

When to Speak Up: Applying the Parol Evidence Rule in Contractual Disputes

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In a terse, seven-paragraph decision, the Court of Appeal for Ontario applied the parol evidence rule, a doctrine fundamental to contract law and how we litigate contractual disputes, to dismiss an appeal. *Fung v. Decca Homes Ltd.*¹ is an interesting case study in the parol evidence rule and its role in contractual disputes.

The Story

Fung overpaid Decca Homes by \$150,000 for a construction project. The parties eventually entered into a demand promissory note for the full amount. After a few miscommunications, Fung made a written demand on the promissory note. Fung sent the demand to Decca Homes' lawyers, who had been given an irrevocable direction to pay the funds to Fung but only if Decca Homes' properties, into which the overpayment had been directed, had sold.

The law firm did not pay, and Fung brought an application for payment. The application was granted. Decca Homes appealed.

Parol Evidence Rule: Oral Agreement Cannot Contradict the Written Agreement

On appeal, Decca Homes argued that the application judge failed to consider an alleged oral agreement, made at the same time as the promissory note, that purportedly modified the promissory note. The Court of Appeal upheld the application judge's refusal to do so. The Court of Appeal explained that the parol evidence rule operates such that, "[e]ven if there was a collateral oral agreement, something that is disputed by the respondent, that oral agreement could not contradict the written agreement. Accordingly, we agree with the application judge that the written agreement prevails and that the respondent could enforce the note."² No further analysis was needed.

In part, the Court of Appeal could be brief because the parol evidence rule has a long history in the common law. In *Leitch Gold Mines Ltd. v. Texas Gulf Sulphur Co.*,³ the Ontario High Court summarized the rule as follows:

A transaction having been reduced to writing, extrinsic evidence is generally inadmissible to contradict, vary, add to or subtract from its terms. This is fundamental in the interpretation of

¹ 2019 ONCA 848 [*Fung*].

² *Fung*, 2019 ONCA 848 at para. 5.

³ [1969] 1 O.R. 469 (Ont. H. Ct.) at para. 238.

written instruments. Parol evidence may, however, be admitted in aid of interpretation.

Parol evidence is evidence relating to the written agreement that is not included in the written agreement itself. A common example of parol evidence is oral evidence given by a party to explain the circumstances surrounding the written contract. Although the law requires us to consider the surrounding circumstances when entering an agreement, the parol evidence rule makes it impermissible to use such extrinsic evidence to interpret the agreement in a way that contradicts or varies the written text of the agreement.⁴

In *Fung*, based on the finding that the oral agreement purported to contradict the written agreement, the rule applied. In cases where the oral agreement does not so clearly contradict the written agreement, counsel can point to an exception to the parol evidence rule. For example, if part of the agreement is oral, or where there is clear evidence that the parties did not include every term of the agreement in the written contract, parol evidence becomes admissible to prove the remaining terms of the agreement. In this way, whether a written contract contains the full agreement of the parties is a presumption which can be rebutted.⁵ In *Fung*, the Court of Appeal likely did not consider this use of parol evidence because the oral agreement appeared to contradict the written document. Also, *Fung* disputed the existence of the oral agreement.

There are several other circumstances in which parol evidence is admissible, although none of them appear to apply on the facts of *Fung*. For example, parol evidence has been admitted where one party challenges the validity of an agreement. Courts will also consider parol evidence where there has been fraud, illegality, mistake in fact or law, lack of capacity in or any other matter which, if proved, would speak to the validity of the document.⁶

Rectification is another scenario in which parol evidence is admissible. Courts have held that where an agreement contains a mistake such that the written terms do not reflect the actual agreement between the parties, parol evidence may be admitted to support rectification.⁷ Rectification allows the parties to revise the document and reconcile the form and language of the agreement with the intention of the parties.⁸

Further, an exception to the parol evidence rule exists where the contract contains a particularly onerous clause that is not brought to the attention of the party seeking to avoid

⁴ See, for example, *C.J.A., Local 579 v. Bradco Construction Ltd.*, [1993] 2 S.C.R. 316; and *Gutierrez v. Tropic International Ltd.* (2002), 63 O.R. (3d) 63 (Ont. C.A.).

⁵ *Cudmore, Civil Evidence Handbook*, (2019) at s. 15.6. See also *Corey Developments Inc. v. Eastbridge Developments (Waterloo) Ltd.* (1997), 34 O.R. (3d) 73 (Ont. Gen. Div.); affirmed (1999), 34 O.R. (3d) 73 (Ont. C.A.).

⁶ *Cudmore, Civil Evidence Handbook*, (2019) at s. 15.7. See also *Haig v. Malfara Holdings Inc.* (1992), 11 C.P.C. (3d) 116 (Ont. Ct. J. [Gen. Div.]) and *Chant v. Infinitum Growth Fund Inc.* (1986), 55 O.R. (2d) 366 (Ont. C.A.) [*Chant*].

⁷ *Waddams, Law of Contracts*, 2nd ed. (1984) at p. 243.

⁸ *Lovell & Christmas Ltd. v. Wall* (1911), 104 L.T. 85 (Eng. C.A.); and *Chant* (1986), 55 O.R. (2d) 366 (Ont. C.A.).

the application of that clause. Parol evidence may be admitted to show that the parties never agreed to the clause, disentitling the first party from relying upon it.⁹

However, parol evidence will not be admitted to establish the subjective intentions of the parties. Rather, where a term is ambiguous, the court must consider what a reasonable person would have taken the words of the document to mean.¹⁰ Relying on the Supreme Court's finding in *Non Marine Underwriters, Lloyd's of London v. Scalera*,¹¹ the Ontario Superior Court held in *Recchia Developments Inc. v. 1059233 Ontario Ltd.* that "[a]mbiguity exists if the contract phraseology is capable of more than one meaning. In that event, the most reasonable interpretation which promotes the intentions of the parties prevails."¹²

Conclusion

Long-established in the history of contract law, the parol evidence rule is often applied strictly and, as seen in *Fung*, with little room for dispute. However, counsel should not be deterred from its strict application in cases that trigger an exception to the rule. The rule's many exceptions are evidence that the interests of fairness and justice guide a court's application of the rule. However, counsel must not forget that the rule's purpose of promoting certainty and finality in agreements guides the court in its consideration of extrinsic evidence. When you intend to introduce parol evidence before the court, carefully assess whether an exception applies or risk swift defeat in the face of the parol evidence rule.

⁹ See *Hoffman v. Sportsman Yachts Inc.* (1990), 47 B.L.R. 101 (Ont. Dist. Ct.), additional reasons (August 17, 1990), Doc. York 335051/88 (Ont. Dist. Ct.), affirmed on other grounds (1992), 89 D.L.R. (4th) 600 (Ont. C.A.); and *Beer v. Townsgate I Ltd.* (1997), 36 O.R. (3d) 136 (Ont. C.A.). See also *MacQuarie Equipment Finance Ltd. v. 2326695 Ontario Ltd. (Durham Drug Store)*, 2020 ONCA 139, where the Ontario Court of Appeal relied on parol evidence and held that a failure in communication between the parties resulted in a lack of real assent on an onerous provision in the agreement at issue.

¹⁰ See, for example, *Kentucky Fried Chicken Canada v. Scott's Food Service Inc.* (1998), 41 B.L.R. (2d) 42 (Ont. C.A.); *Misfud v. Owens Corning Canada Inc.* (2003), 38 C.C.P.B. 109 (Ont. Sup. Ct. J.); and *Commercial Alcohols Inc. v. Suncor Energy Products Inc.*, 2008 ONCA 261.

¹¹ 2000 SCC 24.

¹² (2015), 252 A.C.W.S. (3d) 832 (Ont. S.C.J.) at para. 42.