Interpretation of Construction Contracts

Douglas Sanders and Todd Rattray
November 15, 2001

I. INTRODUCTION

In simple terms, a contract is a meeting of minds between two or more parties. In their purest form, contracts are a means of establishing certainty in the relationship between parties by setting out the obligations of each party and allocating risk between them. In practice, contracts are anything but pure.

In the construction world, contracts more often than not represent one party’s utopia and the other party’s deal with the devil. Selling one’s sole is often a pre-requisite to obtaining work, especially in tendering circumstances, where the cost of the obligations is tallied and then discounted, and the quantum of risk is ignored.

The perfect contract has yet to be written. In many cases, contracting parties employ the same ill-fitting and out-of-date contract form that they have used for years. This practice often results in the contract being the source of problems, rather than the source of solutions.

If a dispute arises between the contracting parties, the courts are often called upon to interpret the contract and determine the meaning of its terms.

II. GENERAL PRINCIPLES OF CONTRACTUAL INTERPRETATION

Interpretation of a contract involves ascertaining the meaning of the words used by the contracting parties and determining the legal effect of those words. Interpretation of contracts involves the application of many legal principles. Some topics relevant to contractual interpretation include:

1. the overriding principle of the objective intention of the parties;
2. the canons of contract construction;
3. the introduction of additional evidence;
4. the methods of resolving ambiguity and uncertainty; and
5. the implication of contractual terms.
The role of the court in interpreting a contract is not to remake the contract for the parties, nor to tell them what they should have written. If the literal meaning of the contract is clear, then the court must follow that meaning and there is no room left for liberal interpretation. However, where there is ambiguity or uncertainty as to the meaning of the contract, it must be analyzed to determine the legal meaning of its terms.

A. The Intention of the Parties

The principal and overriding objective in contract interpretation is to ascertain the reasonable mutual intentions of the parties as to the legal obligations that they assumed under the written contract. During contract interpretation, the court is said to apply an “objective standard”, which requires consideration of what hypothetical reasonable parties standing in the shoes of the actual parties would have intended. The objective standard contrasts with the “subjective standard”, which involves consideration of what the actual parties themselves intended. Therefore, in a contract dispute the court is interested in the “objective intentions” of the parties. In this manner, the parties' agreement should be understood in the way in which the contract language would appear to the ordinary reasonable person looking at it from the outside.

As a result of the objective standard of contract interpretation, intent is relevant only to the extent revealed by the parties' words; the actual subjective intent of the parties is not relevant. The parties have agreed on a formula of words, not an intent. Indeed, the parties may negotiate a formula of words, while still retaining in their minds quite disparate intentions. Parties are not generally allowed to give evidence as to what their actual subjective intention was at the time of negotiating the contract. The objective intention of the parties must be ascertained from the language they have used in the contract, considered in light of the surrounding circumstances and the purpose of the contract. Thus, examining the parties’ objective intention involves interpreting the contract in a manner that is consistent, intelligent and in harmony with both the words of the parties and the circumstances under which they were contracting.

Determination of the objective intention of the parties does not confine the interpreter to looking strictly at the contract itself. An interpreter may use different techniques such as the canons of contract construction and the contractual context as guidelines to assist them in discerning the objective intention of the parties.

B. Canons of Contract Construction

The canons of contract construction are not rules of law; they are simply “pointers” employed by the courts to assist them in discovering the objective intention of the parties from a written contract. The canons of contract
construction are not to be applied slavishly, and where they point in different directions, the judge must select those that will produce a reasonable and just result. Some of the more common canons of contract construction include:

1. Plain and Ordinary Meaning

The “golden rule” of contract interpretation is that the words of a contract should be construed in their grammatical and ordinary sense, and given their plain and ordinary meaning, except to the extent that interpretation or modification is necessary in order to avoid absurdity, inconsistency or repugnancy. In the absence of ambiguity, therefore, the natural or literal meaning of the words set out in the contract should be adopted.

2. Special Meaning

Where words have a customary or special meaning, as often occurs with technical documents in construction contracts, the special meaning takes the place of the ordinary meaning for the purpose of construing the contract. Use of a dictionary is appropriate for determining the special meaning of words, as is use of contractual headings and marginal notations.

3. Reading the Contract as a Whole

A contract should be considered as a whole. In order to arrive at the true interpretation of a document, a clause should not be considered in isolation, but must be considered in the context of the whole contractual document. If there is a conflict between two parts of a document such that effect cannot fairly be given to both clauses, the dominating purpose must prevail as indicating the true intentions of the parties. Furthermore, if a single transaction is effected by several contractual documents, they should all be read together for the purpose of ascertaining the objective intention of the parties.

4. Giving Effect to All Parts of a Contract

In construing a contract, all parts of it must be given effect where possible, and no part of it should be treated as inoperative, surplus, or as having no meaning.

5. Restriction by Express Provisions

Frequently, parties employ standard form contracts, which contemplate that special conditions added by the parties will prevail over the standard form language. In these circumstances, greater weight must be given to the special conditions, and, in case of conflict between the general conditions and the special conditions, the latter will prevail.
6. Commercial Purpose

Commercial agreements are to be interpreted with an eye to the most commercially reasonable result and accepted business principles, unless the language clearly precludes this approach. Where the words of a contract are clear yet have no discernible commercial purpose, the interpreter should still give effect to the written words.

7. Context

The meaning of words is to be determined by the context in which they are found. Broad, general words are not interpreted to be as wide as they appear in isolation. The meanings of such words are to be confined to the purpose at hand, in the clause and the contract in which they are found. Moreover, since a contract must be interpreted as at the date when it was made, words must be given the meaning which they bore at that date.

8. Alternative Interpretations

If the words of a contract give rise to two possible interpretations, one of which is absurd, commercially unreasonable, or unjust, and the other is rational, the latter should be taken as the correct interpretation. Similarly, where the words of a contract are capable of two equally plausible meanings, one of which renders the contract lawful and valid and the other makes the contract unlawful or invalid, the former construction should be preferred. The reasonableness of the result of any particular interpretation is a relevant consideration in choosing between rival constructions.

9. Poorly Drafted Contracts

The English courts have held that a poorly drafted contract affords no reason to depart from the fundamental rules of interpretation of contractual documents. In particular, the objective intention of the parties must be ascertained from the language they have used. This rule applies “if the language used, whatever it may lack in precision, is reasonably capable of an interpretation which attributes to the parties an intention to make provision for contingencies inherent in the work contracted for on a sensible and businesslike basis.” As a result, the courts should, to the extent possible, employ the same rules for contractual interpretation of poorly drafted contracts as they would for perfectly drafted contracts.
10. Contra Preferentum

Where a contract is ambiguous and there are two alternate interpretations, the courts will utilize the interpretation that favours the party that did not write the contract.

C. Introduction of Additional Evidence

In the exercise of contractual interpretation, the primary evidence available for analysis is the contract document itself. In the absence of fraud or mistake, the parties are bound by the terms of the written contract that they have signed. However, there are instances where other extrinsic evidence may be relevant to contract interpretation.

1. Parole Evidence Rule

The parole evidence rule is a general rule, which provides that where a contract is entirely written and its written language is clear and unambiguous, extrinsic evidence is not admissible to add to, vary or contradict the written words. The theory behind the parole evidence rule is that, where the parties have agreed that a document is to constitute the exclusive record of their agreement, their intention will prevail. The common law provides for some exceptions to the parole evidence rule in instances where injustice might otherwise result. Such exceptions include:

(1) explaining incomplete documents or amplifying an incomplete description;
(2) proving that a condition precedent has not been fulfilled; and
(3) assisting to ascertain the intentions of the parties.

2. Factual Matrix

The parole evidence rule does not preclude the interpreter from considering evidence of the factual background known to the parties at or before the date of the contract. This admissible “factual matrix” includes evidence of the “genesis” and the “aim” of the transaction. The general principles of the admissible factual matrix were set out by Ryan J. in Delisle v. Bulman Group Ltd. ((1991), 54 B.C.L.R. (2d) 343 (BCSC)) as follows:

(1) Evidence of facts mutually known to the parties prior to the execution of a contract are admissible to identify the meaning of a descriptive term if they are relevant and not excluded by other evidentiary tests. Ambiguity is not a pre-condition to a consideration of the factual matrix.
(2) In examining the factual matrix, the court ought not to look at the prior negotiations of the parties as an aid to the construction of the written contract. Evidence as to what the parties intended is inadmissible in interpreting a written contract.

(3) If, after examining the agreement itself in its factual matrix, including the particular words used in their immediate context and in the context of the agreement as a whole, there remain two reasonable alternative interpretations, then additional evidence may be admitted. This evidence includes evidence of the facts that led up to the making of the agreement, evidence of the circumstances as they existed at the time the agreement was made, and evidence of the subsequent conduct of the parties to the agreement. The two existing reasonable interpretations may be the result of ambiguity arising from doubt, uncertainty or difficulty of construction.

Applying these guidelines, the court will attempt to place itself in the same factual matrix as that of the parties at the time the contract was entered into. Thus, the factual matrix is a contextual aid to the determination of the objective intention of the parties. It should be used as background, which may deepen the understanding of the parties’ objective intent, but should not be used to interpret an agreement differently from the construction intended by the parties as evidenced by the words they used.

3. Subsequent Conduct

Canadian courts have adopted the view that the subsequent conduct of the parties can be a useful guide to interpreting a written contract, in circumstances where there is ambiguity in the contractual language. Such conduct is admissible, provided that the evidence does not add to or vary the document, but simply helps the court to arrive at a conclusion as to the true intent and meaning of the words used in the document.

D. Methods of Resolving Ambiguity and Uncertainty

1. Ambiguity

A statement or clause is ambiguous when it has two or more meanings, each of which may be adopted without distortion of the language. Traditionally, the law has classified ambiguity into two types: patent and latent. Patent ambiguity is ambiguity that results from the language of the instrument; whereas latent ambiguity only becomes apparent when the contractual language is applied to the factual situation.
Patent ambiguity may arise where the contract:

(1) is self contradictory;
(2) expresses alternative intentions, without choosing between them; or
(3) lacks an essential definition.

The introduction of direct evidence of the intention of the parties is not permitted to resolve patent ambiguity, so the court must do the best it can by applying only the extrinsic evidence that would otherwise be admissible to construe any contract. If the patent ambiguity cannot be resolved using such evidence, then the ambiguous clause(s) will be declared void for uncertainty.

Latent ambiguity only arises after evidence of the factual matrix surrounding the making of the contract has been tendered; consequently, further evidence is admissible to resolve the ambiguity. In order to assist a court in resolving a latent ambiguity, an interpreter may use any relevant evidence that is otherwise admissible. In the normal course of events, the interpreter will receive evidence about the objective facts surrounding the making of the contract, but will not receive direct evidence as to the actual intention of the parties, as such evidence would vary or contradict the terms of the written instrument. With latent ambiguity, a choice must be made between two or more meanings each of which is entirely consistent with the language of the written instrument. The extrinsic evidence does not vary or contradict the written contract, it simply supplements or explains it, and is thus admissible.

A syntactical or grammatical ambiguity is probably the most common ambiguity encountered in practice. Typically, such an ambiguity will raise the question of whether a subordinate clause in a sentence is governed by a particular verb, or whether an adjective applies to a whole list of nouns or only to one or some of them. These types of ambiguities are commonly resolved by a consideration of the commercial purpose of the contract, or by the application of a presumption of contractual interpretation.

After receiving the admissible evidence, a court will attempt to resolve contractual ambiguities through application of the following principles:

(1) considering the whole of the agreement together;
(2) determining the objective intention of the parties when making the contract;
(3) putting into effect the words or clauses which reflect that intention; and
(4) rejecting those terms which would otherwise defeat that intention.

---

In *Skoko v. Chychrun Construction Ltd.* ((1982), 23 R.P.R. 262 (B.C.A.A.)), the Court held that if certain words “dominate” a clause and “control its meaning”, those words will be given effect at the expense of other words that would give rise to the contrary meaning. In the alternative, the court will apply the *Djukastein* test to determine the intention of the contracting parties. The parties’ intention can only be gleaned from what they have written into their agreement and from their conduct.

2. **Uncertainty**

A contract or provision is uncertain where:

(1) it is unintelligible and therefore meaningless;

(2) the interpreter is unable to select between a variety of meanings;

(3) the interpreter is unable to discern the concept that the parties had in mind; or

(4) the terms of the contract require further agreement between the parties in order to implement them.

The task of the interpreter is to construe the document according to the ordinary principles of construction and then to determine whether the document as so construed is void for uncertainty. Where the parties have entered into what they believe is a binding agreement, courts are very reluctant to hold the agreement void for uncertainty, and will do so only as a last resort.

E. **Implied Terms**

1. **General Principles**

Even parties who exercise the utmost diligence in drafting written contracts can omit certain contractual terms. Contractual terms may be implied by a court into a contract, but only to the extent that the contract does not include express terms in relation to the same subject matter. A court will not imply a contractual term that contravenes an express term.

In general, there are three situations in Canada where a court will imply terms into a contract. These situations were canvassed by the Supreme Court of Canada in *C.P. Hotels Ltd. v. Bank of Montreal* ([1987] 1 S.C.R. 711 (SCC)), but perhaps they were expressed more succinctly by the same court in the decision

---

of *M.J.B. Enterprises Ltd. v. Defence Construction (1951) Ltd.* ([1999] 1 S.C.R. 619 (SCC)), where Iacobucci J. (speaking for the entire court) stated:

> The general principles for finding an implied contractual term were outlined by this court in *C.P. Hotels*… Le Dain J., for the majority, held that terms may be implied in a contract: (1) based on custom or usage; (2) as the legal incidents of a particular class or kind of contract; or (3) based on the presumed intention of the parties where the implied term must be necessary “to give business efficacy to a contract or otherwise meeting the ‘officious bystander’ test as a term which the parties would say, if questioned, that they had obviously assumed”

Since 1987, several courts have had a chance to visit the *C.P. Hotels* formulation. In two Supreme Court of Canada decisions, *Machtinger v. H.O.J. Industries Ltd.* ([1992] S.C.R. 986 (SCC)) and *Wallace v. United Grain Growers Ltd.* ([1997] S.C.R. 701 (SCC)), McLachlin J. illuminated the categorization to some degree, although in both cases, McLachlin J. was unable to persuade the majority to agree with her point of view. In her minority concurring opinion in *Machtinger* and her dissenting opinion in *Wallace*, McLachlin J. adopts a distinction formulated by Treitel.³ She finds that terms implied on the basis of custom or usage and terms implied on the basis of the business efficacy/officious bystander test require evidence of the presumed intention of the parties. However, McLachlin J. contends that terms implied “as legal incidents of a particular class or kind of contract” are not dependent on the presumed intentions of the parties, but rather, are based on broader considerations of necessity. Treitel refers to this branch of implied terms as “terms implied in law”, and suggests that the relevant considerations to imply such terms are justice and policy.

McLachlin J.’s distinction between the various branches of implied terms was recently referred to with favor by the entire Supreme Court of Canada in *M.J.B. Enterprises* (*supra*, note 3). In addition, the British Columbia Court of Appeal adopted the distinction in *B.C. Rail Ltd. v. Canadian Pacific Consulting Services Ltd.* ([1990] B.C.J. No. 1496).

In *M.J.B. Enterprises* (*supra*, note 3), the Supreme Court of Canada discussed further the implication of contractual terms involving the business efficacy/officious bystander branch. Iacobucci J., speaking for the Court, stated:

> … a contractual term may be implied on the basis of the presumed intentions of the parties where necessary to give

business efficacy to the contract or where it meets the “officious bystander” test. It is unclear whether these are to be understood to be two separate tests, but I need not determine that here. What is important in both formulations is a focus on the intentions of the actual parties. A court, when dealing with implied terms in fact, must be careful not to slide into determining the intentions of reasonable parties. This is why the implication of the term must have a certain degree of obviousness to it, and why, if there is evidence of a contrary intention, on the part of either party, an implied term may not be found on this basis.

This excerpt from MJB Enterprises makes it clear that the circumstances where a court will imply contractual terms based on the business efficacy/officious bystander branch involve an analysis of the subjective intentions of the parties. As discussed above, the subjective intention of the parties means the actual intentions of the actual parties, as opposed to objective intention, which means the intentions of hypothetical reasonable parties in the same circumstances as the actual parties. In M.J.B. Enterprises the Court did not expressly decide whether a term implied on the basis of the branch involving custom and usage (also dependent on the presumed intentions of the parties) is based on a subjective or objective analysis.

The B.C. Court of Appeal also opined on the implication of contractual terms under the business efficacy/officious bystander branch in Village Gate Resorts Ltd. v. Moore ([1997] B.C.J. No. 2478 (BCCA)). Southin J., speaking for the Court, adopted the decision of the English Privy Council in BP Refinery (Westernport) Pty. Ltd. v. President, Councillors and Ratepayers of the Shire of Hastings, ((1977) 16 A.L.R. 363 (PC)) in holding that there are five conditions, which often overlap, that must be satisfied in order to imply a contractual term under this branch:

1. [the term sought to be implied] must be reasonable and equitable;
2. it must be necessary to give business efficacy to the contract, so that no term will be implied if the contract is effective without it;
3. it must be so obvious that “it goes without saying”;
4. it must be capable of clear expression; and
5. it must not contradict any express term of the contract.
Southin J.’s approach in *Village Gate* appears to represent a somewhat narrower approach than that of the Supreme Court of Canada in *M.J.B. Enterprises*.

In *B.C. Rail* (*supra*, note 8), the Court examined terms implied in law as a legal incident of a particular class or kind of contract and, in following McLachlin J., held that, in order to imply such a term, it may not depend on the presumed intention of the parties, but it must be both reasonable and necessary.

The *C.P. Hotels* formulation of the three scenarios under which a contractual term will be implied has been applied in a number of other cases, but has survived substantially unchanged.

Thus, currently in B.C., a court may imply terms into contracts where the implied terms are not contrary to the express terms of the contract and the circumstances fall into one of the following scenarios:

1. a term may be implied based on custom or usage (involving an analysis of the presumed intentions of the parties, but unclear as to whether such analysis should be subjective or objective);

2. a term may be implied where it is necessary to give business efficacy to a contract or otherwise meeting the ‘officious bystander’ test (involving a subjective analysis of the presumed intentions of the parties and the five conditions expressed by Southin J. in *Village Gate* (*supra*, note 10); and

3. a term may be implied where it is an incidence of a particular class or kind of contract, the nature and content of which have to be largely determined by implication (involving inquiry into whether the term is necessary and reasonable and possibly questions of justice and policy, but not necessarily requiring analysis of the intention of the parties).

### 2. Implied Terms in Construction

The following is a list of arguments that have been advanced, successfully or unsuccessfully, by counsel for the implication of contractual terms into construction law contracts:

---


5 Please note that these cases have not all been reviewed thoroughly to determine whether these cases were overruled on appeal. In addition, this list should not be considered to be exhaustive.
<table>
<thead>
<tr>
<th>Argument</th>
<th>Citation</th>
</tr>
</thead>
<tbody>
<tr>
<td>&gt; an implied term that only a compliant bid would be accepted by the party who sent out an invitation for tenders</td>
<td>M.J.B. Enterprises Ltd. v. Defence Construction (1951) Ltd., [1999] 1 S.C.R. 619 (SCC).</td>
</tr>
<tr>
<td>&gt; an implied warranty of fitness of some construction work for the purpose that it was intended</td>
<td>B.C. Rail Ltd. v. Canadian Pacific Consulting Services Ltd., [1990] B.C.J. No. 1496 (BCCA).</td>
</tr>
<tr>
<td>&gt; an implied term that a party who sent out an invitation for tenders would treat all bids fairly</td>
<td>Martel Building Ltd. v. Canada, [2000] S.C.J. No. 60 (SCC).</td>
</tr>
<tr>
<td>&gt; an implied term that the owner will make payments due under the contract</td>
<td>Twin City Painting Contractors Ltd. v. Penwood Construction Ltd. (1980), 44 N.S.R. (2d) 418 (Co. Ct.).</td>
</tr>
<tr>
<td>&gt; an implied term that the owner will provide sufficient space to enable the contractor to carry out the work</td>
<td>R. v. Walter Cabott Const. Ltd. (1977), 69 D.L.R. (3d) 542 (Fed. C.A.).</td>
</tr>
<tr>
<td>&gt; an implied term that the owner will provide any required plans within a reasonable amount of time</td>
<td>Nordic Construction Ltd. v. Hope Brook Gold Inc. (1991), 47 C.L.R. 8 (Nfld. T.D.).</td>
</tr>
<tr>
<td>&gt; an implied term that the owner will advise a contractor of the existence of hidden obstructions, such as underground pipelines</td>
<td>Henuset Bros. Ltd. v. Pan Can. Petroleum Ltd. (1977), 82 D.L.R. (3d) 345 (Alta. T.D.).</td>
</tr>
<tr>
<td>Argument</td>
<td>Citation</td>
</tr>
<tr>
<td>-------------------------------------------------------------------------</td>
<td>----------------------------------------------------------------------------------------------------------------------------------------</td>
</tr>
<tr>
<td>the contractor's work in a manner that may cause delay or extra cost</td>
<td>Enterprises Blanchet Ltée v. Canada (1988), 95 N.R. 75 (C.A.); Constructions Que. Labrador Inc. v. Canada (1987), 82 N.R. 298 (Fed. C.A.) (note: that contractor must show that unavoidable loss or damage resulted from the delay (where there is delay): Embar Construction Ltd. v. Newfoundland (1995), 22 C.L.R. (2d) 121 (Nfld. C.A.)).</td>
</tr>
<tr>
<td>11. &gt; an implied term that the contractor will finish the work in a</td>
<td>Deminico v. Earls, [1945] O.W.N. 375; Lionel J.L. MacLean Ltd. v. Winters (1990), 35 C.L.R. 148 (N.S. Co. Ct.).</td>
</tr>
<tr>
<td>reasonable amount of time (where there is no express completion date)</td>
<td></td>
</tr>
<tr>
<td>“work-man like” manner</td>
<td></td>
</tr>
<tr>
<td>13. &gt; an implied term that the contractor will comply with the</td>
<td>G. Ford Homes Ltd. v. Draft Masonry (York) Co. (1983) 2 C.L.R. 210 (Ont. C.A.).</td>
</tr>
<tr>
<td>applicable building code</td>
<td></td>
</tr>
</tbody>
</table>
14. > an implied term that any materials supplied by the contractor will be fit for the intended use


15. > an implied warranty that a house to be built will be fit for human habitation upon completion


16. > an implied term of a different rate of pay for the erection of structures not originally covered by the contract (i.e. “extra work”)

Francis v. Domino 251 Ky. 255, 64 S.W. 2d 571 (1933).

17. > an implied obligation of good faith


18. > an implied obligation to keep work in a state of such forward progress as to allow the contractor’s work to proceed expeditiously

<table>
<thead>
<tr>
<th>Argument</th>
<th>Citation</th>
</tr>
</thead>
<tbody>
<tr>
<td>20. &gt; an implied obligation to do that which may be necessary to enable the other party to perform its contracted obligations</td>
<td>Roberts v. Burg Commissioners (1870), L.R. S.C.P. 310.</td>
</tr>
<tr>
<td>21. &gt; an implied duty on the architect to supply necessary information to the builder during construction</td>
<td>London Borough of Merton v. Leach (1985), 32 B.L.R. 51.</td>
</tr>
<tr>
<td>22. &gt; an implied duty to appoint a new architect/engineer if the first dies or retires before the contract is completed</td>
<td>Croudsace v. Lambeth Borough Council (1986), 33 B.L.R. 25.</td>
</tr>
<tr>
<td>23. &gt; an implied term that other contractors of the owner will not impede the contractor</td>
<td>U.S. v. Foley 329 U.S. 64 (1946).</td>
</tr>
<tr>
<td>24. &gt; where information as to expected soil conditions has been supplied by the owner, implied terms that the information was “reasonably accurate or at least not erroneous or misleading” and that the design was “reasonably constructible within the time specified” were rejected, because of the presence of disclaimers in the contract</td>
<td>Catre Industries Ltd. v. Alberta (1990), 63 D.L.R. (4th) 74 (Alta. C.A.) (note: contrast this case with Opron (above)).</td>
</tr>
<tr>
<td>25. &gt; in general, an owner owes no implied obligation to the contractor to do work to render the site easier to work upon</td>
<td>Ibmac v. Marshall (1968), 208 E.G. 851.</td>
</tr>
<tr>
<td>26. &gt; an owner may suspect or know that the contractor has underestimated the difficulties associated with a particular contract, but is under no implied duty to warn him in the absence of fraud or deliberate concealment</td>
<td>Bottoms v. Yorkshire Corporation (1892), (C.A.); Atlas Construction Co. Ltd. v. City of Montreal, [1954] 4 D.L.R. (2d) 124.</td>
</tr>
<tr>
<td>Argument</td>
<td>Citation</td>
</tr>
<tr>
<td>------------------------------------------------------------------------</td>
<td>-------------------------------------------------------------------------</td>
</tr>
<tr>
<td>27. &gt; an implied duty on an owner to disclose “superior knowledge” to those bidding on the contract</td>
<td>Helen Curtis Industries v. United States 312 F. 2d 774 (Ct. Cl. 1963); Opron Construction Co. v. Alberta, [1994] A.J. No. 224 (Alta. Q.B.); (note: other cases have negatived this duty; see: American Ship Building Co. v. United States 654 F. 2d 75 (Ct. Cl. 1981); Piancki Airport Corporation v. United States 667 F. 2d 50 (Ct. Cl. 1981)).</td>
</tr>
<tr>
<td>28. &gt; when an owner supplies plans and specifications to a contractor, the owner impliedly warrants that the provided plans and specifications will be accurate and suitable for the construction of the intended building</td>
<td>Spearin v. United States 248 U.S. 132 (1918).</td>
</tr>
<tr>
<td>29. &gt; an implied duty on an owner to co-ordinate the work of multiple prime contractors</td>
<td>Broadway Maintenance Corp. v. Rutgers 447 A. 2d 906 (N.J. 1982).</td>
</tr>
<tr>
<td>30. &gt; an implied duty on an owner, not only to provide access to the site, but also to maintain access to the site</td>
<td>Northeast Clackamus County Electric Co. Operation v. Continental Casualty Co. 221 F. 2d 329 (9th Cir. 1955).</td>
</tr>
<tr>
<td>31. &gt; implied obligation on an owner to make timely decisions affecting the work in response to changed or unanticipated conditions</td>
<td>Horton Industrial, Inc. v. Village of Moweaqua 142 Ill. App. 3d 730 (1986).</td>
</tr>
<tr>
<td>32. &gt; implied duty to co-operate</td>
<td>J.R. Graham and Sons, Inc. v. The Randolph County Board of Education 25 N.C. App. 163 (1975).</td>
</tr>
</tbody>
</table>
III. FRAUDULENT MISREPRESENTATION AND DECEIT

In general, fraud can be formulated as a claim in contract, as a fraudulent misrepresentation, and/or as a claim in tort, as the tort of deceit.6

Generally, a plaintiff seeking to rely on a contractual claim of fraudulent misrepresentation must demonstrate two factors:

(1) the presence of a material fraudulent misrepresentation; and

(2) the intention of the representor that the representee will be influenced by the misrepresentation to the extent that it affects his or her conduct.

It is well established law that a statement is fraudulent if the representor knows it to be untrue or is reckless as to whether the statement is true or false.7 The burden is on the representee to establish that the representor had an absence of actual and honest belief. If the representor had an honest belief in the statement, there may be negligent or innocent misrepresentation, but there is no fraud.8 Often this is the most difficult element for the plaintiff to prove. Mere silence or passive failure to disclose the truth is not a representation, and therefore not actionable as a fraudulent misrepresentation, however deceptive in fact.9 However, active concealment or intentional suppression of pertinent facts or information may amount to a misrepresentation.10

In order for a fraudulent misrepresentation to carry civil consequences, the statement must also be material. In general, a representation is considered material if it influences and induces the plaintiff to act in a manner that is to its detriment and where, had the misrepresentation not been made, the plaintiff

---

6 The primary difference between a claim of fraud in contract and in tort appears to be the available remedies, which include rescission in the case of a contractual claim where the contract has been executed, but work under the contract has not commenced. In addition, a claim in tort may be brought where there is no privy of contract between the parties.

7 *Derry v. Peek* (1889), 14 App. Cas. 337 (HL).


might have acted differently.\textsuperscript{11} The B.C. Court of Appeal has denied a fraudulent misrepresentation claim on the basis of a lack of materiality, because there was insufficient connection between the misrepresentation and the plaintiff's acting in reliance on that misrepresentation.\textsuperscript{12} In contract cases, materiality is normally demonstrated by showing that the representation was a material factor that led the plaintiff to enter the contract.

A plaintiff must also demonstrate that the representor intended to influence the representative to act on the basis of the representation. In contract cases, this is most often demonstrated by showing that the representor intended the statement to induce the plaintiff to enter into the contract.\textsuperscript{13}

Another consideration pertinent to a discussion of fraudulent misrepresentation is that a representation will be considered to continue from the time that it is made until the time that the representative discovers that it is false. Moreover, if a representor makes a statement and the statement subsequently becomes false (to the knowledge of the representor), then the representor has a duty to disclose the change of circumstances to the representative. A representor who fails to discharge this duty is liable for fraud.\textsuperscript{14}

A fraudulent misrepresentation can attract liability in tort outside of a contractual relationship. In order to successfully make out the tort of deceit, the plaintiff must prove the following elements:

1. the defendant made a false representation of fact;
2. the representation was made with knowledge of its falsity;
3. the representation was made with the intention that it should be acted upon by the plaintiff, or by a class of persons which includes the plaintiff, in the manner which resulted in damage to him or her;
4. the plaintiff acted upon the representation; and


the plaintiff suffered damage by so doing.\textsuperscript{15}

An action for the tort of deceit will lie whether or not there is a contractual relationship between the plaintiff and the defendant. Such an action may include, for example, architects or designers who have made fraudulent misrepresentations.

The law appear less clear on whether parties to a contract can absolve themselves from misrepresentations using disclaimers. A number of Canadian cases have upheld the view that, in the absence of fraud, typical contractual disclaimers are sufficient to absolve owners from negligent or innocent misrepresentations.\textsuperscript{16} The Supreme Court of Canada held that an owner can avail themselves of these types of contractual provisions, but that the contractor may have a cause of action in tort as against the owner’s engineers.\textsuperscript{17}

With respect to disclaimers of fraud and fraudulent misrepresentations, it appears as though the courts in British Columbia have adopted the view of the English House of Lords in \textit{S. Pearson & Son Ltd. v. Dublin Corp.} ([1907] A.C. 351 (HL)), that a fraudulent misrepresentation of fact vitiates the protective terms and exclusion clauses of a contract. This view was adopted by the B.C. Court of Appeal in \textit{Ballard v. Gaskill} ((1955), 14 W.W.R. (N.S.) 519 (BCCA)) and recently noted with favor by Southin J.A. in \textit{Can-Dive Services Ltd. v. Pacific Coast Energy Corp.} ([2000] B.C.J. No. 259 (BCCA)). It may be safe to conclude, therefore, that an owner can not disclaim fraudulent misrepresentation using contractual language in British Columbia.

\textbf{IV. EXCLUSION CLAUSES}

An exclusion clause, which purports to exempt liability must clearly extend to the exact contingency or event which has occurred, if it is to protect the party who relies upon it. This proposition may merely be another way of stating the \textit{contra proferentem} rule, which maintains that these types of exclusion clauses are to be construed strictly against those who drafted them and any ambiguities are to be resolved in favour of the innocent party.

Courts have referred to exclusion clauses variously as “exemption”, “exculpatory”, “exception”, “escape” and “protective” clauses. Limitation or limiting clauses can be categorized as a sub-category of exclusion clauses.


Instead of completely excluding liability for specified events, limitation clauses purport to contain or limit the damages or remedies available to the innocent party upon the happening of specified events. Some courts have taken the position that limitation clauses are different in quality from exclusion clauses and should be given a more liberal interpretation. In other respects, the principles governing the interpretation of exclusion and limitation clauses are the same.

In *B.G. Linton Construction v. C.N.R.* ([1975] 2 S.C.R. 678 (S.C.C.)), the majority of the Supreme Court of Canada held that, if an exclusion clause is drafted sufficiently clearly to leave no doubt about its meaning, then full force and effect will be given to it. An exclusion clause will only be interpreted *contra proferentem* where there is ambiguity as to the meaning of the clause in the contract.\(^{18}\)

Whether a clause is effective to exclude or limit liability depends upon its wording and the particular circumstances of the case. Some of the factors courts will consider when determining whether to give effect to an exclusion clause are:

1. the nature of the breach;
2. the equality of bargaining power of the parties;
3. whether the parties had independent legal advice;
4. whether the innocent party read and/or understood the clause;
5. the experience of the parties in the subject matter of the contract;
6. whether the clause was in the minds of the parties prior to the conduct complained of;
7. whether the contract was negotiated between the parties or was a standard printed form; and
8. whether enforcing the clause would be unconscionable or unfair and unreasonable in the circumstances.

---

\(^{18}\) See also *McClelland and Stewart Ltd. v. Mutual Life Assurance Company of Canada*, [1981] 2 S.C.R. 6, where it was held that the doctrine of *contra proferentem* did not come into play at all as there was no ambiguity in the contract.
V. INCORPORATION BY REFERENCE

In many instances, contracts attempt to draw in terms from other documents or contracts by making reference to them. This is particularly true in subcontracts, which have their own terms and frequently include a generic term that purports to include the entire prime contract and all of its requirements. While this sort of incorporation by reference is not an inappropriate practice, it is usually done without appropriate forethought of the consequences.

There are a number of potential pitfalls to this practice of incorporation by reference. While many of them arise out of poor drafting, these issues should be considered nonetheless:

1. If the subcontractor is to take on some or all of the general contractor’s roles, what are the limits of the assignment/agency? Can the subcontractor, for instance, create a breach of the prime contract? Can the subcontractor deal with changes/extras including accepting reductions in the prime contract price? How do changes/extras impact the subcontract price, obligations and risk allocations?

2. How are the payment provisions (i.e. “pay when paid”) to be applied?

3. From a practical perspective, is a copy of the prime contract (redrafted, perhaps for price etc.) to be attached?

In his treatise on construction contracts, the learned author, Wallace, states:

It is submitted that there is usually little difficulty in giving effect to loose or generalised incorporations where what is referred to is the contract description of the work in question in the main contract (i.e. in the drawings, specification or bills of that contract) and that in cases of doubt it is this part of the main contract which is intended, rather than the detailed application of contractual provisions as to liability, indemnities, or special claims for additional payment. On examination, these are almost always impossible to apply with any precision to the very different relationship between the main contractor and subcontractor.

An American author, Seemann, Jr., stated in a 1993 article:

---

Flow-down and flow-up clauses can create certain practical problems. Occasionally, the contractor will assume a special duty to the owner so that the language of the flow-down provision fails to pass to the subcontractor.

...

Under no circumstances are flow-down and flow-up provisions substitutes for specific language setting forth the rights and obligations of the parties. When the incorporation is clear and unambiguous and when reciprocal flow-down and flow-up provisions are used, the provision will be enforced. If, however, the slightest ambiguity exists between specific and incorporated language, the courts are reluctant to favour the incorporation, especially when ambiguous provisions appear to require the arbitration or if a waiver or lien clause is incorporated.

These excerpts point to some of the pitfalls of incorporation by reference. It is submitted that, where such incorporation extends beyond references to the technical specifications, extreme care must be taken to ensure that the contract is clear and unambiguous.

VI. CONCLUSION

Contract drafting is an art rather than a science. Perhaps, it may best be accomplished by presuming that everything will go wrong and that the parties will disagree on everything. Using such presumptions, a drafter should be able to obtain a contract capable of being interpreted according to the plain and ordinary meaning as intended by the parties, without need to resort to the other interpretation tools discussed herein.