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— Franks & Zalev - This Week in Family Law

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News Item: Transparency Registers and the *Child Support Guidelines*

Let's recall s. 18 of the *Child Support Guidelines*, SOR/97-175:

> 18 (1) Where a spouse is a shareholder, director or officer of a corporation and the court is of the opinion that the amount of the spouse's annual income as determined under section 16 does not fairly reflect all the money available to the spouse for the payment of child support, the court may consider the situations described in section 17 and determine the spouse's annual income to include
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> (a) all or part of the pre-tax income of the corporation, and of any corporation that is related to that corporation, for the most recent taxation year; or
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> (b) an amount commensurate with the services that the spouse provides to the corporation, provided that the amount does not exceed the corporation's pre-tax income.

As we all know, lurking behind s. 18 is the notion of "control" — whether it be *de jure* control or *de facto* control: *Bates v. Welcher* (2001), 17 R.F.L. (5th) 255 (Man. C.A.); *C. (M.) v. O. (J.)* (2017), 93 R.F.L. (7th) 59 (N.B. C.A.); *Kowalewich v. Kowalewich* (2001), 19 R.F.L. (5th) 330 (B.C. C.A.); *Chapman v. Summer* (2010), 82 R.F.L. (6th) 79 (B.C. C.A.); *Potzus v. Potzus* (2017), 91 R.F.L. (7th) 290 (Sask. C.A.); *DBF v. BF* (2017), 98 R.F.L. (7th) 1 (Alta. C.A.); *Sweezey v. Sweezey* (2016), 78 R.F.L. (7th) 398 (Alta. Q.B.).

The "overriding consideration" is whether the payor is in a position to ***influence*** the amounts paid out by the company: *Guenther v. Guenther* (2016), 82 R.F.L. (7th) 311 (Sask. Q.B.); *M. (E.M.) v. M. (J.I.)* (2012), 19 R.F.L. (7th) 498 (B.C. S.C. [In Chambers]); *Henderson v. Henderson* (2021), 58 R.F.L. (8th) 203 (N.B. Q.B.) (factors to consider re "control") (no attribution).

Wouldn't it be nice if there were some official document — somewhere — that set out the people that effectively controlled a corporation. Wouldn't that be nice . . .

On January 1, 2023, certain amendments to the Ontario *Business Corporations Act*, R.S.O. 1990, c. B.16 (the "*OBCA*") came into effect. Those amendments compel private Ontario corporations to create and maintain a register of all "individuals with significant control" or ***influence*** over the corporation. The new document is called a Transparency Register. The requirements can be found is sections 1.1, 140.2 and 140.3 of the *OBCA*.

The amendments mirror similar amendments under Federal and other provincial corporate statutes (including British Columbia, Saskatchewan, Manitoba, Nova Scotia, Prince Edward Island and Newfoundland and Labrador).

A corporation's Transparency Register must include certain personal information about "individuals with significant control", how and when the individuals became "individuals with significant control," and a description of the factors that make the individual an "individual with significant control," including a description of his or her interests and rights in respect of shares of the corporation. And there are significant fines for not properly maintaining the records and disclosing captured individuals.

An "individual with significant control" means:

> • The person holds 25% or more, either by votes or fair market value, directly or indirectly (including legal/beneficial ownership or the ability to direct the shares); or
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> • Considering all factors relevant in the circumstances, the person has *direct or indirect* ***influence*** that, if exercised, would give him or her "control in fact" over the corporation.

It also appears that two or more people with an agreement to act in concert may comprise a control unit of sorts.

In making a "control in fact" determination, the amendments provide that the corporation must consider "all factors that are relevant in the circumstances," and that the existence of a legally enforceable right or ability to effect a change in the board of directors or its powers is not conclusive.

That's one powerful piece of paper.

Now for the bad news — at least for now: the *OBCA* only provides for certain government agencies and officials (police, OSC, tax officials, etc.) to get copies of the Transparency Register. It is not available to the public and is not mandated to be disclosed to shareholders or creditors as are other corporate records: s. 145(1).

However, there is nothing in the *OBCA* — at least nothing we see — to suggest that a court might not be able to order disclosure of the Register.

Change in the Law Alert: To Enforce a Penalty Clause an Order is in Order!

Assayag-Shneer v. Shneer (2023), 81 R.F.L. (8th) 7 (Ont. C.A.) — Miller, Zarnett and Coroza JJ.A.

Disclosure: Epstein Cole LLP was involved in this matter.

This was the appeal of *Assayag-Shneer v. Shneer* (2021), 53 R.F.L. (8th) 349 (Ont. S.C.J.) (Hood J.), which was the subject of our comment in the 2021-33 (August 30, 2021) edition of *TWFL* ("At Least for Now . . . Keep on Pre-Estimating Damages").

Below, Justice Hood offered a reminder that a financial penalty upon default will be unenforceable unless it constitutes a genuine pre-estimate of damages on account of the breach. But here, the Ontario Court of Appeal tells us that some "reminders" need not be remembered. It now appears that, with proper wording, planning and execution, penalty clauses may be enforceable. This represents a significant change in the law. Read on . . .

The parties married in 1994 and separated in 1997. They did not have any children together. When they separated, the husband was the CEO of his own company and earned about $200,000 to $250,000 a year, while the wife was in her second year of chiropractic college.

In 1999, the parties signed a Separation Agreement that provided, among other things, for the husband to pay the wife a total of $388,000 in spousal support, with $100,000 payable by October 1, 1999, and $4,000 a month payable for the next 72 months (starting on November 1, 1999).

The Agreement also provided that in the event of a default, the husband would owe the wife ***twice*** the then outstanding amount, plus an extra $50,000. That would be the alleged penalty clause.

The support provisions of the Separation Agreement — including the penalty clause — were then incorporated into a Consent Order. As we will see below, this turns out to have been incredibly important.

The husband paid the initial $100,000, and made the first 15 payments of $4,000 a month. However, he defaulted on the 16th payment, and never made another payment. Accordingly, in addition to the $228,000 in support he still owed, the terms of the Order and the Agreement required him to pay an additional $278,000.

Neither party took any steps to deal with the matter until 2017 (that is about 15 years after the default), when the Family Responsibility Office started trying to collect the money that the husband owed the wife. At that point, the husband started a variation proceeding, and took the position that the default provision was unenforceable because it was a "penalty clause", and that the support provisions of the Order and Agreement should be varied because his health and finances had declined precipitously since 1999.

Given the husband waited almost 15 years to seek a variation, Justice Hood rejected the husband's request to reduce his outstanding support obligation:

> [32] [The husband] has made choices along the way. In my view these choices were not forced upon him by his circumstances. He chose to stop paying support and made no efforts to pay it after January 2001. He chose to move to a country where he knew he could not work. He chose to start a new family and life ignoring his first wife's needs and the divorce order. His health issues have not truly impacted his earning capacity. His own evidence discloses that this is not the case. The failure of [his business] was a possibility in 1999 and its demise in 2000 was not unforeseen. In my view the company's success or failure was specifically contemplated at the time of the divorce judgment. It was therefore not a material change as that term was defined by the Supreme Court in *Willick v. Willick* [1994] 3 S.C.R. 670, at p. 688, where the Court explains, "if the matter which is relied on as constituting a change was known at the relevant time it cannot be relied on as the basis for variation." See also *L.M.P.*, at para. 67.: see also *L.M.P.*, at para. 67.
>
> [33] Moreover, the failure of [the husband's business] took place in 2000, when [the husband] was 39 years old. There has been ample time since then and well before his health issues, even if they were material, for [the husband] with his self-acknowledged business experience and acumen to find alternative employment so as to put himself in a position to pay the support. As mentioned above, there have been several years where he succeeded in doing just that, and nonetheless declined to pay support.

The more interesting issue, however, was whether the wife could actually enforce the default provisions of the Order and Agreement, or whether these terms constituted an unenforceable penalty clause.

The classic rule against penalty clauses provides that a contractual provision stipulating what would happen in the event of a future breach is unenforceable unless it constitutes a genuine pre-estimate of damages: *Canadian General Electric Co. v. Canadian Rubber Co.*, 1915 CarswellQue 15 (S.C.C.) at paras. 3-5. We all learned that in law school.

The classic rule was heavily criticized over the years, most recently in Justice Wakeling's dissent in *Capital Steel Inc v. Chandos Construction Ltd*, 2019 CarswellAlta 125 (C.A.). In that case, Justice Wakeling would have abolished the classic rule, and replaced it with a rule whereby a term of a contract that stipulated the consequences for a breach should be enforced unless "it is so manifestly grossly one-sided that its enforcement would bring the administration of justice into disrepute." Justice Wakeling's reasons also include a comprehensive history of the classic rule and an analysis of the fundamental problems with it, including the following:

> [161] **First, it is not clear what constitutes a penalty.** "The test for distinguishing penal from other principles is unclear". This is a significant drawback. If an adjudicator does not know what the core element of a principle is, it is impossible to apply it rationally and consistently.

. . . . .

> [167] **Second, because the penalty rule is confusing, it produces inconsistent results that cannot be rationally explained.** This is not a trait of a useful norm. It is the mark of a misleading and suspect measure.
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> [168] **Third, even if the benchmarks of a penalty term were universally acknowledged, it is not readily apparent that the penalty concept captures the essence of judicial reluctance to enforce some contract terms and provides much assistance in deciding whether a contested term should be enforced or not.** A determination that a provision is a penalty provides little assistance to an adjudicator who must decide whether it is appropriate to relieve a promisor of a contractual obligation. How does the knowledge that a term is a penalty assist a court to decide whether it should be enforced? Characterizing a stipulated-consequence-on-breach term as a penalty is no more helpful than describing it as a remedial term or written in English. . . .
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> [169] **Fourth, the distinction between a penalty and a pre-estimate of damages is of limited value.** There are fact patterns which make it exceedingly difficult, if not impossible, to estimate damages. This might mean that a stipulated-consequence-on-breach term is unenforceable even though it makes sound business sense.
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> [170] **Fifth, the penalty aspect of a provision can often be camouflaged by clever drafting.** An onerous obligation can be transformed into a beneficial option, as Justice Heath explained more than 200 years ago in *Astley v. Weldon* . . .
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> . . . . .
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> [173] **Sixth, it is not obvious why a promisor's commitment in a commercial agreement to pay a sum for breach of another term of the agreement that may bear no relationship to the damages that a court would award for non-performance is contrary to public policy.** A stipulated-consequence-on-breach term in a commercial contract and the common law damages principle serve completely different purposes. The former is adopted to avoid the need to utilize the common law damages protocol to resolve the consequences of nonperformance of a contract promise. The latter is resorted to because the parties have been unable to resolve the obligation of the promisor to the promisee on the former's breach of a contractual obligation. [footnotes omitted; emphasis added]

The Supreme Court of Canada granted leave to appeal in *Capital Steel Inc*, but it declined to decide whether the rule against penalty clauses should be reformulated (2020 CarswellAlta 1754 (S.C.C.) at para. 22).

It appears that the courts in British Columbia may also be "relaxing" the strict rule regarding penalty clauses. In B.C., a specific negotiated term to provide for a specific payment is not a penalty clause — it is just part of the contract and a term specifically negotiated by the parties: *Do v. Nichols*, 2016 CarswellBC 706 (C.A.). (Query, however, what would happen if the negotiated sum was so large as to be a clear penalty.)

However, in most of the country, the strict rule is still applied, and the question of whether a clause is a penalty clause depends on its construction and on the circumstances at the time of contracting: *Dundas v. Schafer* (2012), 17 R.F.L. (7th) 307 (Man. Q.B.), rev'd, (2014), 50 R.F.L. (7th) 37 (Man. C.A.) (leave to appeal to SCC ref'd); *Mortgage Makers Inc. v. McKeen*, 2009 CarswellNB 422 (C.A.); *Haas v. Viscardi*, 2019 CarswellOnt 2547 (C.A.)) (a liquidated damages clause will continue to be struck as a penalty if it was not a genuine pre-estimate of actual losses).

The wife in *Assayag-Shneer* argued that the default provision of the Agreement and Order constituted a genuine pre-estimate of her damages in the event of a default, because it recognized the legal fees that she would have to incur, and it implicitly supported her position that the support she had agreed to in the settlement already constituted a sizeable discount over the amount to which she was actually entitled.

Justice Hood disagreed. In finding that the default provision was "a penalty and unenforceable", Justice Hood noted as follows:

> [44] **The doubling of the outstanding support plus an additional $50,000 bears no relationship to any loss or damage that [the wife] could suffer through a default in payment.** It is simply a lump sum payable regardless of the loss or damage. I do not accept her argument that this amount is an attempt to recognize the legal fees that she would necessarily

> incur upon default and is thus a genuine pre-estimate of her loss. **The clause bears no relationship to what her costs might be in the event of a default. Moreover, costs are a separate issue.** If successful in seeking to enforce payment she might be entitled to some indemnity of her legal costs, but to suggest that this was the intention of the clause in the first place and that it is a valid liquidated damages clause or genuine pre-estimate of loss is untenable. [emphasis added]

As a result, Justice Hood dismissed the husband's Motion to Change, but also granted a declaration that the clause in the Consent Order was a penalty and, therefore, unenforceable.

This was the wife's appeal.

The Court of Appeal reasoned that by deleting the "penalty" clause, the motion judge had, in effect, varied the Consent Order. This, according to the Court of Appeal, was an error in law because a support order cannot be varied absent a material change in circumstances. A material change is a requirement whether a court order is imposed on parties, a consent order or the result of converting a separation agreement into an order (see *L.M.P. v. L.S.* (2011), 6 R.F.L. (7th) 1 (S.C.C.)). And, as set out above, Justice Hood had explicitly found that there *had not* been a material change.

This raises an interesting question: would it have made a difference had the husband been more careful in his pleadings (perhaps with the benefit of hindsight) by, for example, pleading to set aside the offending terms in the Consent Order? Probably not. But that said, that pleading may have forced the Court of Appeal to grapple with the idea (as discussed below) that a consent order is only as good as the consent that supports it.

The Court of Appeal also found that neither the common law doctrine regarding penalty clauses in contracts nor s. 98 of the *Courts of Justice Act*, R.S.O. 1990, c. C.43 (which confirms the Ontario Superior Court's power to relieve against penalties and forfeitures on such terms as are just), could justify the motion judge's order. This is because, according to the Court of Appeal, the penalty clause doctrine was meant to apply to *contracts* not to court *orders*. The Court of Appeal reasoned that the Separation Agreement ceased to be a separation agreement when it was incorporated into the parties' Consent Order. If the husband had a problem with the penalty clause, he ought to have raised his concern at the time the Order was entered into. The Court of Appeal stated at paragraphs 41 and 42:

> [41] There can be many reasons why a clause in a contract that is arguably a penalty ends up being enforced by a court order. A party may choose not to argue that the clause is a penalty, or the court might rule that the clause is not a penalty and should be enforced. It does not matter which occurs. **The question of whether a clause in a family law agreement is valid and enforceable is a question that must be raised before the clause is enforced by including its provisions in a court order that directs its performance. Once that occurs, the question of contractual enforceability has been determined, by a judge presumed to know the law and in an order that is presumed correct. The order is then enforceable as a judgment of the court.**
>
> [42] If the [husband] wished to avoid enforcement of a provision of the Minutes he considered to be a penalty, the time to do so was before the term was reflected in the divorce judgment. He could have opposed the inclusion of what became para. 3 of the divorce judgment on the basis of his penalty arguments. If he did not like the outcome, he could have appealed. Having not raised any concerns about the provision being an unenforceable penalty at the time it was converted into a judgment, he cannot now do so.

All this is to say that a penalty clause may still be unenforceable at common law; but the time to argue about it is *before* it is incorporated into a consent order. Once that happens, it is too late. Therefore, the issue is going to have to be addressed by the judge that is being asked to incorporate the clause into a court order.

However, in deciding the matter in this fashion, the Court of Appeal does not actually address whether Justice Hood was correct on the law to rule the clause a penalty clause. Given that spousal support is about need, ability to pay, and compensation — one would think that an automatic doubling plus $50,000 could only be a penalty as opposed to a genuine pre-estimate of damages.

Similarly, s. 98 of the *Courts of Justice Act* gives the court authority to protect parties against penalties or forfeitures provided for in a *contract* — nothing in that section suggests that it applies once a judge has ordered a contract to be performed (and the order has not been appealed). Another judge of the same court did not have the power to review the order and rule on its correctness. The motion judge did not have the jurisdiction to find that a portion of the divorce order was unenforceable as a penalty clause.

The result? A penalty provision that might be wholly unenforceable in a separation agreement *will be enforceable* once incorporated into an order of the court.

While this may result in a welcome change for some — especially those that would like to include such a penal provision in domestic contracts, this ruling results in a few interesting questions — things that make us go "hmmmm?" if you will:

a) First, while a consent order is a binding decision of the court passed on using the court's jurisdiction [*Bank of Montreal v. Coopers & Lybrand Inc.* (1996), 23 R.F.L. (4th) 415 (Sask. C.A.)]; a consent order is ultimately just that — the formal expression of an *agreement* — and is, therefore, generally interpreted as if it was a contract: *D. (B.G.) v. D. (R.W.)* (2003), 35 R.F.L. (5th) 315 (B.C. C.A.); *Shackleton v. Shackleton* (1999), 1 R.F.L. (5th) 459 (B.C. C.A.). Would the usual provision of contract interpretation, including the rule against penalty clause, then not also apply to the interpretation of a such a clause?

b) Having their foundation in contract, a consent order is only as strong as the agreement giving rise to it and may be set aside on the same grounds as the underlying contract: *Rick v. Brandsema* (2009), 62 R.F.L. (6th) 239 (S.C.C.); *Monarch Construction Ltd. v. Buildevco Ltd.*, 1988 CarswellOnt 369 (C.A.); *McCowan v. McCowan* (1995), 14 R.F.L. (4th) 325 (Ont. C.A.); *Shackleton v. Shackleton* (1999), 1 R.F.L. (5th) 459 (B.C. C.A.); *Pond v. Pond*, 2017 CarswellBC 1956 (C.A.); *Ruffudeen-Coutts v. Coutts* (2012), 15 R.F.L. (7th) 13 (Ont. C.A.). Therefore, if a contractual provision is void or invalid, arguably the resulting order would also be invalid. By way of example, an agreement that was negotiated under duress or that is unconscionable does not become enforceable because it was incorporated into a consent order.

c) As noted above, a penalty clause may still be unenforceable at common law (the Court of Appeal does not suggest it is questioning the penalty clause issue as have the courts in B.C. and Alberta); but the time to argue about it is *before* it is incorporated into a consent order. Therefore, the issue is going to have to be addressed by the judge that is being asked to incorporate the clause into a court order. However, this means that courts *can* incorporate these clauses into consent orders. And if a court *can* do so, why would they *not* do so, being presented with a consent where the ink is still wet? This means that such clauses are going to be regularly incorporated into consent orders and enforced.

d) One common reason parties have historically wanted to use penalty clauses in domestic contracts is to penalize a party for claiming support (or other relief) contrary to the provisions of the agreement. See, for example, *Dundas v. Schafer* (2012), 17 R.F.L. (7th) 307 (Man. Q.B.), rev'd, (2014), 50 R.F.L. (7th) 37 (Man. C.A.) (leave to appeal to SCC ref'd). According to the Ontario Court of Appeal in *Shneer*, this may now be possible *if* the provision is incorporated into a consent order (which is presumably more practical for a separation agreement than a marriage contract).

However, a court cannot order a spousal support release; a support release is a creature of contract. And while parties can agree to a consent dismissal of a claim for spousal support, the dismissal of a claim for spousal support can actually be varied if there is a material change of circumstances: *Tierney-Hynes v. Hynes*, 2005 CarswellOnt 2632 (C.A.); *Gill-Sager v. Sager* (2003), 36 R.F.L. (5th) 369 (B.C. C.A.); *Sandy v. Sandy* (2018), 6 R.F.L. (8th) 253 (B.C. C.A.). And once the support provisions of an agreement are incorporated into a consent order, those provisions are variable on a material change: *L.M.P. v. L.S.* (2011), 6 R.F.L. (7th) 1 (S.C.C.) at para. 36.

As a result, counsel would prefer to have a spousal support release in a contract (so as to attract the *Miglin* standard for claiming support contrary to the provisions of a contract) rather that have a consent support dismissal (which is variable on the much lower material change standard).

In *Shneer*, the Court of Appeal found that the penalty clause in question was part of the support provisions of the Agreement; in fact, that is the basis upon which the penalty clause was enforceable. Therefore, we are in a strange position: To have

the penalty clause enforceable (if it is part of the support provisions of a domestic contract), the penalty clause must be in an order. But to have a support release be as effective as possible, the release should be in an agreement.

So now what? Super easy. All counsel must do is include the support release (or other support provisions) and the penalty provision in the separation agreement, but only include the penalty provision (dressed up to not look like part of the support provisions) in the consent order. That should leave support provisions governed by *Miglin* in the agreement; an enforceable penalty provision in the consent order. As we said — real easy.

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