COURT FILE NO.: 04-CV-272021 CM2
DATE: 20050106

ONTARIO

SUPERIOR COURT OF JUSTICE

IN THE MATTER of the *Arbitration Act*, 1991, S. O. 1991, c. 17
AND IN THE MATTER of an arbitration award dated July 10, 2004
AND IN THE MATTER of an arbitration between 407 ETR Concession Company Limited ("407 ETR") and Her Majesty the Queen in Right of the Province of Ontario as represented by the Minister of Transportation and the Minister of Transportation for Ontario ("Province")

APPLICATION UNDER section 45 of the *Arbitration Act*, 1991, S. O. 1991, c. 17 and under section 25 of the Concession Ground Lease Agreement dated April 6, 1999 and Section 5 of the Tolling, Congestion Relief and Expansion Agreement dated April 6, 1999

B E T W E E N:

HER MAJESTY THE QUEEN IN RIGHT OF THE PROVINCE OF ONTARIO AS REPRESENTED BY THE MINISTER OF TRANSPORTATION and THE MINISTER OF TRANSPORTATION FOR ONTARIO

Applicants

John Keefe, Jessica Kimmel and ***Julie Rosenthal*** - - for Her Majesty the Queen

- and -

407 ETR CONCESSION COMPANY LIMITED

Respondent

J. Thomas Curry and ***Nina Bombier*** - - for 407 Concession Company Limited

HEARD: December 1 and 10, 2004

REASONS FOR DECISION

CULLITY J.

[1] By notice of application, the Province appealed from a decision of the Honourable J. Drew Hudson Q.C. (the "Arbitrator") who conducted an arbitration between the parties pursuant to the provisions of the *Arbitration Act, 1991*, S.O. 1991, c. 17, and of an agreement between them. Under these provisions there is a right of appeal only on questions of law. Any findings of the Arbitrator on questions of fact, or questions of mixed law and fact, are binding on the parties and must be accepted on this appeal.

A. The Dispute

[2] The background to the dispute between the parties - and the issues submitted to arbitration - were described by the Arbitrator as follows:

> There has been a tremendous amount of work done since 1950 in trying to understand what the transportation requirements of the GTA will be as it grows and develops.
>
> In 1993 the Ontario Government attempted to interest the private sector in constructing Highway 407. This was unsuccessful because the risk/reward relationship was not attractive to the private sector.
>
> The Ontario Transportation Capital Corporation ("OTCC") was therefore established by the province as a Crown Agency to oversee the design, construction, operation maintenance and management of Highway 407. OTCC's operation of Highway 407 was pursuant to the legislative authority granted to it under the Capital Investment Plan Act, 1993 ("CIPA") and its regulations.
>
> Actual construction of Highway 407 commenced in 1994. Highway 407 opened initially under the management of the OTCC on June 7, 1997. The OTCC only began to charge tolls on October 14, 1997. At the time of opening, Highway 407 was 36 kilometres long and had 79 entry and exit points.
>
> OTCC was continued as a corporation with share capital as 407 ETR Concession Company Limited ("407 ETR") by Articles of Continuance dated April 6, 1999.
>
> Also on April 6, 1999, 407 ETR entered into the Concession and Ground Lease Agreement ("CGLA"), a 99 year concession agreement, with the Province. Also on April 6, 1999, 407 ETR entered into the Tolling, Congestion Relief and Expansion

Agreement ("TCREA") with the Province and this was schedule 22 to the CGLA.

Both the CGLA and the TCREA were agreements between 407 ETR and the Province. Both were executed by "THE CROWN IN RIGHT OF ONTARIO, AS REPRESENTED BY THE MINISTER WITHOUT PORTFOLIO WITH RESPONSIBILITY FOR PRIVATISATION" and "407 ETR CONCESSION COMPANY LIMITED. It should be observed that the CGLA and the TCREA were agreements entered into between the Province and a Crown Agency of the Province.

It should also be observed that there are 24 schedules attached to the CGLA and of these only the TCREA and schedules 13, 15, 18 and 19 are called agreements. In my opinion this is not relevant to the resolution of the present dispute.

The shares of 407 ETR were acquired by 407 International Inc, a consortium of non-public corporations, from the Province under a share purchase agreement dated April 12, 1999 with a closing date of May 5, 1999.

The Province operated Highway 407 first through OTCC and then 407 ETR as a toll highway from October 14, 1997 to May 5, 1999. On May 5, 1999 the highway was 68 kilometres long and had 28 interchanges and a total of 146 entry and exit points.

Over the next 28 months Highway 407 was extended to 108 kilometres and now has 40 interchanges and a total of 193 entry and exit points.

I understand that the cost to the Province of building the 68 kilometre length was about $2 billion dollars. The Province sold the shares of 407 ETR for $3.107 billion dollars. The Province and its taxpayers made a profit of at least $1 billion dollars (50 %) over a period of about three years from the start of construction to the closing of the sale. The cost of extending the highway from 68 kilometres to its present 108 kilometres was about $1 billion dollars which cost was borne entirely by the consortium and at absolutely no cost to the Province.

There is now a dispute between the parties as to the interpretation of the TCREA and certain provisions of the CGLA itself. At issue is whether the Applicant is required to obtain any form of approval or consent from the Province before revising toll rates or administration fees on Highway 407.

> The parties have agreed that the issues to be determined in this arbitration are:
>
> (a) Is the only requirement to be met by 407 ETR prior to the change of any toll or administration fee the provision of notice under Article 2.3 of the TCREA and are the tolls and administration fees set by 407 ETR after compliance with article 2.3 of the TCREA valid and enforceable?
>
> (b) Is 407 ETR required to seek or obtain any form of consent or approval, apart from the provisions of notice under Article 2.3 of the TCREA, prior to the implementation of a change in tolls or administration fees charged in connection with the use of Highway 407?
>
> (c) Did 407 ETR's toll rate increase of February 1, 2004 comply with the terms of the CGLA and the TCREA and was it therefore a valid exercise of the rights of 407 ETR to implement a toll rate change?
>
> (d) Was 407 ETR in default of the CGLA, the TCREA, or the ACT as a result of the February 1, 2004 toll rate increase?
>
> In order to answer these questions we must determine the intention of the parties on April 6, 1999 from the words used in the CGLA and the TCREA and any extrinsic evidence which can be properly considered.

[3] To the above summary I believe it is necessary to add only that the dispute arose as a consequence of 407 ETR's implementation of increased tolls on February 1, 2004 without requesting, or obtaining the approval of the Province. The Province subsequently gave notice that this constituted a default under the CGLA and that 407 ETR was to roll back the increases within 60 days.

B. The Arbitrator's Decision

[4] In his award dated July 10, 2004, the Arbitrator answered questions (a) and (c) in the affirmative and questions (b) and (d) in the negative. The essential issue between the parties was whether pursuant to the provisions of the *Highway 407 Act, 1998* S.O. 1998, c. 28 (the " 407 Act"), and the agreements between them, the approval and consent of the Province was required for the increases in tolls and administration fees that 407 ETR had purported to make. In answering this question in the negative, the Arbitrator relied first on what he considered to be the plain meaning of the provisions. He concluded:

> The contract should, if possible, be interpreted according to its plain meaning. In my opinion, the plain meaning is that the Concessionaire is not required to obtain any form of approval or consent from the Province before revising toll rates or administration fees on Highway 407.

[5] The Arbitrator then continued:

> If I am wrong and there is no plain meaning then I can refer to extrinsic evidence.

[6] He distinguished between three types of extrinsic evidence: *first*, the factual matrix - or the circumstances surrounding the formulation of the contract; *second*, parol evidence - "evidence of subjective intent outside the four corners of the contract"; and, *third*, evidence of the manner in which the contract had previously been performed. The first type of extrinsic evidence he considered to be always admissible but the second and third types would be so only when a finding that a provision in a contract was ambiguous in the sense of being "reasonably susceptible of more than one meaning". Being evidently satisfied that such an ambiguity would exist if the relevant provisions of the agreements had no plain meaning, the Arbitrator then reviewed evidence that included statements made by officials of the Province to the effect that the Concessionaire of Highway 407 would have control over the level of the tolls and fees that would be charged. In addition to this evidence that confirmed the conclusion he had reached independently of it, the Arbitrator found further support for his conclusion in the *contra proferentem* principle, the previous behaviour of the parties and the "commercial absurdity" of the interpretation advanced on behalf of the Province.

C. The Appeal

[7] In the appeal, the Province seeks to have the award varied pursuant to section 45 (5) of the *Arbitration Act* so that questions (a) and (c) would be answered in the negative and questions (b) and (d) in the affirmative. The grounds for the appeal are that the Arbitrator erred in law in interpreting the relevant provisions of the CGLA and the TCREA, and in his consideration of extrinsic evidence for that purpose. Counsel were agreed at the hearing that, the admissibility of such evidence and, to the extent that it could be ascertained from the words of the agreements - without the aid of extrinsic evidence - the question of interpretation, were questions of law that could properly be the subject of an appeal. Counsel for 407 ETR, however, submitted that to the extent that the Arbitrator based his interpretation of the agreements in part on extrinsic evidence, its correctness, or otherwise, was a question of fact or, at least, one of mixed law and fact that could not be reviewed on the appeal. It was accepted that a standard of correctness was to be applied for the purpose of the appeal on the questions of law.

[8] It will be convenient to deal, first, with the Province's challenge to the correctness of the Arbitrator's finding that, on the plain meaning of the agreements between the parties, the approval, or consent, of the province was not required. The questions relating to the admissibility of extrinsic evidence will then be considered.

1. The plain meaning of the agreements

(a) The Arbitrator's reasons

[9] In his references, and findings, with respect to the plain meaning of the agreements, the Arbitrator's approach to their interpretation was consistent with that of the Supreme Court of Canada in *Eli Lilly & Co v. Novopharm Ltd* (1998), 161 D.L.R. (4th) 1, of the Court of Appeal in *Hi-Tech Group Inc. v. Sears of Canada Inc.* (2001), 52 O.R. (3d) 97 and of courts in numerous other cases. The governing principle was stated by Iacobucci J. in *Eli Lilly* as follows:

> ... it is unnecessary to consider any extrinsic evidence at all when the document is clear and unambiguous on its face. In the words of Lord Atkinson in *Lampson v. City of Quebec* (1920), 54 D.L.R. 344 (P.C.):
>
> > ... the intention by which the deed is to be construed is that of the parties as revealed by the language they have chosen to use in the deed itself....[I]f the meaning of the deed, reading its words in their ordinary sense, be plain and unambiguous it is not permissible for the parties to it, while it stands unreformed, to come into a Court of justice and say: "our intention was wholly different from that which the language of the deed expresses..."
>
> ... [T]o interpret a plainly worded document in accordance with the true contractual intent of the parties is not difficult, if it is presumed that the parties intended the legal consequences of their words. This is consistent with the following dictum of this court, in *Joy Oil Co. v. The King*, [1951] S.C.R. 624 at p. 641, [1951] 3 D.L.R.582:
>
> > ... in construing a written document, the question is not as to the meaning of the words alone, nor the meaning of the writer alone, but the meaning of the words as used by the writer.

[10] In determining that the plain meaning of the agreements between the parties was that 407 ETR was not required to obtain the approval of the Province to changes in the tolls or administration fees, the Arbitrator took as his starting point section 14 of the 407 Act which was intended to implement the decision of the Province to privatise the construction, maintenance, expansion and operation of the highway. This decision was announced in February, 1998. The legislation received Royal Assent on December 18, 1998. Section 14 sets out the powers of a tenant under a ground lease of Highway 407 lands - a person referred to in the statute as the "owner" of the highway. Among other things, section 14 (1) confers upon the owner the power "to establish, collect and enforce payment of tolls" and of "administration fees based on such

criteria as the owner considers appropriate". Such powers are conferred subject to the provisions of section 14 (2) that provide that they "shall only be exercised in accordance with the terms and conditions set forth in an agreement to be entered into between the Minister for Privatisation and the owner."

[11] The Arbitrator found that the agreement referred to in section 14 (2) of the 407 Act was the TCREA which was intended to be a "stand alone agreement". Section 2.2 of the TCREA confers on the Concessionaire the right to exercise powers - defined in the same terms as those in section 14 (1) of the 407 Act - at "any time while this agreement is in force in accordance with the provisions of this Agreement".

[12] Section 1.1 of the TCREA defines "Agreement" as "this tolling, congestion relief and expansion agreement including, for the avoidance of doubt, all schedules referred to herein".

[13] The TCREA contains no requirement for the Concessionaire to obtain the approval, or consent, of the Province to a change in tolls or administration fees. The only obligations with respect to such changes are imposed by section 2.3 that requires notice of them to be given to the Province and to the public. In part, it reads as follows:

> 2.3 Notice Of Toll Changes
>
> (a) If the Concessionaire desires to change any toll or administration fee, it shall give notice of such change (the "Pending Toll Change") to the [Province] at least four (4) weeks prior to the implementation of such change.
>
> (b) The Concessionaire shall make commercially reasonable efforts to inform the public of all tolls and administration fees for the use of Highway 407. After the giving of the notice referred to in subsection 2.3 (a), the Concessionaire shall include a description of the pending toll change on or with all invoices or statement sent by the Concessionaire to users of Highway 407 ...
>
> (c) Notwithstanding subsection 2.3 (a), if the Concessionaire desires to establish or terminate a temporary discount in respect of any fee or charge, it shall give notice of the establishment or termination of the said temporary discount to the [Province] at least one (1) Business Day prior to the implementation or termination of the said temporary discount.

[14] In the opinion of the Arbitrator, it followed that, if an obligation of 407 ETR to obtain the approval, or consent, of the Province is to be found in provisions of the TCREA - if, insofar as the establishment, and revision, of tolls and fees are concerned, it was intended to be a "stand alone" agreement – there was no such obligation.

[15] In finding that this was the intention of the parties as revealed by the words of the agreements, the Arbitrator referred to the substantively verbatim inclusion in the TCREA of the powers conferred in section 14 (1) of the 407 Act, an "entire agreement" clause in section 1.14 of the TCREA and a description of the purpose of the agreement in section 1.22. These provisions read as follows:

> 1.14 Entire Agreement
>
> This Agreement constitutes the entire agreement between the parties hereto pertaining to the subject matter hereof and supersedes all prior agreements, negotiations, discussions and understandings, written or oral, between the parties hereto. There are no representations, warranties, conditions or other agreements, whether direct or collateral, or express or implied that form part of or affect this Agreement, or which induced any party hereto to enter into this Agreement or on which reliance is placed by any party hereto, except as specifically set forth in this Agreement.
>
> 1.22 Purpose of Agreement
>
> The purpose of this Agreement is to establish a regime which offers the Concessionaire flexibility to manage the basis on which tolls will be established, the assurance of a minimum level of tolls, administration fees and charges which will be acceptable regardless of traffic levels and the freedom to establish higher tolls if prescribed traffic levels are achieved, while offering to the [Province] the assurance that the Concessionaire will be financially motivated to provide congestion relief to other roads and highways by achieving prescribed traffic levels, providing open access to all highways, providing access on reasonable terms to trucks and expanding Highway 407 as required.

[16] The Arbitrator inferred that the references in the above provisions to "this Agreement" referred to the TCREA in which, as previously indicated, the word "Agreement" was defined - "for the purposes of this Agreement" - to mean "this tolling, congestion relief and expansion agreement, including, for the avoidance of doubt, all schedules referred to herein." He concluded:

> There is no express or implied requirement in section 2.3 of the TCREA to obtain the consent of the Province. If such consent was required then it would have been expressly provided in the TCREA. It defies commercial reality and common sense that the Province, in drafting these agreements, would fail to provide for pre-approval of toll rate or fee increases if that was intended. The

> Concessionaire is only required to give four (4) weeks prior notice to the Province and make "commercially reasonable efforts to inform the Public" of the Pending Toll Change.
>
> Article 3 of the TCREA deals with CONGESTION RELIEF. It is at once apparent that congestion in any calendar year can only be determined after the end of the calendar year. Section 3.2 provides that in the event of Congestion, the concessionaire shall pay the Province an amount equal to two (2) times the excess amount of tolls that have been collected.
>
> In my opinion this would be grossly unfair if the Concessionaire had first to obtain the consent of the Province to the increase. In my opinion no reasonable business executives would agree to such an arrangement.

[17] The Arbitrator then referred to the submissions of counsel for the Province that the agreement referred to in section 14 (2) of the 407 Act was the CGLA and a further submission that 407 ETR requires the Province's approval of changes in toll rates. This further submission was based on an interpretation of provisions of the CGLA to which I will refer. It was rejected on the ground that the complexity of the reasoning on which the interpretation was based precluded a finding that it represented the plain meaning of the agreement.

[18] The Arbitrator referred to two other aspects of the agreements he considered to be relevant to his conclusion with respect to their plain meaning. One was a perceived conflict between the definitions of the word "Agreement" in the CGLA and the TCREA - a conflict that, in his opinion, was required, under the provisions of the former, to be resolved in favour of the definition in the TCREA. Counsel for 407 ETR did not attempt to support this conclusion. In their submission, as in that of counsel for the Province, there is no conflict between the CGLA and the TCREA.

[19] Finally, in support of his conclusion that the TCREA was intended to "stand alone", the Arbitrator referred to the inclusion in it of dispute resolution provisions that are also contained in the CGLA.

(b) Appellant's submissions on the plain meaning

[20] In the submission of counsel for the Province, the Arbitrator erred in law in finding that the TCREA alone was the agreement referred to in section 14 (2) of the 407 Act. In their submission, this agreement is the CGLA in its entirety - and not merely the TCREA that, as schedule 22, forms part of the CGLA.

[21] It was not disputed that the correctness of the submission turns on the construction of the CGLA and the TCREA. As neither agreement is expressed to be that referred to in section 14 (2) of the 407 Act, the question is essentially which of them should be considered to contain the terms and conditions attaching to the exercise of the powers conferred by section 14 (1) of the

statute and section 2.2 of the TCREA. I note that the question does not relate to the interpretation of the 407 Act but, rather to that of the agreements that were executed after its enactment. Section 14 (2) restricts the exercise of the powers in section 14 (1) by reference to terms and conditions to be agreed between the parties. The identification of the terms and conditions - and of the agreement that contains them - depends on the interpretation of the agreements between them and not of the statute.

[22] The significance of the question of interpretation lies in the existence of section 3.3 (b) of the CGLA that reads as follows:

> (b) Change Requests. The Concessionaire may submit or cause to be submitted Change Requests together with all appropriate supporting documentation to the [Province]. No Change Request shall be implemented or incorporated as part of the Work unless and until such Change Request has been approved.

[23] The position of the Province at the arbitration, and on this appeal, is that a variation of the tolls and administration fees requires a Change Request to be made and approved. Section 3.3 (b) does not expressly prohibit changes to be made without the submission of a Change Request. Construed strictly, the prohibition it contains is attached only to the implementation of Change Requests. These are permitted - but not expressly required - to be made. I am satisfied, however, that it is implicit in section 3.3 (b) – when read together with the definition of Change Request in the CGLA - that 407 ETR is not entitled to make changes that fall within the definition without first submitting a Change Request and obtaining the approval of the Province in accordance with the provisions of the CGLA that govern the giving, and withholding, of approval.

[24] Change Request is defined in section 1.1 of the CGLA, in part, as follows:

> "Change Request" means a written request in respect of the Project prepared by or on behalf of the Concessionaire and addressed to the [Province] seeking to(i) dispense with, delete or change the dimensions, character, quantity, quality, description, location or position of the whole or any part of the Work or make other changes to the Work in respect of Highway 407, provided that, for the avoidance of doubt, no Change Request shall be necessary to implement any change in the Work not specifically mandated or prohibited or otherwise regulated by the Governing Documentation or Laws and Regulations, ...

[25] In the submission of counsel for the Province, changes to toll rates and administration fees are changes to the Work in respect of the highway. This was said to follow from the definition of "Work" in section 1.1 of the CGLA and the definition of "OMM Work" which it incorporates and which, in turn, refers to "tolling". These definitions are as follows:

> "Work" means the DDB Work and the OMM Work

> "OMM Work" means the operation, management, maintenance, rehabilitation and/or a tolling of the Project in accordance with the Governing Documentation and Laws and Regulations.

[26] Counsel submitted that the clear meaning of these provisions of the CGLA is that changes to tolling - including changes to toll rates - require the consent of the Province and that the Arbitrator erred in law in finding to the contrary.

[27] Counsel submitted, further, that the finding that the TCREA is a stand-alone agreement is plainly contradicted by the reference to tolling in the definition of OMM Work and by other provisions of the CGLA that grant to 407 ETR the exclusive concession to levy and retain tolls. They relied also on the requirement in section 2.11 of the CGLA that 407 ETR was to

> comply with, and shall cause the Project and the development, design, construction, operation, management, maintenance, rehabilitation and tolling thereof to be in compliance with, all Governing Documentation and Laws and Regulations. ...

[28] "Governing Documentation" is defined in section 1.1 of the CGLA as including, among other things, the CGLA and its schedules and Approved Change Requests.

[29] These submissions on the central issue - which the Arbitrator described as "a tribute to the skill of counsel" - were supplemented by the following criticisms of the reasons of the Arbitrator that were said to disclose subsidiary errors of law:

> 1. the complexity of the process of interpreting an agreement is not antithetical to its plain meaning;
>
> 2. given the requirement for Change Requests in the CGLA, it cannot be said to defy commercial reality and common sense to accept that the province would neglect to provide for the pre-approval of toll increases in the TCREA if that was intended; and
>
> 3. the Arbitrator erred in finding that there was a conflict between the definitions of "Agreement" in the CGLA and the TCREA. The error was compounded by the further finding that the conflicting provisions of the TCREA were to be considered to be an express statement, pursuant to section 1.21 of the CGLA, that would be required, and effective, to exclude the stipulation that the provisions of the CGLA are to take precedence over conflicting provisions of its schedules.

(c) Conclusion on Plain Meaning

[30] I do not believe that the Arbitrator's finding with respect to the plain meaning of the agreements between the parties was vitiated by any error, or errors, of law. Section 2.2 of the

TCREA repeats the provisions of section 14 (1) of the 407 Act by giving 407 ETR the right to establish tolls and adds "at any time while this Agreement is in force". In the absence of any provision to the contrary, it must include the power to determine the rates at which tolls are to be levied from time to time and to make changes to them. Clause 1.14 of the TCREA indicates that it was intended to constitute the entire agreement between the parties "pertaining to the subject matter hereof". The relevant subject matter consists of the right, or power, to establish tolls. I believe it is clear that any limitations that define the ambit of the power, or restrictions that might be imposed on its exercise - as contemplated by section 14 (2) of the 407 Act - pertain to the same subject matter and, in consequence, are intended to be found in the TCREA. It was in this sense that the Arbitrator referred to the TCREA as a stand-alone agreement and I believe he was correct in so doing. The TCREA does deal expressly with changes in tolls or administration fees and imposes restrictions on the exercise of 407 ETR's powers to make such changes. Apart from a few specific exemptions for ambulances and fire-fighting, law-enforcement and diplomatic vehicles, the restrictions are confined to the giving of notice to the Province and to the public and impose no obligation to obtain the consent, or approval, of the former.

[31] In my opinion, the expressed purpose of the TCREA to establish a regime that would provide 407 ETR with "flexibility to manage the basis on which the tolls will be established" supports the correctness of the Arbitrator's conclusion. Section 1.22 includes as one of the purposes of the TCREA "the freedom to establish higher tolls if prescribed traffic levels are achieved". This contrasts with the provision that administration fees and charges may be levied "regardless of traffic levels". As the Arbitrator noted, given the imposition of congestion penalties if tolls are increased without achieving higher traffic levels, it is difficult to understand why prior approval of the Province would be necessary or appropriate. A more reasonable interpretation is that the flexibility and freedom that the TCREA was to confer with respect to the establishment of tolls was intended to be limited, and controlled, only by the existence of the congestion penalties that would be levied if prescribed traffic levels were not achieved. Whether congestion on other roads and highways has been reduced is to be determined by reference to the level of traffic on Highway 407. The penalties imposed if congestion has not been reduced are dependent on, and vary in accordance with, the level of the tolls charged to users of the highway.

[32] I accept that, if an obligation to obtain the consent of the Province was to be found in the body of the CGLA, the relevant provisions would take precedence over those of the TCREA. However, I do not accept that the provisions dealing with Change Requests - on which the Province relies - have that effect. The definition of Change Requests expressly excludes changes "not specifically mandated, prohibited or otherwise regulated by the Governing Documentation or Laws and Regulations." The Governing Documentation includes the TCREA, but I do not consider that changes in toll rates - let alone changes in administration fees - can be said to be a change in tolling specifically mandated, prohibited or regulated by the TCREA or any other provision of the agreements. To argue that changes in toll rates are "regulated" for this purpose because of the notice requirements would be to place a strained construction on the words of the definition. The more natural meaning is, I believe, that which counsel for 407 ETR supported: namely, Change Requests are required only where the change would conflict with an obligation, prohibition or restriction imposed elsewhere in the Governing Documentation.

[33] The criticisms leveled at the Arbitrator's description of the TCREA as a "stand-alone agreement" by counsel for the Province were, in my opinion, unjustified. I do not understand the Arbitrator to have implied that the TCREA exists, and is to be construed, independently of the CGLA for all purposes. This is obviously not the case as the TCREA is one of 24 schedules that form part of the CGLA and which are included in references to " this Agreement" throughout the body of the CGLA. As well as containing the ground lease and transfers of assets, the CGLA provides a framework for, and general provisions applicable to, the matters dealt with specifically in the schedules. Among these general provisions are those relating to Change Requests which are designed to introduce flexibility into the administration of the agreements by providing a procedure for consensual departures from the manner in which specific obligations of 407 ETR would otherwise be required to be performed.

[34] Change Requests would, for example, be required if 407 ETR wished to defer performance of any of its obligations to expand the highway pursuant to the provisions of the TCREA. Hence, the inclusion of section 5.3 of the CGLA that provides that such requests are not required for expansion of the highway in advance of the times stipulated in the TCREA. The section is expressed to be inserted for the avoidance of doubt and I believe it underlines the intention that Change Requests are to be required only to relieve 407 ETR from restrictions, or obligations, with which it was intended to comply. Similarly, if, in particular circumstances, 407 ETR wished to be relieved from strict compliance with the notice provisions of section 2.3 of the TCREA, a Change Request would, I think, be required. Apart from the few specific exemptions, no other restrictions are imposed on the power to establish tolls and administration fees in the TCREA and it "stands alone" in the sense that it is in its provisions that any restrictions, or limitations, on the powers are to be found.

[35] I do not attach significant weight to the other less fundamental criticisms of the Arbitrator's reasoning. While it may be correct that a plain meaning can emerge from a complex process of interpretation, the process to which the Arbitrator referred does not, in my opinion, do so.

[36] Like counsel, I am not sure that I understand fully the Arbitrator's references to - and treatment of - a conflict between the definitions of "Agreement" in the CGLA and the TCREA. In the relevant passages, he was, I think, addressing what he considered to be a flaw in the submissions of counsel for the Province, rather than providing an additional reason for his conclusion on the plain meaning. Even if his analysis in this part of his decision was in error, I do not believe it would invalidate the conclusion or detract from the other reasons for it that he provided.

[37] In consequence, I find that the Arbitrator was correct in law in finding that, on the plain meaning of the agreements between the parties, 407 ETR was not obligated to obtain the approval of the Province to increases in toll rates and administration fees. His answers to the questions to be determined in the arbitration were, in my opinion, correct.

[38] I have reached the above conclusion without regard to the Arbitrator's comments on the unfairness of – and the unlikelihood that reasonable business executives would agree to –

provisions requiring the Province's approval to toll increases. It is not clear whether the comments reflect a conclusion of the Arbitrator from the words of the documents alone, or whether they result from an acceptance of evidence of the Chief Financial Officer of 407 ETR with respect to the commercial consequences of the interpretation favoured by the Province. If the latter was the case, the reasoning of Iacobucci J. in *Eli Lilly*, at paras 55 - 56, that I have quoted earlier in these reasons, might suggest that they were out of place in a consideration of the plain meaning of the documents and should have been deferred until after a decision on the plain meaning had been made, and then considered only if no plain meaning had been found. The Arbitrator's comments were, in effect, repeated at the end of his reasons when he was reconsidering the question of interpretation on the hypothesis that his finding with respect to the plain meaning was not correct, and where he found that the interpretation supported by the Province would be commercially absurd. Even if the earlier comments must be considered to have been based on the evidence of the Chief Financial Officer, I believe the evidence was admissible as part of the factual matrix that explains the commercial consequences and effects of the provisions of the agreements and thereby throws light on their meaning. As Lord Wilberforce stated in *Reardon Smith Line Ltd v. Hansen-Tangen*, [1976] 3 All E. R. 570 (H.L.), at page 574 in a passage quoted with approval in *Hi-Tech*:

> No contracts are made in a vacuum: there is always a setting in which they have to be placed. The nature of what it is legitimate to have regard to is usually described as "the surrounding circumstances" but this phrase is imprecise: it can be illustrated but hardly defined. In a commercial contract it is only right that the court should know the commercial purpose of the contract and this in turn presupposes knowledge of the genesis of the transaction, the background, the context, the market in which the parties are operating.

[39] Evidence of the matters referred to by Lord Wilberforce must, in my opinion, extend to the commercial consequences of competing interpretations advanced by the parties; see, also, *Investors' Compensation Scheme v. West Bromwich Building Society*, [1998] 1 W.L.R. 896 (H.L.), at page 913.

[40] The Court of Appeal in *Hi-Tech* recognised - and the Arbitrator noted – that evidence of surrounding circumstances has been regarded as always admissible although, as Iacobucci J. insisted in *Eli Lilly*, it will be unnecessary if it merely confirms the meaning of the documents that is indicated by their clear and unambiguous language, and, if it is inconsistent with that meaning, it will not be permitted to displace it. Whether the language is reasonably susceptible of more than one interpretation may, however, appear only when the documents are read in their commercial context. Thus, in *Arthur Andersen Inc v. Toronto-Dominion Bank* (1994), 17 O.R. (3d) 363 (C.A.), Grange and McKinlay JJ. A. stated:

> The factual matrix in this case has been referred to earlier in these reasons. The purpose of the agreement was to provide for

> decreased administrative complexity in the operation of all accounts of the Stolp companies, to decrease administrative costs, to allow for transfer of funds between companies, and to provide for payment of interest on credit balances. All of these objectives were accomplished by the agreement, but they could not have been accomplished unless the agreement operated in one way only - by a real transfer of funds into and out of the concentration account. That being the case, viewing the contract in the context of its execution points to only one possible meaning … .

[41] It was held that it followed that the contract in question was not ambiguous.

[42] I am satisfied that the evidence of the commercial consequences of the interpretation favoured by the Province merely confirms the interpretation required by the words of the documents and that – if it was relied on by the Arbitrator - the most serious criticism that could be made is that this was unnecessary for the purpose of determining their plain meaning. In my opinion, the Arbitrator's use of the evidence would not be an error of law that would require his decision to be set aside, varied or remitted for further consideration pursuant to section 45 (5) of the *Arbitration Act*.

2. The Admission of Extrinsic Evidence

[43] In view of my conclusion with respect to the plain meaning of the agreements between the parties, it is not necessary to deal with the grounds for appeal based on the Arbitrator's consideration of extrinsic evidence. I believe this is so notwithstanding the submission of counsel for the Province that the Arbitrator's finding with respect to the plain meaning of the agreements was in some way tainted by his subsequent consideration of extrinsic evidence. I do not accept this submission. The Arbitrator indicated clearly that the subsequent discussion was undertaken only on the supposition that his finding with respect to the plain meaning was wrong. By doing this, he could reduce the likelihood that it would be necessary for the matter to be remitted to him if, on an appeal, his finding on the plain meaning was held to be incorrect. I believe he was entitled to do this and I will adopt essentially the same approach.

[44] As the right to appeal is limited to questions of law, the issue I was asked to address was not whether the extrinsic evidence considered by the Arbitrator confirmed the conclusion he had reached independently of it, but whether the evidence was admissible for the purpose of interpreting the agreements if they had no plain meaning and whether it was properly used for that purpose. The submission of counsel for the Province was, essentially, that the agreements were not ambiguous, the Arbitrator did not identify any ambiguity and, in consequence, the evidence of extrinsic evidence on which he was prepared to rely was not admissible.

[45] As I indicated earlier in these reasons, the Arbitrator distinguished evidence of surrounding circumstances - the factual matrix - from extrinsic evidence of the subjective intention of the parties and of the manner in which the agreements had been performed by them in years prior to 2004.

[46] I do not believe that any serious objection can properly be taken to the Arbitrator's references to extrinsic evidence of surrounding circumstances. If, as counsel for the Province suggested, the purpose for which the evidence was considered to be admissible is not completely clear, this I think, simply reflects the difficulty of reconciling some of the statements in *Eli Lilly* with those referred to in *Hi-Tech* that suggest that some such evidence is always admissible to explain the factual context in which agreements have been made and, by doing so, to cast light on their objectively-determined meaning. I doubt that the Supreme Court of Canada intended to deny the correctness of that proposition. Rather, the decision supports a narrower proposition, which I must accept, that there may be cases where, despite the imperfections of language as a means of communicating intentions, the meaning of a document appears clearly and unambiguously from its words. In such cases inferences from surrounding circumstances will not be permitted to displace that meaning and those that confirm it will be unnecessary. The Arbitrator's reasons are not inconsistent with that approach and, apart from his possible reliance on the evidence of the Chief Financial Officer that I have mentioned, the evidence of surrounding circumstances to which he referred in the event that there was no plain meaning does not appear to have had any significant bearing on the issues he had to decide. It related primarily to the problem of congestion on highways in the Greater Toronto Area and the advantages that privatisation was intended to achieve. In addition, of course, the Arbitrator's description of the background to the dispute between the parties was based to a very large extent on extrinsic evidence of surrounding circumstances.

[47] There are, I believe, difficulties with the Arbitrator's treatment of "parol evidence". Although this term originally referred to evidence given orally, it has long been extended to cover all types of extrinsic evidence - that is, evidence outside the document that is being interpreted. As I indicated earlier in these reasons, the Arbitrator used it in a different, and more limited, sense. Under the heading "Use of Parol Evidence", he stated:

> In Hi-Tech the Ontario Court of Appeal noted that a provision in an agreement is ambiguous when it is "reasonably susceptible of more than one meaning". A finding of ambiguity allows for a consideration of parol evidence (that is, evidence of subjective intent outside the four corners of a contract) and evidence of past performance in interpreting the meaning of the contract.

[48] My understanding of this part of the Arbitrator's reasons is that, if - contrary to his finding - a plain meaning did not emerge from the words of the agreements, it would follow that the relevant provisions of the agreement were reasonably susceptible of more than one meaning; and that that this would constitute an ambiguity that would justify the admission of extrinsic evidence of the parties subjective - or actual – intentions as well as evidence of their conduct in relation to the performance of the agreements in years before 2004.

[49] I am satisfied that the authority cited by the Arbitrator - and, in particular, *Adolf Lumber Co. v. Meadow Creek Lumber Co.* (1919), 58 S.C.R. 306 and *Corporate Properties Ltd. v. Manufacturers Life Insurance Co.* (1989), 63 D.L.R. (4th) 703 (Ont. C.A.) - supported his conclusion that, where an ambiguity in this sense exists, evidence of the past conduct of the

parties is admissible: see, also, *Montreal Trust Company of Canada v. Barn Lodge Ltd et al* (1995), 24 O.R. (3d) 97 (C.A.), at page 108. I do not accept that the Arbitrator's reliance on such evidence required him to "effectively write-out" section 1.15 of the CGLA as counsel for the Province suggested. The section provides that no failure of a party to exercise a right under the agreement shall operate as a waiver of it. Before one determines whether there has been a failure to exercise a right, the documents must be interpreted. The authorities establish that, for this purpose, the conduct of the parties subsequent to execution may be relevant and persuasive. The logic of the reasoning that implies that, taken in isolation, past conduct is equivocal assumes, contrary to experience, that parties are as likely to breach their obligations as to perform them. The no-waiver provision can be applied only after the process of interpretation has been completed and it does not, in my opinion, exclude past conduct from a role in that process.

[50] However, I do not believe the finding that evidence of subjective intention would be admissible was correct in law. I do not think that there is any doubt as to the purpose for which the Arbitrator believed such evidence could be used. It included, for example, evidence of a Vice-President of Corporate Development in the Privatisation Secretariat of the Ministry that government approval of the toll rate setting was specifically rejected as an approach in favour of congestion payments. The Arbitrator considered this to be reliable evidence of a person who could speak to the intention of the Province. If this evidence had been relied on by the Arbitrator as an essential ground for his decision, I would have felt compelled to allow the appeal.

[51] Unfortunately, "parol evidence" is not the only term that has been used in more than one sense in connection with the legal interpretation of documents. The phrase "plain meaning" may, for example, be confined to cases such as *Eli Lilly* where the meaning of a document is found to appear clearly and unambiguously from its words construed in isolation – if, and to the extent, that is ever possible - or it may be extended to cases such as *Arthur Andersen* where the meaning is held to appear unambiguously after extrinsic evidence of the surrounding circumstances – or the factual matrix - has been considered. As those cases illustrate, the converse – "ambiguity" – is similarly ambiguous. Difficulties in distinguishing between evidence of "subjective intention" and evidence of surrounding circumstances – and in determining the inferences that can, and cannot, legitimately be drawn from the latter - do not appear to arise in this case. The evidence that the Arbitrator treated as evidence of subjective intention cannot legitimately be recharacterized as evidence of surrounding circumstances.

[52] Traditional usage of the word "ambiguity" requires a further distinction to be drawn. In the law of wills it is commonly – although not invariably - used in a narrow sense to refer to latent ambiguities or "equivocations" as illustrated by many cases of which *Re Jackson*, [1933] Ch. 237 (Ch. D.) might be considered to be a classic example. In the law of contracts, it is often applied, more broadly, to cases where, for some reason, the provisions of a contract are reasonably susceptible of more than one interpretation. However, the venerable distinction between patent and latent ambiguities in the law of wills and deeds has been imported into the principles applied for the purpose of interpreting commercial contracts: Holdsworth, *History of English Law*, Volume 9, pages 221 – 2; *Chitty on Contracts* (29th edition, 2004), paras 12-124 and 12-125; Lewison, *The Interpretation of Contracts* (3rd edition, 2004), paras 8.02 - 8.05. In either context, extrinsic evidence of the parties' subjective intentions has traditionally been

admissible in cases of latent ambiguity but not otherwise. If I am correct in my understanding of the nature of the ambiguity hypothesised by the Arbitrator, it was not a latent ambiguity that permits the admission of evidence of subjective intention. The traditional approach was applied by Ground J. in *Misfud v. Owens Corning Canada Inc*, [2003] O.J. No. 3866 (S.C.J.) where the learned judge stated:

> It is the position of counsel for the respondent that the only exception to the principle of objective interpretation is in the case of latent ambiguity which arises where the ambiguity is not apparent from the face of the document but becomes apparent when the surrounding circumstances or the factual matrix are considered. Classic examples are where a contract refers to a railway station by name and it is discovered that two railway stations bear that name or where the contract refers to a "plan agreed upon" and it is discovered that two plans had been considered by the parties. The latent ambiguity exception was described in *Alampi v. Swartz et al* (1964), 43 D.L.R. (2d) 11 (Ont. C. A.), by McGillivray J.A. at pages 15 and 16 as follows:
>
>> [Parol evidence] is, however, admitted for the purpose of explaining terms of the contract and to prove the facts upon which the interpretation of the written documents depends and so is admissible to establish the validity of the document or the identity of the parties, to explain technical terms or commercial usage, and in all other places where the admission of such evidence is necessary to enable the Court to construe the document before it: ...
>>
>> Pursuant to the above principle where it is necessary to do so, evidence to ascertain and identify property referred to in a document is admissible so long as it does not contradict a clear description of the property; and so has been admitted to identify properties bearing descriptions such as "the farm", "the Mill Property", "my house", "Mr O's House", or property described as being in a particular parish or place.
>>
>> Evidence so admitted does not offend against the general rule. It may not contradict a term in the contract but, as has been said, is adduced to assign definite meaning to the terms used or to relate them to the proper subject-matter. If, however, after such evidence has been led it then appears that the term under construction is ambiguous and capable of more than one meaning evidence of a different class may be admitted, namely evidence of intention. Such an ambiguity, a "latent ambiguity", because not apparent upon

> the face of the writing, demands evidence of intention to establish whether there was an agreement at all, or if the parties intended a particular one of alternate meanings to prevail. Such latent ambiguities have arisen where it was found that two railway stations bore the name of the one mentioned in the contract ..., or where an agreement was made for a lease of premises "as per plan agreed upon" and it appeared that two plans had been inspected.

> In the case at bar, there is no such latent ambiguity. The provisions of the [agreements] which form part of the factual matrix surrounding the entering into of [a later agreement], must lead one to conclude that the words "the use" of any plan surplus and "remains at the company's discretion" in the [later agreement] are susceptible of more than one interpretation and that there is a patent ambiguity on the face of [the later agreement] itself.

[53] I would reach the same conclusion with respect to the hypothesis considered by the Arbitrator: where the words of the agreement are "reasonably susceptible of more than one meaning". An ambiguity in this broad sense would be apparent on the face of the documentation and, in consequence, it would not justify the admission of extrinsic evidence of the actual intentions of the parties. If the Arbitrator had found that the ambiguity existed and had relied on the extrinsic evidence of subjective intention as an essential ground of his decision, I would have allowed the appeal.

[54] In reaching the above conclusion, I have not overlooked the criticism directed in some recent English cases at some of the traditional significance given to the distinction between latent and patent ambiguities. This criticism was referred to by Lewison, *op. cit.* at para 802 where, after citing *dicta* of Lord Simon in *L. Schuler v. Wickman Machine Tool Sales Ltd,* [1974] A.C. 235 (H. L.) and of Lord Hoffman in *Mannai Ltd v. The Eagle Star Life Assurance Co Ltd,* [1997] A.C. 749 (H. L.), the learned author commented:

> It seems unlikely that the traditional distinction between these two types of ambiguity has survived into the modern law.

[55] However, in neither of those cases was there an issue relating to direct evidence of the actual, or subjective, intentions of contracting parties. In each case, the inadmissibility of evidence of subjective intention was accepted. In *Schuler*, the question was whether evidence of subsequent conduct was admissible and, in *Mannai*, the issue concerned evidence of surrounding circumstances. Lord Simon was of the opinion that the distinction between direct and circumstantial evidence of intention was unsound and that, even where a document was ambiguous on its face, evidence of subsequent conduct - like direct evidence of subjective intention - should be held to be inadmissible. In *Mannai*, a rule that was described by Lord Hoffmann as "not merely capricious but also ... incoherent" was not that which excludes direct

evidence of intention in cases of patent ambiguity and admits it in cases of latent ambiguity but, rather, a supposed rule that

> ... if the words of the document were capable of referring unambiguously to a person or thing ...

extrinsic evidence of surrounding circumstances was not admissible.

[56] While there may be difficulty in reconciling Lord Simon's conclusion with respect to subsequent conduct with the Canadian authorities I have cited, I do not believe any such problem arises from Lord Hoffmann's finding that evidence of surrounding circumstances would be admissible in *Mannai* unless, perhaps, the reasoning in *Eli Lilly* is to be applied to support the "rule" that he rejected.

[57] It may well be that, with the importance given to the factual matrix, or context, in modern principles of interpretation, the distinction between latent and patent ambiguities should be discarded as having outlived its usefulness, and that, instead, attention should be given to the justification for distinguishing between direct, and circumstantial, evidence of intention. However, I have found nothing in the decisions in this jurisdiction - or in the English decisions I have mentioned - to support the proposition that evidence of subjective intention is admissible where there is an ambiguity of the kind considered by the Arbitrator.

[58] As I have indicated, I do not believe a similar objection could validly be made to the Arbitrator's willingness to obtain assistance from the past conduct of the parties in the event that he had found that the provisions of the agreements were reasonably susceptible of more than one interpretation. Nor do I believe it would have been an error of law in such circumstances to place some reliance on the *contra proferentem* principle. The facts with respect to these matters were not materially in dispute. The approval of the Province to toll rate increases in previous years had not been sought, or required, and there was evidence at the arbitration that, although drafts of the agreements were discussed by officials of the Province and prospective purchasers of the shares of 407 ETR, their terms had not been negotiated. If the Arbitrator's conclusion that the past conduct of the parties and the *contra proferentem* principle supported the interpretation he would otherwise have placed on the agreements is open for reconsideration on this appeal, I would agree with it.

[59] The final consideration on which the Arbitrator was prepared to rely if the agreements were found to be ambiguous was the duty of the court to avoid an interpretation that would result in a commercial absurdity. In my opinion, a consideration of the extrinsic evidence of the consequences of the competing interpretations for this purpose would not have been objectionable: *cf.*, *Kentucky Fried Chicken of Canada v. Scott's Food Services Inc.*, [1998] O.J. No. 4368 (C.A.), at para 27.

D. Decision

[60] The Arbitrator found that the agreements entered into by the Province in 1999 did not require 407 ETR to obtain the consent, or approval, of the Province to increases in toll rates and administration fees. For the reasons I have given, I am satisfied that the Arbitrator's decision on the issues of interpretation involved in this appeal was correct on the plain meaning of the agreements in the sense in which that concept was used in *Eli Lilly* - as well as in a wider sense that, as in *Arthur Andersen*, permits a limited use of extrinsic evidence of surrounding circumstances for the purpose of determining whether there is an ambiguity. Accordingly, the decision was not, in my opinion, vitiated by any error of law. If I had found that the meaning of the agreements was not sufficiently clear and unambiguous to compel the decision, I would have found that he was entitled to have recourse to the evidence of past conduct, and to apply the *contra proferentem* principle in the manner he indicated. He was not, however, entitled to rely upon evidence of the subjective intentions of the parties.

[61] Notwithstanding the position now adopted by the Province, it appears that its control over the level of tolls and administration fees charged to users of Highway 407 may be confined to its right to ensure that congestion payments are made by 407 ETR in accordance with the agreements. All, or some, of the implications of that right are to be determined by arbitration in accordance with my earlier decision: [2004] O.J. No. 4516 (S.C.J.).

[62] In view of the above findings, the appeal is dismissed.

[63] Costs may be spoken to or, if counsel would prefer to make their submissions in writing, those of 407 ETR should be filed within 14 days of the release of these reasons and those on behalf of the Province within a further 7 days.

CULLITY J.

Released: January 6, 2004

COURT FILE NO.: 04-CV-27202CM2
DATE: 20050106

ONTARIO

SUPERIOR COURT OF JUSTICE

B E T W E E N:

HER MAJESTY THE QUEEN IN RIGHT OF THE PROVINCE OF ONTARIO AS REPRESENTED BY THE MINISTER OF TRANSPORTATION and THE MINISTER OF TRANSPORTATION FOR ONTARIO

Applicants

- and -

407 ETR CONCESSION COMPANY LIMITED

Respondent

REASONS FOR DECISION

CULLITY J.

Released: January 6, 2005