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The Supreme Court Of Canada Proclaims 10 Rules For The Interpretation Of Contracts And The Review Of Arbitration Awards

The Supreme Court of Canada's recent decision in ***Sattva Capital Corp. v. Creston Moly Corp*.** is a remarkable document. It is more than a judicial decision. It is literally a textbook or checklist for the interpretation of contracts and the review of arbitration decisions.

Background

First, the context. Creston agreed to pay Sattva a finder's fee in relation to its acquisition of a mining property. The parties agreed that Sattva was entitled to a finder's fee of US$1.5 million and was entitled to be paid this fee in shares of Creston. They disagreed on which date should be used to price the shares and therefore the number of shares to which S was entitled. S argued that the share price was to be fixed on one date, and therefore it was entitled to about 11,460,000 shares priced at $0.15. C claimed that the proper date was the date when the compensation was payable, that the agreement's "maximum amount" proviso prevented S from receiving shares valued at more than US$1.5 million on that date and therefore that S should receive approximately 2,454,000 shares priced at $0.70. The parties agreed to arbitrate their dispute under the **B.C. *Arbitration Act***.

The arbitrator found in favour of Sattva. Creston was denied leave to appeal on the basis that the issue was not a question of law. The Court of Appeal reversed that decision and granted C's application for leave to appeal, finding that the arbitrator's failure to address the meaning of the agreement's "maximum amount" proviso raised a question of law, and remitted the matter to the superior court.

The superior court judge then dismissed C's appeal from the arbitrator, holding that the arbitrator's interpretation of the agreement was correct. The Court of Appeal allowed C's appeal, finding that the arbitrator reached an absurd result. The Court of Appeal also held that the superior court judge was bound by the Court of Appeal's prior decision. S appealed to the Supreme Court of Canada which re-instated the decisions of the arbitrator and the superior court judge.

Decision of the Supreme Court of Canada

Here are the major pronouncements in the Supreme Court's decision. They are not listed in the decision in this way but they appear to be the major grounds for the decision.

1. **A contract should be interpreted in light of the surrounding circumstances.**

   The Supreme Court held that a contract should be interpreted in light of all the surrounding circumstance. Moreover, doing so does not contradict the parol evidence rule. The court said:

   "The parol evidence rule does not apply to preclude evidence of the surrounding circumstances. Such evidence is consistent with the objectives of finality and certainty because it is used as an interpretive aid for determining the meaning of the written words chosen by the parties, not to change or overrule the meaning of those words."

2. **The interpretation of a contract is a question of mixed fact and law, not a question of law.**

The Supreme Court held that, except in the "rare" instances in which an "extricable question of law" can be found, the interpretation of a contract is a matter of mixed fact and law, not a matter of law. The court acknowledged that historically, the determination of the rights and obligations under a contract was considered a question of law. However, Justice Rothstein, speaking for the unanimous court, said that rule should no longer apply:

"I am of the opinion that the historical approach should be abandoned. Contractual interpretation involves issues of mixed fact and law as it is an exercise in which the principles of contractual interpretation are applied to the words of the written contract, considered in light of the factual matrix."

Justice Rothstein said that it "may be possible to identify an extricable question of law from within what was initially characterized as a question of mixed fact and law" but that "courts should be cautious in identifying extricable questions of law in disputes over contractual interpretation."

3. **Leave cannot be granted to appeal the interpretation of a contract by an arbitral tribunal award if the test for granting leave is "a question of law"**

Under the arbitration statutes of most provinces, leave to appeal from the arbitrator's award can be granted if there is a question of law involved. A strong argument can be made that the whole regime relating to appeals from arbitral awards was premised on the historical assumption that the interpretation of a contract was a matter of law. In *Sattva*, the Supreme Court held that an interpretation of a contract does not raise a question of law, and so it held that leave to appeal should not have been granted in this case. So in the future, and except in rare instances, a court may no longer grant leave to appeal to determine if the arbitrator was correct in his or her interpretation of the contract.

This decision goes affects much more than applications for leave to appeal. It affects any legal regime relating to the interpretation of a contract. For example, if the parties agree to an appeal on a point of law – and most of the provincial and territorial arbitration statutes allow the parties to do so - now such an agreement will not allow an appeal concerning the interpretation of the agreement.

Accordingly, this decision will require that parties proposing to enter into an arbitration agreement re-think how they express in their agreement the rights of appeal from the arbitral decision. If they intend that the interpretation of the contract by the arbitral tribunal is to be appealable, then it is no longer sufficient for them to provide for an appeal on a question of law. They must now provide for an appeal on a question of mixed fact and law.

In addition, many provincial and territorial arbitration statutes – including British Columbia's - do not allow the parties to agree to an appeal from an arbitral decision on a question of mixed fact and law, only on a question of law. Under this decision of the Supreme Court of Canada, none of those statutes will now allow the parties to include a review of the interpretation of a contract as a ground of appeal. A whole subject of contract law has potentially been removed from the court's review.

4. **The test for leave to appeal is "arguable merit"**

The Supreme Court of Canada held that the test for a superior court to apply when considering an application to appeal from an arbitral award is "arguable merit." The test may be described in many different ways using different words, but they come down to these two words.

This test is met if "the issue raised by the applicant cannot be dismissed through a preliminary examination of the question of law. In order to decide whether the award should be set aside, a more thorough examination is necessary and that examination is appropriately conducted by the court hearing the appeal once leave is granted." In the case of legal issues, "the appropriate threshold ….is whether it has arguable merit, meaning that the issue raised by the applicant cannot be dismissed through a preliminary examination of the question of law."

5. **The court has a residual discretion not to grant leave to appeal**

Even if the court considers that the appeal has arguable merit, the Supreme Court of Canada has confirmed that the court has a residual discretion not to grant leave to appeal. Discretionary factors to consider in a leave application include:

- the conduct of the parties
- existence of alternative remedies
- undue delay and
- the urgent need for a final answer

However, "courts should exercise such discretion with caution." If the court finds an error of law and a potential miscarriage of justice, then the discretionary factors "must be weighed carefully before an otherwise eligible appeal is rejected on discretionary grounds." There should be no double-counting of the relevant factors. For example, "respect for the forum of arbitration chosen by the parties is a consideration that animates the legislation itself and can be seen in the high threshold to obtain leave…Recognition that arbitration is often chosen as a means to obtain a fast and final resolution tailor-made for the issues is already reflected in the urgent need for a final answer." So this factor should not be counted again in exercising a residual discretion not to grant leave to appeal.

In considering misconduct in relation to this residual discretion, the court said that the misconduct of a party need not be directly relevant to the question of law in issue in the appeal.

6. The exercise of discretion should be reviewed by an appellate court with deference

The Supreme Court held that a discretionary decision by the court considering an application for leave to appeal from an arbitral award should be reviewed by another court with deference. An appellate court "should not be interfered with merely because an appellate court would have exercised the discretion differently… An appellate court is only justified in interfering with a lower court judge's exercise of discretion if that judge misdirected himself or if his decision is so clearly wrong as to amount to an injustice."

7. The review of an arbitral decision is not by way of judicial review applicable to administrative tribunals

The Supreme Court drew an important distinction between the review of an arbitral decision by a superior court under the statutes applicable to commercial arbitrations, and a review of the decision of an administrative tribunal by way of judicial review. Arbitral review is not judicial review in the latter sense. Appellate review of arbitral awards "takes place under a tightly defined regime specifically tailored to the objectives of commercial arbitrations and is different from judicial review of a decision of a statutory tribunal." As the court pointed out, "for the most part, parties engage in arbitration by mutual choice, not by way of a statutory process. Additionally, unlike statutory tribunals, the parties to the arbitration select the number and identity of the arbitrators." Furthermore, in the arbitration statutes of some provinces and territories (like British Columbia, but unlike the arbitration statutes in many other provinces and territories), the court is prohibited from reviewing an arbitral tribunal's factual findings. However, in the judicial review of administrative tribunals, a prohibition against the review of an administrative tribunal's factual findings "signals deference" under the Supreme Court's decision in ***Dunsmuir v. New Brunswick*****,** [2008] 1 S.C.R. 190.

8. The *Dunsmuir* test may be helpful to the review of arbitral awards

The Supreme Court did find, however, that the standard of review developed for administrative tribunals may be relevant or useful to the appeal or review of arbitral awards. The court said the two systems of review are:
"analogous in some respects. Both involve a court reviewing the decision of a non-judicial decision-maker. Additionally, as expertise is a factor in judicial review, it is a factor in commercial arbitrations: where parties choose their own decision-maker, it may be presumed that such decision-makers are chosen either based on their expertise in the area which is the subject of dispute or are otherwise qualified in a

manner that is acceptable to the parties. For these reasons, aspects of the ***Dunsmuir*** framework are helpful in determining the appropriate standard of review to apply in the case of commercial arbitration awards."

In applying the ***Dunsmuir*** test, the Supreme Court said the following*:*

"In the context of commercial arbitration, where appeals are restricted to questions of law, the standard of review will be reasonableness unless the question is one that would attract the correctness standard, such as constitutional questions or questions of law of central importance to the legal system as a whole and outside the adjudicator's expertise …The question at issue here, whether the arbitrator interpreted the Agreement as a whole, does not fall into one of those categories. The relevant portions of the ***Dunsmuir*** analysis point to a standard of review of reasonableness in this case."

9. The Court may supplement the reasons of the arbitral tribunal

The Supreme Court of Canada held that, in considering an application for leave to appeal from an arbitral award, the court may supplement the award by its own analysis before undermining the award by finding it deficient. The court quoted from its decision in ***Newfoundland and Labrador Nurses' Union v. Newfoundland and Labrador*** *(Treasury Board)*, [2011] 3 S.C.R. 708:

"even if the reasons in fact given do not seem wholly adequate to support the decision, the court must first seek to supplement them before it seeks to subvert them. For if it is right that among the reasons for deference are the appointment of the tribunal and not the court as the front line adjudicator, the tribunal's proximity to the dispute, its expertise, etc, then it is also the case that its decision should be presumed to be correct even if its reasons are in some respects defective." (underling in both decisions)
The Supreme Court proceeded to supplement the decision of the arbitral tribunal by its own reasoning. Having done so, it concluded that the interpretation of the contract by the arbitral tribunal award met the reasonableness standard and upheld the award.

10. The Leave to Appeal decision is not binding in subsequent hearings

The B.C. Court of Appeal had held that its previous decision granting leave to appeal, and the factual findings in that decision, were binding on the superior court judge and on itself during the subsequent hearings. The Supreme Court held that this was wrong:

"A court considering whether leave should be granted is not adjudicating the merits of the case… A leave court decides only whether the matter warrants granting leave, not whether the appeal will be successful…. This is true even where the determination of whether to grant leave involves, as in this case, a preliminary

consideration of the question of law at issue. A grant of leave cannot bind or limit the powers of the court hearing the actual appeal."

Discussion

This decision has a profound impact on the interpretation of contracts and the appeal and review of arbitral decisions. Some time is required to reflect upon and absorb the decision. The following comments are only a first stab at its full implications.

The decision apparently reduces the authority of the superior court to review arbitral decisions in two respects.

First, it reduces the grounds upon which an existing arbitration agreement may give rise to appellate review: except in rare instances, no leave to appeal on a matter of law may be granted to review the correctness of the interpretation of a contract by an arbitral tribunal, and an agreement providing for an appeal on a matter of law will not encompass such a review.

Second, it reduces the ability of parties to future arbitration agreements to agree on appellate review of the correctness of the interpretation of a contract by an arbitral tribunal; if the applicable arbitration statute does not permit the parties to agree to an appeal on a question of mixed fact and law, then no such appellate review appears possible.

The decision also provides guidance on the practice which applies to applications for leave to appeal from arbitral awards. This guidance particularly applies to the scope of the court's discretion, the impact of a party's improper conduct upon the exercise that discretion, the non-binding effect of the leave to appeal decision and the scope of the reviewing court's entitlement to supplement the reasoning contained in the award. So while the leave to appeal door may have been partially closed by this decision, to the extent that the door is still open the decision clarifies and to some extent broadens the court's powers to deal with the application.

Sattva v. Creston goes into the first drawer of the Contract and Arbitration tool boxes with a big red sticker on it.

***Sattva Capital Corp. v. Creston Moly Corp.,* 2014 SCC 53**

Contracts - Interpretation of Contracts - Arbitration – Appeal and Review of Arbitral Awards

Discretion - Standard of Review

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