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OFNLP and the Scope of "Surrounding Circumstances" in Contract Interpretation

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One of the Honourable Mahmud Jamal's last decisions as a justice of the Court of Appeal for Ontario was *Ontario First Nations (2008) Limited Partnership v Ontario Lottery and Gaming Corporation*[1]—a case involving the interpretation of a contract in the context of a *sui generis* relationship between the government and First Nations. In *OFNLP*, the Court of Appeal considered an arbitration panel's use of evidence of pre-contractual negotiations as an aid to interpret the financing agreement at issue.

As a historical rule, drafts and discussions involved in reaching a written contract are not relevant to the contractual interpretation exercise.[2] However, in the eight years since the Supreme Court of Canada did away with the historical approach to interpreting contracts in *Sattva Capital Corp v Creston Moly Corp*,[3] courts have grappled with the question of whether pre-contractual negotiations may be considered as part of the relevant "surrounding circumstances" when interpreting a contract.

Some have relied on the *OFNLP* decision to suggest that it is appropriate in all cases for triers of fact to look to the pre-contractual negotiations between parties to interpret an agreement. We suggest that the precedential value of the *OFNLP* decision is more limited.[4]

Background

In 2008, the Province of Ontario and the Ontario Lottery and Gaming Corporation ("OLG") entered into a Gaming Revenue Sharing and Financial Agreement ("GRSFA") with a limited partnership of 132 of the First Nations in Ontario (the "First Nations Partnership"), which entitled the First Nations Partnership to a defined annual share of the revenue generated from gaming carried on in Ontario.[5] Specifically, the GRSFA provided that the First Nations Partnership would receive 1.7% of Gross Revenue based on three revenue sources: (1) gaming revenue from lotteries, slots, and table games from operations conducted and managed by OLG; (2) revenues from non-gaming activities ancillary to those operations; and (3) the retail value

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[1] *Ontario First Nations (2008) Limited Partnership v Ontario Lottery and Gaming Corporation*, 2021 ONCA 592 [***OFNLP ONCA***].

[2] This is known as the common law parol evidence rule. See *Indian Molybdenum Ltd v The King*, [1951] 3 DLR 497 (SCC) at 503, which is referred to as binding authority in *Wesbell Networks Inc v Bell Canada*, 2015 ONCA 33 at para 13.

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

[4] Please note that discussions about the standard of review and honour of the Crown doctrines are beyond the scope of this paper.

[5] Arbitration Reasons for Decision dated March 27, 2019 [***Arbitration Decision***] at paras 1-2, 8.

of accommodation, food and beverage services, and other services provided to gaming patrons on a complimentary basis to encourage them to visit and stay at the gaming sites.[6]

A few years later and without notice to the First Nations Partnership, OLG outsourced its non-gaming amenities to private operators as part of a "modernization" process and stopped paying two of the three types of revenue under the GRSFA.[7] OLG and Ontario argued that the GRSFA did not entitle the First Nations Partnership to revenues that neither Ontario nor OLG received.[8] The First Nations Partnership commenced arbitration.

The Arbitration Decision

The arbitration lasted ten days and resulted in a 385-paragraph award in which the majority of the panel ruled that Ontario and OLG breached the GRSFA. Modernization did not relieve them of their payment obligation to share 1.7% of the three revenue sources that existed when they signed the GRSFA in 2008.[9]

The dissenting panel member described Ontario and OLG's unilateral changes to the operation of the GRSFA as "breathtaking in the age of reconciliation",[10] but held that the First Nations Partnership had no right to share in revenues that OLG did not receive. He also found that the majority's interpretation relied on inadmissible evidence of the parties' negotiations.

At the arbitration, the parties led evidence about (i) their history of litigation over revenue sharing, (ii) their shared objective of locking-in three identified revenue streams to ensure stable, predictable, long-term funds for First Nations' communities, and (iii) Ontario's commitment not to convert revenues received to the final account of the Province into revenues that were not.[11]

Notably, the GRSFA negotiations had two phases: the Peterson phase and the Bryant phase. The panel majority considered evidence from both, including: a Term Sheet signed by the negotiating teams that set out a base definition for "Gross Revenue", an Agreement in Principle that outlined the three agreed-upon revenue components, correspondence between the First Nations Partnership and Ontario representatives, correspondence between Chief Toulouse and Minister Bryant, contemporaneous handwritten notes from others involved about the components of Gross Revenue, and affidavit evidence from Minister Bryant about what was said in the final month to build trust between the First Nations Partnership and Ontario.

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[6] Arbitration Decision at para 3.
[7] Arbitration Decision at para 4.
[8] Arbitration Decision at para 114.
[9] Arbitration Decision at para 258.
[10] Arbitration Decision at para 365.
[11] *OFNLP ONCA* at para 64.

At the final meeting, Minister Bryant made the following statement:

> Over 25 years this is a projected $3 billion agreement. It doesn't change, no matter who the Premier is, no matter who the Minister of Aboriginal Affairs is, no matter what colour the Government is…this is an agreement and it provides stability of revenue for 25 years…[I]n the commercial agreement, the old one, there wasn't the respect in that agreement that is deserved in a Nation-to-Nation relationship. So this is an important agreement as well because it's a clear indication, as clear an indication from the Government, not in words, but in deeds and in rights and in dollars, as to our commitment to a new relationship based upon respect and autonomy.[12]

The panel majority held that evidence from the Peterson phase was evidence of the shared understanding of the parties of the components of Gross Revenue that they agreed to in the Agreement in Principle. It was not evidence of negotiations seeking to reach agreement nor evidence of the subjective intention of either party.[13] While the Bryant phase evidence did consist of discussions that took place during the final negotiations of the GRSFA, the panel deemed this admissible as objective evidence of the shared understanding of already settled contract language.[14]

The ONSC Decision

On appeal to the Superior Court of Justice,[15] Ontario and OLG argued that the panel majority erred in admitting and considering extrinsic evidence when interpreting the GRSFA.

The late Justice Hainey rejected this argument, holding that the "witnesses were not relied upon by the majority for what their subjective intention was but rather their evidence was relied upon by the majority to establish the statements made to each other during the negotiations of the GRSFA and their mutual understanding based upon those statements".[16] The shared understanding of the parties is admissible as part of the surrounding circumstances.[17]

The ONCA Decision

Among other issues, Ontario and OLG argued at the Court of Appeal that the appeal judge erred in law by failing to apply the entire agreement clause under section 1.10 of the GRSFA and by

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[12] Arbitration Decision at para 52.
[13] Arbitration Decision at para 179.
[14] Arbitration Decision at para 189.
[15] *Ontario First Nations (2008) Limited Partnership v Ontario Lottery And Gaming Corporation*, 2020 ONSC 1516 [***OFNLP ONSC***]
[16] *OFNLP ONSC* at para 98.
[17] *OFNLP ONSC* at para 96. See also *Canada (Attorney General) v Fontaine*, 2017 SCC 47.

failing to correct the panel majority's decision to admit extrinsic evidence that overwhelmed the words of the GRSFA.[18]

The Court of Appeal rejected this submission by using principles of contractual interpretation laid out in *Sattva*, and more recently, *Corner Brook (City) v Bailey*:[19]

- An entire agreement clause alone does not prevent a court from considering admissible evidence of the surrounding circumstances at the time of contract formation because the surrounding circumstances are relevant in interpreting a contract.[20]

- The nature of the evidence that may be considered as part of the surrounding circumstances will vary from case to case, but should include only "objective evidence of the background facts at the time of the execution of the contract". This is a question of fact.[21]

- The purpose of considering the surrounding circumstances is not to add to, contradict, or vary the terms of the agreement but rather use them as an interpretive aid to determine the meaning of the words in dispute. The surrounding circumstances should never be allowed to overwhelm the words of the agreement.[22]

The Court of Appeal saw no error in how the surrounding circumstances were considered in this matter. The circumstances helped to place the GRSFA "in its proper setting and understand the genesis of the transaction, the background, and the context".[23]

Takeaway

OFNLP teaches that evidence of the factual matrix may include evidence of the parties' negotiations and correspondence at the time they executed a contract. Relevant background and context are often essential to understand contractual language.[24] However, *OFNLP*—decided by three members of the Court of Appeal as opposed to the usual five when it is asked to decline to follow a precedential decision—does not purport to change the law regarding the presumptive inadmissibility of pre-contractual negotiations.

The arbitration panel majority was explicit in its reasons that it was not using the extrinsic evidence of the negotiations of the GRSFA as parol evidence, but rather to identify the parties' shared objective understanding when they agreed to specific contractual terms. It was clearly attuned to the inadmissibility of evidence of a party's subjective intention.

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[18] *OFNLP ONCA* at para 44.
[19] *Corner Brook (City) v Bailey*, 2021 SCC 29 [***Corner Brook***].
[20] *OFNLP ONCA* at para 62; *Sattva* at para 47. See also *IFP Technologies (Canada) Inc v EnCana Midstream and Marketing*, 2017 ABCA 157.
[21] *OFNLP ONCA* at para 46; *Sattva* at para 58.
[22] *OFNLP ONCA* at para 62; *Sattva* at para 57.
[23] *OFNLP ONCA* at para 64.
[24] *OFNLP ONCA* at para 62.

The Supreme Court has acknowledged this tension between the modern approach to contractual interpretation directed by *Sattva*, and the traditional rule that evidence of negotiations is inadmissible when interpreting a contract, but opted to leave the question of "whether, and if so, in what circumstances, negotiations will be admissible in interpreting a contract" for another day.[25]

At the very least, *OFNLP* presents advocates with an example of such a circumstance. It may also mark further erosion of the parol evidence rule. What is clear on the state of the law at present, however, is that extrinsic evidence can only be used to help understand the parties' objective mutual intentions and background facts leading to an agreement so long as such evidence is not used to overwhelm the words of the agreement or to create a new agreement.

[25] *Corner Brook* at paras 56-57.