Parol Evidence Rule in such cases, have held that an "exception" to the rule exists in the case of ambiguous agreements and therefore extrinsic evidence is admissible to resolve any such ambiguity.[160] Indeed, it has been said that the court has a duty to review extrinsic evidence where the contract in question is ambiguous.[161]

The question then arises as to when a contract may be described as being "ambiguous." In Alberta, mere "difficulty of interpretation" is not viewed as being synonymous with "ambiguity."[162] This is not the view taken in some jurisdictions, where it has been held that

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157 *Guaranty Properties*, *supra* note 90 at 383; *Delta Hotels*, *supra* note 3 at 347; *Milano's Dining Room & Lounge (1989) Ltd. v. CTDC #1 Alberta Ltd.* (1994), 19 Alta. L.R. (3d) 171 at 173 (Q.B.), McBain J. [*Milano's*]; *AGP, Inc. v. Chinook Grain* (1999), 75 Alta. L.R. (3d) 273 at 288 (Q.B.), McBain J., all referring to *Gallen v. Allstate Grain* (1984), 53 B.C.L.R. 38 at 49 (C.A.), leave to S.C.C. refused (1984), 56 N.R. 233 [*Gallen*].

158 See *supra* notes 91-130.

159 See *supra* notes 148-55.

160 *Cooke*, *supra* note 22 at 668; *Hoefle v. Bondgard & Co.*, [1945] S.C.R. 360 at 377, 383-84, Kellock and Estey JJ. [*Hoefle*]; *Mechanical Pin Resetters Co. Ltd. v. Canadian Acme Screw & Gear Ltd.*, [1971] S.C.R. 628 at 634 [*Acme*]; *Soper v. Canadian International Paper*, [1931] S.C.R. 708 at 719-20; *Qualico*, *supra* note 30 at 140; *Wimpey (George) Canada Ltd. v. Groveridge Imperial Properties Ltd.* (1985), 40 Alta. L.R. (3d) 339 at 345 (Q.B.), Purvis J. [*Wimpey*]; *Acanthus Resources Ltd. v. Cunningham* (1998), 57 Alta. L.R. (3d) 9 at 15 (Q.B.), Hart J. [*Acanthus*]; *Siler*, *supra* note 4 at 336.

161 *Adolph Lumber v. Meadow Creek Lumber* (1917), 58 S.C.R. 306 at 307, Davies C.J.C. [*Adolph Lumber*]; *Deserres*, *supra* note 38 at 617; *Nathu v. Imbrook Properties Ltd.* (1990), 75 Alta. L.R. (2d) 126 at 133 (Q.B.), Brennan J., aff'd (1992), 2 Alta. L.R. (3d) 48 (C.A.) [*Nathu*].

162 *Calvan Consolidated Oil & Gas v. Manning* (1958), 25 W.W.R. (N.S.) 641 at 658 (Alta. SC. (A.D.)), aff'd [1959] S.C.R. 253; *St. Lawrence Petroleum v. Bailey Selburn Oil & Gas Ltd.* (1963), 41 W.W.R. (N.S.) 210 at 214 (Alta. S.C. (A.D.)), aff'd [1963] S.C.R. 482 at 488; *NW Mechanical*, *supra* note 88 at 164-65; *L&W Moving*, *supra* note 4 at 96; *Paddon Hughes*, *supra* note 97 at 187-88; *Home Oil*, *supra* note 155 at 604-605; *Protection*, *supra* note 4 at 137-38; *Acanthus*, *supra* note 160 at 15-16.

"ambiguity" means no more than "difficulty, doubt or uncertainty."[163] Further, some statements of the Alberta position seem somewhat equivocal.[164]

However, it is submitted that the Alberta case law is sound on this point. If a written agreement reveals a clear contractual intention, mere complexity or unusual terminology is not sufficient justification for the court to use extrinsic evidence to explain the meaning of the words and phrases in the agreement. The subject matter of any given agreement may be difficult to articulate. Complex documents with complex language may therefore be required in order for the document to be clear and accurate. It is submitted that even with the most complex of contracts, the court is entitled to summarily determine the contractual obligations of the parties entirely from the words in the contract so long as the language used is capable of only one resolution.[165]

Alberta case law indicates that a contract will be considered "ambiguous" when the words used give rise to more than one plausible and sensible interpretation. For example, in *Esso Resources Canada Ltd. v. Graham & Hansen Enterprises Ltd.*, the Court of Appeal was called upon to determine whether the word "claims" in a contract meant merely the assertion of a right or rather the actual existence of that right. The Court said, "I see nothing in the sentence that tells me which use is intended. It makes sense either way, and that is ambiguity."[166]

In *Andrews v. General Accident Assurance Co. of Canada*, the parties were disputing the interpretation of an exclusion clause in an insurance contract. In discussing the insurer's interpretation the Court of Appeal stated that "This is not an implausible interpretation. But neither is the interpretation offered by the insured. As it stands, and without external aids to interpretation, the term is ambiguous."[167]

It is the existence of more than one reasonable interpretation that justifies resorting to extrinsic evidence. The use of nomenclature such as "uncertainty," "doubt," "difficulty in interpretation" or "ambiguity" may only serve to obscure this fact. In *Qualico Developments Ltd. v. Calgary (City of)*, Virtue J. made reference to the following passage:

> [I]f, after considering the agreement itself, including the particular words used in their immediate context and in the context of the agreement as a whole, there remain two reasonable alternative interpretations, then certain additional evidence may be both admitted and taken to have legal relevance if that additional evidence will help to determine which of the two reasonable alternative interpretations is the correct one. It certainly makes no difference to the law in this respect if the continuing existence of two reasonable alternative interpretations

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163 *Silver Standard Mines Ltd. (N.P.L.) v. Granby Mining Co. Ltd.* (1971), 19 D.L.R. (3d) 578 (B.C.C.A.); *Leitch Gold Mines Ltd. v. Texas Gulf Sulphur*, [1969] 1 O.R. 469 (H.C.).

164 *Cooke*, *supra* note 22 at 668: "Difficulties of interpretation are not always treated as ambiguities..."; *Galloway*, *supra* note 3 at 234: "I am also aware of the notion that there can be a difference between ambiguity in a contract and difficulty in interpretation."

165 *Suncor v. Canada Wire & Cable Ltd.* (1993), 7 Alta. L.R. (3d) 182 at 186 (Q.B.), Forsyth J.

166 (1991), 79 Alta. L.R. (2d) 394 at 398 (C.A.); see also *Ironside*, *supra* note 73 at 411.

167 (1995), 27 Alta. L.R. (3d) 267 at 270 (C.A.); see also *McLeay*, *supra* note 34 at 81 and *Loyer*, *supra* note 69 at 187.

> after an examination of the agreement as a whole is described as doubt or as ambiguity or as uncertainty or as difficulty of construction.[168]

It is implicit from the passages quoted from these cases that, for there to be an "ambiguity," the competing interpretations must "make sense" and be "reasonable" and "plausible." The court is entitled to, and perhaps has a duty to, reject an interpretation that is obviously absurd.[169]

If the court determines that the contract can reasonably bear more than one interpretation, the court has three basic sources of extrinsic evidence to resolve the ambiguity. In *Alpine*, Virtue J. relied on the following passage: "The types of extrinsic evidence that will be admitted, if they meet the test of relevance and are not excluded by other evidentiary tests, include evidence of the facts leading up to the making of the agreement, evidence of the circumstances as they exist at the time the agreement is made, and in Canada, evidence of the subsequent conduct of the parties to the agreement."[170] Justice Virtue admitted all three types of evidence in *Qualico*.[171] There are, however, distinct considerations that must be taken into account by the court when considering the admission of each of these three types of evidence. These are reviewed below.

The first type of evidence to be considered are the facts leading up to the making of the agreement. As was noted, the law of Alberta is such that the Alberta courts have traditionally had the right to know the "history," "background" and "genesis" of the transaction.[172] Accordingly, the admission of pre-contractual facts, discussions and correspondence is common.[173] Traditionally this evidence was admissible even where there was no ambiguity in the wording of the agreement. Resort to such evidence is almost mandated where the evidence is being used to resolve an ambiguity.[174]

An area of controversy regarding historical evidence relates to the use of prior drafts and the contents of negotiations. Earlier drafts of the contract in question and negotiations leading up to the execution of the contract would initially appear to form part of the "background" or "genesis" of the transaction and would therefore be admissible as part of the "commercial context" of the agreement. The Alberta courts have, however, drawn a clear distinction between evidence of negotiations and earlier drafts on the one hand and "commercial context" evidence on the other. The admissibility of these two types of evidence is dealt with

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168 *Qualico, supra* note 30 at 372-73 citing *Re Canadian National Railways and Canadian Pacific Ltd.*, [1979] 1 W.W.R. 358 at 372 (B.C.C.A.), Lambert J.A., aff'd [1979] 2 S.C.R. 668 [*CNR*]. On the definition of "ambiguity" see also: G.H.L. Fridman, *The Law of Contract in Canada*, 4th ed. (Scarborough: Carswell, 1999) at 482, n. 49 relying on *Imperial Oil Ltd. v. Nova Scotia Light and Power*, [1977] 2 S.C.R. 817; *Atlantic Shopping Centres v. Hutton* (1980), 25 Nfld & P.E.I.R. 320 at 336 (Nfld. S.C. (T.D.)); see also *Westholme Lumber v. St. James Ltd.* (1915), 21 D.L.R. 549 at 558 (B.C.C.A.); *St-Laurent v. Sun Life Assurance* (1989), 37 C.C.L.I. 85 at 91-92 (N.B.Q.B.).

169 *W.H. Hotel, supra* note 25 at 440; *Delhi Oil, supra* note 8 at 518-19; *Begro, supra* note 27 at 27-28; *Suncor, supra* note 24 at 223.

170 *Alpine, supra* note 97 at 148, citing *CNR, supra* note 168 at 372-73.

171 *Qualico, supra* note 30 at 132; see also *Hetherington, supra* note 3 at 212.

172 See *supra* notes 91-130.

173 See *supra* notes 186-88.

174 See *Deserres, supra* note 38 at 617.

quite differently. Justice Virtue noted that English case law treated "negotiation" evidence similar to direct evidence of intention. In *Qualico*, Virtue J. relied on the following passage: "In my opinion, then, evidence of negotiations, or the parties intentions ... ought not to be received, and evidence should be restricted to evidence of the factual background known to the parties at or before the date of the contract, including evidence of the 'genesis' or objectively the 'aim' of the transaction."[175]

The rationale for excluding pre-contractual discussions or negotiations as "commercial context" evidence appears similar to that excluding direct evidence of intention. Firstly, such evidence is not relevant. In *All-Power*, a conditional seller, by virtue of the sales contract, retained title to certain boats until they were paid for. An issue arose as to whether that reservation of title actually formed part of the contract. The Court of Appeal held that the fact that the parties had never discussed or negotiated this matter was irrelevant and that the buyer was bound by the contract he had signed even if he had not read it.[176]

There have been subsequent cases holding that negotiations leading up to the formation of a contract are inadmissible on the grounds that such evidence is irrelevant.[177] It should be noted that in these cases the court found the contract in question to be clear and unambiguous. On that basis such evidence would likely be of no assistance to the court.

The Court of Appeal has also given support to the rule excluding evidence of prior negotiations by reference to the Parol Evidence Rule. The Court of Appeal noted that such evidence is inadmissible where it tends to "vary, add to or subtract from" a clear agreement. The Court held that the admissions of evidence of "what passed between the parties, either before the written instrument was made, or during the time it was in a state of preparation" could substitute a new contract for the one really agreed upon.[178] Such reasoning may also apply to draft agreements.

The creation of draft agreements may, of course, be part of the negotiation process. The "final" contract will sometimes be a draft agreement with the final amendments made on the face of the document. Therefore, if the court looks at the words that were removed, the court is in fact admitting an earlier draft. The issue of whether this is permissible arose in *Knight Sugar Co., Ltd. v. Webster*, a case in which the decision of the Court of Appeal[179] was reversed by the Supreme Court.[180] In that case a line was drawn through certain words and other words were added. The issue was whether the final version of the document could be interpreted by reference to the deleted words. The Court of Appeal held that this could be done. However, the Supreme Court applied the following passage:

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175 *Qualico*, *supra* note 30 at 138 referring to *Prenn*, *supra* note 94 at 241; see also *Mowat*, *supra* note 154 at 155.

176 *Supra* note 84 at 51.

177 See the decisions of Master Funduk in *Whissell*, *supra* note 16 at 325-26; *Mouwen*, *supra* note 143 at 57; *Szantech*, *supra* note 143 at 4.

178 *NW Mechanical*, *supra* note 88 at 162, citing *Goss v. Lord Nugent* (1833), 110 E.R. 713 at 716 (K.B.).

179 [1929] 2 W.W.R. 505 (Alta. SC. (A.D.)).

180 *Supra* note 152.

> Nor can I think ... that it is legitimate to look at those words which appear upon the face of the agreement with a line drawn through them, and which are expressly, by the intention of the parties to the agreement, deleted, that is to say, done away with, and wholly abolished. It is not legitimate to read them and to use them as bearing upon the meaning of that which has become the real contract between the parties, namely, the final arrangement of the document which we must now proceed to construe.[181]

The reasoning in this passage could apply to the admission of any draft agreement or, indeed, to any document that sets out a negotiating position that is later abandoned.

Another argument made for the exclusion of evidence of the negotiations between the parties relates to the need to maintain a fair bargaining process in which the parties can change their position if necessary. This consideration was raised by McBain J. who relied on the following passage in *Milano's*:

> No one can doubt that there are cases where evidence of prior negotiations is properly excluded. Where the parties after negotiations have deliberately agreed to reduce their agreement to written form and have freely signed a document with the intention that it should comprise their whole agreement, there is a strong case for giving effect to their intention. In such a case, as Lord Wilberforce said in *Prenn v. Simmonds*, evidence of prior negotiations is excluded simply because it is irrelevant. A concession given at an earlier stage in the negotiations may have been withdrawn later. People often have to be content with less than they want and may agree to take a risk on some matter rather than cause a breakdown of negotiations by insisting on assent to their wishes. Subsequent events frequently cause a party to regret such agreement but that in itself is no ground for relief. There is nothing improper about a free agreement that a contract shall be reduced to writing. It serves a useful purpose to the parties and to society and enforcement of it is fully in accord with the purposes of contract law.[182]

Justice Estey espoused a similar approach in his concurring judgment in *Molybdenum*.[183]

In the course of his discussion, Estey J. relied on the cases which state that, while evidence of surrounding circumstances is admissible, facts which only tend to show that particular words have a particular meaning are not admissible.[184] It therefore appears that the comments of Estey J. were primarily directed at the admission of evidence of drafts and negotiations as part of the "commercial context," rather than as a means of resolving ambiguities. The apparent prohibition against the use of negotiation evidence may not apply where the contract in question is ambiguous.

There are in fact cases that suggest that such evidence is admissible to resolve ambiguities unless it contains direct statements of the parties' intentions. In *Canadian Atlas Diesel*

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[181] *Ibid.* at 523 quoting *Inglis v. Buttery* (1878), 3 App. Cas. 552 at 558 (H.L.), Lord Hatherly, followed in *Paddon Hughes*, *supra* note 97 at 188. See also *Molybdenum*, *supra* note 99 at 503.

[182] *Supra* note 157 at 172-73, quoting S.M. Waddams, *The Law of Contracts*, 2d ed. (Toronto: Canada Law Book, 1984) at 238-39.

[183] *Molybdenum*, *supra* note 99 at 502-503; see also *Lakewood*, *supra* note 109 at 121.

[184] *Molybdenum*, *ibid.* at 503 referring to Colin Blackburn, *A Treatise on the effect of the Contract of Sale on the legal rights of property and possession in goods, wares and merchandise*, 3d ed. by W.N. Raeburn & L.C. Thomas (London: Stevens, 1910) at 51 and *Grant v. Grant* (1870), L.R. 5 C.P. 727 at 728 (Ex.Ct.); see also *NW Mechanical*, *supra* note 88 at 162.

Engine Co. Ltd. v. McLeod Engines Ltd., the Supreme Court excluded direct statements of contractual intention stating that such evidence does not form part of the "commercial context" of a contract.[185] However, the Supreme Court did review the background discussions and correspondence between the parties leading up to the contract in question.[186] Likewise, the Supreme Court reviewed and discussed the correspondence between the contracting parties in *Clarke's-Gamble*.[187] The evidence in both cases could be described as being "negotiations."

The apparent prohibition against the admission of "negotiation" evidence as part of the "surrounding circumstances" or "commercial context" may not be as absolute as is often suggested. There are a number of decisions by the Alberta courts where pre-contractual correspondence and discussions between the parties were reviewed, apparently as part of the "surrounding circumstances" of the contract.[188] However, these cases for the most part do not directly examine the issue of the admissibility of "negotiation" evidence, as compared to other forms of parol evidence.

It does appear that there is some basis in Alberta for the admission of pre-contractual discussions, such that a statement speculating, "generally, evidence about discussions that preceded a documented contract is not admissible,"[189] may be somewhat misleading. The question of whether any particular evidence is admissible appears to turn on the nature of the evidence, the purpose for it being admitted and its potential effect. Despite a lack of uniform application, it appears that the following statements can be made about the admissibility of pre-contractual evidence in cases where the final contract is clear and unambiguous:

(a) any extrinsic evidence pre-dating the contract that would only tend to show that the words used were intended to have a particular meaning is inadmissible;[190]
(b) any evidence of pre-contractual negotiations is irrelevant to the interpretation of the particular words used in the contract and is inadmissible for that purpose;[191]
(c) earlier drafts of the agreement in question cannot be admitted to interpret the meaning of the final version;[192]
(d) any evidence of a party's subjective intention during negotiations cannot be admitted to interpret the meaning of a written contract;[193]
(e) evidence of pre-contractual negotiations may be admissible in cases where propositions (a), (b), (c) and (d) do not apply and the evidence is only tendered to

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185 [1952] 2 S.C.R. 122 [*Canadian Atlas*].
186 *Ibid.* at 135-38, Estey J., 146-52, Locke J.
187 *Supra* note 105 at 616-17.
188 See *Turbo Resources*, *supra* note 4 at 22-27; *Dilcon*, *supra* note 97 at 57-63; *Kerkhoff*, *supra* note 6 at 131-32; *Nathu*, *supra* note 161 at 128-30; *Delta Hotels*, *supra* note 3 at 348-68; *Alpine*, *supra* note 97 at 148-51; *Labatt (John) Ltd. v. Financial Trustco Capital Ltd.* (1989), 96 A.R. 56 at 58-67(Q.B.), Lomas J. [*Labatt*].
189 *Mouwen*, *supra* note 143 at 57.
190 *NW Mechanical*, *supra* note 88 at 162; *Molybdenum*, *supra* note 99 at 503.
191 *All-Power*, *supra* note 84 at 51; *Chaba*, *supra* note 19 at 637.
192 *Knight Sugar*, *supra* note 152 at 523; *Molybdenum*, *supra* note 99 at 502-503; *Paddon Hughes*, *supra* note 97 at 188; *Milano's*, *supra* note 157 at 172-73.
193 *Canadian Atlas*, *supra* note 185 at 136; *Turbo Resources*, *supra* note 4 at 30; *NW Mechanical*, *supra* note 88 at 162.

> show the surrounding circumstances such as the state of knowledge of the parties, the environment in which the parties were operating and to objectively establish the purpose and aim of the contract.[194]

When the contract is ambiguous, proposition (a), and arguably propositions (b), and (c) do not apply. With reference to proposition (a), there is strong authority that evidence of pre-contractual matters cannot be used for the purpose of showing that particular words in the final contract have a particular meaning.[195] However, it is submitted that this restriction only applies to clear and unambiguous agreements. For example, in *Canadian Atlas*, Estey J. referred to the following passage with approval: "It is well settled that if the surrounding circumstances raise a latent ambiguity in any of the expressions used, parol evidence may be resorted to *for the purpose of ascertaining which of the meanings of an ambiguous expression was contemplated by the parties.*"[196] Indeed, every time parol evidence is admitted to resolve an ambiguity, it is in fact being admitted for the purpose of showing that certain words have one particular meaning.

The Court of Appeal has allowed the terms of an oral agreement preceding the written one to be used as a means of interpreting the ambiguous terms of the subsequent written agreement.[197] Likewise where the contract is ambiguous, the Alberta courts have sometimes referred to negotiating positions taken by parties, as well as the apparent expectations of the parties and have sometimes made reference to draft agreements.[198] In this area, it is often difficult to reconcile what the courts say with what they do.

The next form of evidence that may be used to deal with an ambiguous agreement is evidence of the circumstances as they existed at the time of the agreement. This is perhaps the least controversial form of extrinsic evidence. It has been said that "the facts which the parties had in their minds and were negotiating about" at the time of the making of the contract are "always admissible,"[199] as are extrinsic facts[200] that "the parties themselves either had, or must be held to have had, in view, when they entered into the contract."[201] It has been stated that the proper way to interpret a contract is to "look at the state of facts and circumstances as known to the parties at the time" of contracting.[202]

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194 *Turbo Resources*, *ibid.*; *Re Ulster*, *supra* note 94; *Amerada*, *supra* note 87.

195 *NW Mechanical*, *supra* note 88 at 162; *Molybdenum*, *supra* note 99 at 503.

196 *Supra* note 185 at 136, citing *Frankel v. MacAndrews & Co.*, [1929] A.C. 545 at 567 (H.L.), Lord Warrington [emphasis added].

197 *Johnson Investments v. Pagritide*, [1923] 2 W.W.R. 736 (Alta. S.C. (A.D.)).

198 See *Turbo Resources*, *supra* note 4 at 22-27; *Dilcon*, *supra* note 97 at 57-63; *Kerkhoff*, *supra* note 6 at 131-32; *Nathu*, *supra* note 161 at 128-30, 134-35; *Delta Hotels*, *supra* note 3 at 348-68; *Alpine*, *supra* note 97 at 148-51; *Labatt*, *supra* note 188 at 58-67.

199 *Canada Law Book*, *supra* note 38 at 185, citing *Bank of New Zealand v. Simpon*, [1900] A.C. 182 at 187 (P.C.), Lord Davey.

200 *Ibid.*

201 *A.R. Williams*, *supra* note 38 at 705, citing *Birrel v. Drye* (1884), 9 App. Cas. 345 at 353 (H.L.), Lord Watson.

202 *Ibid.*, referring to *Fowkes v. Manchester & London Life Assurance & Loan Association* (1863), 3 B & S 917.

Likewise, the court has traditionally been entitled to know "what the circumstances were with reference to which the words that were used"[203] and the "market in which the parties were operating."[204]

These statements were made with reference to "commercial context" evidence but they should apply with even greater force to evidence offered to resolve an ambiguity that has been discovered.[205] The Court of Appeal has stated that where a contract is ambiguous, "extrinsic evidence, including evidence of commercial practices and realities relating to the business" is admissible.[206]

By way of example, in one case the Supreme Court referred to statements made at the time of contracting to establish that a purported sale was actually a security agreement that allowed the alleged purchaser to retain the goods until the repayment of its debt.[207]

The third type of evidence to be considered is evidence of facts and conduct subsequent to the making of the agreement. There is some controversy as to whether the court is entitled to examine the subsequent conduct of the contracting parties as an aid to interpreting an ambiguous written agreement. Contrary to relatively recent developments in England, the courts in Alberta have allowed the admission of evidence of subsequent conduct and have viewed such evidence as a useful guide to the interpretation of ambiguous written agreements. In 1916, Beck J. agreed with the following proposition: "Where both parties have acted on a particular construction of an ambiguous document, that construction, if in itself admissible, will be adopted by the Court.... To this extent its original effect, though it cannot be *altered* (unless it amounts to a variation by mutual consent) may be *explained* by the conduct of the parties."[208]

Chief Justice Davis came to the same conclusion during the same period in *Adolph Lumber*.[209] Thereafter, several Alberta decisions approved this approach,[210] and in 1945 the Court of Appeal approved the following statements of law:

> We are to look to the words of the instrument and to the acts of the parties to ascertain what their intention was; if the words of the instrument are ambiguous, we may call in aid the acts done under it as a clue to the intention of the parties.
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> ...

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203 *Re Ulster*, *supra* note 94 at 467.

204 *Turbo Resources*, *supra* note 4 at 30, citing *Reardon Smith Ltd. v. Hansen-Tangen*, [1976] 1 W.L.R. 989 at 995-96 (H.L.); see also *Evans*, *supra* note 148 at 241.

205 See *Deserres*, *supra* note 38 at 617.

206 *Finawest Development Corp. v. Petro-Canada* (1995), 36 Alta. L.R. (3d) 126 (C.A.).

207 *McKean v. Black* (1921), 62 S.C.R. 290.

208 *Cdn. Western Gas*, *supra* note 5 at 414 [emphasis in original], citing Sir Frederick Pollock, *Principles of Contract: a treatise on the general principles concerning the validity of agreements in the law of England*, 8th ed. (London: Stevens and Sons, 1911) at 477.

209 *Supra* note 161 at 307.

210 *Wilson v. Ward*, [1929] 3 D.L.R. 209 at 224 (Alta. S.C. (A.D.)), Harvey C.J.A., rev'd on other grounds [1930] S.C.R. 212; *Majestic Mines Ltd. v. Royal Trust*, [1930] 2 D.L.R. 21 at 25 (Alta. S.C.), Walsh J., aff'd [1930] 3 D.L.R. 1010 (Alta. S.C. (A.D.)).

> [W]e may look at the acts of the parties also; for there is no better way of seeing what they intended than seeing what they did under the instrument in dispute.
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> ...
>
> The intention of the parties must be collected from the language of the instrument, and may be elucidated by the conduct they have pursued.[211]

The Supreme Court came to a similar conclusion in cases decided at around the same time[212] and have subsequently affirmed the position.[213] There have also been a number of more recent Alberta decisions where evidence of subsequent conduct has been admitted to resolve ambiguities.[214]

However, in *Chiles Estate*, Montgomery J. held that such evidence was not admissible.[215] Justice Montgomery held that the statements made in certain cases suggesting that such evidence is admissible[216] were either *obiter* or not binding. He indicated that he preferred the current English rule, as set out in *James Miller & Partners Ltd. v. Whitworth Street Estates (Manchester) Ltd.*,[217] stating that such evidence is inadmissible.

Justice Hunt declined to follow the *Paddon-Hughes* case on this point in the subsequent case of *Galloway*,[218] and held that evidence of the subsequent conduct of the parties could be referred to interpret the ambiguous contracts in question. It is submitted that the *Galloway* decision is consistent with the Canadian case law and the approach taken in that case is to be preferred over the decision in the *Paddon-Hughes* case.

However, this approach would seem to apply only to ambiguous contracts. Where the words of the contract are not ambiguous, evidence of acts done pursuant to the contract cannot be relied on to show the intention of the parties or the sense in which the parties meant to use the language in the contract.[219]

3. EVIDENCE OF CUSTOM AND USAGE

A primary rationale for the Parol Evidence Rule is that the parties "meant what they said." However, this presumes that the words used by the parties have the same meaning for the

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211 *Cooke*, *supra* note 22 at 668; see also *Kasha*, *supra* note 1 at 168.

212 *Firestone Tire and Rubber v. Commissioner of Income Tax*, [1942] S.C.R. 476 at 482; *Hoefle*, *supra* note 160 at 383-84.

213 *Hayduk v. Waterton*, [1968] S.C.R. 871 at 889-90; *Acme*, *supra* note 160 at 634.

214 *Canadian Credit Men's Trust Association Ltd. v. Westergard* (1951), 1 W.W.R. (N.S.) 822 at 827 (Alta. S.C. (A.D.)); *Wimpey*, *supra* note 160 at 345-46; *Hetherington*, *supra* note 3 at 212; *Qualico*, *supra* note 30 at 141; *Duxbury v. Training Inc.* (2002), 308 A.R. 265 at 273-74 (Prov. Ct.), LeGrandeur J.

215 *Supra* note 97.

216 Such as in *NW Mechanical*, *supra* note 88; *Turney and Mercer v. Lauder* (1956), 4 D.L.R. (2d) 225 at 239 (S.C.C.), Locke J.; *CNR*, *supra* note 168; *Leitch Gold Mines Ltd. v. Texas Gulf Sulphur* [1969] 1 O.R. 469 (H.C.).

217 [1970] A.C. 572 (H.L.).

218 *Supra* note 3 at 256; see also *Beller Carreau Lucyshyn v. Cenalta Oilwell Servicing Ltd.* (1997), 211 A.R. 1 at 6-7 (Q.B.), Lewis J.

219 *Delhi Oil*, *supra* note 8 at 526.

parties as they do for the general population. This presumption may be rebutted in certain circumstances. In *Hetherington*, O'Leary J. said:

> Evidence of custom or usage may be considered in interpreting a contract in certain circumstances. Firstly, it may be admitted to prove that the words of the contract are used in a particular sense which differs from the sense in which they are ordinarily used. When adduced for this purpose, the evidence is used as a dictionary to explain the meaning of the words used in the contract. Evidence of custom or usage may also be admitted to annex incidents to the agreement upon which the agreement is silent. The court implies a term which the parties have omitted but which, in the context of the particular locality or particular trade, they mutually understood was applicable to the agreement. Whether the evidence of custom or usage is tendered for the purpose of interpreting the words used or to annex incidents to the agreement, it is not admissible if it varies or contradicts the terms of the document. Furthermore, evidence of custom or usage will not be considered by the court as an aid to the construction of an agreement unless the custom or usage is notorious, certain and reasonable.[220]

While the reference to custom and usage has been approved in recent Alberta cases as an appropriate method of interpretation,[221] the courts have been cautious in their acceptance of such evidence. The courts have expressed such caution in two primary ways. Firstly, they have placed a rather high onus of proof on the proponent of such evidence to prove both the existence and nature of the alleged custom and usage. Secondly, they have been quite vigilant in ensuring that any proposed interpretation or implied term suggested by such evidence does not conflict with the express terms of the written agreement.

For example, in *Georgia Construction v. Pacific Great Eastern Railway*,[222] the Supreme Court rejected evidence suggesting that the terms "extra haul" and "overhaul" had a particular meaning in respect to repair work done on a railway line. The Court held that, in order to accept such evidence, it must be demonstrated that the custom and usage was reasonably certain, notorious and so generally acquiesced to that it could be presumed to form an ingredient of the contract.[223] It was held that the test was not met in that case.

Such evidence was also rejected by the Court of Appeal in *Hidrogas Limited v. Great Plains Development Co. of Canada*,[224] both because of the lack of evidence of a special industry usage of the words in question and also because the proposed meaning conflicted with the written agreement. In *Great Northern Petroleum & Mines Ltd. v. Merland Exploration Ltd.*,[225] Shannon J. excluded custom and usage evidence on similar grounds.

Likewise, while the Supreme Court accepted that there was "a general practice and well understood usage" among stockbrokers in Vancouver, it also held that such evidence could not be relied upon because it contradicted the express words of the agreement.[226]

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220 *Supra* note 3 at 211-12.
221 See *Amerada*, *supra* note 87 at 296; *United Canso*, *supra* note 17 at 82-83.
222 [1929] S.C.R. 630.
223 *Ibid.* at 633, Duff J.
224 (1979), 17 Alta. L.R. (2d) 17 at 25-26 (C.A.).
225 (1983), 25 Alta. L.R. (2d) 67 at 74 (Q.B.), aff'd (1984), 36 Alta. L.R. (2d) 97 (C.A.).
226 *Cartwright, Crickmore, Ltd. v. MacInnes*, [1931] S.C.R. 425 at 430-31.

However, such evidence was relied on by Riley J. in *Re Gainers Ltd. and Local 319 United Packinghouse Workers of America* in relation to the method of choosing an arbitration panel to resolve a dispute. The arbitration clause was contained in the written contract. Justice Riley, in the course of his decision, described the difference between "custom" and "usage" as follows:

> The term "custom" has more or less been identified as relating to practices going back to ancient times. The term "usage" seems more appropriate as describing a course of conduct which is recognized as being normal in various types of occupations and contractual relationships. In other words, usage is a question of fact and does not necessarily involve time immemorial. The application of usage has been well recognized for many years.[227]

Justice Riley concluded that there was an established usage in that case and said, "It would appear that the Supreme Court of Canada has clearly established the proposition that where usage is demonstrated and proved, that usage will be incorporated into any contract which does not specifically contradict that usage which is generally known and accepted."[228] In coming to that conclusion, Riley J. referred to *F.W. Pirie Co. v. Canadian National Railway*,[229] where the Supreme Court accepted usage evidence in relation to a shipping contract. Usage evidence was also accepted by MacDonald J. in *Banks v. Biensch* in relation to the sale of Charolais cattle.[230] In that case, the Charolais Association had published a "code of ethics."[231] It was held that the terms of the contract impliedly included the guarantees established in that code because the code was "so well recognized and established."[232]

4. INCOMPLETE AGREEMENTS

The general presumption is that where the parties have reduced their contract to writing, they have "introduced into the written instrument every material term and circumstance."[233] However, this presumption also stands to be rebutted. The question then becomes whether or not a party to the contract is entitled to lead extrinsic evidence in order to rebut the presumption and demonstrate the document does not constitute the entire agreement between the parties.

There is certainly nothing inherently objectionable in such a process. As the Court of Appeal has stated, "It is trite law that the terms of a contract may be contained in more than one document."[234]

It appears to have been decided very early on in Alberta that such evidence is in fact admissible. In *Eaton*, the plaintiff built a house for the defendant. The plaintiff sued for an

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227 (1964), 47 W.W.R. (N.S.) 544 at 552 (Alta. S.C.).
228 *Ibid.* at 555.
229 [1943] S.C.R. 275.
230 (1977), 3 Alta. L.R. (2d) 41 (S.C. (T.D.)).
231 *Ibid.* at 45.
232 *Ibid.*
233 *Evans*, *supra* note 148 at 241; *NW Mechanical*, *supra* note 88 at 162; *Chaba*, *supra* note 19 at 635; *Catre Industries*, *supra* note 11 at 328.
234 *Hongkong*, *supra* note 69 at 309.

unpaid cash balance. The defendant replied that part of the price was to be paid by the conveyance of certain real estate. The Court of Appeal described both the Parol Evidence Rule, as well as an "exception" to that rule, in the following terms:

> The leading general rule respecting the admissibility of extrinsic evidence to affect what is in writing is, that parol testimony cannot be received to contradict, vary, add to or subtract from the terms of a valid written instrument.... The evidence in question in the present case is not, in my opinion, excluded by force of the general rule; but on the contrary is admissible in accordance with a well established subsidiary rule; namely, that a writing, although on its face it appears to constitute in itself a complete contract, may, by oral evidence, be shown to constitute only a part of the real contract, and in some cases, to be more specific, to be merely a means adopted by the parties to carry their real agreement into effect. If the latter be the purpose there may be an apparent inconsistency by reason of a writing stating a false relationship between the parties a convenient means merely of carrying into effect their real purpose. This is obviously quite different from permitting, in the absence of a case made for rectifications of a mistake, evidence of the omission of a particular provision from an instrument which was intended to be the complete record of the contract. The rule I have stated is established by innumerable cases.[235]

This "subsidiary rule" contains two elements. Firstly, there is the use of parol evidence to prove that the writing is not the complete agreement. The second element is the use of parol evidence to interpret the actual agreement between the parties. Both elements have been subsequently applied.[236] The first element was approved in the subsequent decision of the Court of Appeal in *Brocklebank v. Barter*.[237] In that case one party agreed to sign a formal contract on the understanding that certain additional terms were added. This was done so that the parties would not be put to the trouble of redrafting the formal documents. The Court of Appeal said that "Assuming that the parties did in fact so agree, it would be a monstrous thing if the law or any rule of evidence were such as to make it impossible for either party to prove that the formal contract was not the entire contract but merely an item of another and wider contract."[238] The same rule was later applied by the Court of Appeal with regard to two buildings situated on leased land, one of which was dealt with in the written lease and one of which was not. The Court of Appeal applied the following statement of law: "It has, moreover, been held that parol evidence is admissible to shew that an instrument does not contain the whole of the contract."[239] The Alberta courts have, in later cases, continued to accept that parol evidence may be used to establish that the document in question was not intended to constitute the entire agreement between the parties.[240]

The Alberta courts have also admitted parol evidence to establish the true nature of the contract between the parties.[241] The Court of Appeal approved this second element of the "subsidiary rule" by allowing parol evidence to be used to interpret the oral agreement. The

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235 *Supra* note 141 at 7.

236 See *Canadian Atlas*, *supra* note 186 at 136, Estey J.

237 (1914), 22 D.L.R. 209 (Alta. S.C.).

238 *Ibid.* at 213.

239 *Slywka v. Gamache* (1954), 11 W.W.R. (N.S.) 524 at 528 (Alta. S.C.(A.D.)), citing Wyatt Paine, ed., *Chitty on Contracts*, 15th ed. (London: Sweet and Maxwell, 1909) at 123.

240 *Delta Hotels*, *supra* note 3; *Milano's*, *supra* note 157 at 173, both relying on *Gallen*, *supra* note 157 at paras. 9-14, Lambert J.A.

241 *Francey v. Wawanesa Mutual Insurance* (1990), 75 Alta. L.R. (2d) 257 at 277 (Q.B.), Fraser J.

Court of Appeal said, "It is our view that looking at Ex. 7 by itself, it is quite clear that it does not contain the whole contract between the parties. It was therefore necessary and appropriate for the trial judge to look to oral evidence in order to determine exactly what the contract was between the parties."[242]

Likewise, in *Pawluk v. Bank of Montreal*, Andrekson J. relied upon the following passage in admitting extrinsic evidence to interpret the nature of the contract in question:

> Parties do not always reduce all the terms of their agreement to writing. An agreement may be comprised of partly written terms and partly oral terms. Therefore, it is imperative to determine whether the writing before the court constitutes the complete expression of the contractual arrangements between the parties. If it does not, then the Parol Evidence Rule is inapplicable and that part of the agreement which is oral may be proven by parol evidence."[243]

It therefore appears that, unless the document makes it clear that it comprises the entire agreement between the parties, parol evidence may be admissible both to demonstrate that it was not intended to be their entire agreement and then to establish the true nature of that agreement.

5. COLLATERAL AGREEMENTS

A further issue is whether evidence may be presented to show not just that there are additional terms, but also that there is more than one contract — one being written and another being oral.

This is not quite the same as proving that a contract is partly oral and partly written or that the contract is made up of more than one document. The courts have been quite prepared to interpret the terms of a contract by reading several documents made between the parties.[244] In such cases, all of the relevant documents are admissible to interpret the agreement. As is noted above, the courts have also readily accepted that a contract may be partly oral and partly written.

The courts have had somewhat more difficulty dealing with evidence of the existence of an oral contract or warranty in addition to the written agreement under consideration. Such a "collateral" contract or warranty is often made in consideration of entering into the written agreement. The theoretical existence of a contract given in consideration of entering into another contract has long been accepted by the Supreme Court.[245] Such a collateral contract must be proven in the same fashion as any other contract, primarily by proving an intention to contract between the parties and an agreement on the terms of the contract.[246]

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242 *Francey v. Wawanesa Mutual Insurance* (1991), 82 Alta. L.R. (2d) 339 at 339 (C.A.).

243 (1994), 20 Alta. L.R. (3d) 76 at 98 (Q.B.), citing John Sopinka & Sidney N. Lederman, *The Law of Evidence in Civil Cases* (Toronto: Butterworths, 1974) at 268-69 [footnotes omitted].

244 *Hongkong*, *supra* note 69 at 309.

245 See *Byers v. McMillan* (1887), 15 S.C.R. 194 at 202, 205, Strong J., Henry J.; *Hawrish*, *supra* note 142.

246 *Carman Construction*, *supra* note 142; *Bauer*, *supra* note 142 at 431-32; *Union Properties v. Monenco Advisory Services Ltd.* (1996), 190 A.R. 257 at 264, para. 30 (Q.B.), Smith J. [*Monenco*].

The Parol Evidence Rule provides a major restriction on the admission of evidence of collateral contracts or warranties in the interpretation process. The rule prohibits the use of parol evidence where it would "contradict" or "vary" the written agreement. To the extent that any oral collateral agreement does not purport to "contradict" or "vary" a written agreement, there would seem to be no objection to the admission of the evidence under the Parol Evidence Rule. This was, in effect, the ruling of the Supreme Court in *Hawrish*, where the Court noted that

> In the last half of the 19th century a group of English decisions, of which *Lindley v. Lacey*, *Morgan v. Griffith* and *Erskine v. Adeane* are representative, established that where there was parol evidence of a distinct collateral agreement which did not contradict nor was inconsistent with the written instrument, it was admissible. These were cases between landlord and tenant in which parol evidence of stipulations as to repairs and other incidental matters and as to keeping down game and dealing with game was held to be admissible although the written leases were silent on these points. These were held to be independent agreements which were not required to be in writing and which were not in any way inconsistent with or contradictory of the written agreement.[247]

The corollary of this proposition is that evidence of a collateral oral agreement which is inconsistent or contradictory to the written agreement is inadmissible. Indeed, the governing principle now is that a collateral contract cannot be established where it is inconsistent with or contradictory to the written agreement.[248]

For example, in *Royal Bank of Canada v. King*, the defendants signed a guarantee that was stated to be given as a "continuing guarantee" to secure any ultimate balance due and owing to the Bank by the defendants' company.[249] The defendants argued that the guarantee was only signed to secure a $5,000 promissory note that was the only indebtedness outstanding at the time the guarantee was executed. Justice Miller, relying on this principle, declined to admit evidence to explain the arrangement.[250]

There is some controversy as to whether the principle regarding inconsistent or contradictory collateral contracts is absolute. Two cases decided in May 1988 highlight the issue. In *Color Your World*, the defendant was a franchisee who alleged that there was an oral agreement in place prior to the written franchise agreement. The existence of an earlier oral agreement was not disputed. However, Matheson J. said:

> An oral agreement may not be alleged which conflicts with a written agreement.
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> ...
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> Thus, a prior oral agreement cannot stand if it is inconsistent with a later written agreement.
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> ...

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247 *Supra* note 142 at 518-19 [footnote omitted].

248 *Catre Industries*, *supra* note 11 at 329, para. 30; *United Mine Workers of America District 18 v. Cardinal River Coals Ltd.* (1985), 58 A.R. 371 at 374-75 (C.A.); *Carman Construction*, *supra* note 142 at 201; *Bauer*, *supra* note 142 at 431-32; *Hawrish*, *ibid.* at 520.

249 (1982), 21 Alta. L.R. (2d) 336 at 343-44 (Q.B.).

250 *Ibid.*

> The alleged oral agreement and the written agreement, Exhibit 1, are inconsistent with each other. Therefore, only the written agreement is valid.[251]

By way of contrast, 13 days earlier MacCallum J. had issued Reasons for Judgment in *Curlett v. T.D. Bank*, in which he suggested that the principles referred to by Matheson J. are not absolute.[252]

Justice MacCallum relied on a decision of the British Columbia Court of Appeal[253] to hold that the Parol Evidence Rule may be departed from to do justice between the parties. He acknowledged that there are unreported Ontario decisions in which a contrary view is taken, but held that they "too strictly applied the parol evidence rule."[254]

The reasoning in the *Curlett* decision does not appear to be part of any major change in the law relating to collateral contracts in Alberta.[255] There have been subsequent decisions in which the rule was held to be sufficiently established and certain as to support summary judgment.[256]

6. RECTIFICATION

A primary presumption underlying the Parol Evidence Rule is that the parties meant what they said in the written agreement. But what if this is not the case? Are the parties always bound by their mistakes in preparing the written document?

It has been said that "[t]he most venerable breach in the parol evidence rule is rectification, or reformation, an equitable doctrine based on simple notions of relief against unjust enrichment."[257] The remedy of rectification may be invoked upon proof of a mistake. Rectification has been described the following way: "Rectification is concerned with contracts and documents, not with intentions. In order to get rectification, it is necessary to show that the parties were in complete agreement on the terms of their contract, but by an error wrote them down wrongly."[258] Rectification is not a device for contractual

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251 *Supra* note 154 at paras. 165-68. See also *Re/Max Real Estate*, *supra* note 143 at 218.

252 (1988), 60 Alta. L.R. (2d) 39 at 51-52 (Q.B.) [*Curlett*].

253 *Gallen*, *supra* note 157.

254 *Curlett*, *supra* note 252 at 52.

255 But it was followed on similar facts in *Toronto-Dominion Bank v. Siffledeen*, [1995] A.J. No. 519 (Q.B.) (QL). But see *Dornan*, *supra* note 4 at 262-63.

256 See *Re/Max Real Estate (Edmonton) Ltd. v. MBI Millar Bros. Properties* (1991), 124 A.R. 262 at 266-67 (M.C.) where Master Quinn distinguished both *Curlett* and *Gallen* and applied the Parol Evidence Rule; see also *Steeplejack*, *supra* note 13 at 318.

257 *Alberta Agricultural Development Corp. v. Shamuhn* (1994), 18 Alta. L.R. (3d) 77 at 82 (Q.B.), Andrekson J., citing S.M. Waddams, *The Law of Contracts*, 3d ed. (Toronto: Canada Law Book, 1993) at 219.

258 *Oriole Oil & Gas Ltd. v. American Eagle Petroleums Ltd.* (1981), 24 Alta. L.R. (2d) 121 at 124 (Q.B.), Forsyth J., aff'd (1981), 24 Alta. L.R. (2d) 130 at 132 (C.A.); *Davidson v. Eaton/Bay Trust* (1986), 45 Alta. L.R. (2d) 212 at 222 (Q.B.), Egbert J. [*Davidson*]; *Canada Mortgage and Housing Corp. v. Edinburgh House Apartments Ltd.* (1991), 112 A.R. 104 at 110 (Q.B.), McFadyen J. [*Edinburgh House Apts.*]; *Barrett v. Krebs* (1995), 27 Alta. L.R. (3d) 27 at 38 (Q.B.), Hunt J.; *Monenco*, *supra* note 246 at 267, *Alberta Tractor v. Noralta Clearing* (2003), 14 Alta. L.R. (4th) 150 at 158 (Prov. Ct.), Skitsko P.J., all relying on *Frederick R. Rose (London) Ltd. v. Wm. H. Pim & Co.*, [1953] 2 All E.R. 739 at 747 (C.A.), Denning L.J.

interpretation. It is an equitable remedy designed to remedy conduct that amounts to fraud or is equivalent to fraud.[259] However, rectification impacts on matters of contractual interpretation in two ways.

First, a party relying on rectification is entitled to rely on parol evidence to prove its case. Such evidence will, of necessity, contradict the written agreement. This exception to the Parol Evidence Rule was described in the following passage adopted by the Court of Appeal in *Jadis v. Porte*:

> The rule at law that evidence is not admissible to contradict or explain a written instrument, stated *simpliciter*, is received in equity as well as at law. A Court of equity does, nevertheless, assume a jurisdiction to reform instruments which, either by the fraud or the mistake of the drawer, admit of a construction inconsistent with the true agreement of the parties. And, of necessity, in the exercise of this jurisdiction, a Court of equity receives evidence of the true agreement in contradiction of the written instrument.[260]

The second way that rectification impacts on matters of contractual interpretation is that it calls upon the court to use the parol evidence to interpret the nature of the contract between the parties. The court is then called upon to interpret the words of the written agreement to determine whether the contract expressed in the written agreement conforms with the contract formed in light of the parol evidence. If the two interpretations are different, then rectification is potentially available. However, the party seeking rectification must still meet a very high onus of proving that the written agreement does not reflect the true contract between the parties. The exact standard of proof to be met is a matter of some controversy. It has been described as proof "beyond a reasonable doubt" or evidence that "leaves no fair or reasonable doubt," but most recently the term "convincing proof" has been accepted by the Supreme Court.[261] A very high onus of proof, approaching a criminal standard, tends to dominate the Alberta case law.[262]

The prerequisites to rectification have been summarized in a number of cases arising out of Alberta:

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259 *Sylvan Lake Golf & Tennis Club Ltd. v. Performance Industries Ltd.*, [2002] 1 S.C.R. 678 at para. 31 [*Sylvan Lake*].

260 (1915), 8 Alta. L.R. 489 at 494 (S.C. (A.D.)); see also *Colonial Investment v. Borland* (1911), 5 Alta. L.R. 71 at 84 (S.C. (T.D.) and S.C. (A.D.)), Beck J.; *Pointe Anne Quarries Ltd. v. "M.F. Whalen" (The)* (1921), 63 S.C.R. 109 at 126, aff'd [1923] 1 D.L.R. 45 (P.C.); *Edinburgh House Apts., supra* note 258 at 109; *Eastcal Development Ltd. v. Whissel Enterprises Ltd.* (1980), 25 A.R. 92 at 95 (C.A.).

261 *Sylvan Lake, supra* note 259 at 17-18; see also *ITT Industries of Canada Ltd. v. Toronto Dominion Bank* (1988), 63 Alta. L.R. (2d) 87 at 92 (Q.B.); *Farm Credit Corp. v. Lacombe Nurseries* (1992), 2 Alta. L.R. (3d) 20 at 24 (C.A.); see also *Guaranty Properties, supra* note 90 at 384-85, paras. 30-32.

262 *Oneil v. Road King Truck Stop Ltd.* (1995), 181 A.R. 112 at 113-14 (C.A.); *Beneficial Canada v. 524191 Alberta Ltd.* (1996), 190 A.R. 81 at 82 (Q.B.); see also *SCS Western, supra* note 65 at para. 61; *Halwa v. Olsen*, [1948] 1 W.W.R. 1049 at 1056 (Alta. S.C.), Parlee J.A.; *Fuhr v. Davidson*, [1948] 1 W.W.R. 1057 at 1060 (Alta. S.C.), H.J. MacDonald J.; *Stagg v. Petronick* (1958), 24 W.W.R. 651 at 654-55 (Alta. S.C.), Primrose J.; *Brittain v. Gartner* (1963), 46 W.W.R. (N.S.) 112 at 117 (Alta. S.C.), Riley J.; *Scotia Centre Ltd. v. EBJ Investments Ltd.* (1994), 22 Alta. L.R. (3d) 80 at 85 (Q.B.), McMahon J.; *Tatarchuk v. Sidor* (1951), 1 W.W.R. (N.S.) 435 at 449 (Alta. S.C. (A.D.)), Clinton J. Ford J.A., dissenting on another point. However see *Shorb, supra* note 57 at 665; *Johnson v. Fisher*, [1921] 3 W.W.R. 680 (Alta. S.C. (A.D.)); *Henderson v. Montreal Trust* (1955), 14 W.W.R. 210 (Alta. S.C. (A.D.)).

- The parties were completely *ad idem* on the terms and conditions of their inconsistent oral contract;
- The party resisting rectification either does not deny the alleged variation of the agreed upon terms of the contract as supported by the parol evidence of the other party or that party knew or ought to have of the mistake in reducing the oral contract writing;
- The precise form of the agreement must be shown; and
- Proof of the above conditions has been established by "convincing proof" and not merely by a preponderance of evidence.[263]

V. "ENTIRE AGREEMENT" AND "NO RELIANCE" CLAUSES

Commercial contracts often contain clauses which attempt to invoke the Parol Evidence Rule and exclude any representations, warranties or obligations between the parties, other than those set out in the document. Two of the most common forms of such clauses may be generically described as "entire agreement" clauses and "no reliance" clauses.

An "entire agreement" clause typically states that the written document constitutes the complete and entire agreement between the parties and that there are no representations, warranties or understandings between the parties other than those expressed in the document. Such clause may also state that the written document supersedes and replaces all prior agreements and that no implied terms shall be read into the document. It may also state that any amendments or waivers of the contract must be in writing and signed by the parties.

A "no reliance" clause has a similar purpose and is common in construction contracts or agreements of purchase and sale. The clause typically states that the purchaser or builder has inspected the property or the work site and confirms that it is relying entirely on its own inspection and agrees that it is placing no reliance on any representation, warranty or statement made by the other contracting party.[264]

There are numerous variations on these types of agreements and many clauses contain both "complete agreement" and "no reliance" language along with other restrictions and exclusions.

The "complete agreement" clause is, in theory, a very effective means of invoking the Parol Evidence Rule. If the contract itself expressly states that it is the "entire" or "complete" agreement between the parties, then any attempt to introduce further representations would be in direct conflict with the contract and evidence of such representations, collateral warranties or implied terms should be inadmissible. This type of clause is probably more effective in Alberta than in other jurisdictions. In Alberta, this type of clause is, *prima facie*, an almost complete answer to an attempt to imply further terms beyond those found in the document.

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263 *Sylvan Lake*, *supra* note 259 at 16-18; see a similar formulation in *Davidson*, *supra* note 258 at 222-23, Egbert J.; *Edinburgh House Apts.*, *supra* note 258 at 110, McFadyen J.; *Alberta (Treasury Branches) v. Koska* (1995), 175 A.R. 339 at 351-52 (Q.B.), Hutchinson J.

264 *Catre Industries*, *supra* note 11 at 325; *Carman Construction*, *supra* note 142 at 962, 966-67, 969.

Two early cases that give effect to "complete agreement" clauses and that are referred to in later Alberta cases are the Supreme Court's decision in *Case Threshing Machine v. Mitten*[265] and the Court of Appeal's decision in *Kaster v. Cowan*.[266] The effect of the complete agreement clause in *Case Threshing Machine* was described as follows by Duff J.:

> The written contract declares in explicit words that the terms of the agreement between the parties are to be found in the writing and in the writing exclusively. In face of this provision it is not, in my opinion, competent for a court of law to resort to contemporary conversations or prior conversations or even to the legend on the article for the purpose of discovering a contract differing in its terms from that expressed in the unambiguous language of the instrument.[267]

Much the same ruling was made by the Court of Appeal in *Kaster*.[268] Both cases were relied upon by Master Funduk in *Marwood Cedar*[269] to grant summary judgment against a party who claimed that the contract he signed was different from that intended. This line of authority has been relied upon by the Alberta courts in numerous summary judgment applications so as to exclude evidence of warranties or understandings outside of the written agreement on the grounds that the agreement contains "entire agreement" language.[270]

The basic enforceability of "entire agreement" clauses has also been confirmed by the Court of Appeal so as to preclude the existence of implied terms.[271] Such clauses have even been held to exclude the imposition of fiduciary or equitable obligations beyond those expressly set out in the contract.[272]

VI. SUMMARY

The ultimate objective of the court when engaging in contractual interpretation is to discover, give effect to and advance the real and true intent of the contracting parties. This is normally done by giving effect to the plain and ordinary meaning of the words used and not by the court imposing its views of fairness on the parties. Where the written agreement is ambiguous or incomplete the court may make reference to extrinsic evidence to resolve those difficulties so long as this evidence does not conflict with the express terms of the written agreement. The court is always entitled to interpret the agreement in the context of the surrounding circumstances, but this process is normally unnecessary if the words used in the agreement are clear and unambiguous. Extrinsic evidence may also be used to support

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265 *Supra* note 142.

266 [1925] 2 W.W.R. 186 (Alta. S.C. (A.D.)) [*Kaster*].

267 See *supra* note 142 at 119-20.

268 *Supra* note 266.

269 *Supra* note 137.

270 *C Corp. (Ontario) Ltd. v. Wesbru Holdings Ltd.* (1988), 91 A.R. 210 at 213 (M.C.); *Steeplejack, supra* note 13 at 313-14; *Everall Construction Limited v. Stuart Olson Construction* (1990), 74 Alta. L.R. (2d) 357 at 361-62 (M.C.); *Wye Gardens, supra* note 13 at 109; *Mouwen, supra* note 143 at 58; *West Edmonton Mall Ltd. v. Clock Gallery Ltd.* (1993), 7 Alta. L.R. (3d) 327 at 332-33 (M.C.); *Westmount, supra* note 143 at 276-77.

271 *Volker, supra* note 17 at 173-74.

272 *Luscar Ltd. v. Pembina Resources Ltd.* (1994), 24 Alta. L.R. (3d) 305 at 342-43 (C.A.). See also *International Brotherhood of Boilermakers, Iron Shop Builders, Balcksmiths, Forgers and Helpers, Local D331 v. Lafarge Canada* (1999), 250 A.R. 125 at paras. 13-15 (C.A.).

an application for rectification so as to avoid a result that would be equivalent to fraud. While these basic principles can be easily and shortly stated, they conceal a complex web of at times contradictory and evolving concepts that will continue to attract debate and controversy.