Toronto Law Journal

"Act or Omission": A Case Study in Condominium Law
Lozano v TSCC No. 1765, 2020 ONSC 4583; 2021 ONSC 983 (CanLII)

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Chargebacks and Acts and Omissions

Condominium living boasts many benefits, including, among other things, a wide array of physical amenities, provision of various services (i.e. security, concierge etc.) and having ownership of a financially growing and profitable real estate asset. However, condominium living also carries a degree of responsibility on the unit owners in respect to their units. Of these responsibilities, perhaps one of the most prominent, is an owner's responsibility to ensure that their unit is well maintained and is not the source of property damage to any other units or the common elements of a corporation.

Subsection 105(2) of the *Condominium Act, 1998* ("***Act***") provides that if an owner, a resident or guest of a unit ("**Origin Unit**"), causes damages to the Origin Unit, through an act or omission, the amount that is lesser of the cost of repairing the damage to the Origin Unit and the deductible limit of the corporation's insurance policy, shall be added to the Origin Unit as a common expense.

Thus, subsection 105(2) of the *Act*, has two qualifications:

(1) The chargeback can only be applied to the cost of repairing the Origin Unit and cannot be applied to the cost of repairing any other affected units and/or common elements which were damaged from a cause that originated in the Origin Unit; and,

(2) The chargeback can only be applied if the corporation can establish "an act or omission" on the part of the Owner of the Origin Unit that has caused and/or resulted in the damage.

Most Ontario condominium corporations have a deductible bylaw which eliminates the first qualification of subsection 105(2) and, thereby, allows a corporation to chargeback the Origin Unit not only the costs of repairing the Origin Unit but also the costs of repairing any other affected units and common elements, up to the corporation's insurance deductible. Significantly, however, standard deductible bylaws commonly preserve the second qualification of subsection 105(2), requiring a corporation to establish "an act or omission" on behalf of the Owner of the Origin Unit that had caused and/or resulted in the damage, before being able to impose a chargeback against the Origin Unit.[1]

[1] Not all deductible bylaws preserve the requirement for the corporation to establish an act or omission on the part of an Owner before a chargeback, up to the corporation's insurance deductible amount, can be imposed. The analysis

But what is an "act or omission"? And how is this broad term interpreted and applied by our courts?

Until recently, a debate ensued between opposing lawyers, with those representing condominium corporations insisting that the term "act or omission" imposed a strict liability standard on owners, while those representing unit owners insisted that the term "act or omission" is to be defined as negligence.

In the leading decision of *Lozano v. TSCC 1765*, 2020 ONSC 4583 ("***Lozano***"), subsequently upheld on appeal, J.E. Ferguson J. dispelled much of this confusion and provided some clarify to an otherwise ambiguous term.

Factual Overview

The Lozanos owned a condominium unit (the "**Unit**") in Toronto. In April 2018, the float in their en-suite toilet tank cracked (the "**Toilet**"). The Lozanos replaced the Toilet's float themselves. No other work or repair was done to the Toilet, nor did the Lozanos encounter any other problems with the Toilet.

In November 2018, the Lozanos went to the Philippines for five (5) months. The Unit was unoccupied during their absence; however, their nephew and family friend attended at the Unit once every two weeks to check the premises to ensure that the heat was turned on and to collect the mail. Neither the Lozanos' nephew, nor their family friend, used the Toilet while they were in the Unit.

On April 12, 2019, approximately twelve months after the Lozanos replaced the Toilet float, a flood occurred in the Unit (the "**Flood**"). The Flood caused damage to the Unit, the unit below, and the third and fourth floor hallways.

The Flood was caused by a broken ballcock at the base of the stem of the Toilet, which caused water to constantly fill and overflow the Toilet. The Lozanos' condominium corporation, Toronto Standard Condominium Corporation 1765 ("**TSCC 1765**"), has a by-law which provides that unit owners are responsible for the cost of repairing damages (up to TSCC 1765's insurance deductible limit) when the damage is caused by the unit owners' "act or omission".

TSCC 1765 paid to repair the damage caused by the Flood and, subsequently, demanded reimbursement of same from the Lozanos (the "**Chargeback**"). TSCC 1765 took the position that the Lozanos were responsible for the payment of the Chargeback, in accordance with its by-law.

The Lozanos' home insurer, Allstate Insurance Company ("**Allstate**"), contested the validity of TSCC 1765's Chargeback demand. Allstate argued that the Lozanos did not commit an "act or

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discussed in this article does not apply to those corporations that have a deductible bylaw that does not contain the "act or omission" qualification.

omission" which caused and/or resulted in the Flood, as required by TSCC 1765's by-law in order for the Chargeback to be imposed.

TSCC 1765 registered a lien against the Unit for the amount of the Chargeback. Allstate, on behalf of the Lozanos, paid the Chargeback under protest, in order to discharge the lien. Allstate then commenced an application against TSCC 1765, seeking, *inter alia*, a declaration that TSCC 1765 had no lawful right to the Chargeback.

Application Judge's Findings

There was no dispute that the Flood originated from a malfunction of the Toilet. The material question for the Application Judge was whether the Lozanos committed an "act or omission" which caused and/or resulted in the Toilet's malfunction (and subsequent Flood).

The Application Judge reviewed s. 105(2) of the *Act*, which provides:

> If an owner […] **through an act or omission causes damage** to the owner's unit, the amount that is the lesser of the cost of repairing the damage and the deductible limit of the insurance policy obtained by the corporation shall be added to the expense payable for the owner's unit. [**emphasis added**]

TSCC 1765 argued that: (1) the Lozanos committed an "unreasonable act by failing to have a plumber repair their toilet when its plastic parts first showed signs of decay in April 2018"; and (2) "when the Lozanos made repairs in 2018, they should have replaced the entire ballcock mechanism and not just the float element" of the Toilet.

Allstate, on the other hand, argued that the Lozanos did not commit an "act or omission" that caused the Toilet's malfunction and subsequent Flood. The Lozanos diligently maintained the Unit and made the necessary repairs in April 2018. In fact, the Toilet functioned properly after being repaired, and the decay on the plastic mechanism was "completely unforeseeable".

The Application Judge relied on the decision of *Cornerstone Heights Condominium Corporation v. Payam and Sanaz Holdings Limited,* 2019 SKBC 70 in holding that that an "act or omission" does not depend on a finding of negligent behavior. In that regard, the Judge held that the standard of establishing liability, under s.105 of the *Act*, is between the standard of negligence, and strict liability, and is "perhaps closer to the latter".

Thus, despite finding that the Lozanos diligently maintained their Unit, the Application Judge determined that the Lozanos' decision in not hiring a plumber in 2018 to undertake thorough repairs of the Toilet, was an "omission" for which the Lozanos were responsible. In addition, and importantly, the Application Judge found that the Lozanos should have shut off the water to the Unit during their prolonged absence from the Unit. Consequently, the Application Judge held that the Lozanos were liable to TSCC 1765 for payment of the Chargeback.

Divisional Court's Findings

On appeal, Allstate argued, *inter alia*, that the Application Judge adopted the wrong legal test in determining whether an "act or omission" "caused" the Flood. Allstate's proposed test sought to import an element of "reasonableness" and "foreseeability" into the s. 105 analysis. Specifically, Allstate argued that, in order to find liability, a unit owner must "ordinarily and reasonably" be expected to maintain a unit component, and that failure to "use, maintain, monitor, or repair a unit component" must foreseeably result in damage.

The Divisional Court confirmed that a s.105 analysis does not import any requirement of unit owner negligence, and in that regard, a reasonableness inquiry as to the unit owner's "act or omission" does not form part of the liability analysis. Similarly, the court also confirmed that a strict liability analysis is not appropriate.

The Divisional Court offered guidance on what a condominium corporation must prove when seeking to claim a chargeback pursuant to s.105 of the *Act*. Specifically, to invoke liability, the loss/damage must be "caused by the unit owner's act or omission". In other words, the Court held that TSCC 1765 carries the evidentiary burden of proving, on a balance of probabilities, that the Flood was **caused** by the Lozanos' "act or omission". Therefore, the liability analysis is entirely dependent on TSCC 1765's ability to establish a causal link between the Flood and the Lozanos' alleged "act or omission".

Further emphasizing the causation analysis, and rejecting a negligence standard, the Court stated:

> [24] … Theories of liability have long held that there are two components to the causation analysis: cause in fact; and cause in law. Cause in fact is the more purely factual enquiry, sometimes described as the "but for" or the "necessary condition" test. "But for" the defendant's act (or omission), would the damage have occurred? Cause in law is the more vexed question, involving more "policy oriented" considerations. These typically include questions like: was the alleged act or omission too "remote" from its purported effect; was the result abnormal when compared to what might otherwise have been expected; was the damage "unforeseeable", lacking in "proximity" or coincidental; and, were there other, intervening causes.

Having set out this framework, the Divisional Court rejected the first of TSCC 1765's arguments, namely, that the Lozanos committed an "omission" by failing to hire a plumber to perform the original repair work of the Toilet in April 2018. The Court held that "[t]here was no evidence that the [Lozanos'] replacement of the cracked float in April 2018 was the cause of the leak in April 2019. Likewise, there was no evidence that, if a plumber had attended in April 2018, he or she would have found a defect or failure in the ballcock mechanism and replaced this entire mechanism with a new one, thus avoiding the damage". Consequently, the Court found TSCC 1765's argument a matter of "pure speculation" because there was no form of notice or warning such as an ongoing problem that required attention which the Lozanos ignored.

However, the Court found TSCC 1765's second argument – relating to the Lozanos' failure to shut off the water to the Unit during their extended absence - more convincing; specifically, the Court held this "omission" to have been the "cause" of the Flood. In simple terms, "but for" the "omission", the damage would not have occurred. The Divisional Court specified that but for the Lozanos' five-month absence, if the Unit were occupied or inspected daily, the leak would have been discovered and remedial action would have been taken immediately, thus preventing the damage that occurred.

Conclusion

Thus, in order to enforce a chargeback for repairs against a unit, up to a corporation's insurance deductible amount, the corporation has to be able to identify an act or omission by the owner that caused the damage. A chargeback can be enforced as long as the corporation is able to establish a causal link between an owner's act or omission and the damage that occurred. The owner's act or omission does not have to be reasonable nor does the damage have to be foreseeable in order to enforce a chargeback against the unit from which the damage had originated (up to the corporation's insurance deductible amount). For instance, in the Lozano decision, the Lozanos' act of travelling outside of the country for five months while having a family member attend at the unit every 2 weeks was reasonable. Further, the Lozanos' omission of not turning off the water supply to the unit, during their absence, was not unreasonable. Nonetheless, the Lozanos were found liable for the chargeback strictly on the basis of there being a causal link between their omission (i.e., failure to turn the water supply off) and the subsequent water leak.

In summary, the Divisional Court provided much needed guidance on the applicable framework for establishing liability against unit owners under section 105 of the *Act*. The court held that the loss or damage must be caused – in fact and in law - by the owner's "act or omission".

Finally, although the legal test is clear, the question of whether an "act or omission" is the cause of certain damage will depend on the particular facts of each case.

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In Australia, Google has the last laugh – maybe

Howard Winkler, Winkler Law[1]

A recent decision of Australia's highest court is a major victory for Google, clarifying that it is not liable for facilitating the publication of content created by others, even if given notice of the defamatory nature of the content. From a Canadian point of view, what is interesting is that large portions of this well-reasoned judgment rely on a ruling handed down by the Supreme Court of Canada (SCC).

In *Google LLC v Defteros*, Australia's highest court set aside a ruling that found Google should be considered a publisher if it links to defamatory material after being put on notice of the defamatory nature of the content. The case involved a Melbourne-based criminal lawyer who "acted for persons who became well-known during Melbourne's 'Gangland Wars'".

The article suggested that he had crossed the line from being a professional lawyer to becoming a confidant and friend of criminal elements.

According to the judgment, the lawyer successfully sued Google for (AUD) $40,000 after the search engine refused to take down a hyperlink leading to the specific article.

Australian court references Canadian judgment

To explain why the search engine should not be held liable for linking to that article, the Australian court drew heavily on the 2011 SCC decision in *Crookes v Newton*, delivered by Justice Rosalie Abella and who is referenced throughout the Australian judgment.

"As observed in *Crookes v Newton*, a hyperlink is content-neutral," the Australian judgment reads. "A search result is fundamentally a reference to something, somewhere else. Facilitating a person's access to the contents of another's webpage is not participating in the bilateral process of communicating its contents to that person."

- Anti-SLAPP legislation is failing. Here's a possible fix
- Court ruling a small step in closing Google's 'gateway to harm'
- Google must do more to combat defamatory online reviews

The Australian court repeatedly returns to *Crookes v Newton*, noting, "Referencing on its own does not involve exerting *control* over the content. Communicating something is very different from merely communicating that something exists or where it exists. The former involves

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dissemination of the content and suggests control over both the content and whether the content will reach an audience at all, while the latter does not."

This is a significant common-law defamation decision. It clearly establishes that search engines such as Google are not *prima facie* a publisher for the purposes of defamation simply because they facilitate access to the content of others.

Not an absolute win for Google

Yet this is not an absolute win for Google. That is because the court leaves open the possibility that the snippet of content – made up of 20 or so words – that Google provides in search results could itself be defamatory. A snippet that is itself defamatory or incorporates, adopts or endorses the content linked to may give rise to liability. Further, a snippet that invites or encourages comment might also give rise to liability.

That latter situation is more of an issue for platforms such as Facebook or Google reviews, rather than Google search results per se.

The judgment is also important in that it manages to reconcile all of the previous legal decisions in Australia involving Google, Facebook and claims of defamation, on issues not yet considered by Canadian courts. I have addressed some of those in previous posts, including Australia proves that Google and Facebook can be tamed and Australia is winning the battle against Google and Facebook.

Our courts will find the ruling persuasive

Because the decision is so well-reasoned and relies so heavily on the ruling of the SCC, it is likely Canadian courts will find this decision persuasive when considering these other issues.

No matter how you look at it this was a significant victory for Google. As the Australian judgment notes, "Facilitating a person's access to the contents of another's webpage is not participating in the bilateral process of communicating its contents to that person."

In Australia and elsewhere, including Canada, attention now will be focused on snippets or the manner in which links to the content of others is described.

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The Impact of Secret Trusts on Wills and Testamentary Gifts

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Gift-giving is often perceived as an act of generosity, or even altruism, but sometimes gifts come with "strings attached" – meaning that the gift, if accepted, "involves special demands or limits."[1] Perhaps there is no greater string to attach to a gift, at least a testamentary bequest, than a secret trust. Under this doctrine, a testator appears to leave property in his will to one beneficiary, when in fact the parties have made a separate arrangement to have the beneficiary hold the property for the benefit of a third party – an ultimate beneficiary. As long as the beneficiary named in the will agrees to act as trustee, or simply acquiesces to the arrangement, a secret trust may be made out and enforced.[2]

Secret trusts may seem confounding, as they are counterintuitive to the overarching law that otherwise governs wills and estates. Testators can use secret trusts to make bequests that need not be included in any will, and which can be upheld despite failing to comply with statutory will formalities.[3]

Creating a Secret Trust

Secret trusts are not a recent legal innovation, despite having been addressed numerous times by appellate courts over the last decade – this doctrine dates back to the 1700s.[4] Like other express trusts, secret trusts must satisfy three certainties. Language of intention is needed to form the trust, plus the trust property and the beneficiaries or objects must be certain.[5] These certainties must be exhibited at the time the trust is created.[6]

Additional requirements must also be satisfied to establish a secret trust, namely:

- the deceased must intend to impose a trust obligation on the beneficiary;
- the deceased must communicate his or her intention to the beneficiary that: (1) the property be held in trust by the beneficiary, and (2) the beneficiary transfer that property to the ultimate beneficiary after the death of the donor; and

[1] *Cambridge Dictionary*, sub verbo "strings attached": online *Cambridge Dictionary*, retrieved 6 July 2022 from https://dictionary.cambridge.org/us/dictionary/english/strings-attached.
[2] See C. A.W., J. Finkelman and John Willis, "Case and Comment" (1937) 15:2 *Canadian Bar Review* 101 at 101, online: 1937 CanLIIDocs 71 <https://canlii.ca/t/t83v> [1937 Case Comment].
[3] *Ibid.*
[4] According to Alastair Hudson, "[t]he case law in this area can be traced back at least to *Sellack v Harris* (1708), 2 Eq Ca Ab 46 (Eng) through *McCormick v Grogan* (1869), LR 4 HL 82." See Alastair Hudson, "Conscience as the Organising Concept of Equity" (2016) 2:1 *Canadian Journal of Comparative and Contemporary Law* 261 at 286, fn 86: online: 2016 CanLIIDocs 48 <https://canlii.ca/t/q7>.
[5] *Peters v. Peters Estate*, 2015 ABCA 301 at para 18 [*Peters*].
[6] *Gefen Estate v Gefen*, 2022 ONCA 174 at para 49 [*Gefen*], citing *Champoise v Prost*, 2000 BCCA 426 at para 16.

- the beneficiary must either agree to act as trustee and hold the property in trust for the ultimate beneficiary, or acquiesce to the arrangement.[7] On this point, the British Columbia Court of Appeal recently confirmed that acceptance of a secret trust can be "spelled out of silence", as the law imposes an obligation on a trustee-beneficiary to be forthright and actually advise the donor if he or she will not uphold the donor's intentions.[8]

A secret trust may take the form of either oral or written instructions to hold the donor's property in trust.[9] If a written agreement is utilized, the agreement ought to be signed by both the donor and the beneficiary-trustee who will receive legal title to the trust property upon the donor's death.[10] To give rise to a secret trust, there must also be an actual transfer or grant of property between the parties to the agreement.[11] It further warrants noting that a written agreement giving rise to a secret trust is not a testamentary instrument, meaning that if the donor subsequently creates a new will, the agreement will not be revoked by that will.[12]

In addition to secret trusts, there are also half-secret trusts, in which the donor's will indicates that the property is to be held in trust but does not disclose the identity of the ultimate beneficiary.[13] In comparison, with a secret trust, the deceased's will will not disclose the existence of either the trust or the name of the ultimate beneficiary. While secret trusts often arise in the context of wills, a bequest inherited on intestacy can also be subject to a secret trust.[14]

A Moral Obligation Is Not Enough

Even though secret trusts are an equitable remedy, a moral obligation "intended to guide the recipient's conscience" cannot, on its own, be the basis of a secret trust.[15] This was a live issue in *Gefen Estate v Gefen*,[16] a case in which the testator signed an agreement with one of his sons, who ultimately received a significant portion of the testator's estate. The testator's other sons argued that the agreement gave rise to a secret trust, which compelled the son to share the property he had received with his siblings. However, no secret trust was found, both at trial and on appeal. One of the reasons for this decision was that the document only spoke of the father's intentions and did not give rise to a binding obligation. There was no evidence that the son who signed the agreement agreed to receive assets in trust for his siblings.

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[7] *Peters*, *supra* note 5 at para 20.
[8] *Bergler v Odenthal*, 2020 BCCA 175 at para 29 [*Bergler*].
[9] *Peters*, *supra* note 5 at para 19.
[10] See *Gefen*, *supra* note 6 at paras 54-56.
[11] *Ibid*.
[12] See *Gough v Leslie Estate*, 2022 NSCA 25 at para 56 [*Gough*].
[13] *Gefen*, *supra* note 6 at para 46, citing A. H. Oosterhoff, "Secret and Half-secret Trusts," Ontario Bar Association Continuing Legal Education, Trusts, Trustees, Trusteeships – All You Need to Know and More …, September 18, 2006 at 3.
[14] See *Bergler*, *supra* note 8.
[15] *Gefen*, *supra* note 6 at para. 50.
[16] *Ibid*.

Enforcing a Secret Trust

In order to enforce a secret trust, it would be advisable to establish detrimental reliance. In *Gough v Leslie Estate*,[17] the Nova Scotia Court of Appeal confirmed that secret trusts function because "legal title [is] granted in reliance on the undertaking to hold title for the benefit of others."[18] Legal commentary also notes that one reason equity can be used to enforce a secret trust is because the donor is unable to perfect the trust and ensure that the intended beneficiary receives the trust property him or herself – the deceased has no choice but to rely on the secret trustee's promise to carry out the trust.[19]

Inequitable conduct should also be established when enforcing a secret trust. Often the primary reason for enforcing a secret trust is "to avoid fraud, as absent intervention by equity, the trustee who received property might keep it, rather than [abide] by the terms of the trust."[20] Typically, a secret trust will be enforced to prevent unjust enrichment, or as restitution of a wrong committed by the trustee.[21]

Like all civil matters, the burden of proof is the balance of probabilities. There must be evidence available to prove that the deceased donor advised the beneficiary-trustee of an intention to have property held in trust, and that the donor advised who was to be the ultimate beneficiary of the trust. The evidence must also establish that the beneficiary of the estate either agreed to hold the property in trust or acquiesced to the testator's request. Without such evidence, a secret trust will not be recognized, let alone enforced.[22] As a secret trust operates outside a will, it may be proven by extrinsic oral or written evidence.[23]

On an interesting note, a secret trust does not need to be secret in order to be enforceable. According to the Nova Scotia Court of Appeal, "[t]he secrecy of the trust simply means that the obligations described do not appear in the testator's will."[24]

However, if a secret trust is truly secret, proceedings to enforce it, or alternatively prove that the trust was not performed, ought to be pursued during the lifetime of the beneficiary-trustee. If the terms of the trust are not disclosed by the beneficiary-trustee prior to death, there may be insufficient evidence to subsequently prove that a secret trust was established, as was the case in *Hayman v. Nicholl*.[25] The testatrix's codicil in this case stated that she was leaving funds to her beneficiary "in full confidence that she [would] dispose of the same in accordance with the wishes which [the testatrix] expressed to her." The beneficiary used some of the funds for

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[17] *Gough*, *supra* note 12.
[18] *Ibid* at para 43, emphasis added.
[19] Robert Chambers, "Constructive Trusts in Canada" (1999) 37:1 *Alta LR* 173 at 191, online: 1999 CanLIIDocs 188, <https://cttanlii.ca/t/skt4> [Chambers article]. See also 1937 Case Comment, *supra* note 2 at 104: "it is the promise notion, with its resulting reliance (often invoked by the courts as a substitute for consideration), that the courts fastened on as creating a 'duty'."
[20] *Gefen*, *supra* note 6 at para 47.
[21] Chambers article, *supra* note 19 at 189-190.
[22] See *Peters*, *supra* note 5.
[23] *Spylo v. Spylo*, 2014 ONSC 3843 at para. 55, aff'd 2016 ONCA 151.
[24] *Gough*, *supra* note 12 at para 50.
[25] *Hayman v. Nicholl*, 1944 CanLII 70, [1944] SCR 253 (S.C.C.).

her own benefit before passing away, but took no steps to distribute the funds to any other party and did not tell any third party about how the testatrix had wanted the funds to be disposed of. The residuary beneficiaries of the estate argued that the unused funds were subject to a secret trust and ought to go into the residue of the estate, as the funds had not been disposed of in accordance with the testatrix's wishes. The Supreme Court of Canada dismissed the residuary beneficiaries' claim on several bases, including that a secret trust had not been proven. Without evidence of how the testatrix intended the funds to be used, or evidence from the beneficiary-trustee about what the testatrix's wishes were, there was no basis to find a secret trust. Justice Rand did acknowledge, however, that in some cases such circumstances might give rise to an inference that a trust was intended, depending on the evidence before the court.[26]

Closing

While equity provides a way to dispose of an estate outside the confines of a will or other testamentary instruments, relying on the courts to enforce a secret trust (should a trustee go rogue and refuse to fulfill the donor's wishes) is fraught with risk. Appellate courts have confirmed in a number of cases that secret trusts are still enforceable,[27] but the outcome in cases like *Gefen Estate v. Gefen*[28] demonstrate that even with a written agreement in hand, a secret trust may not be established. The surest way to control the administration of an estate remains the same – recording all instructions for the distribution of the testator's estate in a valid will.

[26] *Ibid* at 259.
[27] See *Bergler*, *supra* note 8; *Gough*, *supra* note 12.
[28] *Gefen*, *supra* note 6.

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The Dough Does Not Rise for the Licensor

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In *Milano Pizza Ltd. v 6034799 Canada Inc.* (**"Milano"**), the Federal Court of Canada expunged Milano Pizza Ltd.'s (the **"Licensor"**) trademark registration because of the Licensor's failure to exercise sufficient control over the trademark.

Background Facts

The Licensor had been granting to independent pizzerias in Ottawa licenses to use the Milano design mark (the **"Milano Design Mark"**) and the words MILANO PIZZERIA and MILANO PIZZA. The licenses required that the licensees operate in a certain territory and purchase MILANO branded products from approved suppliers. The licences were often verbal arrangements rarely reduced to writing. Any agreements that might have been reduced to writing before the mid-2000s were destroyed by a flood. As well, most licensees operated with different menus and different recipes for the various menu items.

The defendants, 6034799 Canada Inc. o/a Milano Pizzeria – Baxter Road, et. al. (collectively, **"603"**), purchased the Milano Pizza Baxter Road location in 2001. 603 had purchased the business from the previous owners, the Khorrami brothers, who owned 50% of the business. The purchase documents did not require 603 to enter a licence agreement with the Licensor. No trademark clearance search was conducted during the purchase, and the asset purchase agreement did not mention any trademarks. Nonetheless, 603 continued to comply with the unwritten license agreement by, in addition to using the Milano Design Mark and the unregistered word marks, purchasing branded products from approved suppliers and complying with the territorial restrictions imposed by the Licensor.

After a series of disputes, the Licensor terminated 603's licence in 2016. Despite 603's license being terminated, 603 continued to operate the business using the same social advertising, menus, and signs except for the storefront logo which was changed to a similar variation of the Milano Design Mark. As a result, the Licensor brought a claim against 603 for trademark infringement for continuing to use the Milano Design Mark without authorization. In the counterclaim, 603 sought the expungement of the Milano Design Mark.

Was the Milano Design Mark valid?

The Court examined whether the registration of the Milano Design Mark was valid under section 50(1) of the *Trademarks Act* (the **"Act"**). This subsection of the Act governs licensing and deems that the use, advertisement, or display of a trademark by an authorized licensee to be that of the trademark owner if the owner maintains, under licence, direct or indirect control

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of the character or quality of the goods or services in association with which the trademark is used, advertised, or displayed. Although a written licence agreement is not a requirement to establish licensed use of a trademark, the trademark owner must provide evidence of control over the use of the trademark under a licensing arrangement. If a trademark owner fails to demonstrate such sufficient control and exercise, then the trademark may lose any distinctiveness it benefits from under section 50(1) of the Act.

Was there sufficient control over the licenced goods and services?

The Court acknowledged that the Licensor exercised some control over the quality and character of the goods and services by requiring licensees to purchase ingredients from approved suppliers. However, this was insufficient to protect the distinctiveness of the trademark under section 50(1) of the Act. The Court emphasized that a trademark owner must oversee both the input and output of goods and services to properly control the licensed trademark. Although the Licensor controlled the quality of the branded ingredients, it failed to monitor the finished product, the pizza, and other items on the menu. The Licensor also failed to impose a uniform standard for the menu items and did not enforce a right of inspection. The Court emphasized that controlled licensing includes regular inspections by trademark owners and the documentation of such inspections.

Lengthy Co-Existence of a Non-Affiliated Pizzeria

The Court also examined the co-existence of a non-affiliated pizzeria. For over 40 years, Pizzeria Milano had operated independently in Masson, Quebec, and used the same menu and store sign display. Since they were working in the same industry, the Court concluded that the similarities found between the trademarks of the two separate businesses resulted in the Licensor's trademark not being tied to a distinctive single source. This further undermined the distinctiveness of the Milano Design Mark.

The Court's Decision

The Court ultimately found the Milano Design Mark to be non-distinctive for two reasons. First, the Licensor had not established sufficient control over the character or quality of the goods and services used by the licensees under the trademark. Second, the Licensor could not enjoy any acquired distinctiveness from the trademark because of the existence of the non-affiliated pizzeria in Masson, Quebec, that had used the trademark MILANO PIZZERIA for over 40 years. Thus, the Court ruled in favour of 603 by finding the Milano Design Mark to be invalid and ordered the expungement of the Milano Design Mark pursuant to section 18(1)(b) of the Act.

Practice Takeaways

This decision is a helpful reminder for brand owners to maintain direct or indirect control over the use of their trademark licences. Registered trademarks are national in scope, and even a single co-existing competitor can risk the distinctiveness of the trademark. Trademark owners should require that their licensees execute proper license agreements, regularly inspect the

way licensees use the trademark and document such inspections, control the character and quality of both the input and output of licensed goods and services, and police any non-authorized uses of the trademark. Failure to do so may result in the invalidation of a registered trademark.

A copy of the Federal Court decision can be found here.