COMMERCIAL LITIGATION REVIEW

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LITIGATION

Jonathon Baker
Baker & Baker

The Court of Appeal decision in United States of America v. Yemec *is a welcome clarification of the issue of enforceability of final foreign equitable judgments.*

Enforcing Foreign Injunctions: Pro Swing is a Hit

Counsel who obtain U.S. domestic orders now have the satisfaction of knowing that foreign equitable injunctive orders *are* enforceable in Canada.

As those of us who practise litigation, as well as many of our clients, are painfully aware, obtaining judgment is only half the battle. The judgment must also be enforced. Otherwise, it is a piece of paper rendered less valuable by the fact of having words printed on it. Moreover, while enforcement within the jurisdiction of the court granting judgment presents challenges, in our increasingly globalized economy, enforcement may require the crossing of borders. This raises the specter of the additional challenges of recognition and enforceability. The enforceability of out-of-jurisdiction money judgments was clarified and made easier by the Supreme Court of Canada in *Beals v. Saldanha.*[1]

However, less clear was whether a foreign equitable judgment, such as an injunction, would also be enforceable. The Supreme Court of Canada considered this issue in *Pro Swing Inc. v. Elta Golf Inc.*[2] and suggested that the common law should be extended to permit the enforcement of foreign non-money judgments. However, the court did not do so in that case, and seemed to raise some barriers. Fortunately, a recent case of the Ontario Court of Appeal has clarified that foreign permanent injunctions are indeed enforceable.

For 20 years, the defendants in *United States of America v. Yemec*[3] had operated a cross-border telemarketing business selling Canadian and foreign lottery tickets to consumers in the United States. The defendants typically sold packages of tickets at a cost of between $100 and $500 per package. These packages included a markup of between five and eight times the cost of the lottery tickets.

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In the Fall of 2002, the United States Federal Trade Commission ("FTC") brought proceedings in both Illinois and Ontario to prevent the defendants from continuing to operate the business. In Illinois, the FTC was successful in obtaining a temporary restraining order enjoining most of the defendants. In Ontario, it obtained *ex parte* Anton Piller and Mareva orders (which were subsequently set aside). The FTC then brought a summary judgment motion in Illinois, obtaining a final order that the defendants pay consumer redress in the amount of US$19 million, together with a permanent injunction. The injunction included a specific order that the defendants

> *are hereby permanently restrained and enjoined from engaging in, participating in or assisting in the telemarketing, in any manner, of any product or service to any person in the United States.*

An appeal to the United States Court of Appeals for the Seventh Circuit was dismissed.

The FTC brought a motion in Canada to recognize and enforce the final judgment of the United States District Court, including the permanent injunction. The defendants challenged the enforceability of foreign judgment at all, and particularly the injunctive relief component. The defendants argued that the judgment should not be enforced because they had been denied a "meaningful opportunity to be heard" in the U.S., which the defendants characterized as a "new" defence under *Beals v Saldanha.* The defendants also argued that the injunction ought not to be enforced since enforcing equitable orders requires, quoting *Pro Swing Inc. v. Elta Golf Inc.*,

> *a balanced measure of restraint and involvement by the domestic court that is otherwise unnecessary when the court merely agrees to use its enforcement mechanisms to collect a debt..*

The defendants were initially successful in opposing the motion for summary judgment to enforce the foreign judgment. The motion judge held that, while the defendants had not been able to establish the traditional defences of lack of jurisdiction, denial of natural justice, or public policy under *Beals v. Saldanha*, they had raised a triable issue on the "new" defence. The motion judge held that, in light of the *ex parte* Anton Piller and Mareva orders that had been set aside, there were material facts in dispute regarding whether the defendants may have been denied a meaningful opportunity to be heard in the United States proceeding due to the manner in which the litigation on both sides of the border had been conducted.

The Court of Appeal disagreed. The court held that it was clear that the defendants had had a meaningful opportunity to be heard in the United States and that they had exercised that right. They had fully defended and had an appeal *de novo.* The defendants had not suggested, either at the District Court or on appeal, that they had been denied natural justice or a meaningful opportunity to be heard.

Of more general import, the court noted that the denial of a "meaningful opportunity to be heard" could not be a "new" defence under *Beals v Saldanha.* Any new defences had to be narrow in scope, and could not raise issues covered under the existing defences of jurisdiction, failure of natural justice, or public policy. The motion judge had in fact found that there had been no denial of natural justice. The Court of Appeal noted that

> *[t]he right to be heard is one of the cornerstones of natural justice. A right to be heard that is not meaningful would not comply with the traditional test for natural justice … Therefore the addition of the word 'meaningful' does nothing to change the nature of the test already recognized in Beals.*

As such, there was no basis to deny the recognition and enforcement of the monetary or injunctive relief granted in the judgment.

Helpfully, the Court of Appeal also specifically addressed the injunctive aspect of the foreign judgment. After considering the various factors enumerated in *Pro Swing v Elta Golf Inc.* for a court determining whether to enforce a foreign equitable order, the Court noted that they were almost entirely satisfied, favouring enforcement of the order. The terms of the injunction were simple, clear and specific, such that it would be obvious to the defendants what they would be restrained from doing. While the order could have been narrower, the complete prohibition of telemarketing aimed at people in the United States was neither unfair nor unreasonable. Furthermore, the United States order specifically directed that the District Court would retain jurisdiction to enable any party to seek modifications. The order did not contain any unforeseen obligations on the defendants, and enforcement of the order would not place an undue burden on the Canadian justice system. Finally, the Court noted that the U.S. order was consistent with the types of orders that would be enforced for domestic litigants.

The Court of Appeal decision in *United States of America v. Yemec* is a welcome clarification of the issue of enforceability of final foreign equitable judgments. While *Pro Swing v. Elta Golf Inc.* held up the possibility, questions remained regarding whether such judgments would in fact be recognized and enforced. The Court of Appeal has now clearly answered those questions affirmatively.

1 [2003] S.C.J. No. 77, [2003] 3 S.C.R. 416.
2 [2006] S.C.J. No. 52, [2006] 2 S.C.R. 612.
3 [2010] O.J. No. 2411, 2010 ONCA 414.

ADR

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Settlement Counsel — Another Approach to Resolving Disputes

When the likelihood of settling a case far exceeds the likelihood of a hearing on the issues, it is prudent to select Settlement Counsel to conduct the settlement process.

Introduction

Among clients, it is almost trite to say that litigation has been steadily losing ground as the tool of choice for resolving legal disputes. Uncertain in cost and outcome, and burdened by an increasingly complex web of rules, the value and appeal of litigation has been diminishing across a wide range of sectors, type of dispute and type of client. The wide-ranging development of various form of alternative dispute resolution (mediation, arbitration, negotiation, etc.) has been an attempt to expand the dispute resolution tool kit. In this article we introduce a recent addition to that tool kit.

What is Settlement Counsel?

Settlement Counsel is litigation counsel that is engaged for the sole purpose of settling a case. His role is to develop and implement a strategy that results in early settlement. The Settlement Counsel role rests on the premise that litigation advocacy is not the same as settlement advocacy and that the task of settling a case is also not the same as the task of litigating it. While the objectives may be the same, the approaches, clearly, are not. Trying to pursue both roles at the same time, as the traditional litigation models try to do, risks a loss of both credibility and effectiveness.

How would it work?

Settlement Counsel does not participate in the litigation. She reports directly and exclusively to the client and in the context of a given dispute focuses on negotiation, mediation (formal or informal) risk analysis, strategic goal development and in the generation of suitable settlement structures. Settlement Counsel will be well-versed in the client, its business, risk tolerance and long-term interests, and will have timely and direct access to key client decision-makers and resources.

Settlement Counsel can work with or without litigation counsel. He can be engaged as early as the first possibility of a dispute arises and can get to work on a resolution as early as that point. Settlement Counsel working on his own from the onset of a dispute, behind the scenes or at the forefront, could well find a quick, creative solution that avoids the significant time and costs that are often unavoidable in full-blown litigation.

If there *is* litigation counsel, Settlement Counsel takes the lead in any settlement process that is part of the litigation but is not constrained by it. Settlement Counsel can initiate or pursue settlement discussions at any point, including before any lawsuit starts, without the loss of credibility that might result if the litigator did it. If working in parallel with the litigator, the two-track approach allows each to exploit the best features of their respective roles.

There clearly could be cost implications for the client in the two-track approach, all the more so if the case does not settle early. One way to address this is to structure the retainer of Settlement Counsel to include an early success incentive. If litigation regularly goes with the client's business territory, the use of Settlement Counsel will likely save the client money in the long run as both client and Settlement Counsel develop familiarity and expertise in risk assessment and management and in workable outcomes for the client in different types of cases. Experience south of the border so far suggests that more cases settle sooner with the use of Settlement Counsel, resulting in savings which would not have been realized through the efforts of litigation counsel alone.

Settlement Counsel obviously needs to understand the merits and demerits of the case. The litigator therefore shares information with Settlement Counsel, but not the other way around. This is a key component of this scheme. To be most effective, the work of Settlement Counsel needs to remain confidential and outside the litigation process. (This is one of the main weaknesses of the standard model of the litigator who at one and the same time is trying to settle the case: there can be a basic inconsistency between trying to win and at the same time trying to compromise). The two roles must remain distinct and be seen to remain distinct. All settlement overtures would be referred to Settlement Counsel and handled by him. The information flow to Settlement Counsel would involve such things as case evaluation, identification of key issues (both legal and factual), the overall strategy for the case and the outcome of any interlocutory proceedings.

Why two tracks? Different task, different focus and different tools. The focus of Settlement Counsel is less on what happened and more on what the client would like to *see* happen. It is less rights-based and more interest-based. It is a free-ranging problem-solving exercise, unbound by what happened or by what can be proved. What can often take significant time and resources, ascertaining the historical facts and sorting out what the applicable law is or might be, is of lesser importance in this process. For settlement purposes, often it is facts different from those that one can get through the litigation process that are the ones that matter. (These "settlement facts" often are in fact hard, if not impossible, to get in the litigation process.) Settlement Counsel is more likely to get open and timely disclosure than through the standard litigation process. By virtue of this separation of functions, having Settlement Counsel involved also strengthens the ability of the litigator to just litigate, meaning the focus of all energy in obtaining the most favorable outcome for the client within the established rules.

Advantages of Settlement Counsel

The greatest value of Settlement Counsel comes from the freedom to engage in a critical evaluation of the case at every stage of the case. Settlement Counsel is better able to avoid the dangers that often come from too close an identification with one's client (and with the case) that can be a feature of the litigator-as-"hired gun" model. Unhindered by procedural rules, precedent and a court process often at its institutional limits, Settlement Counsel is able to bring a different tone, a broader range of alternatives and a much broader frame of reference to any given dispute and to the exercise of judgment that is always involved in generating acceptable litigation outcomes for the client.

Settlement Counsel is free to get opposing counsel to the table at any point, free as he would be from the dynamics of the litigation process (timetables, motion outcomes, posturing, incomplete information, unexpected disclosure, case management rules, etc.). Willing to cut to the heart of the dispute and free of the need to posture, the single goal of Settlement Counsel is not a legal remedy rooted in precedent, but an early and particularized *business* solution to the case.

Conclusion

Not every case can or should be settled. But for those where settlement is practicable and appropriate, Settlement Counsel represents yet another tool at the disposal of the client and its counsel. With Settlement Counsel the interests of legal counsel and those of the client can be made to align themselves perfectly. Particularly if an early success fee is built into the retainer, there can be no opportunity for a conflict to arise between the interests of the client in resolving the case early and cheaply and those of litigation counsel in, for example, proving himself right, besting opposing counsel, garnering publicity or continuing to earn fees. And because settlement takes a lot less time than litigating, Settlement Counsel is able to handle a larger caseload for a client.

In the right cases, the use of Settlement Counsel can be a more effective and efficient way to manage the desire that is almost always present in all parties to litigation, whether stated or not: to obtain some measure of vindication while doing so in a manner that is cost- and time-effective and which limits damage to the company and its business to the greatest extent possible.

[*Editor's note*: The author wishes to extend his thanks Jim McGuire of JAMS.]

Franchise Litigation

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Courts Clarify Rescission Rights under Ontario's Franchise Law

Rescission of a franchise agreement can lead to significant costs for an unwary franchisor, where a deficient disclosure document obliges it to make its franchisee financially whole.

Franchise legislation, currently in each of the provinces of Alberta, Ontario and Prince Edward Island, requires franchisors to provide a disclosure document to prospective franchisees for the purposes of allowing these prospective franchisees to make an informed investment decision regarding their purchase of, and investment in, a franchised business. The disclosure document required by the legislation in each of these provinces must contain, among other prescribed information and documents, information regarding the franchisor, the business to be franchised, and certain particulars regarding the franchise system. Although substantially similar, the disclosure requirements of these provinces do have some significant differences. This article will focus on Ontario's franchise law, *The Arthur Wishart Act (Franchise Disclosure), 2000* [the *Act*][1] and recent Court decisions made under the *Act*.

Failure to comply with the disclosure requirements gives rise to a statutory right of rescission in favour of the franchisee under two specific scenarios. Upon rescission, the franchisor is obliged to repay all monies paid to it by the franchisee, to buy back all of the franchisee's equipment, supplies and inventory and to compensate the franchisee for any losses that the franchisee has incurred in establishing and operating the franchised business. The consequences of a franchisor not complying with its disclosure obligation is therefore significant. Nonetheless, until recently, the availability to a franchisee of this statutory remedy has not been so clear. In fact, soon after the passage of the *Act*, lawyers began to debate the distinction between the two time periods for a franchisee to avail itself of the recission remedy when there has been non-compliance with the *Act*'s disclosure requirements.

The *Act* provides a franchisee with a right of rescission in two separate and distinct circumstances. Section 6(1) of the *Act* allows a franchisee to rescind the franchise agreement no later than 60 days following its receipt of the disclosure document if the franchisor failed to provide the disclosure document within the time required under the *Act*, or if a disclosure document did not meet the requirements of the *Act*. Under s. 6(2) of the *Act*, the franchisee has two years from the date of entering into the franchise agreement if the franchisor fails to provide a disclosure document. These two provisions have raised the question as to whether a disclosure document that is lacking in the information provided is in fact a disclosure document, for purposes of the *Act*.

The Court of Appeal, and subsequent cases that followed, now make clear that a deficient disclosure document can be deemed to be no disclosure at all, thus entitling a franchisee to rescind within two years following the execution of the franchise agreement. These decisions demonstrate the necessity for strict compliance by a franchisor with the *Act*'s disclosure obligations so as to enable a prospective franchisee to make an informed investment decision.

In *6792341 Canada Inc. v. Dollar It Limited*,[2] a franchisee attempted to rescind its franchise agreement pursuant to s. 6(2) of the *Act* and made application to the Superior Court for declaratory relief. The Court dismissed the application on the grounds that, as the franchisee had received a disclosure document, it was entitled only to the right of rescission under s. 6(1) of the *Act*. The franchisee's notice of rescission was delivered well after the expiry of the 60-day period following its receipt of the disclosure document. The franchisee's appeal to the Court of Appeal was granted and in her reasons, MacFarland J.A. held that the deficiencies in the disclosure document were so material that "the only reasonable conclusion is that the franchisor never provided the disclosure document within the meaning of s. 6(2)".

The respondent franchisor acknowledged that the disclosure document was missing required information required under the *Act* and its regulations [the *Regulations*][3] but took the position that a disclosure document having been provided, the franchisee was entitled to rescind only within the 60-day period provided by s. 6(1) of the *Act*.

The Court, in its reasons, looked to the purpose and intent of the *Act*, being to protect the interests of franchisees and to permit a prospective franchisee to make an informed decision about whether to make the investment. Among the deficiencies noted by the Court, the disclosure document provided by Dollar It Limited did not include, among other information:

(1) a signed and dated Certificate of disclosure;

(2) financial statements or an opening balance sheet;

(3) a copy of the lease for the premises under which the franchisee was the subtenant;

(4) information about the franchisor's affiliate which was the tenant and sublandlord of the premises;

(5) prescribed information pertaining to the franchisor's advertising program; and

(6) a description of the exclusive territory to be granted and the franchisor's policy on proximity between franchised locations.

The Court held that the provisions of ss. 6(1) and 6(2) must be read and interpreted broadly in light of the intended purposes of the *Act* and that to interpret those provisions strictly would "lead to absurdity". Taken together, the deficiencies were substantial enough to preclude the franchisee from making an informed decision and thus concluded that a disclosure document was never provided within the meaning of s. 6(2) of the *Act*. An order was granted declaring that the franchisee had the right to rescind the franchise agreement within the two-year period following execution of the franchise agreement.

In its decision, the Court acknowledged that each case must be considered on its own facts and accordingly, it is not clear whether any of these deficiencies alone would have been sufficient to constitute a failure to provide disclosure within the meaning of the *Act* or whether the Court relied on the fact of a number of deficiencies. Of particular significance is the Court's inclusion in the noted deficiencies the failure to provide a copy of the lease for the premises and information regarding the franchisor's affiliate, both of which the Court held to be "material facts" to be disclosed pursuant to s. 5 of the *Act*.

In rendering its decision, the Court relied on the decision of the Alberta Court of Appeal in *Hi Hotel*

Limited Partnership v. Holiday Hospitality Franchising Inc.[4] which held that the absence of a signed and dated Certificate alone was sufficient to establish that there was no disclosure provided and accordingly the franchisee was entitled to the two-year rescission period under Alberta's franchise legislation. The Court rejected the franchisor's argument that, as the franchisee was a sophisticated purchaser, it should not to be able to get out of the deal on a technical defect. The Court strictly construed the requirements of Alberta's *Franchises Act*[5] that the disclosure document must include a certificate that must be dated and must be signed. The Court held that neither the level of sophistication of the franchisee nor whether the franchisee relied upon the absence of the signature and date on the certificate (the franchisee candidly admitted that they did not) was relevant to its determination of the case. The case simply turned on whether the franchisor complied with the statute.

A similar decision was rendered by the Superior Court of Ontario in which a franchisee of the Houston Steaks & Ribs franchise system was permitted to rescind a franchise agreement approximately 14 months after its restaurant opened for business.[6] The Court held that the document delivered to the franchisee candidate was not a "disclosure document" for a number of reasons including that it did not contain a certificate of disclosure. The lack of a signed certificate was one of at least four deficiencies that the Court held was alone sufficient to render the disclosure document non-compliant with the *Act*'s requirements. In his decision, Mr. Justice Wilton-Siegel stated:

> *The certificate is an important means of implementing the policy of the Act of ensuring complete and accurate disclosure of all material facts pertaining to a proposed franchise investment. It is also the mechanism for imposing liability for misrepresentations in the disclosure document on certain parties as contemplated by paragraph 7(1)(e) of the Act.*[7]

The other deficiencies which alone rendered the disclosure document non-compliant included the failure to include financial statements, the failure to provide the basis for, or assumptions underlying, the earnings projections and the failure to deliver a disclosure document as single document at one time.

Of equal consequence in this case, the franchise system had been sold and the franchise agreement assigned to a new franchisor between the date that the disclosure document was delivered and the date that the franchisee delivered its notice of rescission. The Court held both the original franchisor and the assignee liable to the franchisee for the post-rescission compensation that the franchisee was entitled to under the *Act*. The original franchisor and the new franchisor were ordered to pay to the franchisee in excess of $1 million which was the cost of establishing the restaurant as well as a further amount to compensate the franchisee for its operating losses.

In view of these decisions, it is imperative that franchisors in Ontario comply strictly with the disclosure requirements of the *Act* and its regulations including the disclosure of material information particular to the specific location at which the franchised business will be operated. A generic, "standard form" disclosure document will not suffice to protect a franchisor from the severe penalties imposed under the *Act* for non-compliance.

1 S.O. 2000 c.3.
2 [2009] O.J. No. 1881, 2009 ONCA 385.
3 O.Reg. 581/00.
4 [2008] A.J. No. 892.
5 R.S.A. 2000 c. F-23.
6 *Sovereignty Investment Holdings, Inc. v. 9127-6907 Quebec Inc.*, [2008] O.J. No. 4450 (S.C.J.).
7 *Ibid*. para. 19.

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