John A.D. Vellone
T 416.367.6730
F 416.361.2758
jvellone@blg.com

Borden Ladner Gervais LLP
Scotia Plaza, 40 King St W
Toronto, ON, Canada M5H 3Y4
T 416.367.6000
F 416.367.6749
blg.com

April 13, 2016

Delivered by RESS, Email and Courier

Ms. Kirsten Walli
Board Secretary
Ontario Energy Board
2300 Yonge Street, Suite 2701
Toronto, ON M4P 1E4

Dear Ms. Walli:

Re: Ottawa River Power Corporation ("ORPC")
Board File No. EB-2014-0105
Reply Submissions

We are counsel to ORPC in the above captioned matter. Please find enclosed ORPC's Reply Submissions and related supporting documentation in regards to this matter.

Yours very truly,

BORDEN LADNER GERVAIS LLP
Per:

Original signed by John A.D. Vellone

John A.D. Vellone

cc: Jane Donnelly, Ottawa River Power Corporation
Parties in EB-2014-0105

EB-2014-0105

IN THE MATTER OF the *Ontario Energy Board Act, 1998*, S.O. 1998, c.15, (Schedule B);

AND IN THE MATTER OF an Application by Ottawa River Power Corp. for an order approving just and reasonable rates and other charges for electricity distribution to be effective May 1, 2016.

REPLY SUBMISSIONS OF OTTAWA RIVER POWER CORP.

April 13, 2016

BORDEN LADNER GERVAIS LLP
Barristers and Solicitors
Scotia Plaza, 40 King Street West
Toronto, Ontario M5H 3Y4

John A.D. Vellone
Tel: (416) 367-6730
Fax: (416) 361-2758
jvellone@blg.com

Counsel to the Applicant

REPLY SUBMISSIONS OF OTTAWA RIVER POWER CORP.

A. INTRODUCTION

1. Ottawa River Power Corp. ("**ORPC**" or the "**Applicant**") is pleased to present this written reply to the submissions on the costs of long term debt from Board staff ("**Staff**") presented orally on March 31, 2016, the School Energy Coalition ("**SEC**") received on April 3, 2016, and the Vulnerable Energy Consumers Coalition ("**VECC**") received on April 7, 2016 (Staff, SEC and VECC shall be referred to collectively as the "**Parties**").

2. Each of the Parties have raised concerns about the rate impact associated with the Board approving an affiliate debt rate of 7.25% in a manner consistent with the Board's Decision and Order in ORPC's last cost-of-service application (EB-2009-0165).[1] In general terms, the Parties have challenged particular facts and have then relied upon the Board's RRFE, and in particular to the *customer preference* outcome to argue that the Board should approve a lower cost of affiliate debt. Certainly as representatives of customer interests, the Parties are entitled to challenge the Applicant as they have.

3. The Applicant readily concedes that a lower cost of affiliate debt would result in lower rates. However, the Applicant submits that the Board should not consider the customer preference for lower rates on its own. Rather, in the Applicant's submission those preferences need to be balanced against another RRFE objective: *financial viability*. In this regard, the Applicant submits that financial viability is best maintained through a stable and predictable application of the Board's well understood policy on cost of capital.[2]

4. In this regard, each of the four (4) municipalities have a legitimate expectation to earn the agreed-to 7.25% fixed rate of interest on the debt that is owed until that debt expires in 2022. This is consistent with the Board's policy on cost of capital, has previously been approved by the Board, and reflects an agreed-to allocation of risk that was established prior to market opening.

[1] EB-2009-0165, Decision and Order, Pg. 20.
[2] As such policy is detailed in EB-2009-0084 Report of the Board on the Cost of Capital for Ontario's Regulated Utilities, December 11, 2009.

B. GOVERNING LAW

5. The law governing the replacement of lost promissory notes is detailed in the *Bills of Exchange Act*, R.S.C., 1985, c. B-4 ("**BEA**"). The relevant provisions of the BEA have been included in Appendix "A" to these submissions for ease of reference. The Parties' submissions tend to muddle the law as it relates to the replacement of lost promissory notes in the Province of Ontario. The Parties are not necessarily experts in contract law, debt instruments, and promissory notes more specifically. The Applicant believes it would be helpful for the Board to have a solid understanding of the governing legal principles.

B.1 THE LAW GOVERNING THE REPLACEMENT OF LOST PROMISSORY NOTES

6. Under section 176(1) of the BEA, a promissory note is defined as:

> […] an unconditional promise in writing made by one person to another person, signed by the maker, engaging to pay, on demand or at a fixed or determinable future time, a sum certain in money to, or to the order of, a specified person or to bearer.

7. A promissory note is <u>not</u> the same thing as a bill of exchange. However, section 186 (1) of the BEA provides that the provisions of the BEA referenced in this reply submission relating to bills apply, with such modifications as the circumstances require, to promissory notes.

8. ***What does the BEA say about a lost promissory note?***

9. Section 155 of the BEA describes the process to follow to issue a replacement note when a promissory note has been lost before it is due to be paid:

> 155 (1) Where a bill has been lost before it is overdue, the person who was the holder of it may apply to the drawer to give him another bill of the same tenor, giving security to the drawer, if required, to indemnify him against all persons whatever, in case the bill alleged to have been lost is found again.
>
> (2) Where the drawer, on request, refuses to give a duplicate bill, he may be compelled to do so.

10. By operation of section 186 (1) of the BEA, this provision applies equally to promissory notes.

11. ***Can a person sue on a lost promissory note?***

12. Yes, a person still has the right to sue for breach of a lost promissory note pursuant to Section 156 of the BEA, which states that:

> 156 In any action or proceeding on a bill, the court or a judge may order that the loss of the instrument shall not be set up, if an indemnity is given to the satisfaction of the court or judge against the claims of any other person on the instrument in question.

13. By operation of section 186 (1) of the BEA, this provision applies equally to promissory notes. "Shall not be set up" is a term of art. It means that the loss of the instrument will not prohibit the former holder of the note from suing for breach of that instrument, provided the requisite indemnity has been given to address a situation where a third party finds the lost note and attempts to sue on that original instrument.

14. This provision is relevant, as it goes directly to the ability of the municipalities to sue the Applicant on the promissory notes even though the promissory notes could not be found. The legal obligation on ORPC to make payments remained.

15. ***Does the issuance of a replacement note constitute a new promissory note?***

16. Like other contracts, a promissory note can be enforced only by a person who has given valuable consideration for the promise.

17. This is shown in section 52 (1) of the BEA which provides that:

> 52 (1) Valuable consideration for a bill may be constituted by (a) any consideration sufficient to support a simple contract; or (b) an antecedent debt or liability.

18. By operation of section 186 (1) of the BEA, this provision applies equally to promissory notes.

19. If there has been no additional consideration given, a replacement note cannot be characterized as giving rise to a new liability on the maker of the note. Instead, the replacement promissory note simply memorializes an already existing liability of the maker created when consideration was actually given.

20. ***What is required for a promissory note to be payable on demand?***

21. Section 22 (1) of the BEA states that:

> A bill is payable on demand (a) that is expressed to be payable on demand or on presentation; or (b) in which no time for payment is expressed.

22. By operation of section 186 (1) of the BEA, this provision applies equally to promissory notes.

B.2 WHAT IS THE LAW ON "AGREEMENTS TO AGREE"?

23. The Parties all made submissions on the language "term and interest to be renegotiated annually". However the Parties have chosen to ignore a fundamental principle of contract law: there cannot be a contract to enter into a contract[3] or an "agreement to agree"[4]. This is because all of the terms of an agreement between parties must be settled, and nothing left for negotiation.[5] The cases summarized below and attached with these submissions provide an overview of the courts' interpretation of "agreements to agree" in situations similar to this case.

24. In *Bank of Nova Scotia v. Sharrun*, [1990] A.J. No. 1120,[6] the plaintiff claimed against the defendant for monies owing under a promissory note. At the time of negotiation of the terms, the plaintiff requested a shortened term of loan with high monthly payments and then represented to the defendant that if the defendant had difficulty making the payments, the plaintiff would be willing to renegotiate the loan, extending the term of the loan. The defendant lost their employment and could no longer manage the high monthly payments. The plaintiff refused to renegotiate the loan.

25. At page 2, Master Funduk of the Alberta Court of Queen's Bench held that:

> **<u>An agreement to re-negotiate is not enforceable in law because it is an agreement to agree</u>**. To the extent that the Defendant's position is that there was an agreement to renegotiate the position does not show a triable issue.

26. In *Mannpar Enterprises Ltd. v. Canada, [1998] 1 C.N.L.R. 114*[7] the defendant, the federal Crown issued a permit to the plaintiff Mannpar Enterprises to remove sand and gravel from the Skyway Indian Reserve No. 5. The permit was issued for a period of five years and contained a clause granting a "right to renew" for a further five year period subject to "satisfactory performance and renegotiation of the royalty rate and annual surface rental."

---

[3] *Courtney & Fairbairn Ltd. Tolaini Brothers (Hotels) Ltd*., [1975] 1 All E.R. 716 (C.A.).
[4] *P.P. (Portage) Holdings Ltd. v. 346 Portage Portage Avenue Inc.* (1999), 138 Man. R. (2d) 217 at 222 (Man. C.A.).
[5] *Imperial Oil Ltd. v. C. & G. Holdings Ltd.* (1986), 58 Nfld. & P.E.I.R. 326 at 344 (Nfld. T.D.); affirmed (1989), 78 Nfld. & P.E.I.R. 1 (Nfld. C.A.).
[6] Attached as Appendix "B".
[7] Attached as Appendix "C".

27. Shortly before the expiry of the original five year period, the plaintiff issued a notice to renew the permit, but the Skyway Band and the Crown refused. The plaintiff argued that the right to renewal created an obligation to negotiate in good faith. The plaintiff took the position that the defendant Crown was repudiating its contractual obligation to renew, withheld payments due under the permit, and sued for damages. The Crown counterclaimed for royalty payments withheld and for reclamation costs as set out in the permit. The Crown, as defendant, argued that the right to renew was void for uncertainty in that it was only an agreement to agree.

28. The British Columbia Supreme Court held at paragraph 55, upon a review of the authorities, that the renewal provision was a mere agreement to agree and was void for uncertainty, creating no obligation on the Crown or the Band to negotiate in good faith. **An agreement to negotiate in the absence of some objective measure is void in law and unworkable in practice.** While not reproduced here, the British Columbia Supreme Court presented an excellent overview of case law on this topic at paragraphs 31-54 of its decision.

29. Finally, in *Canada Trustco Mortgage Co. v. 1098748 Ontario Ltd. (c.o.b. Canyyz Properties Limited Partnership)*, [1990] O.J. No. 963,[8] Canada Trustco sought an order declaring that the "option to renew" contained in s. 19.02 of a lease agreement was valid and enforceable. The Ontario Court of Justice held at paragraph 18 that the provision in question was:

> "… **at most an agreement to agree which is, in reality, merely an agreement to negotiate. Such an "agreement" is not enforceable.** There are several reasons according to "classical" contract law why the agreement to agree in this case is not enforceable, and at least one more modern explanation. As Professor Atiyah puts it (P.S. Atiyah, An Introduction to the Law of Contract, 5th ed., (Clarendon Press: 1995)) at p. 112:
>
>> [T]he court cannot enforce a contract unless it knows what the terms are which it is sought to enforce. It is very old law that ... 'an agreement to agree' cannot be a valid contract. ... What the parties cannot do is to bind themselves to negotiate and reach agreement, because the negotiations may genuinely fail to lead to an agreement.

[8] Attached as Appendix "D".

C. REPLY SUBMISSIONS: THE TERMS OF THE PROMISSORY NOTES

30. The Applicant submits that the Replacement Notes represent the original promissory notes in law. They are legally binding in accordance with their terms, and they should be referred to by the Board as evidence of affiliate debt.

31. Each of the Parties have challenged the facts as they relate to the terms of the promissory notes. When considering the facts and these challenges, it is important that the Board apply the correct legal test, which was summarized during argument-in-chief, and which none of the Parties challenged.

32. The test is: <u>What were the intentions of the parties (being ORPC and each of the four (4) municipalities) at the time the notes were issued?</u> This is the same legal test that a court would use if it were asked to enforce the terms of the promissory notes.

33. When considering this test, each of the Parties have focused their challenges on certain anomalies contained in various ancillary documents. In doing so the Parties argue that the Board should ignore some of the most compelling evidence of the intentions of ORPC and each of the four (4) municipalities.

34. First, the Board has the benefit of the understanding of all of the parties to the notes. The understanding of ORPC is detailed in Exhibit 5 of the Application, is consistent with the evidence given in EB-2009-0165, and was further confirmed during oral testimony. The understanding of the municipalities is detailed in the affidavit of Mr. Scott, Exhibit K.1, and was further confirmed during oral testimony.

35. Admittedly, this is the stated understanding of the parties as it exists today. How should the Board assess the intention of the parties when the notes were issued? One approach, which is routinely used by the courts is to ask: What did the parties actually do?

36. None of the Parties dispute the fact that ORPC consistently paid interest at a fixed rate of 7.25% every year since market opening (2002). This fact is directly relevant because the board’s current cost of capital policy was not released until late 2009. Prior to 2009—before anyone knew what the Board’s cost of capital policy would be or how it would apply the parties had consistently acted for over seven (7) years on the basis of the notes having a fixed interest rate of 7.25%. The parties actions were not biased by a particular policy outcome (unlike the submissions of the

Parties – which have a singular goal of achieving a lower debt rate). Rather, in this case, actions speak louder than words.

37. Another approach which is routinely used by the courts is to look at other documentary evidence of the terms of the notes. This will be addressed in greater detail below.

C.1 Allegations that there was something improper about BLG's involvement.

38. In argument, SEC has made allegations that something improper occurred as a result of Borden Ladner Gervais LLP ("**BLG**") being involved in the creation of the replacement notes. The Applicant denies these allegations.

39. On Wednesday, March 10, 2016, BLG was retained to advise and assist the Applicant in connection with the replacement of four (4) original promissory notes.

40. The Applicant, instead of retaining local counsel, chose to retain BLG, a national full-service law firm with over 700 professionals, because (1) BLG helped identify that the notes could in-fact not be found; and (2) the banking lawyers at BLG have experience and expertise in how to handle lost promissory notes in accordance with governing law.

41. While Mr. Vellone acted as client relationship lawyer, Mr. Vellone <u>did not</u> prepare the replacement notes (it is not his area of expertise). Rather, and as was explained during argument-in-chief,[9] banking lawyers in BLG's financial services practice advised on and prepared the replacement notes.

42. BLG prepared the replacement notes in a manner consistent with its legal and ethical obligations, its reputation for professional excellence, in accordance with the law governing lost promissory notes (described above), and in accordance with the same evidence which the Board has before it in this proceeding.

C.2 Are the replacement notes new affiliate debt?

43. Staff has suggested that the four (4) replacement notes "should be considered as new affiliate debt, as there is no evidence of the original note."[10] On this basis, Staff suggest that the Board's findings in its Niagara-on-the-Lake Hydro ("NOTL") decision in EB 2008-0237 should apply. The Applicant has four submissions in response.

[9] Tr. Pg. 112, Lines 11-20.
[10] Tr. Pg. 135, Lines 10-16.

44. First, at law, a missing piece of paper does not negate the existence of a legally binding contract. A person still has the right to sue for payment under a lost promissory note pursuant to Section 156 of the BEA (the legal obligation remains). This is because what we look for is offer, acceptance and consideration. There is no doubt that this occurred. There are transfer bylaws that clearly indicate that assets, liabilities, employees, were transferred into the utility corporation, and in return for that transfer, shares and promissory notes were issued. The principal, term (20 years from market opening), and other key terms and conditions of each of the promissory notes are known and not contested by any Party.

45. Staff's argument is premised on speculation that the original promissory notes never existed. The evidence is clear that the original promissory notes could not be found.[11] However, the evidence is also clear that the Applicant simply does not know why the original promissory notes could not be found.[12] Any attempt to explain why the original promissory notes could not be found is mere speculation. This is why Mr. Scott in response to Mr. Shepherd's questioning qualified his response with: "might be fair to say that they just were not done, yes." Mr. Scott was responding to a speculative question, with a speculative answer.

46. Second, like other contracts, consideration must be provided for a promissory note to exist. This requirement is set out in Section 52(1) of the BEA, which explains the types of consideration that would be acceptable to form an enforceable promissory note. Staff has not explained what consideration has been given to ORPC to allow for the characterizing the replacement notes as "new affiliate debt". That is because no new consideration has been given and, consequently, a new debt obligation has not been created.

47. By contrast, the Applicant has clearly demonstrated that consideration did flow pursuant to the four transfer by-laws attached to Exhibit K.1. For example, Schedule G of the Pembroke Transfer By-law[13] states: "Consideration given for the transfer of assets, liabilities, rights and obligations shall be the issuance and allotment to the Corporation of the City of Pembroke of four thousand three hundred and sixty-four (4,364) fully paid and non-assessable common shares of Ottawa River Power Corporation, and the issuance by Ottawa River Power Corporation to the Corporation of the City of Pembroke of a Promissory Note having a principal amount equal to

[11] Four affidavits of loss can be found attached to Exhibit K.1.
[12] Tr. Pg. 30, Lines 14-16.
[13] Exhibit K.1, Tab C.

four million three hundred and sixty-four thousand ($4,364,000.00) dollars." The evidence is also clear that the term of the promissory notes continue until May 1, 2022.[14] They have not expired.

48. Third, Staff's argument ignores the terms of Section 155 of the BEA, which: (1) contemplates that promissory notes may be lost prior to their expiry; and (2) provides a clearly defined process pursuant to which a creditor may request, and can require, a debtor to issue a replacement promissory note.

49. This is exactly what happened in this case. It doesn't matter how or why a promissory note is lost. Rather, based on Section 155 of the BEA, affidavits of loss and indemnities were signed by each of the municipalities,[15] and in accordance with Section 155 of the BEA, four (4) replacement notes evidencing the original debt obligation were issued (collectively, the "**Replacement Notes**").[16]

50. Pursuant to the terms of Section 155 of the BEA, the Replacement Notes are legally binding replacements of the original promissory notes. They embody the original debt obligation and they are enforceable at law in accordance with their terms. They are not "merely argument" as suggested by SEC, and they are not "new affiliate debt" as suggested by Staff.

51. Finally, unlike NOTL, the Applicant was not at liberty to "re-negotiate" any of the terms of the Replacement Notes upon their issuance. Section 155 of the BEA clearly states that the replacement note must be "of the same tenor". There is clear evidence in the documentation, oral testimony, and behaviour of the Applicant and its affiliate parties that the original promissory notes had a fixed interest rate of 7.25%. Accordingly, the Replacement Notes, being issued in accordance with section 155(1) of the BEA, had to be on the same terms as the original promissory notes, being documentary evidence of the existing debt obligation which was and is continuing.

---

[14] Exhibit K.1, Tab J.
[15] Exhibit K.1, Tabs L, M, N and O.
[16] Exhibit K.1, Tabs P, Q, R, and S.

C.3 Are the notes callable on demand?

52. SEC states that "there is no evidence for or against" whether the debt is callable on demand. SEC goes on to suggest that the debt is in-fact callable because of the ownership relationship as between the Applicant and each of the municipalities.[17]

53. SEC's submission regarding the affiliate relationship between the municipalities and the Applicant is not a relevant consideration when determining whether or not the notes are callable on demand. If all affiliate debt was, because of the affiliate relationship, deemed to be callable on demand, then the provision of the Board's policy which applies only to affiliate debt with a fixed rate that is not callable on demand would be moot.

54. Rather, when preparing the Replacement Notes, BLG carefully considered Section 22 (1) of the BEA, which states that:

> A bill is payable on demand (a) that is expressed to be payable on demand or on presentation; or (b) in which no time for payment is expressed.

55. The time for payment of each of the promissory notes is clearly evidenced: it is 20-years from market opening, being May 1, 2022.[18] This, in turn, is properly reflected in the Replacement Notes.

56. As correctly noted by SEC, there is simply no other evidence that expressly makes the promissory notes payable on demand or presentation. By the application of Section 22(1) of the BEA, the promissory notes are therefore not payable on demand. This, in turn, is properly reflected in the Replacement Notes.

C.4 Do the notes have a fixed or variable interest rate?

57. Each of Staff, SEC and VECC argue that the promissory notes have a variable interest rate. The principal basis for this contention is the inclusion of the words "term and interest to be renegotiated annually" in each of the four transfer by-laws.

58. BLG carefully considered this wording in preparing the Replacement Notes and concluded that it is not indicative of a variable rate note. As summarized above, and as shown in the case law attached with this submission, the law is clear that an "agreement to agree" or an agreement to negotiate in the absence of some objective measure is void in law and unworkable in practice.

---

[17] Submissions of SEC at para. 5.1.4.
[18] Exhibit K.1, Tab J.

59. Therefore the words "term and interest to be renegotiated annually" must be struck as void for uncertainty, in the absence of **some other objective measure**. The words "to be renegotiated annually" is not sufficient in itself to discern the intent of the parties – some other objective measures would be required.

60. The evidence is that there is another objective measure for the term: being an agreed to amendment to set the term of the note at 20-years after market opening.[19]

61. The evidence is that the other objective measures available in respect of interest rate are:

   a. the "currently" 7.25% interest rate stipulated in each of the transfer by-laws;[20]

   b. the reference to a 7.25% interest rate in various ancillary documents;[21]

   c. the evidence that the 7.25% interest rate has been paid consistently since 2002 (the rate has never once varied);[22]

   d. the evidence that both ORPC and the municipalities have always understood that the notes to have had a fixed interest rate of 7.25%;[23] and

   e. the evidence that none of the municipalities would voluntarily agree to an interest rate of less than 7.25%.[24]

62. Each of these factors support a conclusion that the interest rate is fixed at 7.25%. This, in turn, is properly reflected in the Replacement Notes.

63. By contrast, there is simply no objective evidence to support the interest rate being a variable rate. In somewhat circular logic, the Parties each refer to the words "to be renegotiated annually" as evidence of a variable interest rate. That is not evidence of a variable rate, it is evidence of a void and unenforceable agreement to agree. What the law actually requires is other objective measures of the parties' intent.

64. Neither Staff nor VECC attempt to address this problem: that the very words they are relying on to support their submissions that the interest rate is variable amount to nothing more than an

[19] Supra note 14.
[20] Exhibit K.1, Tab C at pg. 31, Tab E at pg. 108; Tab F at pg. 123; and Tab H at pg. 131.
[21] Exhibit K.1, Tab D at pgs. 97 and 98, and Tab K at pgs. 168 and 169.
[22] Exhibit 5, Page 15, Lines 8-9.
[23] Tr. Pg. 59, Lines 18-19; Pg. 71, Lines 3-5; Pg. 80, Lines 19-21; and Pg. 81, Lines 1-4.
[24] Exhibit K.1, para. 23.

"agreement to agree" that is void at law. They deliberately avoid this legal truth, despite the fact that the Applicant made this issue clear in its argument-in-chief. [25]

65. SEC, to its credit, does attempt to address this issue in its submissions, arguing that: "With respect, that is not the law. There is no agreement to agree. There is an agreement to negotiate, and as a matter of Canadian law if the intention of the parties is to negotiate, and it is expressed in a binding way, the parties are obligated to negotiate. Failure to do so is a breach of the contract."

66. SEC cited no case law to support this assertion. By contrast, the Applicant has cited specific case law, including quotations from legal texts, and has included that case law in its submissions. Perhaps, if SEC had made reference to the cases they would have realized that their argument was exactly the issue that was litigated in *Mannpar Enterprises Ltd. v. Canada* (described above and attached). The court in *Mannpar* rejected the interpretation that SEC has proposed, concluding at paragraph 55 that, upon a review of the authorities, a renewal provision that required renegotiation was a mere "agreement to agree" and was void for uncertainty, creating no obligation to negotiate in good faith.

67. Each of the Parties also make reference to Sections 13(e) and (f) of the Shareholders' Agreement to argue that these terms make the interest rate on the promissory notes variable.

68. It is the Applicant's submission that Section 13(e) and (f) do not prescribe a variable interest rate. Rather they stipulate a maximum or upper limit on the interest rate payable under the terms of the promissory note. This, in turn, is properly reflected in the Replacement Notes.

69. It is worth noting that the Board had this same Shareholders' Agreement before it when it decided that the notes had a fixed interest rate during ORPC's last cost-of-service application (EB-2009-0165).[26] Both the Board, and Board Staff agreed, that the evidence supported the Board's finding that the interest rate was fixed.

70. This reflects an understanding that when the promissory notes were issued and the long-term debt rate was set, each of the Municipalities and ORPC accepted risk that the interest rates would inevitably shift over time. Interest rates could rise above 7.25% and the municipalities would accept a lower market interest rate until the note expired. And interest rates could fall below

---

[25] Tr. at Pg. 114, Lines 7-21.
[26] EB-2009-0165, Decision and Order, Pg. 20

7.25% and the municipalities would earn a higher than market interest rate until the expiry of the note.[27]

71. Pursuant to Section 13(e) and (f) of the Shareholders' Agreement, the interest rate of 7.25% <u>can never go up</u>. This clause reflects a shift in the allocation of risk, by providing a single narrow situation where the interest rate might be required to be adjusted downwards. It is not indicative of a variable rate note. Rather it provides a cap on a fixed rate note which reflects an understanding and concession that the Board's policies and approach may change over the term of the note.

[27] See also Exhibit K.1 at para. 23.

D. REPLY SUBMISSIONS: APPLYING THE BOARD'S COST OF CAPITAL POLICY

72. The Applicant's submits that since, on the facts as further described above, the Replacement Notes:

   a. are affiliate debt with a fixed interest rate of 7.25%;

   b. are not callable on demand; and

   c. have a fixed term that expires in May 2022,

   that in these circumstances, the Board's policy is to apply the lesser of: (i) the rate of the affiliate debt; and (ii) the deemed long-term debt rate at the time of issuance. This would result in the Board approving use of a long-term debt rate of 7.25%, in a manner consistent with the Board's decision in EB-2009-0165.

73. In this context, each of the Parties have argued that the Board should not apply its cost of capital policy in this case. Specifically:

   a. Staff argues:

   > "So when we are talking about the reasonableness of this rate, just to summarize, there is no evidence that we have on the record that this rate is a rate that is in the customer's interests. And when I say customer, I'm referring to the ratepayer versus the taxpayer.
   >
   > […]
   >
   > Board Staff is also concerned with having the shareholder benefit by having a higher interest rate note paid to it at the expense of the ratepayer. This is, in Staff's view, a prima facie conflict of interest that is occurring.
   >
   > So for these reasons, Board Staff submits that the reasonableness of a 7.25 percent rate, when looking at what today's current market rates are, is something that is not acceptable, in Staff's submission."[28]

   b. SEC argues:

   > "The argument from the point of view of the ratepayers starts with the recognition that the Applicant is seeking permission to pay above-market interest to its shareholder/debtholders, and to recover that interest from ratepayers. In normal circumstances, this would not be allowed, as it would be contrary to the statute that requires rates be "just and reasonable"."[29]

[28] Tr. Pg. 132 at Lines 9-13 and Line 26 to Pg. 133 at Line 6.
[29] Submissions of SEC at para. 6.1.1.

c. VECC argues:

> "To complicate ORPC's case further, the imposition of an above-market rate based on the scenario that ORPC entered into a 20 year term at a fixed rate of 7.25% collides with the reasonable fairness to their ratepayers that is required."[30]

74. This is not the first time that parties have sought to challenge an LDC's cost of capital by arguing that customer preference for lower rates should outweigh another RRFE objective: *financial viability*, which is achieved through a stable and predictable application of the Board's well understood policy on cost of capital.

75. We would refer the panel to three other decisions where cost of capital issues were raised by the intervenors: (i) the Board's Decision and Order in EB-2009-0139 dated April 9, 2010; and (ii) the Board's Decision and Order in EB-2009-0259 dated March 1, 2010; and (iii) the Board's Decision and Oder in EB-2013-0116 dated August 14, 2014.

76. The principle established by the Board in these cases is that the party proposing a departure from the Board's policy on cost of capital must support it with evidence (at pg. 12 of EB-2009-0139, pg. 18 of EB-2009-0259, and pg. 9 of EB-2013-0116).

77. We have already addressed the challenges to the underlying evidence in the section above. We will not repeat those submissions again here. Rather, this section of the reply will be limited to the policy issues raised by the Parties.

D.1 Prudence of management in entering into the promissory notes.

78. The Parties have challenged the prudence of ORPC in entering into these promissory notes. Specifically:

a. "The law is clear that utilities under cost of service are allowed to recover their prudently incurred costs of providing distribution services, but not more than that. Paying interest above market rates is prima facie imprudent."[31]

b. "While it is understandable that the Applicant could not force its shareholders to take a lesser interest rate, their failure to even look at the possibility was, it is submitted,

[30] Submissions of VECC at para. 39.
[31] SEC Final Argument, Para 6.1.1, Pg 10.

contrary to their obligations to the ratepayers, and contrary to their fiduciary obligations to the company."[32]

c. "So for these reasons, Board Staff submits that the reasonableness of a 7.25 percent rate, when looking at what today's current market rates are, is something that is not acceptable, in Staff's submission."[33]

d. "Board Staff also asked in its submissions whether or not it might be more prudent for management to have several loan agreements as opposed to one loan agreement over a fixed term of 20 years and one rate, and the answer to that question that it may be. Board Staff does submit that having only one note for a term of this length would be potentially -- or could be potentially imprudent."[34]

e. "To complicate ORPC's case further, the imposition of an above-market rate based on the scenario that ORPC entered into a 20 year term at a fixed rate of 7.25% collides with the reasonable fairness to their ratepayers that is required."[35]

79. Decisions of a utilities' management are generally presumed to be prudent. However, those decisions can be challenged on reasonable grounds. The test, when determining prudence, is whether a decision was reasonable <u>under the circumstances that were known or ought to have been known to the utility at the time the decision was made</u>. Hindsight should not be used in determining prudence.

80. However, each of Staff, SEC and VECC make the mistake of resting their submissions entirely on the benefit of hindsight. Specifically, they rely on the knowledge that market interest rates have gone down from 7.25% since the date the notes were first issued. Neither ORPC, nor any of the municipalities, knew how interest rates would change when the promissory notes were entered into. And it would be unreasonable to expect that ORPC or the municipalities could accurately predict exactly how interest rates would change in the future.

81. Prudence should not be assessed using a very narrow, single-factor lens. Rather, an assessment of prudence should account for all of the considerations relevant to a utility management's decision making. When considering ORPC's prudence as it relates to entering into these the

[32] SEC Final Argument, Para 6.1.8, Pg 11.
[33] Tr. Pg. 133 at Lines 3-6.
[34] Tr. Pg 132, lines 19-25.
[35] VECC Final Argument, Para 31, Pg 10.

promissory notes – the Board should take into account the circumstances more broadly. Each of Staff, SEC and VECC fail to account for the context - the implementation of the *Energy Competition Act, 1998*, including a new obligation imposed on municipalities to create new corporations pursuant to Section 142 of the *Electricity Act, 1998*, the subsequent transfer of assets, liabilities and employees into the utility.

82. In this context, the Applicant submits that the Replacement Notes were prudently entered into. Notably:

a. The issuance of both debt (in the form of promissory notes) and equity in consideration for the transfer of assets, liabilities and employees into an LDC was necessary to implement the Board's policy on capital structure at the time the notes were issued.[36]

b. The interest rate of 7.25% was equal to the Board's deemed long-term debt at the time the notes were entered into.

c. The Board's decision in RP-1999-0034 at para 4.2.9 states that "it is expected that, in the meantime, utilities will be making their capital financing decisions mindful of the application of the IPI to their operations and rates." Because of this, management of ORPC took an additional step to reduce risk. Specifically, management obtained legally binding commitments from each of the municipalities that the interest rate on the notes would be subject to a maximum rate not to exceed the rate permitted by the Board. This maximum rate ensured that the promissory notes would be consistent with the Board's application of the IPI. The maximum rate is a key feature in the Shareholders' Agreement and in the Replacement Notes.

d. It is prudent commercial practice for utilities to consolidate their debt needs into a single larger debt issuance, rather than multiple smaller debt issuances with different rates. A single larger instrument reduces overall transaction costs associated with each debt issuance and reduces administrative costs associated with managing multiple debt instruments which may come up for renewal at different times.

e. It is prudent commercial practice for utilities to enter into long-term debt arrangements (20 years or more) so as to better match their liabilities with the useful lives of their

[36] See the Board's Decision in RP-1999-0034 dated January 18, 2000.

underlying distribution assets. By entering into long-term debt with a fixed rate, the Applicant creates cost certainty for budgeting purposes and for ratepayers. This eliminates risk associated with refinancing, including the risk of rate shock should interest rates suddenly increase.

83. In short, the prudence of management's decisions should not be judged on the basis of information that was not available to management at the time the promissory notes were issued. Management should be given an opportunity to do their job: this means honouring existing legal obligations such as those detailed in the Replacement Notes, to avoid lengthy and protracted litigation. It also means searching for various options, including any possible lower cost options, for long-term debt to use once the Replacement Notes expire in May of 2022.

84. Several of the Parties argue that the Applicant was imprudent because they did not go back to the municipalities to ask for a lower interest rate. This illustrates just how little experience the Parties have with commercial debt arrangements. The promissory notes are fixed term, fixed rate notes. If the rate goes down, you don't go back and ask for a lower rate from the lender – they will simply say "no." The expectation in a commercial context is that the parties will honour their legal commitments. If the interest rate goes up, the lenders don't come back and ask for a higher rate – they too are expected to honour their legal commitments.

85. In this respect, the evidence is clear: Mr. Les Scott at paragraph 23 of his affidavit states (emphasis added): "I can speak on behalf of Pembroke, and I spoke with representatives of the other Municipalities, and can confirm that we do not agree to voluntarily reduce the fixed interest rate below 7.25%. There are two key reasons for this. First, we have budgeted for and rely on this interest income from ORPC. Second, the fixed interest rate reflects an agreed to allocation of risk which was accepted by both the Municipality and ORPC at the time the Promissory Notes were issued. When the long-term debt was issued with a fixed interest rate, the Municipalities and ORPC each accepted risk that the interest rates inevitably would shift over time. Interest rates could rise above 7.25%, and the Municipalities would accept a lower than market interest rate until expiry of the note. And interest rates could fall below 7.25%, and the Municipalities would earn a higher than current market interest rate until expiry of the note."[37]

[37] Exhibit K.1 at para. 23.

86. Consider for a moment - after you lock-in your mortgage for 5 years at a fixed rate - would you go back to the bank in year 3 and ask for a lower interest rate because interest rates have go down? Would you not expect the bank's answer: "no, that's not the deal." In addition, would you not also be concerned that your lender would interpret your request as saying: "I don't want to honour our existing contract anymore - would you be willing to break it so I can get a better deal now?" You might be concerned about looking foolish. You might be concerned about losing credibility with your bank.

D.2 The Applicant has discharged its burden of proof.

87. The Applicant concedes that this Board panel must determine the debt treatment, including the rate allowed based on the record before it and considering the Board's policy and practice. In the Applicant's submission, it has discharged its burden of proof to establish the need for and prudence of its actual and forecasted debt, including the cost of such debt.

88. The dispute in this proceeding has arisen principally because the promissory notes were lost and replaced in accordance with the process stipulated in the BEA. In this regard, the Applicant has erred on the side of full disclosure. The Board has copies of the Replacement Notes – which at law are evidence of the original promissory notes. The Board also has been briefed on the law governing the replacement of lost promissory notes, and how that law was applied in these circumstances. Finally, the Board also has copies of all of the original documentation that is available. Nothing was omitted, including documents that create confusing and messy facts – such as "agreements to agree." Everything has been done above board, and subject to the full scrutiny of the Board's regulatory process. The Applicant has stood up to this scrutiny, and for each criticism has provided a clear a cogent explanation of what was done and why.

89. The best evidence the Board has before it is reflected in the terms of the Replacement Notes, which at law are evidence of the original promissory notes. The evidence is that the Applicant does have a need for its forecasted debt cost. The Applicant is party to four (4) legally binding promissory notes. Each have a fixed term expiring in May of 2022, a fixed interest rate of 7.25%, and they are not callable on demand.

90. The Board's policy in this context is:

> "For affiliate debt (i.e., debt held by an affiliated party as defined by the Ontario Business Corporations Act, 1990) with a fixed rate, the deemed long-term debt rate <u>at the time of issuance</u> will be used as a ceiling on the rate allowed for that debt."

91. The Board's policy strikes an effective balance between preserving the financial viability of utilities, on the one hand, and protecting ratepayer interests on the other. It is intended to honour the commercial arrangements and the legitimate expectations of affiliate debt holders. However, it also imposes a mandatory ratepayer protection, by imposing a ceiling or maximum on the rate that is allowed for that affiliate debt.

92. The ceiling stipulated in the Board's policy is not today's market rates. Rather, it is the Board's deemed long-term debt rate at the time of issuance. It is <u>7.25%.</u>

93. The Board panel could elect not to apply its policy to the Replacement Notes in this case. However, in the Applicant's submission it would seriously undermine the intent of the Board's own cost of capital policy.

94. The evidence on the record is clear: each of the four (4) municipalities have a legitimate expectation to earn the agreed-to 7.25% fixed rate of interest on the debt that is owed until that debt expires in 2022. A 7.25% interest rate is consistent with the Board's policy on cost of capital, has previously been approved by the Board, and reflects an agreed-to allocation of risk that was established prior to market opening.[38] The evidence elicited by Staff is also clear that the municipalities rely heavily on this investment income to fund their municipal operations, and that the loss of this income would have dramatic consequences to each of the municipalities.[39]

95. If the Board chooses not to apply its cost of capital policy to the facts of the Replacement Notes in this case, it will have several negative impacts that will affect customers.

96. First, access to capital (whether debt or equity) will become more difficult for the Applicant. Lenders and investors will question whether the Board will in the future again choose to disregard a consistent, stable and predictable application of its cost of capital policy in favour of lower rates. Return on investment would be less certain. And the cost of capital would increase. Second, a certain class of investor with a particularly low risk tolerance may become disheartened by the Board's decision in this case and in the future may withhold future capital

---

[38] Exhibit K.1.
[39] Tr. at Pg. 86, Line 3 to Pg. 87 at Line 16.

contributions or loans, or may choose to divest themselves of their existing equity and/or loan interests.

97. Put simply, the benefits of applying the Board's cost of capital policy in a stable, consistent and predictable manner is that it preserves the ongoing financial viability of the Applicant. It prevents an increase in the cost of capital in the future (which would be added to account for regulatory uncertainty if the Board choose not to apply its policy). And it prevents the risk of outright capital flight.

98. The Applicant has discharged its burden of proof and as the Board panel, you have an opportunity to do right by the municipal debt holders while still satisfying your obligation to protect ratepayer interests. The decision is yours.

E. CONCLUSIONS

99. For all of the foregoing reasons, ORPC submits that the Board should make an order for just and reasonable rates in the test year approving the Applicant's proposed cost of long term debt rate of **7.25%,** which is a direct application of the Board's policy on cost of capital to the terms of promissory notes, as supported by the oral evidence of Mr. Scott and Ms. Donnelly, the Replacement Notes filed in this hearing, and the ancillary documents supporting the replacement notes. The 7.25% is directly reflective of the Applicant's actual cost of long-term debt as evidenced by over 15 years of practice.

All of which is respectfully submitted this 13th day of April, 2016.

Original signed by John A.D. Vellone

John A.D. Vellone

APPENDIX A: BILLS OF EXCHANGE ACT

***Exerts of the Bills of Exchange Act*, R.S.C., 1985, c. B-4**

22 (1) A bill is payable on demand
(a) that is expressed to be payable on demand or on presentation; or
(b) in which no time for payment is expressed.

[…]

52 (1) Valuable consideration for a bill may be constituted by
(a) any consideration sufficient to support a simple contract; or
(b) an antecedent debt or liability.

[…]

155 (1) Where a bill has been lost before it is overdue, the person who was the holder of it may apply to the drawer to give him another bill of the same tenor, giving security to the drawer, if required, to indemnify him against all persons whatever, in case the bill alleged to have been lost is found again.

(2) Where the drawer, on request, refuses to give a duplicate bill, he may be compelled to do so.

156 In any action or proceeding on a bill, the court or a judge may order that the loss of the instrument shall not be set up, if an indemnity is given to the satisfaction of the court or judge against the claims of any other person on the instrument in question.

[…]

176 (1) A promissory note is an unconditional promise in writing made by one person to another person, signed by the maker, engaging to pay, on demand or at a fixed or determinable future time, a sum certain in money to, or to the order of, a specified person or to bearer.

[…]

186 (1) Subject to this Part, and except as provided by this section, the provisions of this Act relating to bills apply, with such modifications as the circumstances require, to notes.

APPENDIX B: BANK OF NOVA SCOTIA V. SHARRUN

See attached.

Indexed as:

Bank of Nova Scotia v. Sharrun

Between
Bank of Nova Scotia, Plaintiff, (Respondent), and
Kenneth Sharrun, Defendant, (Applicant)

[1990] A.J. No. 1120

No. 9003 16694

Alberta Court of Queen's Bench
Judicial District of Edmonton
(In Chambers)

Master Funduk

December 14, 1990

R. Max Gold, for the Plaintiff.
Lister & Associated, for the Defendant.

MEMORANDUM OF DECISION

MASTER FUNDUK:--

Facts

The Defendant applies to set aside the default judgment. The only issue is whether a triable issue is disclosed. The nub of the claim is found in paragraph 2 of the statement of claim:

> 2. The Plaintiff claims against the Defendant for the sum of $6753.05 for monies owing under a Promissory Note which the Defendant promised to repay and interest at the rate of 15.25% per annum from August 31, 1990 to and including the date of Judgment, which interest the Defendant agreed to pay.

The nub of the defences are found in paragraphs 7 to 10 of the Defendant's affidavit:

> 7. The alleged Promissory Note was executed as collateral security to a Chattel Mortgage on a motor vehicle I purchased. At the time I negotiated the terms with the Plaintiff, the Plaintiff requested a shortened term of loan with hight monthly payments and then represented to me that if I had difficulty making the payments, it would be willing to renegotiate the loan, extending the term of the loan thereby creating lower monthly payments.
> 8. Subsequently, I lost my employment and could no longer manage the high monthly payments. I requested of the Plaintiff a renegotiation of the term of the loan but the Plaintiff refused to renegotiate and it repossessed my motor vehicle and subsequently sold it. I relied on the initial representations of the Plaintiff to renegotiate the loan when entering into the alleged contracts to my detriment.
> 9. Further, and in the alternative, I am informed by my Edmonton Solicitor and do verily believe that the alleged Promissory Note is unenforceable on its face because it does not state that I have received valuable consideration for entering into it, rather it states that if such a sum were paid to me, then I would repay it in such a manner, thus that it is not a contract but merely a promise on a promise. Attached hereto as Exhibit "C" is a copy to the alleged Promissory Note.
> 10. Further, and in the alternative, the alleged Promissory Note was never presented to me for my acceptance, pursuant to the Bills of Exchange Act, thus the Plaintiff's action herein is premature.

There is no dispute that the Defendant did obtain a loan from the Plaintiff. The "promissory note" shows that the total loan was for $23,498.02, to be paid by a payment of $794.38 on January 1, 1989, then 35 equal monthly payments of $656.93 and the balance on December 1, 1991.

One

An agreement to re-negotiate is not enforceable in law because it is an agreement to agree. To the extent that the Defendant's position is that there was an agreement to renegotiate the position does not show a triable issue.

To the extent that the Defendant says that a representation was made to him, that he relied on it and prejudicially altered his position the matter should more properly be one of a counterclaim, not a defence.

More important, what is the possible prejudice? The best the Defendant can say is that he would not have taken out the loan. But it cannot be prejudice to require the Defendant to pay an indebtedness. He got the loan and he had the benefit of the loan.

The inability of the Defendant to repay the loan was not brought about by the Plaintiff. The Defendant fell on hard times. That is the cause of his problem with the plaintiff.

I do not see a possible defence in paragraphs 7 and 8.

Two

Whether the document is a promissory note is irrelevant. This action is between the original parties so the document's value is evidentiary. Even if the document is not a promissory note it evidences a contract between the parties.

The Defendant is liable in debt. It is not necessary to label the document.

The document shows a loan of $23,498.02 to be repaid in a certain manner. It is not disputed (and more important no evidence by the Defendant to dispute it) that the Defendant has defaulted in making the payments called for.

The document allows the Plaintiff to accelerate the balance in the event of default. The statement of claim does just that.

I do not see any triable issues in paragraphs 9 and 10.

Decision

The application is dismissed with costs to the Plaintiff on the same column as costs were taxed at when judgment was entered.

MASTER FUNDUK

APPENDIX C: MANNPAR ENTERPRISES LTD. V. CANADA

See attached.

Indexed as:

Mannpar Enterprises Ltd. v. Canada

Mannpar Enterprises Ltd. (Plaintiff)
v.
Her Majesty the Queen in Right of Canada (Defendant)

[1998] 1 C.N.L.R. 114

British Columbia Supreme Court

Macaulay J.

April 16, 1997

P.G. Voith and J.K. Wright, for the plaintiff
R.S. Whittaker and D. Patrick, for the defendant

The defendant, the federal Crown, with the approval by Band Council Resolution (BCR) of the Skyway Band, issued a permit to the plaintiff Mannpar Enterprises to remove sand and gravel from the Skyway Indian Reserve No. 5. The permit was issued for a period of five years and contained a clause granting a "right to renew" for a further five year period subject to "satisfactory performance and renegotiation of the royalty rate and annual surface rental." Under the terms of the permit, the plaintiff was obligated to carry out restoration work on the land subject to the permit within six months of the expiration of the permit. Through the original five year term commencing in 1989, the parties agreed to a plan to carry out restoration work over a ten year period.

Shortly before the expiry of the original five year period, the plaintiff issued a notice to renew the permit but the Band and the Crown were not prepared to renegotiate the royalty rate before expiration of the original permit. The plaintiff Mannpar took the position that the defendant Crown was repudiating its contractual obligation to renew, withheld payments due under the permit, and sued for damages.

The defendant counterclaimed for royalty payments withheld and for reclamation costs as set out in the permit. The defendant argued that the Band's express consent was required by ss.28(2) and 58(4) of the Indian Act and that the right to renew was void for uncertainty in that it was only an agreement to agree. The plaintiff argued that the right to renewal created an obligation to negotiate in good faith.

Held: Plaintiff's claim dismissed; defendant's counterclaimfor royalties allowed; defendant's claim for-reclamation costs dismissed.

1. The purpose of ss.28(2) and 58(4) of the Indian Act is to preserve and protect Reserve lands for the use of the Band and to allow the Band to make use of its interests in the Reserve lands in order to promote development on the Reserve.
2. The Band was bound by the terms of its BCRs. The initial BCR and the permit included the renewal provision. If the Band wanted to retain the right to refuse renewal of the permit that should have been included in the BCR and the permit. The Band consented to the whole agreement in its original BCRs and its consent is not required for the renewal. Sections 28(2) and 58(4) of the Indian Act should not be read restrictively to require consent at every stage of the permit process, including renewal.
3. The renewal provision was a mere agreement to agree and was void for uncertainty, creating no obligation on the Department of the Band to negotiate in good faith. An agreement to negotiate in the absence of some objective measure is void in law and unworkable in practice.
4. It was not possible to imply a term requiring good faith negotiation. The plaintiff must convince the court that an obligation to negotiate is not merely reasonable or desirable in light of the contract, but actually necessary to give business efficacy to the contract. Absent some agreement between the parties that renewal rates were to be fair market value, there were no means of measuring good faith in the negotiation process
5. The plaintiff conceded that the royalties were owing.
6. The claim for reclamation costs was rejected. It is clear that the reclamation was intended to occur over ten years and the plaintiff, through no fault of his own, did not have an opportunity to work over the ten years. The plaintiff is relieved of the reclamation responsibilities that would have been incurred in the second term.

---

1 **MACAULAY J.**:-- The plaintiff Mannpar Enterprises Ltd. ("Mannpar") seeks damages for breach of contract against the Federal Crown arising out of an alleged failure of the Department of Indian Affairs (the "Department") to renew a permit, by the terms of which, Mannpar was entitled

to extract sand and gravel on the Skway Indian Reservation No. 5 located near Chilliwack, B.C. (the "Reserve"). Rempel Bros. Concrete Ltd. ("Rempel") or its subsidiary Steelhead Aggregates Ltd. ("Steelhead") extracted, removed and sold the sand and gravel pursuant to a contract with Mannpar.

2 At all times, the Department was required to act in the best interests of the residents on the Reserve (the "Band"). Some members of the Band were employed as part of the operation by Rempel.

3 The permit was dated August 25, 1987, and was between Her Majesty the Queen in Right of Canada as "grantor" and the plaintiff as "permittee". The term of the permit commenced on January 1, 1988 and extended for a five year period ending on December 31, 1992 "without any further notice as to its termination". By amending agreement dated August 31, 1988, the initial term was extended to August 31, 1993. Under the permit the plaintiff was entitled to remove sand and gravel up to a total of 6 million cubic metres (3 million tonnes).

4 The plaintiff was required to make certain payments as follows:

(a) A royalty at the rate of $0.72 per cubic metre of sand and gravel removed from the permit lands during the period January 1, 1988 to December 31, 1988 and $0.92 per cubic metre thereafter until the expiration of the term.

(b) A royalty prepayment of $53,200.00 payable in advance of the 1st day of January in each and every year of the term.

(c)

(i) A clear yearly rental of $450.00 per hectare on all working area plots under operation.

(ii) A clear yearly rental of $15.00 per hectare on all the permit lands due in advance of the 1st day of January in each and every year of the term.

(d) Interest on any royalty monies outstanding at a rate equal to the prime lending rate of the Bank of Canada.

5 Royalty monies were to be accompanied at the time of payment by crusher yardage tally slips satisfactory to the Department as well as a statutory declaration certifying the amount of sand and gravel taken.

6 There were a number of other clauses in the permit, some of which are particularly relevant to the issues in this lawsuit. They are as follows:

7. The Permittee shall have the right to renew this Permit for a further five (5) year period subject to satisfactory performance and renegotiation of the royalty rate and annual surface rental. Under no circumstances shall the royalty rate or surface rental be less than the rates received in the preceding term.

10. The Permittee will provide the Grantor with a performance bond, or an irrevocable letter of credit valid until July 31, 1993, or a damage deposit, in the amount of Five Hundred Thirty Thousand Dollars ($530,000.00). Upon restoration of the permit lands to a condition satisfactory to the Grantor, any portion of the performance bond, irrevocable letter of credit or damage deposit not utilized pursuant to Clause 20(e) hereof, or used to pay outstanding royalties or rentals pursuant to Clause 5 hereof, shall be refunded to the Permittee.

18. Where, in the opinion of the Grantor, the Permittee has breached a condition of this Permit or failed to perform any of the covenants or obligations contained herein, the Grantor may, by notice in writing, order the Permittee to remedy the breach or perform the covenant or obligation. Where the Permittee has not complied with an order within thirty (30) days of the receipt of that order, the Grantor may:

    (a) take whatever measures are necessary to comply with the terms of such order and the Permittee shall reimburse the Grantor for the total costs of taking the measures, together with interest at the prime rate as and from the time that the costs were incurred by the Grantor. The Permittee shall also pay costs on a solicitor-client basis of any legal action taken by the Grantor to recover any amount payable herein;

    (b) cancel this Permit by giving notice in writing to the Permittee and thereupon this Permit shall be terminated.

20. Upon the expiration or sooner determination of this Permit, the Permittee shall:

    (a) cease and desist all operations involved in the extraction, processing and removal of sand and gravel from the permit lands;

    (b) peaceably surrender and give up possession of the permit lands, removing therefrom any stockpiled, crushed or processed sand and gravel within ninety (90) days and all vehicles, machinery, equipment or constructions within six (6) months;

(e) clean up and restore the permit lands to the satisfaction of the Grantor within six (6) months ... Mined out gravel areas are to be backfilled with inert natural materials including selected construc-tion material, subject to approval by the Federal and Provincial Environmental authorities and the Grantor. The Permittee shall be allowed to backfill the mined out gravel areas to the average elevation existing prior to excavation on the working area plot or to the average elevation plus two (2) metres. Failure of the Permittee to restore the permit lands to the satisfaction of the Grantor will result in restoration being undertaken by the Grantor. The cost of such restoration will be supported firstly by means of the damage deposit, irrevocable letter of credit or performance bond and secondly, should this prove insufficient to complete restoration, the remaining cost of restoration shall be recovered from the Permittee together with interest at the prime rate on all monies outstanding as and from the time the costs were incurred by the Grantor;

23. The Permittee shall hire a minimum of fifty (50) percent of the labour requirement from the Skway Band or other Indian Bands in the area, with the approval of the Skway Band Council, provided they have the required capacity and availability to work or supply a given good or service on a basis which is competitive both as to price and quality with other equally available sources but excluding trucking, loading and office staff, at a minimum hourly rate of Seven Dollars ($7.00) per hour.

26. The rights granted by this Permit shall not be assigned or otherwise transferred or subleased without the prior written consent of the Grantor, which consent shall not be unreasonably withheld.

7 Although the royalty rate relates to cubic metres, it is more convenient to convert it to metric tonnes, as most of the witnesses did. There are roughly 2 tonnes per cubic metre and, accordingly, the royalty rate at the end of the term of the permit was approximately $0.47 per tonne.

8 It is clear, in my view, that the initial permit was granted to Mannpar with the consent of the Band. The Band Council passed a Resolution ("BCR") dated August 25, 1987 consenting to the granting of a permit to Mannpar which contained the following term:

> Mannpar shall be allowed to renew this permit for a further 5-year term subject to satisfactory performance and renegotiation of the royalty rate and surface rentals with the Skway Band.

9 Then, at the written request of the Department, the Band Council passed a further BCR on September 23, 1987 as follows:

> That we substantially agree to the terms and conditions of the attached Sand and Gravel Permit No. MP 4014 which reflect the terms and conditions of our BCR No. 87-88-570-13, dated August 25, 1987 (copy attached).

10 The BCR dated August 25, 1987 expressly contemplated renewal, albeit subject to renegotiation with the Band. The second BCR expressly approves the permit, which sets out a right of renewal. The only difference is that the permit is silent as to whether or not renegotiations are to be with the Band.

11 After obtaining the permit, Mannpar entered into an agreement dated November 4, 1988 with Rempel.

12 The relevant provisions of that agreement are as follows:

> 1. Subject to the provisions of this agreement Mannpar agrees to assign to Rempel the exclusive right to excavate and remove aggregate and sand, for the purpose of sale by Rempel to third parties, pursuant to the conditions in the Skway permit and amendments thereto, and Rempel agrees to accept that assignment and sublease subject to any terms and reservations herein set forth.
> 2. The term hereof shall be either until Rempel may be in breach of any of subparagraphs 2(a), (b), (c) or paragraphs 5 or 10 of this agreement, or five years from September 1, 1988, or until Rempel has removed a total of 2,500,000 tonnes, whichever event may first occur; PROVIDED that Rempel shall in each year take a minimum number of tonnes of aggregate or sand pursuant to the permit, as follows:
>
>   (a) In the first year of the agreement Rempel agrees to remove a minimum of 200,000 tonnes prior to September 1, 1989, or pay to Mannpar on or before October 1 of said year .427 dollars per tonne for each tonne that they are short of the 200,000 tonnes, in order to retain the right to continue removing any aggregate or sand from the site, granted pursuant to this agreement;
>
>   (b) In subsequent years of the agreement Rempel agrees to remove the minimum of 300,000 tonnes prior to September 1 of each year, or pay to Mannpar on or before October 1 of said year .427 dollars per tonne for each tonne that they are short of the 300,000 tonnes in order to retain the right to continue removing any aggregate or sand from the site, granted pursuant to this agreement;

(c) If in any year Rempel should remove the amounts required by 2(a) and (b) herein but fail to take 500,000 tonnes on or before September 1 of that year, Rempel may keep the aforesaid exclusive rights by paying to Mannpar, in addition to all other payments due Mannpar, on or before October 1 of said year, a sum equal to .427 dollars per tonne that Rempel was short of the 500,000 tonnes.

13 The agreement provides for various payments to be made by Rempel to Mannpar. The payments included a non-refundable payment of $250,000.00 upon execution of the agreement as well as royalty payments in relation to aggregate or sand taken and sold by Rempel. The royalty payments were calculable as follows:

(a) For all aggregate or sand that Rempel sells for $6.25 average or less, the sum of $1.00 per tonne, and
(b) For all aggregate or sand that Rempel sells for more than $6.25, a sum equal to 7.5% of the gross sale price received by Rempel together with a further $0.67 per tonne, and
(c) Any aggregate or sand used by Rempel and not in fact sold to a third party shall be deemed to be sold at a price equal to $0.50 per tonne less than the current price charged by Rempel to third parties as of the date the aggregate or sand is removed from the site by Rempel.

14 Some of the other terms of the agreement are also significant. They are as follows:

11. Rempel agrees to abide by and follow all the terms and conditions set forth in the Skway permit and amendments thereto.
12. Rempel agrees to pay for and provide the operational plan that is required by the terms of the Skway permit and amendments thereto.
13. Rempel agrees to remove all topsoil and over burden and place same in locations upon the site as directed by Mannpar from time to time.
16. Unless otherwise instructed by Mannpar, Rempel agrees that all waste, over burden, and sand shall be replaced by Rempel into any depressions created as a result of the removal of aggregate from the said permit site. However, Mannpar shall spread and level all such waste, over burden and sand.
22. Mannpar agrees that Rempel shall have the right to renew this agreement for a further five year term, if the Skway permit and amendments thereto is extended for a further five years, upon payment to Mannpar of a further Two Hundred Fifty Thousand ($250,000.00) Dollars upon the same terms as this agreement sets forth, but provided that the price per tonne to be paid to Mannpar shall be adjusted between the parties to ensure that Mannpar receives the same net payment after deducting any royalties and bonds

> payable by Mannpar pursuant to the Skway permit and amendments thereto but in the event Rempel removes more than 2.5 million tonnes they shall pay an additional $0.10 per tonne for a total of $1.10 per tonne.

15 After obtaining the permit the plaintiff was required to commission certain consultants' reports and obtain various government approvals. It took a considerable period of time for Mannpar to obtain the necessary approvals. As a result, the commencement of the permit was delayed approximately eight months and the first term extended accordingly, as indicated earlier in these reasons. Mannpar in fact commenced operations in May 1989.

16 Mannpar's business plan for the operation was based on 10 years and much of the regulatory approval within the Department was predicated on the expectation that Mannpar would extract sand and gravel over a 10 year period, during which time Mannpar would also carry out its reclamation responsibilities under the terms of the permit. The foregoing is not, however, reflected in the initial 5 year term of the permit and could only be achieved by renewal.

17 In early 1993, Mannpar gave written notice of its intention to renew the permit for an additional term of 5 years commencing September 1993. In spite of Mannpar's repeated attempts to renegotiate the royalty rate for the purpose of the renewal, neither the Department nor the Band were prepared to do so prior to the expiration of the original permit on August 31, 1993. Ultimately, Mannpar took the position that the Department was repudiating its obligation to renew and elected to accept the repudiation and sue for damages.

18 In light of my conclusion as to the enforceability of the renewal clause, it is unnecessary to set out my findings respecting the attempts to negotiate the renewal in detail. On all of the evidence, I have no hesitation in concluding that the Band was not prepared to accede to a renewal of the existing permit for a further five year term, although the Band may have been prepared to negotiate a new permit, probably with a significantly shorter term and higher royalties. It is apparent from the evidence that the Band wanted a greater measure of control over the permitted operations. I also find that as at August 31, 1993, the Department was not prepared to agree to a renewal on any terms, absent the express consent of the Band. Although the question of Mannpar's compliance with the terms of the permit was raised, particularly by the Band, I am satisfied that Mannpar was substantially in compliance. It is noteworthy that the Department representatives at a meeting on August 31, 1993 were unable to provide a list confirming areas of noncompliance, nor had the plaintiff been given any notice of default as required by the terms of the permit.

Is The Band's Consent To Renewal Required?

19 The defendant argued that it is not enough to find consent to the original permit, but that the Band's express consent to the renewal is required by ss.28(2) and 58(4) of the Indian Act, R.S.C. 1985, c.I-5.

20 The sections provide as follows:

> 28.(2) The Minister may by permit in writing authorize any person for a period not exceeding one year, or with the consent of the council of the band for any longer period, to occupy or use a reserve or to reside or otherwise exercise rights on a reserve.
>
> 58.(4) Notwithstanding anything in this Act, the Minister may, without an absolute surrender or designation
>
> (a) dispose of wild grass or dead or fallen timber, and
> (b) with the consent of the council of the band, dispose of sand, gravel, clay and other non-metallic substances upon or under lands in a reserve, or, where such consent cannot be obtained without undue difficulty or delay, may issue temporary permits for the taking of sand, gravel, clay and other non-metallic substances upon or under lands in a reserve, renewable only with the consent of the council of the band, and the proceeds of such transactions shall be credited to band funds or shall be divided between the band and the individual Indians in lawful possession of the lands in such shares as the Minister may determine.

21 It must therefore be considered whether ss.28(2) and/or 58(4) create an additional requirement of Band consent for a permit renewal in the present circumstances.

22 There has been little jurisprudence regarding s.58 beyond Boyer v. The Queen (1986), 26 D.L.R. (4th) 284 [[1986] 4 C.N.L.R. 53, 65 N.R. 305], which dealt exclusively with s-s.(3) of s.58. That subsection deals with leases of land to band members by the minister. It is apparent that there is no express requirement for consent, unlike s-s.(4). The court rejected the argument that band council consent was required by necessary implication. In the circumstances, Boyer, supra, is of limited assistance.

23 I note that the subject of renewals is expressly dealt with in s.58(4)(b) of the Act, where Parliament has provided that renewals of temporary permits (issued in situations of emergency without band consent) may be granted "only with the consent of the council of the band". The permit in the case at bar is not a temporary permit. I agree with Mr. Voith, on behalf of the plaintiff, that if Parliament had intended that permits already containing renewal provisions and granted with band council consent should require the further consent of the band upon the renewal itself, one would expect such a requirement to have been expressly stated.

24 Most of the cases involving s.28 have dealt with the validity of reserve land dispositions where the absence of a proper s.28(2) permit was not in dispute. See for instance The Queen v. Devereux (1965), 51 D.L.R. (2d) 546 [[1965] S.C.R. 567] (S.C.C.), Springbank Dehydration Ltd. v. Charles, [1978] 1 F.C. 188 (T.D.) and Descoteaux v. Canada, [1995] F.C.J. No. 1353 [[1996] 1

F.C. 667, 109 F.T.R. 45] (T.D.). In the instant case, there is a proper s.28(2) permit. It is therefore necessary to refer to cases which have considered the purpose and effect of s.28.

25 The policy behind s.28 was considered at length by the British Columbia Court of Appeal in Opetchesaht Indian Band v. Canada (1994), 89 B.C.L.R. (2d) 145 [[1994] 5 W.W.R. 594, [1994] 4 C.N.L.R. 68], leave to appeal to S.C.C. granted (1994), 95 B.C.L.R. (2d) xxxiii. In that case, an Indian band applied to have a s.28(2) permit declared invalid. The permit was issued in 1959 and allowed B.C. Hydro to have a right-of-way for power lines through the band's reserve. The application was granted at trial on the basis that the indefinite length of the permit was not authorized by s.28. An appeal was allowed by the Court of Appeal, which stated that s.28(2) authorizes the granting of a permit for either a definite period or until the happening of a future event, the date of which cannot be known at the commencement of the term.

26 Taylor J.A., for the court, made some statements regarding the purpose of s.28 and the approach to be taken in interpreting it. He stated at page 148 [B.C.L.R.; p. 70 C.N.L.R.]:

> The overall purpose of the sections of the Act dealing with reserve land, as they stood at the time with which we are concerned, can in my view be shortly stated.
>
> Subject to very limited exceptions, their purpose was to preserve reserve land for the exclusive use and benefit of members of the band for whom title was held by the Crown unless and until the Crown, as represented either by the minister or the Governor-in-Council, and the band, through its council or by general vote, as specified in the particular provision, should together decide to transfer title to a third party or to grant to a third party some right to occupation or use. The Act contemplates that, with the concurrence of the Crown and the band, title to or rights to occupation or use of reserve lands may be transferred to third parties. Some of the amendments enacted in 1956 show an intention on the part of Parliament that increased authority be given to band councils to speak and act for their bands with respect to various aspects of band business.
>
> The fact that the federal authorities had a duty in exercising their powers over reserve land to endeavour to serve the best interests of the band for whom the land was held requires no emphasis. The existence of that impor-tant duty, which is dealt with in Guerin v. R., [1984] 2 S.C.R. 335 ... cannot, however, assist us in construing the provisions relevant to this appeal.

27 Taylor J.A. continued at pages 154-5 [B.C.L.R.; pp. 75-76 C.N.L.R.]:

> Having in mind that s.28 empowers the minister to make grants on behalf of the Crown on which the grantees and others must thereafter rely, a court ought not,

in my view, to conclude that Parliament intended to impose any restriction on its scope which is not apparent from the plain meaning of the section, unless such restriction clearly arises by implication from a fair reading of the whole of the statute.

I find myself unable to accept the submission made by counsel for the band that sections of the Act dealing with the granting of rights of occupation and use of reserve lands to third parties should be strictly construed so as to limit narrowly the circumstances under which it is possible to erode the "land base" held for the use and benefit of the band. That would in my view certainly be inappropriate in the case of those sections which permit such grants to be made only with the concurrence of the band. R. v. Devereux (1965), 51 D.L.R. (2d) 546 (S.C.C.), was cited in this regard for the band, and particularly the proposition stated by Mr. Justice Judson (at p. 550):

> The scheme of the Indian Act is to maintain intact for bands of Indians, reserves set apart for them regardless of the wishes of any individual Indian to alienate for his own benefit any portion for the reserve of which he may be a locatee.

But that case was concerned with the validity of a testamentary disposition made by an individual band member to a non-Indian. The statement cited does not seem to me helpful in the present case. While the policy of the Act is, of course, to preserve reserve land against dispositions to third parties made by individual band members it is equally the policy of the Act to permit the transfer of rights to third parties made by the Crown with the concurrence of the band itself - that is to say by vote of the members as a whole or by resolution of their council.

If in fact the grant in this case was not beneficial to the band - a matter yet to be decided, and on which other claims turn - that cannot influence us in interpreting the relevant provisions of the statute. These are provisions intended to enable the band, with the concurrence of the Crown, to get the best return from band property where it appears that this will be achieved by permitting third parties to use reserve lands on appropriate terms. The objectives of the statute would not, in my view, be served by placing a narrow interpretation on the scope of s.28(2). That would impede band councils in doing what seems to them best in the management of reserve lands, and cast doubt on the security, and therefore the value, of licences issued with their approval under the section. The right of

> alienation being an important incident of the ownership of property, it is not in my view appropriate that a court cut down that right by placing a narrow construction on those powers of alienation granted by the statute which are to be exercised with consent of the band council. [My emphasis]

28 The Court of Appeal identified two competing values behind s.28 and its related provisions. On the one hand, the land should be preserved for the band and protected from "erosion" by the Crown. On the other hand, the band should be allowed to make use of its interest in reserve land, in conjunction with the Department, in order to promote development on the reserve. The Court of Appeal interpreted the Act so as not to take away from a band's right to use its land in a way comparable to ownership, subject of course, to Departmental approval. The consequence of this however, is that a band will be bound by the terms of the permit it authorizes in attempting to encourage development.

29 This interpretation is also consonant with the purpose of s.58(4), supra, which allows for the sale of reserve resources for the monetary benefit of the band and its members (s-s.(5)). This interpretation of ss.28(2) and 58(4) enhances the band council's right to alienate its interest in reserve land to encourage development, and suggests that a band council must be bound by its consent where given.

30 Applying this interpretation to the instant case, ss.28(2) and 58(4) should not be read restrictively to require consent at every stage of the permit process, including renewal. The band was capable of disposing of reserve resources, with the Department's cooperation, in a way it saw fit, and is bound by the terms of its BCRs dated August 25 and September 23, 1987. Both the initial BCR and the permit included the renewal provision, albeit with different language. The wording of the renewal provision in both the BCR: "Mannpar shall be allowed to renew ...", and the permit: "The Permittee shall have the right to renew ..." make it clear that the renewal is at the option of the plaintiff, subject to the conditions later stated. If the band wanted to retain the right to refuse renewal of the permit, that could have been included in the BCR and the Department could have been instructed to include such a term in the permit. Instead, the Band consented to the renewal provision which was included in the permit and BCR. I therefore find that the band consented to the whole agreement in its initial BCRs and its consent was not required to the renewal.

Is The Renewal Clause Void For Uncertainty?

31 The principal argument advanced by the defendant is that the renewal term, clause 7 of the permit, is void for uncertainty in that it is only an agreement to agree. Clause 7 states:

> The Permittee shall have the right to renew this Permit for a further five (5) year period subject to satisfactory performance and renegotiation of the royalty rate and annual surface rental. Under no circumstances shall the royalty rate or surface rental be less than the rates received in the preceding term.

32 On its face, it appears to be a bare agreement to negotiate, qualified only by the reference to the minimum royalty and rental rates, namely those received in the first term.

33 Traditionally, agreements to negotiate or agreements to agree have been held to be void for uncertainty. The law in this regard was reviewed by Lord Denning M.R. in Courtney and Fairbairn Ltd. v. Tolaini Brothers (Hotels) Ltd., [1975] 1 All E.R. 716 [[1975] 1 W.L.R. 297] (C.A.). The agreement in that case involved the building of a motel, filling station and hotel. It included a statement that the parties would negotiate "fair and reasonable contract sums in respect of each of the three projects as they arise". Lord Denning concluded that the price of a building contract is of fundamental importance, such that there is no contract unless the price is agreed, or unless there is a method for determining the price independent of the two parties. If the price is left to the negotiations between the two parties, there is no enforceable contract. Lord Denning M.R. also stated that a contract to negotiate could not be recognized by the court because there is no way to estimate damages, since it is impossible to tell if the negotiations would have been successful.

34 One of the leading cases in British Columbia in this regard is Young v. Van Beneen, [1953] 3 D.L.R. 702 [8 W.W.R. (N.S.) 702] (B.C.C.A.). In that case, the tenant leased premises from the landlord for a period of three years. The lease contained an option which entitled the tenant to an additional three year term at a rental "to be agreed upon by the lessor and the lessee". The Court of Appeal determined, at page 704, that:

> An agreement for a lease, if its terms are sufficiently certain, may be specifically enforced, like any other contract, but if the parties fail to express what they mean with reasonable certainty, the agreement is unenforceable, and will be held void: ...

35 And, as well:

> It is to be observed that here the option clause does not provide for renewal of the lease. The lessee is thereby given "the first option to rent the building for an additional three-year period". No reference is there made to the terms of the new lease, other than its duration; nor is it made to appear with any degree of certainty, that the terms of the old lease were to apply to the new. Moreover, the rental is left to be determined by agreement between the parties. In my view, the clause is too vague and indefinite to be capable of enforcement, and does not confer upon the tenant any right to a tenancy which is enforceable in law.

36 Although it is arguable that the reference to "renew this permit" in the case at bar incorporates the other terms of the original permit by reference, there can be no doubt that the royalties and rents were left entirely to be determined by agreement between the parties.

37 A renewal term was held to be void for uncertainty in Calford Properties Ltd. v. Kelly's Billiards Ltd., [1973] 4 W.W.R. 532 (Alta S.C.). The renewal clause called for the renewal of the lease on the same terms as the original term, save for the rental which would be "in such sum as may be agreed upon by the lessor and the lessee". The court found that the essential matter of rent was left to be determined and was unenforceable.

38 In Nor-Isle Sales Ltd. v. Cadwallader (1977), 1 B.L.R. 256 (B.C.S.C.), an option to purchase at the end of the first year of a lease was held to be unenforceable because the price was left to further agreement by the parties. As the option was an essential term of the lease agreement, the entire agreement was rendered void by the vagueness of the option term.

39 In Allarco Developments Ltd. v. Novelty Pipe Shoppe Ltd. (1982), 47 A.R. 160 (Q.B. Master), there was a renewal clause in a commercial lease which provided for a renewal rent "agreed between the parties, but shall not be less than the rent reserved hereunder". The latter phrase closely mirrors the wording of the renewal clause in the case at bar. The master found that the inclusion of the lower limit on the renewal rent did not distinguish this case from the weight of authority which suggested that the court was being asked to supply an essential term to the contract. The option to renew was found to be void for uncertainty.

40 In Commertec Capital Corp. v. Stabler (1991), 16 R.P.R. (2d) 38 (B.C.S.C.), an option given to the vendor to purchase a residential unit to be developed on property she sold was held to be unenforceable because all the major terms were left to further negotiation. Here, since the option was an essential part of the purchase agreement, the whole contract was rendered unenforceable.

41 The plaintiff relies primarily upon Empress Towers Ltd. v. Bank of Nova Scotia (1990), 50 B.C.L.R. (2d) 126 [73 D.L.R. (4th) 400, [1991] 1 W.W.R. 537, 14 R.P.R. (2d) 115, 48 B.L.R. 212] (C.A.) in support of the proposition that while an agreement to agree may not be enforceable, an agreement which leaves the price to be negotiated can create an obligation to negotiate in good faith and an obligation not to withhold agreement unreasonably. The key words of the Court of Appeal appear on page 130:

> In my opinion, the effect of the requirement for mutual agreement must be that the landlord cannot be compelled to enter into a renewal tenancy at a rent which it has not accepted as the market rental. But, in my opinion, that is not the only effect of the requirement of mutual agreement. It also carries with it, first, an implied term that the landlord will negotiate in good faith with the tenant with the objective of reaching an agreement on the market rental rate and, second, that agreement on a market rental will not be unreasonably withheld.

42 The Court of Appeal in that case felt that implying the obligation to negotiate in good faith was necessary under officious bystander and business efficacy principles to give effect to a clause which was clearly intended to have legal effect. As the parties had agreed that there would be a right of renewal at prevailing market rental, that term should be given effect to.

43 The principle in Empress Towers, supra, was applied in Hirex Holdings Ltd. v. Chrysler

Canada Ltd. (1991), 16 R.P.R. (2d) 154 [1 B.L.R. (2d) 58] (B.C.S.C.). That case involved a similar renewal clause which left the renewal rent up to negotiation, based on the market value. Meredith J. held that there was an implied term to negotiate in good faith, and that the parties did negotiate in good faith and did not unreasonably withhold agreement. As the parties were unable to come to an agreement despite their good faith attempts, the renewal clause was held to be void for uncertainty.

44 Empress Towers, supra, was also mentioned with approval by the Supreme Court of Canada in Mitsui & Co. (Canada) Ltd. v. Royal Bank of Canada (1995), 123 D.L.R. (4th) 449 [1995] 2 S.C.R. 187, 142 N.S.R. (2d) 1, 407 A.P.R. 1, 180 N.R. 161]. That case involved an application by creditors to determine whether an option to buy helicopters amounted to a conditional sale under the Conditional Sales Act, R.S.N.S. 1989, c.84. The option included the following term:

> If this option is exercised, the purchase price shall be the reasonable fair market value of the helicopter as established by the Lessor.

45 In the course of his judgment for the court, Major J. stated that an option to purchase at fair market value can be enforced as it is an objective matter which can be determined by the court.

46 In relation to Empress Towers, supra, counsel for the defendant emphasized the Court of Appeal's assertion that an agreement to agree is not enforceable. Counsel also pointed to the words of Lambert J.A. at page 130:

> I do not have to decide in this case whether a bare right of renewal at a rental rate to be agreed carries with it an obligation to negotiate in good faith or not to withhold agreement unreasonably.

47 Earlier at page 129, Lambert J.A. also said this:

> On the other hand, it is well established that if all that the parties say is that they will enter into a lease at a rental to be agreed, no enforceable lease obligation is created. ... There may, however, be an obligation to negotiate.

48 One of the cases cited with respect to the foregoing is Calford, supra.

49 Counsel for the defendant also questioned the need to imply terms to ensure business efficacy where such a term is not necessary to the agreement. The law in this area was reviewed by the B.C. Court of Appeal in Olympic Industries v. McNeill (1993), 86 B.C.L.R. (2d) 273 [38 B.C.A.C. 254, 1994] 3 W.W.R. 268]. In that case, the trial judge had implied a term into a contract which required a former employee to repay monies advanced under a draw system where income was paid against future commissions. The Court of Appeal allowed the appeal, and concluded that for a term to be implied by the court it must be more than simply reasonable or logical or even preferable to the actual terms of the contract; the term must be necessary to give business efficacy to the contract. The onus is on the person asserting the implied term to persuade the court of its necessity.

According to Finch J.A. at page 280, "A higher burden of proof must be met, upon the authorities referred to above".

50 Defendant's counsel also pointed to a recent case of the House of Lords to suggest that where there is a term left to further negotiations, there is no obligation to negotiate in good faith. In Walford v. Miles, [1992] 2 A.C. 128, the House of Lords found that an obligation to negotiate in good faith was unworkable in practice and contrary to the adversarial position of parties involved in negotiations. The court stated that parties are entitled to use whatever tactics they want in negotiating, and further, are entitled to withdraw from negotiations at any time and for any reason.

51 On these bases, counsel for the defendant submitted that Empress Towers, supra, has not overruled Young, or Calford, supra, and that the general common law rule that agreements to agree or negotiate are void for uncertainty, is still the law in British Columbia.

52 Counsel for the plaintiff submitted that Empress Towers, supra, did change the law in this regard and has created an obligation to negotiate in good faith when there is a renewal term such as clause 7 of the permit agreement in the case at bar. Counsel referred to B.I.H. Investments Inc. v. Kim (5 January 1996) New Westminster S027979 (S.C.). That case involved a five year lease which left the rental rate for the last four years open to "be mutually agreed upon by both parties". The parties failed to agree on a rental rate after the first year. Leggatt J. found that the lease was for five years, not one year with a four year renewal, and that, according to Empress Towers, supra, there was an obligation to negotiate in good faith. The court found that the landlord had failed to negotiate in good faith by rejecting any proposal to sublease, rejecting arbitration and failing to provide copies of other leases in its complex. The court implied a term that the rent for the balance of the term would be market rent. It should be pointed out that in this case, Leggatt J. stated that he was acting under his general power to relieve against forfeiture in implying the term that rent would be market rent. As well, the decision in this case related to the original term of the contract rather than a renewal term. This case therefore has unique facts which do not easily fit with the facts of the case at bar.

53 In Hargreaves v. Fleming, [1995] S.J. No. 149 (Sask. Q.B.), a right to renew a lease at a rental "to be negotiated" without reference to market rate or any other mechanism for determination was held to create an obligation to negotiate. The court applied Empress Towers, supra, and concluded that the lease clearly created a positive covenant to negotiate. Importantly, the court found that while the parties could discuss any matters during negotiations, they could not insist on the other party accepting such matters as a condition of agreeing to a rental rate.

54 In Malahat Chalet Limited v. Pfizenmaier (4 April 1996), Victoria 92/9261 (B.C.S.C.), the court considered an agreement which, among other things, granted one party an easement to build a road over a portion of land, "mutually agreed on as to location". Murphy J. was called upon to determine the location of the easement. Referring to Empress Towers, supra, he determined that the clause above created an implied term that the parties were to negotiate in good faith. He also recognized that his task was made more difficult by the fact that the clause did not provide any objective criterion similar to "prevailing market rental". Murphy J. reviewed the evidence and suggested some principles for determination of the location of the easement. It should be pointed out that in this case, none of the parties were alleging that the easement clause above was void.

55 Upon a review of the authorities cited by the parties and the additional authorities referred to above, I have concluded that the renewal clause was a mere agreement to agree and should be declared void for uncertainty, creating no obligation on the Department or the Band to negotiate in good faith. The ratio in Empress Towers, supra, was explicitly limited by the Court of Appeal in that case. Subsequent cases either had an objective measure such as market rate against which to set the renewal or option price, or contained some unique characteristics or facts, such as the mid-term negotiation requirement and relief against forfeiture in B.I.H. Investments, supra, or the lack of an allegation that the term is void in Malahat Chalet Ltd., supra. Only the Saskatchewan case, Hargreaves, supra, implied a term requiring negotiation in good faith into a renewal clause which granted a bare right of renewal subject to negotiations. Considering the unfortunately broad wording of the renewal clause, which does not provide any objective measure of what the renewal rates would be, the long line of authority which precedes Empress Towers, supra, makes it clear that an agreement to negotiate in the absence of some objective measure is void in law and unworkable in practice. Lastly, the limits to the Empress Towers case, supra, necessitate a finding that the renewal clause is void as a mere agreement to agree.

56 I have also considered whether implying an obligation to negotiate in good faith would give effect to the contract, and if so, what that effect would be. Following the principles in Olympic Industries, supra, the plaintiff must convince the court that the term was not merely reasonable or desirable in light of the contract, but actually necessary to give business efficacy to the contract. Absent some agreement between the parties that renewal rates were to be fair market value, I have no means of measuring good faith in the negotiation process. Since it is inappropriate for the court to insert an essential term simply because it appears reasonable or desirable, then it follows that it would be inappropriate also to imply a term requiring good faith negotiations in order to achieve exactly the same result.

57 For the reasons outlined above, I find that the renewal term of the permit is void for uncertainty, and further, I am not prepared to imply a term requiring the defendant to negotiate in good faith. Accordingly, the plaintiff's claim is dismissed.

58 In the circumstances, I do not propose to assess damages for loss of opportunity to negotiate. To do so in this case would necessitate determining appropriate royalty rates between not only the plaintiff and the defendant, but also the plaintiff and Rempel. Absent an implied term in the agreements that the rates reflect market values, the exercise appears speculative at best.

Counterclaim

59 By counterclaim, the defendant claims that the plaintiff withheld royalty payments totalling

$159,883.00 due for the final three months of the first term. At commencement of trial, the plaintiff conceded that this amount was properly owing.

Reclamation

60 The defendant further claims reclamation costs pursuant to clauses 10 and 20(e) of the permit, supra. Brent Mann's father, John Mann, had been the principal officer of Mannpar. Since shortly before his father's death in early 1993, Brent Mann has taken over his role in Mannpar. He testified that the performance bond required by clause 10 was later changed to a damage deposit calculated at $0.15 per cubic metre, or about $240,000.00. The change was approved in an amendment to the permit dated August 31, 1988. Although it is correct that the plaintiff was required to "clean up and restore the permit lands to the satisfaction of the grantor within six (6) months", I have no evidence before me that the grantor has given notice of default pursuant to clause 18, supra, or undertaken the restoration itself, thereby entitling it to rely on the default provisions of clause 20(e).

61 Three reports respecting reclamation were prepared on behalf of Mannpar:

(1) First Lang Engineering report of February 16, 1989 (initial operational plan for Phase I excavation);
(2) Gaudry report dated April 8, 1990 (reclamation plan);
(3) Second Lang Engineering report of May 1991 (expanding operating pits from 6 to 18 hectares).

62 Each of the above were reviewed and approved by the Department and the Band Council.

63 The working area of the permit was originally set at two 6 hectare plots (Phase I). By written amendment to the permit dated August 14, 1991 the working areas for Phase I and for a new operating area known as Phase II were expanded to 18 hectares each. At the same time clause 10 was changed as set out above.

64 By agreement with the Band Council the plaintiff was able to use the sand and overburden mined from the Phase II pit to fill the expanded Phase I site. It was clear to all concerned that it would take several years to excavate Phase II and in particular that such work would extend well beyond 1993.

65 The defendant has made the following admissions in relation to the reclamation process:

5. The materials (top soil and sand) which were to be excavated from Phase II operating areas are ample to complete the reclamation activities necessary for Phase I.

The Defendant admits this allegation of fact.

71. In approving the Kip Gaudry Reclamation Plan, the Department understood that Mannpar's reclamation activities under that Reclamation Plan would extend into the second five year term of Sand and Gravel Permit No. MP-4014.

The Defendant admits that since Mannpar had commenced no reclamation activities by April 1990, given the Kip Gaudry estimate of four years to carry out the Reclamation Plan, that reclamation activities would extend beyond the first five years of the Permit.

73. In allowing Mannpar to extend and expand upon the operations within Phase I, the Department of Indian Affairs understood that Mannpar's reclamation obligations as originally contemplated by the Kip Gaudry and Associates' report, would necessarily be modified.

The Defendant admits this allegation of fact.

75. The Department of Indian Affairs understood that the reference in the Kip Gaudry report to having a final cover placed on the first quadrant within two years related to the original Phase I excavation site and not to the expanded Phase I operation.

The Defendant admits this allegation of fact.

76. The Department of Indian Affairs understood that by enlarging the area of operations within Phase I, the length of time required for reclamation of Phase I areas would necessarily be extended.

The Defendant admits this allegation of fact.

66 The first Lang Engineering report, supra, sets out the approved operational plan for Phase I. Figure 1 showing typical sections shows a final cap of clayey silt/topsoil. The Gaudry report, supra, was prepared "to clearly define the exact reclamation plan for phase I". At the time, Phase I was described as the first six hectare site. In a covering letter to the Department dated April 1990, Mr. Gaudry submitted the plan for approval; he expressly states that the reclamation of Phase I "will take approximately 4 years."

67 In his report, Mr. Gaudry allows for 0.5 to 1.0 metres of final cover. The approved final cover material is to be spread, compacted, and sloped. The area to be covered is to be broken into quadrants, with final cover placed on the first quadrant within two years. Although the report does not define approved final cover, Appendix 2, Figure 1, shows the use of clayey silt as capping material similar to the first Lang Engineering report, supra. In my view, the Department approved a reclamation plan for Phase I that was expected to extend into the anticipated renewal term of the permit and further, approved the use of clayey silt as a capping material.

68 It is apparent from the foregoing that the plaintiff and the defendant both proceeded in the expectation that there would be a renewal term to the permit thereby affording the plaintiff the opportunity to carry out its full reclamation responsibilities.

69 The second Lang report, supra, sets out the operational plan for Phase II, including site decommissioning and reclamation. Two further pits were proposed, only one of which was started during the first term of the permit. Part 3 of the report deals with reclamation and describes the objective as the creation of two recreational lakes for use by Band members and/or future campsites. This was to be accomplished, in part, by contouring the slope around the lakes in such a manner as to ensure stability and to allow recreational use. As well, a berm was to be built to the east of the proposed lake to divert surface run-off from nearby agricultural lands.

70 The Department retained Mr. Prashant Pandit, an environmental engineer, to provide an opinion as to the estimated cost of decommissioning the Phase I pit as well as the first Phase II pit, in accordance with the above reports.

71 With respect to Phase I, he concluded that final cover is required for 2.1 hectares at an estimated cost of $272,185.00. It is apparent that he defines final cover differently than Mr. Gaudry as he specifically incorporates the specifications set out in the B.C. Landfill Criteria by the provincial Ministry of the Environment, as follows:

> Final cover for landfill sites is to consist of a minimum of 1 metre of low permeability compacted soil plus a minimum of 0.15 metre of topsoil with approved vegetation established.

72 There is at least a quantitative, and perhaps, a qualitative difference between this requirement and the approved reclamation plan. Mr. Pandit views it as a qualitative difference as he explained in his evidence that he considered it necessary that the capping material used for final cover should be clay in order to provide an impermeable layer. This goes beyond the approved requirement in the case at bar and may exceed the provincial requirements as well. Mr. Pandit estimated the cost of clay as cover material at $210,000.00 plus a 5% contingency mark-up, approximately 81% of his total estimate for Phase I.

73 As I have observed earlier, the Department has not carried out any of the reclamation work itself. Accordingly, the actual cost of restoration remains unknown.

74 Although Mr. Pandit assumes that the reclamation obligation had to be carried out immediately upon determination of the first term, this ignores the fact that Mannpar, with the approval of the Department and the Band, expected the reclamation process to extend well into the anticipated renewal term.

75 In respect to Phase II, Mr Pandit recognized that the shape and contours of the first lake have been altered considerably by Rempel since August 1993. Accordingly, he limited his cost estimate to the projected cost of moving overburden stockpiles to create the berm to the east of the lake. That cost is estimated at $543,900.00. In cross-examination, it was apparent that Mr. Pandit did not appreciate that overburden had been stockpiled on behalf of Mannpar for such purpose, but that it had been moved subsequently to accommodate the eastern expansion of the lake. In the circumstances, I am not prepared to accept his evidence in regard to Phase II.

76 In cross-examination, Mr. Pandit was often non-responsive and unnecessarily argumentative. I did not consider him to be objective.

77 It is clear that the reclamation was intended to occur over 10 years, yet the plaintiff, through no fault of its own, did not have an opportunity to work over 10 years. In my view, the plaintiff is relieved of the reclamation responsibilities that would have been incurred in the second term.

78 Having regard to all of the foregoing, I reject the defendant's claim for reclamation costs.

Conclusion

79 In summary, the plaintiff's claim is dismissed. The defendant is entitled to judgment on the counterclaim in the amount of $159,833.00 together with court order interest calculable from the due dates of each of the royalty payments. If there is any aspect of costs which should be brought to my attention, counsel may have leave to do so; otherwise the defendant is entitled to its taxable costs on Scale 3.

Action dismissed; counterclaim allowed.

APPENDIX D: CANADA TRUSTCO MORTGAGE CO. V. 1098748 ONTARIO LTD. (C.O.B. CANYYZ PROPERTIES LIMITED PARTNERSHIP)

See attached.

Indexed as:

Canada Trustco Mortgage Co. v. 1098748 Ontario Ltd. (c.o.b. Canyyz Properties Limited Partnership)

Between
Canada Trustco Mortgage Company, applicant, and
1098748 Ontario Limited carrying on business as Canyyz Properties Limited Partnership, respondent

[1999] O.J. No. 963

97 O.T.C. 282

22 R.P.R. (3d) 82

87 A.C.W.S. (3d) 371

Court File No. 98-FA-6648

Ontario Court of Justice (General Division)

Cumming J.

Heard: March 18, 1999.
Judgment: April 6, 1999.

(9 pp.)

Landlord and tenant -- *The lease* -- *Renewals* -- *What constitutes an enforceable renewal.*

Application by Canada Trustco for declaration that a renewal option in its lease agreement with Canyyz Properties was enforceable, and that it had exercised its option to renew. The parties signed a lease agreement for Canada Trust to have a branch in Canyyz's mall. The lease was for an initial term of 10 years ending on July 31, 1999. The option to renew under the lease provided that a renewal was to be on terms and conditions as mutually agreed upon. A year before the lease was to expire, Canyyz obtained approval to redevelop the mall. It informed Canada Trust that under any new tenancy agreement, Canyyz would control the management and operation of the shopping centre. This and other provisions were unacceptable to Canada Trust. On September 23, 1998, counsel for Canada Trust sent a letter to Canyyz exercising the renewal option. Canyyz conceded it had received the letter and that it was clear as to its content. Two months later, Canyyz's solicitor wrote to Canada Trust indicating that because the letter was not signed by Canada Trust, the notice of renewal was not binding.

HELD: Application dismissed. The letter of September 23, 1998 was effective notice of Canada Trust's intention to renew notwithstanding the absence of its signature on the letter. The renewal clause allowed either party to bring new concerns and preferences to the table when renegotiating the lease. To require that the lease continue under its former terms and conditions would eviscerate the power of both parties to renegotiate and be contrary to the expressed intent of the renewal clause. The clause in question was at most an agreement to agree, or an agreement to negotiate. Such an agreement was not enforceable. At best, the renewal provision merely demonstrated an intention of the parties to enter into further contractual relations. While that was an integral step in the formation of an enforceable contract, the parties never went on to conclude any anticipated agreement of substance.

Counsel:

Diane E. Klukach, for the applicant.
Howard W. Winkler, for the respondent.

CUMMING J.:--

Nature of the Application

1 The applicant, Canada Trustco Mortgage Company ("Canada Trust"), seeks an order declaring that the "option to renew" contained in s. 19.02 of a lease agreement is valid and enforceable. The lease pertains to premises used for commercial banking operations in a shopping plaza mall on Kennedy Road in Toronto, known as the Agincourt Mall. As well, the applicant is seeking an order declaring that it has exercised its option to renew and that the landlord defendant be prevented from interfering with the applicant's possession. The lease agreement dated November 19, 1987 was for an initial term of ten years which ends July 31, 1999. The provision of the lease agreement in issue reads:

Section 19.02 OPTION TO RENEW

> If the Tenant is not then in default,
>
> ... then the Tenant shall have the option of renewing the Lease for a further term of five (5) years ("1st Renewal Term"), by giving written notice to the Landlord of its intention to renew at least nine (9) months before the expiration date of the Lease, such renewal to be on terms, conditions and at a Minimum Rent ** to be as is mutually agreed upon between the Landlord and the Tenant, ** such Minimum Rent not to be less than the rental payable under this Lease.
>
> ** such Minimum Rent to be fair market rent for premises of comparable age, location and construction
>
> Provided further that, if the Tenant shall not be in continuing default in any of its obligations under the terms of the Lease for the 1st Renewal Term and if the Tenant shall have complied with all of the tests set forth above, the Tenant shall have the option of renewing the Lease for a second Renewal Term of five (5) years ("2nd Renewal Term"), by giving written notice to the Landlord of its intention to renew at least nine (9) months before the expiration date of the 1st Renewal Term, such renewal to be on terms, conditions and at a Minimum Rent** to be as is mutually agreed upon between the Landlord and the Tenant, in the event that the Landlord and the Tenant fail to agree upon the amount of Minimum Rent, the determination of the rental shall be subject to arbitration in accordance with the Ontario Arbitration Act, such Minimum Rent not to be less than the rental payable under the 1st Renewal Term, and there shall be no further right of renewal.

The Issues

2 There are two issues. First, did Canada Trust effectively exercise its "option to renew"? Second, is the "option to renew" enforceable against the landlord and if so, what are the rights and obligations through the exercised option to renew?

(1) Did Canada Trust effectively exercise its option to renew?

3 Senior corporate counsel for Canada Trust sent a letter September 23, 1998 to the defendant expressly giving notice of the applicant exercising the renewal option contained in s. 19.02. Hence, written notice was given to the landlord of the intention to renew more than nine months before the expiration date of the lease. It is conceded this letter was received and that it is clear as to its intent.

4 The landlord's solicitor wrote to Canada Trust November 26, 1998 claiming that because the

September 23, 1998 letter was not signed by the tenant, then the notice of renewal was not binding. I find there is no merit to this contention. I find that the letter of September 23, 1998 was effective notice of the tenant's intention to renew notwithstanding the absence of a signature of the tenant on the communicating letter.

5 (It is noted as an aside that the letter of September 23, 1998 presumptively stated that the renewal would be at a rental rate as to be agreed by the parties and that "... all other terms and conditions were to remain the same, in accordance with the lease". It might be argued that if the terms of the lease to govern the new five-year renewal period would differ from this presumption as they required negotiation, there was an ineffective renewal. However, this point was not argued and it is not necessary to address it.)

(2) Is the Option to Renew Enforceable or is it Void for Uncertainty?

6 I have found that there was effective notice of the intention to renew the lease. The landlord refuses to renew the lease. The landlord takes the position that the renewal provision in the lease is not an enforceable right to renew the lease but is merely an unenforceable agreement to renew. Is s. 19.02 of the lease enforceable and if so, what does it require?

7 In July, 1998 the municipal government approved an application by the landlord to redevelop the Agincourt Mall. The record establishes that because of the landlord's intention to redevelop, the landlord insists upon certain provisions in any new tenancy agreement with Canada Trust whereby the landlord would control the management and operation of the shopping centre. Sections 9.05, 9.06 and 9.07 in the proposed new lease put forward by the landlord during negotiations would allow the landlord to terminate the lease in certain circumstances, albeit with a requirement of reasonable efforts to relocate the tenant. These provisions are unacceptable to Canada Trust. Given this impasse the parties are before the court.

8 The landlord submits that the option to renew is void for uncertainty. Canada Trust seeks a declaration that it has an enforceable option to renew which has been exercised.

The Option to Renew

9 The first option to renew in s. 19.02 states that such renewal is

> "... to be on terms, conditions and at a Minimum Rent ** to be as is mutually agreed upon ... such Minimum Rent not to be less than the rent payable under this Lease [and] such Minimum Rent to be fair market rent for premises of comparable age, location and construction."

10 If the only term requiring negotiation were the "Minimum Rent" payable for the new five year term, it would be arguable that there is an objective standard ("fair market" rent for premises of comparable age, location and construction") seen in the option to renew for the determination of the

Minimum Rent. See, for example, Re Nishi Industries Ltd. (1978), 91 D.L.R. (3d) 321 (B.C.C.A.). If the parties could not agree through negotiations, then the court could determine the Minimum Rent. The tendency of modern courts is to favour enforcement, in particular, where there has been reliance. Sudbrook Trading Estate Ltd. v. Eggleton, [1983] 1 A.C. 444 (H.L.). However, that is not the only term requiring determination.

11 The option to renew does not say that apart from Minimum Rent the same terms and conditions as seen in the existing lease will apply to the new term. To the contrary. The renewal is "to be on terms, [and] conditions ... as is mutually agreed upon ..."

12 What is meant to be covered by "as is mutually agreed upon" by the parties? The copula verb "be" is employed to link the subject to its complement. The form of the verb ("is") is properly used for a single subject. If the parties had to agree on: (1) terms, (2) conditions and (3) minimum rent, then the provision would properly read "as are mutually agreed upon." As the phrase reads, the requirement to agree, arguably, might only apply to the Minimum Rent. However, why would the parties use the words "as is mutually agreed" just in respect of "minimum rent" when they include further wording for an objectively determinable "free market rent"? Also, this interpretation would leave the words "terms" and "conditions" without qualifiers: the renewal would "be on terms [and] conditions." I think it is fair to infer from the overall phrase that the renewal terms and conditions would have to be as agreed between the parties, or else the reference to "terms [and] conditions" would not make sense. If the parties intended the reference to be to "the same terms and conditions" presumably those words would have been included.

13 The existing lease has a great many terms and conditions. It is apparent that the terms and conditions thereof were negotiated on a basis of many concerns and preferences expressed by both parties to the original lease. It is apparent that there was some give and take in arriving at the final terms and conditions of the lease. It cannot be said that this is a 'standard form' lease with standard terms and conditions, even if such could be said about any lease of commercial premises in a shopping centre. The present landlord is an assignee of the original landlord's interest in the lease. The new landlord has a redevelopment project with new concerns and preferences and this is seen in the terms and conditions discussed with, but unacceptable to, Canada Trust. This is a contingency contemplated by the lease, and by the parties to the contract at the time it was entered into. The renewal clause allows either party to bring new concerns and preferences to the table when renegotiating the lease. To require that the lease continue under its former terms and conditions would eviscerate the power of both parties to renegotiate and be contrary to the expressed intent of the renewal clause.

14 Canada Trust submits that the second option for renewal seen in s. 19.02 for a further five years term refers to arbitration in the event of an inability to mutually agree. Canada Trust states that this arbitration provision should fairly be imported into the first option to renew, the subject of the application at hand. However (leaving aside the fact there is no reference at all to any arbitration mechanism in the first option to renew), the provision as to arbitration in the second option to renew applies only to the determination of the Minimum Rent amount.

15 Contracts such as the lease at hand involve private law-making. The freedom to contract in the marketplace creates reasonable expectations that constitute legally enforceable obligations upon the parties to the contract. The sanctity of contracts is fundamental to commercial efficacy. However, before there can be an enforceable contract, a court must be able to discern the prerequisites to an enforceable obligation (for example, the intention to contract, offer and acceptance and consensus ad idem) and the nature of the obligations intended. It would be the antithesis of the societal objectives of freedom of contract for the court to impose what it would presume ought to be the terms and conditions of a bargain to be struck between the parties. In the case at hand, the lease constitutes a contract between two sophisticated parties, with legal advice and an equality of bargaining power.

16 I start with the presumption that s. 19.02 intends to create some obligation simply because of its presence in the lease. That is, the presumption is that the provision is not merely hortatory in nature. The court will try to do justice to the parties looking at substance as well as form. The wording of the agreement will be considered broadly and with due regard to all the implications.

17 However, in the case at hand all terms and conditions are to be mutually agreed upon before there is an extension of the tenancy for a five-year term. The parties cannot agree as to these terms and conditions. Canada Trust asks for the same terms and conditions as in the original lease, but the option to renew expressly states that the terms and conditions for the renewal period are to be agreed upon. Canada Trust then says that there should be arbitration. But the parties have not contractually agreed that there is to be arbitration.

18 Section 19.02 is at most an agreement to agree which is, in reality, merely an agreement to negotiate. Such an "agreement" is not enforceable. There are several reasons according to "classical" contract law why the agreement to agree in this case is not enforceable, and at least one more modern explanation. As Professor Atiyah puts it (P.S. Atiyah, An Introduction to the Law of Contract, 5th ed., (Clarendon Press: 1995)) at p. 112:

> [T]he court cannot enforce a contract unless it knows what the terms are which it is sought to enforce. It is very old law that ... 'an agreement to agree' cannot be a valid contract. ... What the parties cannot do is to bind themselves to negotiate and reach agreement, because the negotiations may genuinely fail to lead to an agreement.
>
> Emphasis in original

19 Lord Wright's speech in Scammell & Nephew Ltd. v. Ouston, [1941] A.C. 251 (H.L.) elucidates two of the reasons why a court cannot enforce a "contract to contract." The first difficulty is an interpretation problem. He explains at p. 268 that such a provision is so vague that the court cannot properly imply a term. Though, as in Hillas & Co. v. Arcos (1932), 147 L.T. 503, a court may invoke a standard of reasonableness to imply a term of the contract at issue, where the language is too obscure or incapable of any definite or precise meaning, the court cannot attribute to the parties any particular contractual intention:

> Its terms must be so definite, or capable of being made definite without further agreement of the parties, that the promises and performances to be rendered by each party are reasonably certain.
>
> Scammell at 268-69.

20 Lord Wright's second reason for not enforcing an agreement to agree relates to the nature of the contractual relationship. A mere agreement to agree shows that the parties lacked the necessary common intention to form an enforceable contract. The agreement to enter into a hire-purchase agreement in Scammell was, according to Wright L.J. at p. 269, evidence that the parties' "agreement was inchoate and never got beyond negotiations. ... The furthest point they reached was an understanding or agreement to agree upon hire-purchase terms." As stated by Viscount Simon L.C. in the same case at p. 254, the provision at issue showed that there was required further agreement to be reached between the parties before there would be consensus ad idem, and, therefore, an enforceable contract. See also Foley v. Classique Coaches, [1934] 2 K.B. 1 and May & Butcher v. The King, [1934] 2 K.B. 17.

21 At best, the renewal provision in the case at hand merely demonstrates an intention of the parties to enter into further contractual relations. That is certainly an integral step in the formation of an enforceable contract. However, the parties here never went on to conclude any anticipated agreement of substance.

22 Counsel for Canada Trust referred in argument to an alleged requirement of the landlord to negotiate the terms of renewal in good faith. This raises the issue of good faith in performance of contractual terms, which has in recent years been the subject of some debate. Some, such as Professor O'Byrne in her article "Good Faith in Contractual Performance: Recent Developments", [1995] 74 C.B.R. 70, say that the common law has come to recognise a general duty to act in good faith when performing contractual terms. Others, such as Professor Bridge, "Does Anglo-Canadian Contract Law Need a Doctrine of Good Faith?" (1984), 9 C.B.L.J. 385, argue that contract law should not adopt such an imprecise concept as good faith and that implying such a duty amounts to inappropriate judicial intervention into the private law of parties to a contract. See also Belobaba, "Good Faith in Canadian Contract Law," (1985) Special Lectures of the Law Society of Upper Canada - Commercial Law 73.

23 I do not have to decide whether a duty to perform in good faith exists as an underlying tenet of contract law. Whether it does or not, I would imply in this case a duty on both parties to make a good faith attempt to negotiate renewal terms. As I have found, the agreement to agree on renewal terms and conditions amounts to an agreement to negotiate. Of course, the parties could have begun to negotiate a new contract before or after the old contract came to an end; they did not need a contractual provision to bring them to the table. So we are faced with what appears to be a redundant clause in the contract.

24 The position at common law is that there may well be an implied term of a contract that the parties will act in good faith in the performance of their obligations. However, it is problematical as to whether there is any duty of good faith in the negotiation of a contract.

25 The lease in question, however, contemplates a potential further agreement that is based in part on the previous and continuing contractual relationship of the parties. The inclusion of a term to negotiate following the exercise of the parties' option to renew must give rise to something. This approach is consistent with the values of commercial efficacy and certainty that I outlined above. It is appropriate to interpret the provision in question here as demonstrating the intention of the parties to preserve the goodwill of their former contractual relationship. A previous relationship and an agreement to negotiate on renewal terms and conditions may not allow the court to infer what those terms and conditions would be, but the context imparts a duty of the parties to negotiate in good faith for renewal terms and conditions following exercise of the renewal option. By "duty of good faith" I mean nothing more than a requirement that the parties not negotiate in bad faith.

26 The record does not show any indication of bad faith conduct on the part of the landlord after the exercise of the renewal option. The landlord made a concerted effort to negotiate a new lease. It is true that the position the landlord put forward was in its own interest, but it was fully entitled to do so. There is nothing to show that the landlord acted with malice or fraud in putting forward its position. That Canada Trust would not accept the landlord's offers does not amount to bad faith.

Disposition

27 In the plainest words, the court cannot make a contract for the parties. At most, the provision in question was an agreement to negotiate subsequent terms and conditions upon the exercise of the renewal option. The agreement does not contemplate that a new lease will necessarily follow the previous lease; it only says that the parties will make good faith efforts to negotiate. It is contemplated in the circumstances of the parties' relationship and the renewal provision that subsequent negotiations may fail. This is a risk that the parties accepted; otherwise there would be more definite renewal terms.

28 The application for a declaration that the exercise of the option to renew created a valid and enforceable right of renewal is denied.

29 I may be spoken to as to costs.

CUMMING J.