December 14, 2016

The limits of applications: when are trials necessary in contractual disputes?

The Ontario *Rules of Civil Procedure* allow for certain matters to proceed by way of application, where a court can determine a discrete legal issue without the need for a full trial. Although an application can be an expeditious and cost-effective way to resolve a legal dispute, lawyers should be careful to ensure the issues in the case are the proper subject matter of an application. The Ontario Court of Appeal's decision in *Jackson v Solar Income Fund Inc* is an important reminder of the limits of an application and the court's unwillingness to make rulings on the basis of a limited evidentiary record.

In that case, Jennifer Jackson, the applicant/respondent on appeal, was successful in an application before Dow J. to enforce the payment of $260,000 on a promissory note against the respondent, Solar Income Fund Inc ("Solar").

Although the promissory note was on its face a demand note, Solar argued that in the context of the broader transaction, its purpose was to serve as evidence of a debt between the parties. Solar also contended that a related side-agreement actually changed the terms of the note to not be payable on demand. While Ms. Jackson acknowledged the side-agreement, her evidence was that it did not change the clear wording of the note. She argued there was no need to consider the factual matrix to interpret the note.

Solar appealed the application decision on the basis that the judge had failed to look beyond the face of the promissory note to the factual matrix, which included related contractual agreements that were part of a larger corporate transaction.

The Court of Appeal identified the parties as sophisticated commercial parties who, in structuring the merger transaction, had engaged legal and professional advice. The court noted that the evidentiary record was unclear as to the details surrounding the broader transaction and how the different contractual agreements were intended to work together. The court agreed with Solar that the insufficient evidentiary record was the result of the proceeding being improperly commenced as an application.

Under Rule 14.05(3)(d), an application may be heard where the matter involves “the determination of rights that depend on the interpretation of a…contract or other instrument.” Here, however, the Court of Appeal held that the issue was not the interpretation of the promissory note; it was whether the promissory note was modified by subsequent agreement, despite its clear wording. This required a consideration of the broader factual matrix.

The Court of Appeal also found the respondent could not rely on Rule 14.05(3)(h), which authorizes a proceeding by way of application where there is unlikely to be material facts in dispute. In this case, there were factual disputes—that is, whether there was an agreement to convert the promissory note from a demand note to a note not payable on demand.

The court allowed the appeal and directed the matter to proceed by way of trial.

This decision is an important reminder of the limits of proceeding by way of application. While this case involved the interpretation of a contract, the specific nature of the dispute required an investigation and determination of the surrounding facts, which the court was not willing to do on the basis of a limited evidentiary record.