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Unilateral Mistake in Integration: When is Rectification an Appropriate Remedy?

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Case commented on: *Johnson v Moody*, [2014 ABQB 80](#)

A written contract may be executed by the parties on the basis of a unilateral mistake as to a term or terms of the contract. For example, the parties may reach an oral agreement but the terms of the oral agreement may not be accurately recorded in the written contract signed by the parties. This type of mistake, usually referred to as ‘mistake in integration’, may be remedied by an order of rectification particularly where the non-mistaken party’s attempt to take advantage of the written contract would amount to fraud or the equivalent of fraud. As discussed subsequently, a mistake in integration occurred in *Johnson v. Moody*, a recent decision of the Court of Queen’s Bench of Alberta.

The purpose of the equitable remedy of rectification is to restore the parties to their original agreement. An order of rectification corrects the written contract in a manner that restores the parties to their antecedent agreement. As the Supreme Court of Canada observed in *Performance Industries Ltd. v. Sylvan Lake Golf & Tennis Club Ltd.*, [2002] 1 SCR 678 at para 40, “[t]he court’s equitable jurisdiction [to rectify a contract] is limited to putting into words that - and only that - which the parties had already orally agreed to.” Thus, in an action for the rectification of a contract, the overarching duty of the court “is to restore the parties to their original bargain, not to rectify a belatedly recognized error of judgment by one party or the other” (*Performance Industries* at para 31). The remedy of rectification prevents the inaccurately recorded (written) contract “from being used as an engine of fraud or misconduct ‘equivalent to fraud’” (*Performance Industries* at para 31).

Facts

In 2002, Johnson and Moody commenced negotiation for the purchase of Johnson’s business. In June 2002, a draft agreement was prepared by Johnson’s counsel. Among other things, the draft agreement had Moody as a party to the contract; described Moody as guarantor of the purchaser, Greggor Promotional Ltd.; contained a personal guarantee on the part of Moody as well as a signature line for both Greggor Promotional Ltd. and Moody; and provided for a Certificate of Notary Public pursuant to the *Guarantees Acknowledgement Act*, RSA 2000, c G-11.

Moody refused to sign the draft contract. Rather, Moody revised the contract in a manner that differed significantly from the draft contract prepared by Johnson’s counsel. The revised contract provided that, of the purchase price of \$105,000.00, Johnson shall be paid \$65,000.00 on closing while the remainder is to be paid in installments. Perhaps more significantly, the revised contract neither included Moody as a party nor contained a provision for a Certificate of Notary Public.

Although Johnson signed the revised agreement, the transaction was never closed because Moody was not able to obtain the \$65,000.00 required to be paid on closing of the transaction. Inevitably, Johnson and Moody negotiated a new arrangement. The parties agreed that \$25,000.00 shall be paid to Johnson on closing. They also agreed on a schedule of payment with regard to the balance.

Johnson's counsel drafted a contract reflecting the new arrangement ("the June draft"). The June draft identified Moody as both a party and a guarantor. It also contained a personal guarantee clause ("section 18"), a Certificate of Notary Public, as well a line for Moody's signature. Johnson's counsel testified that he instructed his assistant to type up this draft and send it to Moody's counsel. However, at trial Johnson's counsel testified that a copy of the revised typed draft was not on his file.

Eventually, a contract was signed by the parties but the contract did not contain a provision on personal guarantee. The contract, which identified Moody as the "Guarantor", was signed by Moody for himself and on behalf of Greggor Promotional Ltd. Pursuant to the contract, Moody executed a Certificate of Notary Public. Johnson and his wife (the Plaintiffs) signed the contract at their counsel's office. Johnson did not read or review the contract prior to signing the contract. Perhaps more significantly, prior to Johnson's signature his counsel failed to review the contract to ensure that it contained all essential terms orally agreed by the parties.

The Plaintiffs sought the equitable remedy of rectification on the basis of a unilateral mistake with regard to the personal guarantee. The Plaintiffs contended that the parties agreed that Moody would provide a personal guarantee given the lower amount of the payment on closing. They also alleged that the personal guarantee clause was either mistakenly or deliberately removed by Moody from the final draft executed by the parties. Moody disputed the Plaintiffs' contention and testified that he could not remember discussing a personal guarantee with Johnson.

Conditions Precedent to Rectification

Canadian courts recognize that unless restrictions are imposed on the remedy of rectification, it could potentially open the floodgates to individuals and business outfits seeking to avoid contractual obligations where they consider that the contract does not fully promote their personal interest. Thus in *Performance Industries*, the Supreme Court of Canada held that:

[35] high hurdles are placed in the way of a businessperson who relies on his or her own unilateral mistake to resile from the written terms of a document which he or she has signed and which, on its face, seems perfectly clear. The law is determined not to open the proverbial floodgates to dissatisfied contract makers who want to extricate themselves from a poor bargain.

There are several 'high hurdles' or conditions precedent to the rectification of a contract induced by unilateral mistake. To be entitled to rectification of a contract induced by unilateral mistake, the plaintiff must prove:

1. the existence of a prior oral contract whose terms are definite and ascertainable;
2. that the written document does not correspond with the prior oral agreement (that is, that the terms agreed to orally were not written down properly);
3. that at the time of execution of the contract the defendant either knew or ought to have known of the mistake in reducing the oral terms to writing and the plaintiff did not;
4. that the attempt of the defendant to rely on the erroneous written document amounts to "fraud or the equivalent of fraud" (*Performance Industries* at paras 31, 35-41).

In addition, the plaintiff must offer a “convincing proof” of their case. In other words, the plaintiff must prove the conditions precedent on a ‘convincing’ basis. Although the ‘convincing proof’ standard falls short of the criminal standard (proof beyond a reasonable doubt), it “goes beyond the sort of proof that only reluctantly and with hesitation scrapes over the low end of the civil ‘more probable than not’ standard” (*Performance Industries* at para 41).

These conditions precedent prevent contract makers from seeking to re-write their contracts simply because they are unhappy with the bargain they struck. For example, by requiring proof of a prior oral agreement, the ‘floodgate’ is closed “to unhappy contract makers who simply failed to read the contractual documents, or who now have misgivings about the merits of what they have signed” (*Performance Industries* at para 37). In *Shafroon v. KRG Insurance Brokers (Western) Inc.* [2009] 1 SCR 157, a contract of employment contained a restrictive covenant preventing the defendant from engaging in insurance brokerage business within the “Metropolitan City of Vancouver” for three years after the termination of his employment with the plaintiffs. The defendant left the plaintiffs’ employment in December 2000 and in January 2001 he began working for an insurance brokerage firm in Richmond, British Columbia. The plaintiffs asked the court to rectify the contract such that the “Metropolitan City of Vancouver” becomes “the City of Vancouver and the surrounding towns of Richmond and Burnaby”. The Court declined to rectify the contract because the plaintiffs did not prove a prior agreement between the parties that the “Metropolitan City of Vancouver” meant the City of Vancouver and surrounding towns. According to the Supreme Court of Canada (at para 54), “[w]ithout pointing to a prior agreement that was departed from when the contract was put into writing, rectification is not available.” The Court concluded thus:

[52]... this is not a case in which rectification is properly applicable. ... Here, there was nothing to indicate what the parties intended by the use of the term “Metropolitan” when they entered into the covenant and nothing to indicate that they agreed on an area and then mistakenly wrote down “Metropolitan”.

In view of the above-stated position of the law, we now proceed to consider the decision of the Court of Queen’s Bench of Alberta in *Johnson v. Moody*. Our purpose here is to determine whether the trial judge correctly applied relevant legal principles, especially those espoused by the Supreme Court of Canada in *Performance Industries*.

Analysis of the Decision

The Court of Queen’s Bench of Alberta (Justice B.E. Romaine) held that “the Johnsons are entitled to rectification, and that Mr. Moody is bound by the personal guarantee” (para 1). The court analyzed the conditions precedent to rectification as articulated by the Supreme Court of Canada in *Performance Industries* and held that the Plaintiffs offered a ‘convincing proof’ of their case. More specifically, the court held (at paras 24-31) that:

1. the parties had a prior agreement containing a term as to a personal guarantee;
2. the terms of the prior agreement were not written down properly;
3. at the time of execution of the contract Mr. Moody knew that an error had been made, while the Plaintiffs did not know an error had been made;
4. Mr. Moody’s attempt to rely on the erroneous agreement amounted to fraud or the equivalent of fraud.

Ultimately the court held (at para 32) that “the Plaintiffs are entitled to rectification and a clause using the language of section 18 of the June draft will be added to the written agreement”.

The trial court's decision is supported by the evidence. It is beyond dispute that the parties had a prior agreement. The dispute in this case involved the precise terms of the prior agreement and more specifically, whether the prior agreement included a personal guarantee. The court was justified in concluding that the prior agreement included a personal guarantee. In arriving at its decision, the court did not rely solely on the parol evidence of the Plaintiffs. Rather, it found that the Plaintiffs' evidence was corroborated by several other pieces of evidence, including the conduct of Mr. Moody and documentary evidence such as the text of the several drafts of the agreement and the Certificate of Notary Public. For example, there was evidence to the effect that Moody's counsel's office advised Johnson's counsel that Moody came to their office to sign the guarantee in the presence of a different lawyer as the original counsel was on holidays (paras 12 & 13).

A more significant piece of corroborative evidence is the fact that Moody signed the Certificate of Notary Public in the presence of a Notary Public. As the trial court rightly held:

[15] The Certificate of Notary Public attached to the final agreement certifies that Mr. Moody, "the Guarantor" in the sale agreement made between Dave Johnson, Greggor Promotional Ltd. and Greg Moody as Guarantor appeared in person before the notary public and "acknowledged that he had executed the Agreement as Guarantor". It also certifies that the Notary Public was satisfied "by examination of [Mr. Moody] that he [was] aware of the contents" of the agreement and understands it. It includes a "Statement of Guarantor" signed by Mr. Moody indicating that he was the person named in the certificate.

The court continued as follows:

[16] Section 3 of the *Guarantees Acknowledgment Act* requires that a guarantor appear before a notary public, acknowledging that he executed the guarantee and signing a statement at the foot of the certificate in the prescribed form before a guarantee has any effect, all of which was done.

In addition to these corroborative pieces of evidence, the contract identified Moody as the "Guarantor".

Given the fact that the prior agreement included a personal guarantee, it follows logically that the terms of the prior agreement were not correctly recorded in the contract executed by the parties (para 25). The evidence also points to Moody's knowledge that an error had been made in integrating the terms of the prior agreement. He received a copy of the 'June draft' containing a personal guarantee (para 30). In addition, while Moody claimed that he was unaware of the nature of the contract prior to executing the contract, the court found his evidence to be "disingenuous and unpersuasive" (para 20).

Finally, Moody's attempt to rely on the erroneous contract qualifies as 'fraud or the equivalent of fraud' because it would be unconscientious for him to avail himself of the advantage gained through the omission of the personal guarantee (*First City Capital Ltd. v. British Columbia Building Corp.* (1989), 43 BLR 29 (BCSC), cited with approval in *Performance Industries* at para 39). Put simply, Moody's conduct in not drawing the error in integration of the contract to the attention of the Plaintiffs was unconscionable.

Although the trial court's decision is supported by the evidence, the decision is susceptible to criticism on grounds that the court did not give sufficient consideration to the issue of negligence. Negligence arises in this case in two senses: omission or deletion of the personal guarantee from the contract and the Plaintiffs' failure to read the contract prior to signing it. The question is, if the Plaintiffs' counsel was responsible for omitting or deleting the personal guarantee from the contract, should the Plaintiffs nonetheless be entitled to rectification of the contract?

On the issue of negligence the court held that “it doesn’t ultimately matter if the Section 18 guarantee language was deleted in error by Mr. Johnson’s counsel’s office or by the other law firm” (para 11). The court observed that the omission of the personal guarantee from the contract “could have happened by mistake, in either lawyer’s office, or Mr. Moody and his counsel eliminated the language from the draft that was sent to them” (para 25). The court then went on to say, “I do not have to decide which was the case, as either an innocent or fraudulent error will do” (para 25).

With respect, the court’s position on the issue of negligence is unsatisfactory. Rectification is an equitable remedy granted in the discretion of the court. Although negligence or “due diligence on the part of the plaintiff is not a condition precedent to rectification”, negligence is a factor to be considered by the court (*Performance Industries* at para 66). Thus the court ought to determine whether the Plaintiffs were negligent and if so, whether their negligence was sufficiently serious to deny them the equitable remedy of rectification. As the Supreme Court of Canada observed in *Performance Industries* (at para 66), “[t]he conduct of the plaintiff is relevant to the exercise of [the court’s] discretion.” Thus, “[i]n a case where the court concludes that it would be unjust to impose on a defendant a liability that ought more properly to be attributed to the plaintiff’s negligence, rectification may be denied” (*Performance Industries* at para 66).

It may well be that the trial judge refrained from a detailed analysis of the issue of negligence because she did not want to impugn the professional integrity of counsel. While, on the evidence, it is unclear whether the Plaintiffs’ counsel was responsible for omitting the personal guarantee from the contract, it is certainly the case that the Plaintiffs’ failure to read the contract prior to signing amounts to negligence or want of due diligence. However, this is not sufficient to deny the Plaintiffs an order of rectification because the peculiar circumstances of this case extenuate their failure to read the contract. As noted by the trial court, “the agreement that was returned to them looked on its face to be identical to the re-draft done by Mr. Johnson’s counsel” (para 31). Besides, the Plaintiffs checked the contract not only “to ensure that Mr. Moody was named as a guarantor” but also to ensure that the Certificate of Notary Public had been signed (para 31). Thus the trial judge was right to observe (at para 31) that “[t]his is not a case where the Plaintiffs’ lack of due diligence makes it unjust to impose a liability on the Defendants.”

Finally, this case offers a lesson for the practicing bar. The lesson is that lawyers should read documents before they are signed by clients. The pressure to close a deal sometimes makes lawyers overlook basic safeguards enjoined by the legal profession. As I often remind students in my Contracts course, the pressure of work is never an excuse for neglecting to read or review a document prior to signing the document.

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