Conflict of Interest, Duress and Unconscionability in Quebec Civil Law: Comment on "The Origins of a Coming Crisis: Renewal of the'Churchill Falls Contract"

Sarah P. Bradley
Dalhousie University

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As Professor James Feehan and archivist-historian Melvin Baker describe the circumstances in which the fateful renewal provision of the 1969 Churchill Falls hydro contract was negotiated, they suggest that the legal doctrines of conflict of interest or economic duress might offer a basis upon which the contract, or perhaps the renewal provision, could be impugned. In addition to interesting historical insights, their analysis offers the intriguing possibility that the government of Newfoundland may yet succeed in its long-standing battle to rid itself of its obligations under the grossly disadvantageous Churchill Falls contract.

Whether by design or by fate, the Churchill Falls contract, together with the corporate structure of the Churchill Falls (Labrador) Corporation ("CFLCo"), has proven remarkably resistant to Newfoundland’s efforts to repatriate the bounty of one of the world’s largest hydro-electric generating facilities. Successive provincial governments and some of Canada’s finest legal minds have grappled with the issue, so far without success. Hydro-Québec, for its part, has always staunchly and effectively defended the contract as one that was fairly negotiated between sophisticated commercial parties with ample legal and business advice.

The legal disputes over the contract began over thirty years ago, arising only a few years after the Churchill Falls facility became operational. It is interesting to note however, that the Newfoundland government never directly attacked the contract itself. Newfoundland’s first challenges to the contract were political, rather than legal, in nature. When its political options had been exhausted, Newfoundland’s first legal challenge to the contract was launched in the mid-1970s, when it sought a judicial declaration that it was entitled to additional power from the Churchill Falls plant for use within the province under the statutory lease it had granted to CFLCo. This action was defeated at all levels of court.¹ Subsequently,
Newfoundland attempted to expropriate the Churchill River water rights from CFLCo by enacting the *Upper Churchill Water Rights Reversion Act 1980.* The constitutionality of this Act was upheld by the Newfoundland Court of Appeal, but the Supreme Court of Canada struck it down as ultra vires of the Newfoundland legislature. Since that time, there have been no further legal challenges, but the perceived unfairness of the Churchill Falls contract remains at the forefront of Newfoundland’s political consciousness, representing for many Newfoundlanders the epitome of the exploitation of the province and its people by outsiders, particularly the province of Quebec and the federal government. The contract continues to be a hot-button topic in Newfoundland nearly forty years after its execution in part because of the ongoing nature of the province’s obligations, which see hundreds of millions of dollars flowing almost literally from the Churchill River into the coffers of Hydro-Québec each year.

The factual circumstances described by Feehan and Baker raise the prospect of new avenues of legal argument by which the renewal provision of the contract might be impugned. Their research reveals that the renewal provision was inserted at the eleventh hour in the negotiations, at a time when CFLCo was facing imminent bankruptcy. They point out that because the province of Quebec refused to allow CFLCo to transport power across its territory to other markets, Hydro-Québec was the only possible purchaser of power from the Churchill Falls site. Additionally, they highlight the fact that the president of Hydro-Québec insisted on being appointed to CFLCo’s board of directors, putting him in a position to know exactly how close CFLCo was to collapse when Hydro-Québec demanded additional concessions, including the twenty-five-year renewal provision, in the final stages of negotiation. Facts such as these call into question the fairness and validity of the agreement.

Counterbalancing this intuitive reaction however, is the fact that courts rarely vary or refuse to enforce commercially negotiated contracts. The reliable enforcement of such contracts is integral to the functioning of a free-market economy, allowing businesspeople to negotiate agreements and structure their dealings as they see fit, thereby facilitating business efficiency, economic activity and growth. Nevertheless, Canadian courts have the jurisdiction to refuse to enforce a commercial contract,

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vary its terms, or declare it void on a number of grounds, including unconscionability and duress.

A provision in the 1969 Churchill Falls contract attorns to the laws of Québec. In accordance with this provision, the governance and interpretation of the contract is to be carried out pursuant to the laws of Québec, and any disputes under the contract are to be adjudicated by the Québec courts, subject to ordinary rights of appeal.

Unconscionability, undue influence and duress are inherently equitable doctrines, incorporated over the centuries into the common law of contract. These doctrines, familiar in Canada’s common law jurisdictions, are not directly applicable in the civil law jurisdiction of Québec, where matters of contract are governed by the Civil Code of Québec ("CCQ").

Notwithstanding the differences of form and provenance however, both the common law and the civil law offer relief to contracting parties who have entered into agreements under duress, or in grossly unfair circumstances. The nature of this relief in each legal system is discussed below, followed by an analysis of the duties that the directors of CFLCo owed to the corporation, and whether these duties may have been breached.

Additional matters that are relevant to a legal analysis of this case include whether historical laws or the law as it has been amended over the years will apply to the matter, and the effect of the passage of time on the availability of legal remedies. These matters, including the common law doctrine of laches and its civil law equivalent are also discussed below.

**The civil law requirement of good faith vs. the common law doctrine of unconscionability**

In civil law jurisdictions generally, the foundation of the law and all legal principles is a written code, which addresses matters typically addressed by statute in common law jurisdictions, as well as matters typically not addressed by statute in common law jurisdictions, including the fundamental tenets of property and contract law. This code is interpreted by judges in the course of adjudication and by academics in the preparation of articles and treatises. When applying the legal rules set out in the code to the facts of a particular case, civil law judges are strongly influenced by earlier judicial decisions, though these earlier decisions are not considered to be a source of law as they are in the common law system, and are not strictly binding. The interpretation of the code described by legal academics is also often considered by civil law judges, though it is typically less
influential than earlier judicial interpretations. In this manner, civil law systems attempt to ensure that like cases will be tried alike, and that the application of the code will be reasonably predictable.

In Quebec, the CCQ does not recognize the common law doctrines of unconscionability or duress, per se, but rather uses the concepts of good faith and consent vitiated by fear to achieve similar purposes. With respect to general relief from unfair contracts, the rules of the civil law system are considerably more restrictive than they are under common law, which has developed voluminous jurisprudence on the subject of unconscionability.

Under the CCQ, where one party is a minor or under a legal disability, special protection is available in the form of the doctrine of lesion, described below. As between sui juris parties, however, relief on the basis of unfairness is generally not available. The CCQ does contain a general requirement that contracts are to be negotiated and carried out in good faith:

Art. 6. Every person is bound to exercise his civil rights in good faith.

Art. 7. No right may be exercised with the intent of injuring another or in an excessive and unreasonable manner which is contrary to the requirements of good faith.

Art. 1375. The parties [to a contract] shall conduct themselves in good faith both at the time the obligation is created and at the time it is performed or extinguished.

Despite these requirements however, the CCQ does not provide any specific remedy where a contract has not been negotiated or carried out in good faith. Rather, bad faith is required in order to invoke certain specific remedies. For example, as discussed more fully below, the proof of bad faith can be persuasive in demonstrating a defect of consent, such as fear.

In the common law system, courts of equity and common law have long been willing to refuse to enforce a contract as a result of unfair overreaching in the negotiation process. A modern articulation of the unconscionability doctrine was that of Lord Denning, M.R. in the 1975 case of Lloyds Bank Ltd. v. Bundy, where he reviewed a number of related equitable principles that then allowed courts to grant relief from unfair contracts, and reconciled these various principles in the following, often cited passage:

Gathering all together, I would suggest that through all these instances there runs a single thread. They rest on 'inequality of bargaining power'. By virtue of it, the English law gives relief to one who, without independent advice, enters into a contract upon terms which are very unfair or transfers property for a consideration which is grossly inadequate, when his bargaining power is grievously impaired by reason of his own needs or desires, or by his own ignorance or infirmity, coupled with undue influences or pressures brought to bear on him by or for the benefit of the other. When I use the word 'undue' I do not mean to suggest that the principle depends on proof of any wrongdoing. The one who stipulates for an unfair advantage may be moved solely by his own self-interest, unconscious of the distress he is bringing to the other. I have also avoided any reference to the will of the one being 'dominated' or 'overcome' by the other. One who is in extreme need may knowingly consent to a most improvident bargain, solely to relieve the straits in which he finds himself. Again, I do not mean to suggest that every transaction is saved by independent advice. But the absence of it may be fatal. With these explanations, I hope this principle will be found to reconcile the cases.7

A number of Canadian cases considered the doctrine in the 1960s and 70s. In Harry v. Kreutziger,8 Lambert J.A. considered the principles discussed in the earlier cases and set out the broader “community standards of commercial morality test”:

In my opinion, questions as to whether use of power was unconscionable, an advantage was unfair or very unfair, a consideration was grossly inadequate, or bargaining power was grievously impaired, to select words from both statements of principle, the Morrison case and the Bundy case, are really aspects of one single question. That single question is whether the transaction, seen as a whole, is sufficiently divergent from community standards of commercial morality that it should be rescinded.9

Professor Waters, in a discussion of unconscionability, cites an earlier source for the “business morality” test:

Unlike the doctrine of undue influence, equity is not concerned in these situations with whether the mind of one party was overborne by another so that the victim's true consent was lacking; it asks the question as to whether, looked at objectively, the transaction in all the circumstances was sufficiently unconscionable that it cannot be allowed to stand.

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9. Ibid. at 241 [emphasis added].
As Professor Sheridan put it, writing in 1957, the question is whether, given the weakness of one party's bargaining position and the undervalue which he received, "a greater advantage" was obtained by the stronger party "than the current morality of the ordinary run of business allows."  

The Supreme Court of Canada considered the test in *Lloyds Bank* in the 1992 case of *Norberg v. Wynrib*. Dealing in that case with a tort claim between a patient and doctor that raised issues of consent, the Court examined contractual rules relating to consent and unconscionability. The court signalled its willingness to remain flexible in its approach to the unconscionability doctrine:

It may be argued that an unconscionable transaction does not, in fact, vitiate consent: the weaker party retains the power to give real consent but the law nevertheless provides relief on the basis of social policy. This may be more in line with Lord Denning's formulation of "inequality of bargaining power" in *Lloyds Bank Ltd. v. Bundy*, supra, when one takes into account his statement that it is not necessary to establish that the will of the weaker party was "dominated" or "overcome" by the other party. But whichever way one approaches the problem, the result is the same: on grounds of public policy, the legal effectiveness of certain types of contracts will be restricted or negated.  

Thus, Canadian common law courts remain willing to rescind contracts between parties whose relationship is one of significant power imbalance, where the contractual terms are unfairly advantageous to the stronger party. This imbalance has been found to exist in cases where individuals have entered into contracts for rescue services, a land sale transaction from an unsophisticated vendor to a businessman without legal advice, a mortgage entered into by an elderly widow without legal advice, and the sale of a fishing vessel and license by an unsophisticated fisher to a sophisticated businessperson with limited legal advice; but such an imbalance was not found to exist in a case involving the purchase of Crown land by a corporation, where the corporation had paid over $1 million as

11. [1992] 2 S.C.R. 226 at 250 (La Forest J.) [emphasis added].  
part payment, but was unable to complete the transaction, and the Crown retained the deposit as forfeit.\footnote{Dimensional Investment Ltd. v. Canada, [1968] S.C.R. 93.}

Thus, though considerably broader than the remedies available in the civil law system, the common law system has evolved a threshold of fairness for the doctrine of unconscionability that requires a significant disparity of power as well as substantively unfair terms.

If the negotiation of the Churchill Falls contract were to be tried on the basis that there was a lack of good faith, it is doubtful that any remedy would be available under the CCQ. Even if the common law doctrine of unconscionability were applied to the case, to establish that the requisite disparity of power existed between the representatives of CFLCo and Hydro-Québec would be very difficult, given the level of sophistication of the parties, their commercial and legal expertise and the protracted nature of their negotiations, though establishing the unfairness of the terms of the contract may be less difficult. It is possible that the “commercial morality” test set out in earlier jurisprudence,\footnote{Harry v. Kreutziger, supra note 8.} might be stretched to take into account the conflict of interest inherent in Hydro-Québec’s presence on CFLCo’s board and the eleventh-hour amendments to the renewal provision, but such a finding would represent an expansion of the doctrine as it has been applied in Canada to date.

The civil law concept of vitiation of consent by economic fear vs. the common law doctrine of economic duress

It is a reality of business life that it is often to the advantage of one party to exploit another party’s weakness or neediness, and such commercial pressure is common in mercantile negotiations. However, both the common law and the civil law will provide relief to a contracting party that has been subject to “undue pressure,” duress, or circumstances that create a degree of fear so significant that it vitiates consent. This relief is based upon the principle of mutuality of intention that provides the foundation of contract law in both legal systems.

Under the CCQ, contracts can be voided on the basis that the consent of one of the parties has been vitiates. One of the specific remedies available is relief for a contracting party who has entered into a contract in circumstances of duress that are analogous to the common law doctrine of economic duress. The general power to contract is set out in art. 1385:
1385. A contract is formed by the sole exchange of consents between persons having capacity to contract...

This general power is modified by the subsequent art. 1399 which sets out the three principal arguments which can be used to have a contract annulled\(^8\) on the grounds that it was entered into without consent:

1399. Consent may be given only in a free and enlightened manner. It may be vitiated by error, fear or lesion.

In art. 1399, “error” refers to cases of fraud, misrepresentation and mistake. “Lesion” refers to a doctrine similar to the common law doctrine of abuse of power or abuse of authority. Lesion is a concept that is applied exclusively to minors or to persons under a legal disability who have suffered contractual exploitation, and is not generally available to legally competent adults\(^19\).

The concept in art. 1399 that “fear” can vitiate consent is applied in a manner akin to the common law doctrine of duress. It is expanded upon in art. 1402, which makes it clear that the fear of a serious injury to one’s property can be sufficient to vitiate consent, if the fear is induced by a threat that is known to the other party:

1402. Fear of serious injury to the person or property of one of the parties vitiates consent given by that party where the fear is induced by violence or threats exerted or made by or known to the other party...

The degree of injury sufficient to constitute “serious injury” for the purposes of art. 1402 was considered by professors Langevin and Vézina,\(^20\) who describe a test with both objective and subjective elements. They suggest that a court will consider the seriousness of the injury that is feared objectively, but will also take into consideration the seriousness of that injury with respect to the age, sex, characteristics and general condition of the person in question. They suggest that a court will inquire objectively

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18. The remedy of annulment is set out in art. 1407: “A person whose consent is vitiated has the right to apply for annulment of the contract; in the case of error occasioned by fraud, of fear or of lesion, he may, in addition to annulment, also claim damages or, where he prefers that the contract be maintained, apply for a reduction of his obligation equivalent to the damages he would be justified in claiming.”

19. CCQ art. 1405: “Except in the cases expressly provided by law, lesion vitiates consent only in respect of minors and persons of full age under protective supervision.”

into whether a reasonable person with the same characteristics and in the same circumstances would have feared a serious injury.\(^{21}\)

With respect to the question of the degree of fear that is required to vitiate consent under art. 1402, professors Didier Lluelles and Benoit Moore\(^{22}\) have advanced a theory that "l'état de nécessité circonstantielle," or a state of circumstantial necessity, is required. They suggest that circumstantial necessity arises where circumstances are such that a party has no choice but to enter the contract: circumstances so compelling that the party has not entered into the contract voluntarily. Professors Lluelle and Moore thus seem to have arrived at an interpretation of art. 1402 that is very similar to the common law doctrine of economic duress enunciated by the Privy Council in the 1980 case of Pau On v. Lau Yiu Long.\(^{23}\)

In Pau On v. Lau Yiu Long, the court considered whether English law recognized a category of duress known as "economic duress," and the question of the degree of pressure that would be required to constitute "undue pressure" in such a case. Lord Scarman expressed the view that economic duress was a valid claim in English law, but made it clear that the degree of economic duress had to be sufficiently strong to render the party's consent effectively involuntary. He stated:

\begin{quote}
Duress, in whatever form it takes, is a coercion of the will so as to vitiate consent... [I]n a contractual situation, commercial pressure is not enough... [I]t is material to enquire whether the person alleged to have been coerced did or did not make protest; whether, at the time he was allegedly coerced into making the contract, he did or did not have any alternative course open to him such as an adequate legal remedy; whether he was independently advised; and whether after entering the contract he took steps to avoid it... [T]here is nothing contrary to principle in recognizing economic duress as a factor which may render a contract voidable, provided always that the basis of such recognition is that it must amount to a coercion of will, which vitiates consent. \textit{It must be shown that the payment made or the contract entered into was not a voluntary act.}\(^{24}\)
\end{quote}

This acknowledgment of the legitimacy of claims of economic duress at common law was followed by the Ontario Court of Appeal in Stott v. Merit Investment Corporation,\(^{25}\) where Finlayson J.A. echoed the requirement

\begin{enumerate}
\item For an example of an application of this test, see J.J. Joubert Ltée c. Lapierre, [1972] C.S. 476.
\item \textit{Droit des obligations} (Montréal: Les éditions Thémis, 2006).
\item [1979] 3 All E.R. 65 at 79 (P.C.) [emphasis added].
\end{enumerate}
that the duress in question must be of such magnitude that consent is vitiating.

Lluelles and Moore go on to discuss the application of art. 1402 in situations of economic fear. In their interpretation of the article, where one party to a contract has clearly taken advantage of the fragile economic situation of the other, for example, by imposing an extraordinary price or particularly onerous requirements, and the economically fragile party has agreed to the contract on the basis of fear, the latter party could argue that their consent was vitiating pursuant to art. 1402.

Similarly, scholars Jobin and Vézina point out that a mere relationship of economic dependence is insufficient to create a defect of consent based on fear. Their interpretation of art. 1402 is that something greater is required, such as a threat in the course of business negotiations to refuse to carry out an existing obligation. They liken the behaviour that is required to invoke art. 1402 in economic circumstances to “economic violence.”

The CCQ provides an additional hurdle for a party alleging that its consent has been vitiating by fear. In addition to the provisions of art. 1402, art. 1404 provides that the fact that a party has entered into a contract out of fear will not be sufficient to vitiate that party’s consent if the other party to the contract is acting in good faith:

Article 1404: Consent to a contract the object of which is to deliver the person making it from fear of serious injury is not vitiating where the other contracting party, although aware of the state of necessity, is acting in good faith.

Thus, the fear of serious injury on the part of one party must be accompanied by bad faith on the part of the other party in order for the fearfule party’s consent to be vitiating. The onus to prove this bad faith rests with the person alleging it, as good faith is generally presumed under the CCQ.

Some courts have interpreted this provision to mean that the cause of the

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fear must "emanate from the co-contractant or from a third party at the co-contractant's knowledge."\(^{28}\)

In this respect, the civil law remedy for economic duress is analogous to the common law doctrine, which also requires some undue, illegitimate or illegal action on the part of the party who is alleged to have placed the other in circumstances of economic duress. In *Stott v. Merit Investment Corporation* the Ontario Court of Appeal discussed the requirement that the pressure exerted by the stronger party must be "illegitimate," stating:

The term "economic duress" as used in recent cases, particularly in England, is no more than a recognition that in our modern life the individual is subject to societal pressures which can be every bit as effective, if improperly used, as those flowing from threats of physical abuse. It is an expansion in kind but not class of practices that the law already recognizes as unacceptable such as those resulting from undue influence or from persons in authority. But not all pressure, economic or otherwise, is recognized as constituting duress. **It must be a pressure which the law does not regard as legitimate and it must be applied to such a degree as to amount to "a coercion of the will," to use an expression found in English authorities, or it must place the party to whom the pressure is directed in a position where he has no "realistic alternative" but to submit to it,** to adopt the suggestion of Professor Waddams (S.M. Waddams, The Law of Contract (2nd ed., 1984), at p. 376 et seq.). Duress has the effect of vitiating consent and an agreement obtained through duress is voidable at the instance of the party subjected to the duress unless by another agreement or through conduct, either express or implied, he affirms the impugned contract at a time when he is no longer the victim of duress.\(^{29}\)

In *Stott* the court held that economic pressure, even pressure that could not be recognized in law as legitimate, was insufficient to establish the defence of duress in that case, because the court found that the plaintiff had other practical alternatives, and could have repudiated the contract entered into, but did not.\(^{30}\)

Thus, the degree of economic duress required to render a contract voidable at common law, particularly in the commercial context, is high. There is an onus on the party pleading economic duress to prove that the stronger party exerted pressure that was not only of sufficient magnitude that it vitiates the weaker party's consent, but that was also illegitimate


\(^{29}\) Supra note 25 at 305 [emphasis added].

\(^{30}\) See, however, *W.H. Violette Ltd. and Violette Motors Ltd. v. Ford Motor Co. of Canada Ltd.* (1980), 31 N.B.R.(2d) 394; 75 A.P.R. 394.
This degree of pressure has been found in cases where a creditor or a person entitled to the benefit of a contract has been pressured into accepting something less than he is entitled to receive by law, or coerced into paying something more than he was otherwise obliged to pay. However, the requisite degree of pressure has not been found where an insurer refused to release the funds due for a destroyed building until the plaintiffs agreed to a settlement, effectively "starving the plaintiffs into submission," or where economic duress was found to exist, but the pressure exerted was not proven to be illegitimate. Canadian courts typically also consider the four factor test set out in *Pau On v. Lau Yiu Long*, i.e., whether the party protested at the time of entering into the contract, whether there was an alternative course open to the party, whether the party was independently advised, and whether, after entering the contract, the party took steps to avoid it.

There are few Quebec cases where the court has found that the consent of a party to a commercial contract was vitiated by economic fear. One early example is the case of *Vinet c. Canadian Light and Power Co.* In that case, the plaintiff, Vinet, was a contractor who had undertaken several construction projects for the defendant. Midway through one project, the defendant approached Vinet and had him sign an agreement by which he agreed to a particular method of calculation of his price for the work he was performing. Vinet recognized that the agreement was disadvantageous to him, but was told by the defendant that if he did not sign, then all further payments to him would be stopped, which would cause his financial ruin. The court found that Vinet's consent had been vitiated by economic fear, describing the circumstances under which Vinet had entered into the contract as "under...coercion, violence and fear..."
[created by] the defendant, who threatened...to suspend his payments; which [would] have had [the] effect to force him into liquidation."

In the more recent case of J.J. Joubert Ltée c. Lapierre, the court held that an employee who had agreed to acquire the equipment and clientele of his employer under threat of dismissal was entitled to have the contract annulled on the grounds that his consent had been vitiates by economic fear. The employer’s purpose was to have the plaintiff become an independent contractor so that the employer could rid itself of its employees’ union. In considering whether the plaintiff had experienced sufficient fear of serious injury to vitiate his consent, the court in Joubert emphasized the importance of a subjective analysis. The court considered the dependent relationship that existed between the employee and the employer and the plaintiff’s particular circumstances. In considering what was required to establish fear sufficient to vitiate consent, the court also stated that simple pressure to enter into a contract was not enough, but that illegitimate threats were required, whether such threats were illegitimately made, or made in order to further illegitimate goals.

Absent the element of outright threat or abuse of rights, however, Quebec courts have interpreted art. 1402 very strictly in commercial contexts. In the case of Verdi c. Société des alcools du Québec, the court refused to find that the plaintiff’s consent had been vitiates on the basis of economic fear. In that case, Verdi, a wine producer, had entered into a contract with the Société des Alcools du Québec (“SAQ”) to market and sell Verdi’s wines. The contract between Verdi and SAQ contained a provision allowing the SAQ to withdraw from its obligations under the contract if sales of Verdi’s wine were unsatisfactory. After the commencement of their relationship under the contract, SAQ determined that the sales were unsatisfactory and invoked its right to withdraw from the contract, leaving Verdi with over $1.5 million in merchandise that he was unable to sell and placing him in dire financial circumstances. Following some negotiations, Verdi and the SAQ then entered into another contract for the sale of the excess merchandise, on terms substantially less favourable to Verdi. Verdi later brought an action to have the latter contract annulled on the basis that his consent had been vitiates by economic fear and that SAQ had acted in

40. Which are dealt with separately in art. 1403: “Fear induced by the abusive exercise of a right or power or by the threat of such exercise vitiates consent.”
bad faith in its negotiations. Verdi pleaded that at the time of entering into the second contract, he was in such a fragile economic situation that he had no other choice but to enter the contract with the SAQ.

The Quebec Court of Appeal rejected Verdi’s claim of economic fear on the basis of a subjective analysis of his circumstances, holding that Verdi was an experienced businessman who had entered into contracts of equal significance on many prior occasions. The court also held that the onus was upon Verdi to prove that the SAQ had acted in bad faith and that this onus had not been met. Upon an examination of the evidence, the Court stated that it was unable to find that the SAQ had exercised illegitimate threats in its negotiations with Verdi.

In the case of Valla-Gaumond c. Cie des chemins de fer nationaux du Canada, the Quebec Superior Court considered the application of a sixty-one-year old pharmacist of limited business expertise who had entered into a lease assignment agreement in order to avoid otherwise certain bankruptcy. The pharmacist’s business was failing, and her landlord, Canadian National Railways, demanded the sum of $25,000 in order to allow her to assign her lease to a new tenant. Without the permission to assign the lease, she faced imminent bankruptcy, so she paid the amount demanded and then brought an action to have the contract annulled on the basis that her consent was vitiated by economic fear and that CN had acted in bad faith by exploiting her circumstances when it demanded the $25,000.

The Superior Court found that CN had not acted in bad faith. The court did not go so far as to offer a definition of bad faith, but stated that bad faith requires more than merely negotiating an agreement that promotes one’s rights. The Court quoted a dictionary definition of good faith (roughly translated) as “sincerity, honest behaviour and straightforwardness based on the certainty of acting within the framework of one’s legal rights.” The court analyzed the plaintiff’s economic fear subjectively, and considered the choice she faced either to agree to pay the $25,000 demanded or to face personal bankruptcy. The Court held that although bankruptcy is an unpleasant experience, it was not a shameful one, and that the plaintiff’s fear of bankruptcy was not sufficient to vitiate her consent to the agreement. In the course of its decision, the Court explicitly mentioned the policy consideration that it should promote the stability of contracts when possible.

43. Ibid. at para. 31. Trahan J. cited the definition given in the Dictionnaire Hachette (Paris, 1991): “la sincérité, la droiture dans la manière d’agir fondée sur la certitude d’être dans son bon droit.”
It would therefore appear that there are two elements that must be proven by the plaintiff who seeks to invoke the provisions of art. 1402 in the context of commercial contracts: an objectively reasonable fear of dire economic consequences, possibly beyond mere bankruptcy; and proof of bad faith or illegitimate threats on the part of the adverse party. The Quebec courts have demonstrated that these tests are difficult to establish in the commercial context, particularly between sophisticated and well-advised parties. In the context of the Churchill Falls contract, it is uncertain whether CFLCo's fear of imminent bankruptcy would be deemed to be sufficient to vitiate its consent. CFLCo's ability to prove Hydro-Québec's bad faith is also doubtful. It is possible in this case that the court would take Lessard's conflict of interest into account when considering whether Hydro-Québec acted in bad faith in the course of the negotiations, but without question, this would be a difficult onus to meet.

Even at common law, it would be difficult for CFLCo to establish it executed the Churchill Falls contract under economic duress. As discussed above, the threshold issue at common law is whether the pressure exerted by Hydro-Québec was sufficient to constitute "undue pressure," and the application of the four-factor *Pau On* test. Hydro-Québec's knowledge of the dire economic circumstances of NFLCo at the time the renewal provision was amended and CFLCo's lack of alternative development opportunities would be relevant to both determinations. It may be that if Hydro-Québec knew of CFLCo's imminent bankruptcy and intentionally prolonged the negotiations until CFLCo had no effective choice but to enter into the contract, and if a court deemed this to be an illegitimate exercise of Hydro-Québec's superior bargaining power, that this could constitute "undue pressure." With respect to the four-factor test, it is not clear from the evidence presented by Feehan and Baker how this analysis would proceed. For example, it is not clear whether the negotiators for CFLCo protested the inclusion of the renewal provision or to what extent such a protest may have been feasible. It is also not clear at law when a contracting party might be expected to take steps to avoid a renewal provision; whether it must be "avoided" at the time of contract, or at the time of renewal. The precise application of the common law doctrines to the facts of this case is therefore not entirely clear.

**The duties of corporate directors**
Though the legal battles over the Churchill Falls contract have largely been championed by the Newfoundland government and its agents, as a matter law, the party that has directly experienced losses arising from the terms of the contract is CFLCo itself. As such, the company may have had a claim
against its directors for breach of their fiduciary duties to the corporation. The board of directors as a group may be liable if they were negligent in approving such an improvident contract, and Lessard in particular may be liable for voting to approve the contract in circumstances where his duties to CFLCo were in conflict with his duties as a director of Hydro-Québec and for using information he acquired as a director of CFLCo to benefit Hydro-Québec. CFLCo is a corporation incorporated under the Canada Business Corporations Act, and as such, its directors are obliged to comply with the duties imposed on them by that Act and at common law.

Directors of a corporation are in a fiduciary relationship with the corporation, and are obliged to carry out their duties to the corporation "honestly and in good faith with a view to the best interests of the corporation." This rule generally prohibits all forms of conflict of interest, and may preclude directors from acting on the boards of directors of multiple companies, particularly those in direct competition with one another, or where acting as a director of one company will harm the other. It is entirely possible, perhaps even likely, that Lessard acted in breach of his duty of loyalty to CFLCo by simultaneously acting as an officer and director of Hydro-Québec during a time when the companies were engaged in such intense and adversarial negotiations.

Directors are also required to "exercise the care, diligence and skill that a reasonably prudent person would exercise in comparable circumstances." Very few claims succeed against directors on the ground of breach of duty of care in Canada however, because Canadian courts are traditionally quite deferential to directors of business corporations with respect to matters of "business judgment," though there have been a few where directors have been found liable for negligent performance of their duties. The standard of deference of the courts to directors in matters

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44. R.S.C. 1985, c. C-44.
45. Ibid., s.122(1)(a).
46. In Aberdeen Railway Co. v. Blaikie Bros. (1854), [1843-60] All E.R. 249 at 252, Lord Cranworth set out the guiding equitable principle that "no one, having such duties to discharge, shall be allowed to enter into engagements in which he has, or can have, a personal interest conflicting or which possibly may conflict, with the interests of those whom he is bound to protect." For a modern discussion of the duty, see Canadian Aero Services Limited v. O'Malley et al., [1974] S.C.R. 592.
47. See, for example, Abbey Glen Property Corporation v. Stumborg et al. (1976), 65 D.L.R. (3d) 235; aff'd (1978), 4 B.L.R. 113 (Alta. S.C.A.D.).
of business judgment was described by the Ontario Court of Appeal in
*Maple Leaf Foods Inc. v. Schneider Corporation* in the following terms:

The court looks to see that the directors made a reasonable decision not a perfect decision. Provided the decision taken is within a range of reasonableness, the court ought not to substitute its opinion for that of the board even though subsequent events may have cast doubt on the board’s determination. As long as the directors have selected one of several reasonable alternatives, deference is accorded to the board’s decision.\(^{51}\)

It is therefore open to the courts to examine the question of whether a particular business decision taken by the directors was reasonable. In light of the grossly improvident bargain negotiated on behalf of CFLCo, it may have been possible for a court to find that the directors of CFLCo did not enter into the 1969 contract reasonably, though the legal and other business advice received by the directors throughout the negotiation process may mitigate against such a finding.

A practical question might be whether there is any point in pursuing the directors in this case, as it is very unlikely that any of them, or their estates, would have sufficient resources to make such a claim feasible or palatable. However, recovery might be possible from at least one director, Lessard, who, as an officer and director of Hydro-Québec, is likely to have been indemnified by that company for any actions taken by him in the course of his service.

Additionally claims against the directors for breach of their fiduciary obligations could have properly proceeded in the courts of Newfoundland, where the common law fiduciary tests would have been applied. Forty years after the execution of the contract however, such claims would be subject to the doctrine of laches, which, as discussed below, would be difficult to overcome.

*Applicable law and the consequences of delay*

Some forty years have passed since the negotiation and execution of the Churchill Falls contract. This passage of time raises questions as to the law that would be applicable to the matter, and whether any claim might be barred by legal rules requiring actions to be brought within a reasonable time.

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Applicable law

The question of the applicable law arises because the CCQ has been amended on a number of occasions since the mid-1960s, most notably by the addition of a number of new articles relating to contractual remedies that were introduced in the 1990s. It is necessary, therefore, to inquire into whether the laws in effect in the 1960s would apply to the interpretation of the contract, or those presently in force.

The answer to this query is relatively straightforward, because when the 1994 amendments were implemented, a number of transitional provisions were also enacted that clarify that the new articles of the CCQ are applicable to contracts entered into prior to the implementation of the reforms.\textsuperscript{52}

Delay

Perhaps the greatest legal difficulty faced by CFLCo if it should attempt to challenge the Churchill Falls contract is the effect of the legal rules in both the common law and the civil law that require cases to be brought to the courts within a reasonable time. In most common law jurisdictions, strict time limits for the bringing of actions are also set out in limitations statutes.

Under the common law, equitable claims such as breach of fiduciary duty and unconscionability are subject to equitable defences, including the doctrine of laches, which can bar a claim that is not brought within a reasonable time. Laches is a form of acquiescence on the part of a party who is aware of a right of action against another but fails to bring the action within a reasonable time of its discovery. The purpose of the rule is to allow people to move forward with their affairs, without concern that they may be called upon to argue issues from their ancient past or pay damages for liabilities that were incurred but left unchallenged for a long period of time.

The leading case on the doctrine is \textit{Lindsay Petroleum Co. v. Hurd}, in which the Privy Council made it clear that the fact of delay alone is not enough to invoke the laches doctrine, but that the doctrine also requires

\textsuperscript{52} Act Respecting the Implementation of the Reform of the Civil Code, S.Q. 1992, c.57. Section 78 provides "The provisions of articles 1407, 1408 and 1421 of the new Code concerning, respectively, the remedies available to the person whose consent is vitiated, the power granted to the court to maintain, in certain cases, a contract in respect of which a demand for annulment has been made, and the presumption of relative nullity of a contract which does not meet the necessary conditions of its formation, are applicable to contracts formed before 1 January 1994." Section 79 continues, "[t]he relative nullity of a contract made before 1 January 1994 may, in the conditions set forth in article 1420 of the new Code, be invoked by the party contracting with the person in whose interest the nullity is established."
some corresponding detriment to the other party in the case. As with most equitable doctrines, the test is flexible in nature, and its application will depend upon the overall equities of the case. The Privy Council described the test for laches as follows:

Where it would be practically unjust to give a remedy, either because the party has, by his conduct, done that which might fairly be regarded as equivalent to a waiver of it, or where by his conduct and neglect he has, though perhaps not waiving that remedy, yet put the other party in a situation in which it would not be reasonable to place him if the remedy were afterwards to be asserted, in either of these cases, lapse of time and delay are most material. But in every case, if an argument against relief, which otherwise would be just, is founded upon mere delay, that delay of course not amounting to a bar by any statute of limitations, the validity of that defence must be tried upon principles substantially equitable. Two circumstances, always important in such cases, are, the length of the delay and the nature of the acts done during the interval, which might affect either party and cause a balance of justice or injustice in taking the one course or the other, so far as relates to the remedy.53

Lindsay Petroleum has been followed by the Supreme Court of Canada on a number of occasions.54

The doctrine of laches will require a consideration of whether the plaintiff’s delay in bringing the action either constitutes acquiescence in the defendant’s conduct, or results in circumstances that have caused the defendant to alter their position in reasonable reliance on the plaintiff’s acceptance of the status quo, or otherwise makes the prosecution of the action unjust. Laches is an inherently flexible doctrine, used for the purpose of furthering justice as between the parties. In Erlanger v. New Sombrero Phosphate Co., Lord Blackburn comments:

I have looked in vain for any authority which gives a more distinct and definite rule than this; and I think, from the nature of the inquiry, it must always be a question of more or less, depending on the degree of diligence which might reasonably be required, and the degree of change which has occurred, whether the balance of justice or injustice is in favour of granting the remedy or withholding it. The determination of such a question must largely depend on the turn of mind of those who have to decide, and must therefore be subject to uncertainty; but that, I think, is inherent in the nature of the inquiry.55

53. (1874), L.R. 5 P.C. 221 at 239-40 (P.C. – Ont.) [emphasis added].
55. (1878), 3 App. Cas. 1218 (H.L.) at 1279-80.
Where the doctrine of laches depends upon the acquiescence or neglect of the party who knows of his cause of action, the date upon which the party discovers the cause of action is clearly material, as a person cannot commit laches with respect to a claim he does not know he has, unless a court determines that he ought to have known it was available. Most limitations statutes have a similar requirement of “discoverability,” with stipulated time periods running from the date upon which a claim was, or ought to have been, discovered. A key issue in any laches case therefore, is when the plaintiff in the case found out that he or she had been injured or that a cause of action existed against the defendant. It is therefore open to CFLCo to argue that it did not know of the existence of its possible equitable claims against the directors until relatively recently, which may be plausible if the facts revealed by Feehan and Baker were previously unknown. However, the equities of the case may still favour the directors, who, after nearly forty years may reasonably have come to rely on CFLCo’s acceptance of the status quo, and organized their affairs accordingly.

In the civil law, the concept of “extinctive prescription” functions in a similar, though somewhat less flexible way, by extinguishing claims that are not brought within the prescription period. Article 2922 of the CCQ provides that “[t]he period for extinctive prescription is 10 years, except as otherwise fixed by law,” and a number of specific prescription periods follow. Article 2927 sets out the specific prescription for actions to annul a contract: “[i]n an action in nullity of contract, the prescriptive period runs from the day the person invoking the cause of nullity becomes aware of such cause or, in the case of violence or fear, from the day it ceases.”

Therefore, unless the findings of Feehan and Baker can be said to have revealed a cause of action previously unknown to CFLCo, it may be difficult for the company to justify its delay in bringing any claim relating to the Churchill Falls contract on any basis recognized by the civil law, as any fear for its property that may have induced the company to enter into the contract initially surely ceased shortly after the contract was executed. It is therefore doubtful at this point whether any contractual remedy is available to CFLCo.

**Conclusion**

The Churchill Falls contract is widely regarded as a travesty for Newfoundland, but CFLCo’s legal options now are limited. Feehan and Baker raise some interesting and perhaps disturbing issues relating to the negotiation of the 1969 Churchill Falls contract, but unless these issues

can be proven to have revealed to CFLCo a cause of action that it did not previously know that it had, and that any potential defendant has not been prejudiced by the delay, any claim that may have been possible is now likely to be barred by the doctrine of extinctive prescription and/or laches.

Though a successful legal attack on the Churchill Falls contract itself seems unlikely to succeed at this point, it is challenging to consider whether there may be other legal avenues that offer at least the possibility that Newfoundland may yet be able to repatriate some of the bounty of the Churchill River. It is interesting to consider, for example, the exclusive power to govern the production of electrical energy and to tax electrical generation facilities granted to the provinces by section 92A of the Constitution. Though these provisions clearly prohibit price and supply discrimination for power exported from a province to another part of Canada, as compared with power not exported from the province, they do not appear to prohibit, for example, provincial limits on the size or output of electrical generation facilities, or taxation regimes that discriminate on the basis of whether energy is exported from Canada. Of course, any action taken by the Newfoundland government in the exercise of its constitutional powers could not be taken for the purpose of interfering with Hydro-Québec’s rights under the Churchill Falls contract. Recalling the Re Upper Churchill Water Rights Reversion Act 1980 case, those rights are situate in Quebec and therefore, any act intended to interfere with them is ultra vires the government of Newfoundland.

In any event, as grossly unfair as the Churchill Falls contract is considered to be in Newfoundland, there may be little appetite for further political confrontation over the contract in the province today, considering the province’s recently announced new energy strategy, its unprecedented prosperity and its ongoing negotiations with Hydro-Québec for the development of electrical generation facilities on the Lower Churchill River.

Though the factual circumstances described by Feehan and Baker provide little hope that a legal challenge of the Churchill Falls contract would succeed in the courts today, they nevertheless illuminate the legal pitfalls and far-reaching complications which can arise in the context of the negotiation of any long-term commercial contract. If nothing else, we can hope that the lessons learned from the negotiation of the Upper Churchill contract will be to Newfoundland’s advantage in its negotiation
of the development of the Lower Churchill and the exploitation of its other natural resources.