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Ontario's court rules arbitrator not free to ignore contract law, judge's instructions

By **Mitchell Rose**

Law360 Canada (May 7, 2024, 12:46 PM EDT) -- As a general principle, "domestic" arbitrations in Ontario — being those governed by the province's *Arbitration Act, 1991* — "must be decided in accordance with the law. Arbitrators are accorded broad deference for matters within their jurisdiction and in defining the scope of their jurisdiction. But they are not free to ignore the law or to decide cases in accordance with their whims."

Mitchell Rose

These are the opening lines of Justice Fred Myers's reasons in *Eyelet Investment Corp. (c.o.b. Treasure Hill Homes) v. Song*, 2024 ONSC 2340, a recent decision of Ontario's Divisional Court. The decision describes a multiyear saga of a domestic commercial arbitration "gone wrong" after an arbitrator applied his own legal principles and then disregarded a lower court ruling overturning one of his awards. It is essential reading for litigators and arbitrators.

Background

The appellant is a builder of new residential homes. The respondents are homebuyers pursuant to separate agreements of purchase of sale (APS) who refused to close. The builder accepted the buyers' repudiation. It incurred carrying costs, resold at a loss due to a declining market and treated the buyers' deposits as forfeited.

Arbitration proceedings were commenced, as required by Tarion Warranty Corporation (Tarion) in accordance with the *Ontario New Home Warranties Act* (ONHWA).

The liability award

The arbitrations proceeded together, and the buyers raised a common defence. Following a hearing on liability alone, the arbitrator released his partial award in December 2018.

The buyers' defence rested on the builder having not checked the "yes" or "no" boxes in the Tarion standard terms incorporated into their APS. "The tick boxes indicated whether the agreements were subject to any early termination conditions ... None of the purchases involved any issues over any of the listed optional early termination clauses. No one tried to exercise any rights under any of the clauses for example."

However, the "Arbitrator held that the builder was required to tick a box in the Tarion form and its failure to do so, no matter how immaterial on the facts, amounted to a lawful basis for the buyers to walk away from their agreements," and "the builder was not entitled to accept their anticipatory repudiation of their agreements."

Instead, he ordered the builder to return the purchasers' deposits, contrary to Ontario contract law.

The builder appealed.

Appeal

In October 2019, Justice Shaun O'Brien of the Superior Court of Justice allowed the appeal, set aside the liability award, held the purchasers liable for breach of contract and referred the matters back to the arbitrator to assess damages and costs.

Final award and the present appeal

In July 2023, the arbitrator released his final award on damages and costs in which he critiqued the decision of Justice O'Brien and ruled that it was not binding on him. For example:

> The fact that the appeal decision is binding on the parties concerned does not mean that it is binding on the tribunal…
>
> ... remitting the award to determine further issues based on [Justice O'Brien's] conclusion makes me feel that I'm given an assignment to do: substantiate her decision with merits which I don't believe exist. Without being convinced that it is not the Vendor that breached the contract, but the contrary, and without proper grounds for setting aside the award, I find it difficult to make an award to the opposite of the original one ...

The builder again appealed, but this time to the Divisional Court.

According to Justice Myers, writing on behalf of the three-member panel, it was "not open to the Arbitrator to ignore the findings of the court on appeal regardless of whether he believes that he is correct in his view of the merits."

However, the "Arbitrator revisited whether, in his view, the buyers should be responsible for the builder's damages."

Justice Myers added that:

> As best as I can tell, the Arbitrator found that the builder committed a "contributory breach of contract" by being primarily at fault for failing to tick the correct box in the agreements of purchase and sale. On that basis he determined that the parties should each bear their own "fair share" of damages ... and the builder's damages were limited to the forfeiture of the buyers' deposits.

Of course, as the court pointed out, there is no such thing as a "contributory breach of contract."

Therefore, the arbitrator erred in law: "When a buyer breaches a contract to buy a house and the vendor re-sells at a loss, the correct measure of damages is the difference in price to the respondent vendors, together with a number of consequential loss items ... In most cases ... the vendor must account for or give credit for the deposits already held."

As a result, "the decision cannot stand because the Arbitrator did not assess damages in accordance with the applicable legal principles. Moreover, he denied both parties the right to adduce evidence on the issue that had been deferred previously. As a result, we have an insufficient record to even attempt to assess damages."

The court ordered a new hearing on damages and costs but before a different arbitrator.

Jurisdiction

Justice Myers also addressed the fact that two separate levels of court heard each of the appeals. Section 17 (4) of the ONHWA provides for appeals to the Divisional Court while s. 45 of the *Arbitration Act, 1991* provides for appeals to the Superior Court. According to Justice Myers, "It is not clear to me that the Superior Court is necessarily deprived of its jurisdiction to hear an appeal under s. 45 ..."

However, he added that "If the appeal before O'Brien J. is a nullity, then so too is the subsequent award by the Arbitrator taken pursuant to the referral back to him ... In that case, the final award by the Arbitrator must be set aside in any event ... It was wrong, unreasonable, legally unintelligible, and palpably so. If O'Brien J. lacked jurisdiction to hear the appeal before her, I would transfer it to this proceeding and allow the appeal as she did ..."

Final thoughts

While the decision is a warning to arbitrators about the limits of their jurisdiction, *Eyelet Investment Corp*. also demonstrates how easily the potential benefits of arbitration can be undermined when that warning goes unheeded: the matter is still ongoing more than five years after the liability hearing, and the builder incurred almost $140,000 in legal fees on the recent appeal alone.

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