Court File No. CV-15-10832-00CL

ONTARIO
SUPERIOR COURT OF JUSTICE
COMMERCIAL LIST

IN THE MATTER OF THE *COMPANIES' CREDITORS ARRANGEMENT ACT*, R.S.C. 1985, c. C-36, AS AMENDED

AND IN THE MATTER OF A PLAN OF COMPROMISE OR ARRANGEMENT OF TARGET CANADA CO., TARGET CANADA HEALTH CO., TARGET CANADA MOBILE GP CO., TARGET CANADA PHARMACY (BC) CORP., TARGET CANADA PHARMACY (ONTARIO) CORP., TARGET CANADA PHARMACY CORP., TARGET CANADA PHARMACY (SK) CORP., and TARGET CANADA PROPERTY LLC (the "**Applicants**")

MOTION RECORD OF PHARMACIST REPRESENTATIVE COUNSEL
(motion returnable, Wednesday, September 13, 2017 at 11:15 a.m.)
PART II of II

September 5, 2017

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Court File No. CV-15-10832-00CL

ONTARIO
SUPERIOR COURT OF JUSTICE
COMMERCIAL LIST

IN THE MATTER OF THE *COMPANIES' CREDITORS ARRANGEMENT ACT*, R.S.C. 1985, c. C-36, AS AMENDED

AND IN THE MATTER OF A PLAN OF COMPROMISE OR ARRANGEMENT OF TARGET CANADA CO., TARGET CANADA HEALTH CO., TARGET CANADA MOBILE GP CO., TARGET CANADA PHARMACY (BC) CORP., TARGET CANADA PHARMACY (ONTARIO) CORP., TARGET CANADA PHARMACY CORP., TARGET CANADA PHARMACY (SK) CORP., and TARGET CANADA PROPERTY LLC (the "**Applicants**")

AFFIDAVIT OF CHARLES SCERBO

I, CHARLES SCERBO, of the City of Winnipeg, Province of Manitoba, MAKE OATH AND SAY:

1. I am a licensed Manitoba pharmacist. I am an officer, director and majority shareholder of Charles Scerbo Drugs Ltd., a Winnipeg corporation which owned and operated Target Pharmacy T3682 located in Winnipeg, Manitoba. I am a Claimant in the Claims Adjudication Process. I was a board member and vice-president of the Pharmacy Franchisee Association of Canada ("PFAC") until I resigned from PFAC on August 31, 2016. After my resignation from PFAC, I remained involved in the ongoing conduct of these proceedings by continuing to consult with Pharmacist Representative Counsel together with several other regional representatives of PFAC. As such, I have personal knowledge of the matters to which I hereinafter depose, unless stated to be

based upon information and belief, in which case I state the source of my information and believe it to be true.

2. This affidavit is supplementary to and re-affirms my affidavit sworn November 17, 2016.

3. I have consulted and provided instructions to Pharmacist Representative Counsel throughout these proceedings and I have continued to consult with Pharmacist Representative Counsel to the present date.

4. I am informed by Pharmacist Representative Counsel that 53 Franchisees settled their claims on or before September 14, 2016. I have been advised by Pharmacist Representative Counsel that the total amount initially allowed by Monitor in the Notices of Revision or Disallowance for these 53 Franchisees totalled approximately $11,786,135 and the Offers to Settle and Revised Offers to Settle were accepted by the 53 Franchisees in the amount of $15,137,666.

5. I have been advised by Pharmacist Representative Counsel that following the October 25, 2016 Ruling of the Claims Officer and as a result of further negotiations between the Monitor and Counsel, an additional 22 Pharmacy Franchisee Claims were settled in December 2016 and January 2017 in the approximate amount of $4,397,039.

6. It was an express term of these settlements that the Target Canada Entities will contribute a total of $1 million to the approved fees and expenses of Counsel otherwise owing by the Franchisees under the February 12, 2016 order.

7. Pharmacist Representative Counsel was initially instructed by 26 Franchisees to appeal the Rulings of the Claims Officer, and one Franchisee (T Pharmacy Ltd.) retained separate counsel for the appeal. As noted above, 22 Franchisees settled prior to the appeal hearing on February 23, 2017. My own claim was one of the four unsettled claims as of February 23, 2017.

8. On February 23, 2017, the Honourable Regional Senior Justice Morawetz heard the appeals on behalf of the four unsettled Pharmacy Franchisees represented by Counsel and one claim by T Pharmacy Ltd. as represented by Stavros Gavrilidis.

9. On May 19, 2017, the Honourable Regional Senior Justice Morawetz released his endorsement *Target Canada Co. (Re)*, 2017 ONSC 2595 dismissing all of the appeals.

10. Following the dismissal of the appeal, four of the remaining claims, including my own, were settled, for the amount of $302,636. As of the date of this affidavit, I have been advised by Pharmacist Representative Counsel that T Pharmacy Ltd.'s claim is the only one that remains outstanding.

11. The total settled claims are as follows:

Group	Settled	Amount
1	53 Pharmacy Franchisees	$15,137,666.00
2	22 Pharmacy Franchisees (approx.) - Pre-Appeal	$ 4,397,039.00
3	4 Pharmacy Franchisees (approx.) - Post-Appeal	$ 302,636.00
	Total (Approximate)	**$19,837,341.00**

12. I have reviewed the affidavits of Harvey T. Strosberg, Q.C., Josie Parisi of BDO Canada LLP, Robert M. Macdonald of MRM Consulting and Ian Manning of Edward & Manning LLP, and I agree with their contents.

13. This affidavit is sworn in support of a motion for:

(a) An Order approving the fees and disbursements of Pharmacist Representative Counsel, including those of its experts and advisors, and taxes thereon ("Fees");

(b) An Order for final payment of Fees; and

(c) Such further and other relief as this Court may deem just.

SWORN BEFORE ME at the City of Winnipeg, in the Province of ~~Saskatchewan~~ Manitoba, this 6th day of September, 2017.	))))))	
ROBERT HUCAL ~~Commissioner for Taking Affidavits~~ A NOTARY PUBLIC IN AND FOR THE PROVINCE OF MANITOBA. MY APPOINTMENT DOES NOT EXPIRE		CHARLES SCERBO

#1534692

Court File No. CV-15-10832-00CL

ONTARIO
SUPERIOR COURT OF JUSTICE
COMMERCIAL LIST

THE HONOURABLE DENNIS O'CONNOR,	)	FRIDAY, THE 24TH
	)	
CLAIMS OFFICER	)	DAY OF JUNE, 2016

IN THE MATTER OF THE *COMPANIES' CREDITORS ARRANGEMENT ACT*, R.S.C. 1985, c. C-36, AS AMENDED

AND IN THE MATTER OF A PLAN OF COMPROMISE OR ARRANGEMENT OF TARGET CANADA CO., TARGET CANADA HEALTH CO., TARGET CANADA MOBILE GP CO., TARGET CANADA PHARMACY (BC) CORP., TARGET CANADA PHARMACY (ONTARIO) CORP., TARGET CANADA PHARMACY CORP., TARGET CANADA PHARMACY (SK) CORP., and TARGET CANADA PROPERTY LLC (the "**Applicants**")

ORDER

(Common Issue #4 and Revised Litigation Timetable)

THIS HEARING, pursuant to the *Companies' Creditors Arrangement Act*, R.S.C. 1985, c. C-36 and the Order of Regional Senior Justice Morawetz dated February 12, 2016 in the above-referenced proceedings was heard this day by teleconference.

ON READING the Common Issues List attached as Schedule "A" to my order dated May 3, 2016 (the "**Common Issues List**"), my order of June 14, 2016, the report of BDO dated May 31, 2016 and filed by Pharmacist Representative Counsel on June 17, 2016 (the "**BDO Report**"), the submissions of the Monitor filed June 21, 2016, and on hearing submissions from counsel to the Monitor and Pharmacist Representative Counsel:

1. THIS COURT ORDERS that Issues 4(i) and 4(ii) on the Common Issues List shall be answered in the affirmative such that Issue 4 is hereby fully and finally resolved without the need for any further adjudication.

2. THIS COURT ORDERS that the Monitor shall not be required to file any evidence in respect of Issue 4.

3. THIS COURT ORDERS that nothing in this Order shall restrict the parties from making reference to the BDO Report for any purpose with respect to the remaining Common Issues in these proceedings or any individual adjudications which may follow the determination of the Common Issues.

4. THIS COURT ORDERS that the procedural timetable set out at Schedule "A" of the Claims Officer's Order (Pharmacist Claims Dispute Timetable for Remaining Common Issues) of June 14, 2016 shall be deleted and is hereby replaced by the revised and amended timetable attached as Schedule "A" hereto.

Schedule "A"

REVISED SCHEDULE FOR CONTINUED PROCEEDING

Date	Action
June 28	Monitor to deliver affidavit evidence with respect to Common Issues 7 and 6 (if necessary)
July 12	Pharmacist Representative Counsel to deliver evidence, including expert evidence, in response to Monitor's evidence
July 19	Monitor to deliver reply evidence, including expert evidence
July 27	Opening submissions to be exchanged
August 2 to 5	Hearing with respect to Common Issues 7 and 6 (if necessary)

IN THE MATTER OF THE *COMPANIES' CREDITORS ARRANGEMENT ACT*, R.S.C. 1985, c. C-36, AS AMENDED
AND IN THE MATTER OF A PLAN OF COMPROMISE OR ARRANGEMENT OF TARGET CANADA CO., *et al*

Court File No. CV-15-10832-00CL

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PROCEEDING COMMENCED AT
TORONTO

ORDER
(Common Issue #4 and Revised Litigation Timetable)

6540905

Court File No.: CV-15-10832-00CL

ONTARIO
SUPERIOR COURT OF JUSTICE
COMMERCIAL LIST

IN THE MATTER OF THE *COMPANIES' CREDITORS ARRANGEMENT ACT*, R.S.C. 1985, c. C-36, AS AMENDED

AND IN THE MATTER OF A PLAN OF COMPROMISE OR ARRANGEMENT OF TARGET CANADA CO., TARGET CANADA HEALTH CO., TARGET CANADA MOBILE GP CO., TARGET CANADA PHARMACY (BC) CORP., TARGET CANADA PHARMACY (ONTARIO) CORP., TARGET CANADA PHARMACY CORP., TARGET CANADA PHARMACY (SK) CORP., AND TARGET CANADA PROPERTY LLC (THE "APPLICANTS")

RULING

Alan Mark, Francy Kussner, Jesse Mighton – Goodmans LLP (counsel to the Monitor)

William V. Sasso, Sharon Strosberg – Sutts, Strosberg LLP (Pharmacist Representative Counsel)

Stephen Ferguson – Alvarez & Marsal Canada Inc. (the Monitor)

Shawn Irving, Christine Jackson – Osler Hoskin Harcourt LLP (counsel to the Target Canada Entities)

Stavros Gavrilidis – Pharmacist Franchisee Representative

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(b) Issue # 2: If the answer to Issue 1 is yes, does the common law duty of good faith and/or the statutory duty of good faith and fair dealing under applicable franchise legislation in the Regulated Provinces impact TCC Pharmacy's ability to rely on such provision to limit the recoverable losses of Franchisees? Can the question be answered 'No' without further evidence? 23

Issue #3: If the answer to Issue 1 is yes, does the common law duty of honest performance impact TCC Pharmacy's ability to rely on Section 12.1 of the Franchise Agreement to limit the recoverable losses of Franchisees? Can the question be answered 'No' without further evidence? 23

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Introduction

1. On February 12, 2016 R.S.J. Morawetz appointed me as a Claims Officer to determine the validity and amount of the Pharmacy Franchisee Claims under the Claims Procedure Order he had made in this CCAA proceeding.[1]

2. Justice Morawetz directed me to implement a summary process for the resolution of each disputed claim by identifying and limiting to the extent possible common issues in dispute.

3. On May 3, 2016, I made an Order setting out the Final List of Common Issues Applicable to the Pharmacy Franchisees' Claims. The list of Common Issues is attached as Schedule A to this Ruling.

4. This Ruling addresses Common Issues 1, 2, 3, 5 and 8(a).

5. For the reasons I set out below, I have found that:

(a) The Franchisors are entitled to damages in the amount required to place them in the position they would have occupied, had the Franchisor performed the Franchise Agreements in the manner least burdensome to it.

(b) The least burdensome manner of performance would have been for the Franchisor to terminate each Franchise pursuant to the early termination clause in the relevant Franchise Agreements.

(c) There is some lack of clarity as to the operation of the sixty day notice period required by the termination clause. The Franchise Agreements could be read either as: (i) permitting the Franchisor to give notice only after the expiry of three years from the date the

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[1] Capitalized terms herein have the meaning referred to in the Common Issues List attached hereto as Schedule A. However, for readability, I will often refer to TCC Pharmacy as the Franchisor and the Pharmacist Franchisees as the Franchisees. Where reference is made to the *Company's Creditor's Arrangement Act*, R.S.C., 1985, c. C-36 ("CCAA") proceedings, capitalized terms shall be the meanings as defined in the Initial Order dated January 15, 2015, the Claims Procedure Order, or other orders or documents referenced in the proceedings unless otherwise defined.

relevant pharmacy opened, with the termination taking effect sixty days thereafter; or (ii) permitting the Franchisor to give notice sixty days prior to the expiry of three years from the date of the pharmacy opening, such that the termination would take effect on that date. I am prepared to receive further evidence from the parties with respect to this narrow issue, before deciding which interpretation should prevail.

(d) With one possible exception, I conclude that the answers to Issues 2 and 3 are in the negative. However, I am prepared to consider further evidence directed solely at the issue as to whether or not the Franchisor's exercise of its rights under the early termination clause of the Franchise Agreements was fettered by a duty of good faith as a result of interactions between the parties in respect of the EBIT Support Program (as defined in the Factum of the Monitor) introduced after the Franchisees were operating under the Franchise Agreements.

(e) With respect to the types of expenses listed under Issue 5, I find that they are generally not recoverable. I am prepared to hear additional submissions as to whether or not a limited category of expenses should be recoverable. This category is limited to any expenses that the Franchisees have in fact incurred a result of the disclaimer of the Franchise Agreements, but that they would not have had to incur had the Franchisor terminated the Franchise Agreements after three years, pursuant to Section 12.1.

(f) The Franchisees are not entitled to any Rebates,[2] other than as provided for in the Franchise Agreement and the Disclosure Documents. The Franchisees are not entitled to further disclosure in this regard.

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[2] I use the term "Rebates", as it is defined in the Franchise Agreements, to mean "all payments, profits, rebates, discounts, advantages, goods, commissions, incentives, or other allowances or benefits … which Franchisor and/or its Affiliates may earn or be granted by suppliers related, directly or indirectly, to the sale of products and services to Franchisee."

<u>Facts</u>

(a) Background

6. Schedule A sets out a useful summary of the relationship between TCC Pharmacy as Franchisor and the Pharmacy Franchisees.

7. TCC Pharmacy was franchisor to 94 separate franchisees operating in-store Target-branded pharmacies across Canada, outside of Quebec. The in-store pharmacies were operated pursuant to Franchise Agreements and related documents between each TCC Pharmacy and each Franchisee.

8. The Franchise Agreement granted each Franchisee a license to operate the Target-branded pharmacy using certain Target Pharmacy trade-marks. The Franchisees were typically independent corporations which, in the majority of cases, were wholly-owned by a licensed pharmacist.

9. Both the Franchisee and the Pharmacist are parties to each Franchise Agreement because, among other things, in order to operate a pharmacy franchise, a licensed pharmacist is required under applicable regulations to be present at the premises during operating hours.

10. TCC Pharmacy introduced and implemented the EBIT Support Program in February 2014 to provide financial support to eligible Franchisees. This program was modified and enhanced for the benefit of eligible Franchisees in June 2014. The EBIT Support Program provided benefits to eligible Franchisees in addition to entitlements under the Franchise Agreements.

11. In January 2015, the Franchisor was one of the Target Canada group of companies that filed for protection under the CCAA with the intent of affecting an orderly wind-down of their business and affairs.

12. On January 15, 2015, the Superior Court of Justice made the Initial Order granting CCAA protection.

13. On January 26, 2015, the Franchisor, with the approval of the Monitor, delivered individual Notices of Disclaimer in respect of each Franchise Agreement and other ancillary agreements pursuant to Section 32(1) of the CCAA.

14. The Franchisees sought an Order under Section 32(2) seeking to set aside the Notices of Disclaimer. On February 18, 2015, Justice Morawetz denied the Franchisees' request.

15. The Franchisor agreed to permit the Franchisees to continue operating until the earlier of March 30, 2015 or three days following written notice by Target Canada of the anticipated closure of a store. Thus, the Franchisees were able to continue operating for longer than the 30 day period contemplated by Section 32(5) of the CCAA.

16. Between the date of the CCAA filing and the effective date of each Notice of Disclaimer, each Franchisee received or was entitled to receive, payment in the normal course in respect of their entitlements under the Franchise Agreement, including so-called OTC Royalty Payments, generic prescription drug product ("GPDP") rebates or volume discounts, as applicable, (in each case based on a percentage of the Pharmacist Franchisee's purchases of specific generic drugs), and, where eligible, EBIT Support Program payments. Common Issue 4 raises the correctness of the Monitor's methodology for measuring loss of future profits (including treatment of the OTC Royalty Payment and EBIT Support Program payments) and the Gross Sales Payout. The present ruling does not address common Issue 4.

(b) The Franchise Agreement

17. The evidentiary record before me includes copies of the relevant Franchise Agreements (including Amending Agreements where applicable). Section 2.2 of each Franchise Agreement provides that the Initial Term of the Franchise Agreement is for five (5) years. It reads:

> Subject to the provisions of this Agreement, Franchisor hereby grants to Franchisee the right, license and privilege to develop, own and operate a

> Pharmacy at the Licensed Space within the Territory, and to use the System and the Marks and any Intellectual Property in connection therewith, for an initial term of five (5) years from the date the Pharmacy opens (the "Initial Term"), **subject to earlier termination as provided herein**.
>
> [Emphasis added]

18. Section 12.1 provides TCC Pharmacy with a right to terminate without cause. It reads:

> At any time following the third anniversary of the opening date of the Pharmacy, Franchisor may, at its option, terminate this Agreement without cause and all rights granted herein effective immediately, upon sixty (60) days prior written notice.

19. Section 12.8(b) provides for payments upon Termination or Expiration. It reads:

> If the Franchisee does not exercise its first right of renewal and the Agreement expires at the end of the Initial Term, **or if this Agreement is terminated without cause by Franchisor prior to the expiration of the Initial Term**, in consideration for the termination of this Agreement and Franchisee's right hereunder, Franchisee will be paid two percent (2%) of the previous twelve fiscal month period's Gross Sales provided that Franchisee and Pharmacist have delivered to Franchisor a complete release, in a form provided by Franchisor, of Franchisor and its Affiliates, and their respective shareholders, directors and officers from all obligations of and claims against any such persons under or in connection with the Agreement.
>
> [Emphasis added]

(c) The Disclosure Documents

20. In addition to the Franchise Agreements, the parties filed nineteen versions of the Franchise Disclosure Documents which were provided to prospective franchisees prior to entering into a Franchise Agreement.

21. The Disclosure Documents were prepared in conformity to the *Arthur Wishart Act (Franchise Disclosure), 2000*[3] in Ontario and other similar provincial legislation in some other provinces. In unregulated provinces, the Disclosure Documents were prepared voluntarily but conformed with the regulatory requirements in regulated provinces. In general terms, the

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[3] S.O. 2000, c. 3 [*Arthur Wishart Act*].

purpose of the Disclosure Documents is to provide relevant information regarding the business opportunity for a prospective Franchisee, including financial information of the Franchisor, fees and other payments. The Disclosure Documents were updated from time to time. Apparently, there were over 100 versions in all.

22. The record does not contain all of the Disclosure Documents that were delivered. However, none of the parties have directed me to any differences in the Disclosure Documents that I do not have that would be relevant to the issues I am deciding. It appears, therefore, that the key terms outlining legal entitlements and obligations of the Franchisees are substantially identical in each case. I intend to proceed and decide the Common Issues referred to herein on the basis of the Disclosure Documents in the record. I am adopting this approach because of the importance of getting on with the process in a timely manner. If there is anything in the remaining Disclosure Documents that could affect my rulings herein on an individual claim, counsel should bring that to my attention.

23. The record also includes documents relating to the EBIT Support Program that the Franchisor introduced for the Franchisees as well as the enhanced EBIT Support Program introduced in June 2014. Throughout this ruling, when I refer to the EBIT Support Program, I intend this to include the enhancements made in June 2014, unless I specifically indicate otherwise.

(d) This Proceeding

24. The claimants before me are 80 former Franchisees who filed Proofs of Claim in the CCAA proceedings. In each case, the Monitor issued a Notice of Revision or Disallowance. The law firm, Sutts, Strosberg LLP, which had been appointed by Justice Morawetz to represent the Franchisees as a group, filed a Notice of Dispute of the Notices of Revision and Disallowance on behalf of the claimants in this proceeding.

25. The disputes arising from the above-referred to notices form the basis of my Order directing a Final Common Issues List.

26. It is common ground that the Franchisees' claims are as unsecured creditors in the CCAA proceedings.

27. In this proceeding, the Monitor has taken the primary role to argue that I should reject the Franchisees' Notice of Dispute. The applicants in the CCAA proceedings (the Target group of companies), support the Monitor's position.

28. In taking this position, the Monitor submits that I should make decisions with respect to the Franchisees' claims based solely on the applicable law and legal principles. To be successful, the Franchisees' claims must be based on legal entitlement only.

29. The Monitor points out that there are many other unsecured creditors in the CCAA proceedings. There will not be full recovery for the unsecureds. The Monitor has attempted to address all claims on the basis of valid legal entitlement only.

30. In a situation such as this, the more one creditor receives, the less others receive. I agree with the Monitor that claims should be assessed on the basis of legal entitlement. Where there is no entitlement, there can be no recovery. While that will no doubt result in many creditors, including some Franchisees, suffering what will be very painful losses, the scheme of the CCAA and fairness amongst creditors, require this approach. Were it otherwise, the administration and wind-up of the debtor's estate could be unfair to some creditors. Thus, in addressing the Common Issues, I will do so on the basis of legal entitlements arising from the Franchise Agreements, including related documents and the applicable law and legal principles.

31. That said, I accept the Franchisees' argument that I should make my decisions on a *de novo* basis. By that I mean I should not show deference to the decisions of the Monitor. Instead, I should consider each Issue on the basis of all of the relevant evidence and the law. I should make my rulings on what I consider to be the correct answer.

32. As I will discuss below in relation to each of the Common Issues, the Monitor takes the position that the evidentiary record referred to above is sufficient for me to rule on the Common

Issues. The Franchisees argue that in the case of each Issue, I should provide them with the opportunity to call further evidence.

33. The parties agree, however, that in determining whether I should provide the opportunity to the Franchisees to call further evidence, the test I should apply is whether such evidence could make a difference to my decision. Could it be of assistance to me in reaching a conclusion? Only if I am satisfied that hearing further evidence could not make a difference to the decision on a particular Issue, should I proceed to rule. This is obviously a high threshold and I will discuss it in the context of each of the Issues.

Analysis

(a) Issue #1: Based on ordinary contractual interpretation and damages assessment principles, does Section 12.1 of the Franchise Agreement operate to limit the Franchisees' recoverable losses under the Franchise Agreement to a period of three years from the opening of such Franchisees' pharmacy? Can the question be answered, 'Yes' without further evidence?

Introduction

34. It is common ground that the Disclaimer Notices constituted a breach of the Franchise Agreements. On January 18, 2014, the date that the Franchisor sent the Notices, none of the Pharmacies of the Claimants had been open for three years. Thus, the Franchisor did not have a right to terminate under Section 12.1. The question then becomes, what is the appropriate measure of damages for those breaches?

35. I note that in the Final List of Common Issues, the Monitor and the Pharmacists' representative counsel have agreed that the appropriate measure of damages arising from the disclaimer of each Franchise Agreement is that the Franchisee should be put in the same position in which it would have been had the Franchise Agreement been performed by TCC Pharmacy. I agree that is a proper approach.

36. In my analysis of Issue 1, I have not considered the various arguments that the Franchisees have advanced that rely upon the duty of good faith. I will address those arguments

in my discussion of Issues 2 and 3. As a result, all of my findings with respect to Issue 1 should be understood to be subject to issues of good faith.

Legal Principles Governing Contractual Damages

37. Pursuant to Section 32(1) of the CCAA, a debtor company is entitled to disclaim or resiliate any agreement it is a party to, subject to certain exceptions set out in the section:

> Subject to subsections (2) and (3), a debtor company may – on notice given in the prescribed form and manner to the other parties to the agreement and the monitor – disclaim or resiliate any agreement to which the company is a party on the day on which proceedings commence under this Act. The company may not give notice unless the monitor approves the proposed disclaimer.

38. Thus, pursuant to Section 32(1), a debtor may terminate or breach a contract forcing a non-defaulting party to claim as an unsecured creditor for its damages in the CCAA proceedings.[4]

39. In this case, the Franchisees are entitled to claim, as unsecured creditors, damages for breach of contract as a result of the Disclaimer Notices.

40. In considering Issue 1, I have applied following general principles:

(a) The Supreme Court of Canada has held that the usual measure of damages for breach of contract are expectation damages. Those damages focus on the value which the plaintiff would have received if the contract had been performed.[5] Restitution damages are rarely ordered and are not applicable to the facts of this case.

(b) Where an agreement has multiple modes of performance (such as an early termination provision), the Supreme Court of Canada has held, in *Hamilton v. Open Window Bakery Ltd.*, that expectation damages assume the mode of performance that is the least burdensome to the defendant.

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[4] *Blue Range Resource Corp., Re:*, 2000 ABCA 239, at para. 28.

[5] *Bank of America v. Mutual Trust Co*., 2002 SCC 43, at paras. 25 and 30.

> However, under the general principle applicable in breach of contracts with alternative performances […] it is not necessary that the non-breaching party be restored to the position they would likely, as a matter of fact, have been in but for the repudiation. Rather the non-breaching party is entitled to be restored to the position they would have been in if the contract had been performed.
>
> …
>
> The assessment of damages required only a determination of the minimum performance the plaintiff was entitled to under the contract, *i.e.* the performance which was least burdensome to the defendant.[6]

(c) The principle of "least burdensome performance" stipulated in *Open Window* applies to this case, regardless of whether the Franchise Agreements are considered to be contracts of adhesion (as the Franchisees argue that they should be). The Ontario Court of Appeal has specifically applied the *Open Window* principle to contracts of adhesion.[7]

(d) The damage analysis for a breach of contract resulting from a Section 32(1) disclaimer in a CCAA proceeding is the same as that for a breach outside of the insolvency context. The cases involving breach of contract claims in CCAA and bankruptcy proceedings of which I am aware apply the usual contractual principles when awarding damages. The Franchisees have cited no authority that holds that a court should apply different principles when awarding breach of contract damages to an unsecured creditor in a CCAA proceeding than it would apply if the defendant were solvent. I can think of no principled reason for applying a different approach in this case, simply because it arises out of a CCAA disclaimer.

Open Window and the Right of Early Termination

41. Under the principles set out above, the Franchisees are entitled to damages for the benefit (the profits) that they would have received had the Franchise Agreements been performed in the manner least burdensome to the Franchisor.

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[6] *Hamilton v. Open Window Bakery Ltd.*, 2004 SCC 9 [*Open Window*], at paras. 17 and 20.

[7] *Agribrands Purina Canada Inc. v. Kasamekas*, 2011 ONCA 460 [*Purina*] at paras. 44-53.

42. The question arises, for what period of time should the Franchisees be entitled to damages to cover their loss of profit? Applying the decision of the Supreme Court of Canada in *Open Window* leads inevitably to the conclusion that the manner of performing the Franchise Agreements that would have been least burdensome to the Franchisor would have been for the Franchisor to terminate the Franchise Agreements as soon as it was able to do so in accordance with Section 12.1. This means that I must assume that, with respect to each Franchisee, the Franchisor would have terminated the Franchise Agreement three years after the date of the opening of the pharmacy.[8]

43. The Franchise Agreements are clear that the Franchisor may terminate the Franchise Agreements without cause at any time following the third anniversary of the opening day of the pharmacy. Section 2.2, which sets out the Initial Term, explicitly says that the term is: "subject to earlier termination as provided herein."

44. The language of Section 12.1 is clear as to the Franchisor's right to terminate. There is no ambiguity or lack of clarity. Moreover, the representations in the Franchise Disclosure Documents which were given to each Franchisee before entering into the Franchise Agreement are entirely consistent with the language in Sections 2.2 and 12.1 of the Franchise Agreement. The representations are equally clear.

45. A threshold issue that arises when interpreting Section 12.1 concerns whether the clause should be regarded as an exclusionary clause that purports to limit the Franchisor's liability (as argued by the Franchisees) or as a clause that simply provides for an alternate method of performing the contract.

46. The Supreme Court of Canada held in *Open Window* that an analogous termination clause provided for an alternate method of performing a contract, and I approach Section 12.1 of the Franchise Agreement on the same basis. In *Open Window*, the principal in an agency

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[8] There is a dispute between the parties as to the operation of the 60 day notice period stipulated under section 12.1 of the Franchise Agreement. This issue turns on the meaning of the words "effective immediately" as used in that section. I address this issue, which I refer to as the "Effective Immediately Issue" under a separate heading, later in my reasons.

agreement had an unconditional right to terminate the contract after the commencement of the 19th month of the term of the contract. The Supreme Court of Canada viewed the contract as one with an alternate mode of performance. The defendant breached the contract by terminating it prior to the earlier termination date in the agreement.

47. In adopting the least burdensome to the defendant approach, the Supreme Court of Canada held that:

> [W]here there are several ways in which the contract might be performed, that mode is adopted which is the least profitable to the plaintiff and the least burdensome to the defendant.[9]

48. In *Open Window*, the contract was not terminated in accordance with the early termination clause. However, that clause still formed the basis for the determination of the defendant's minimum damage exposure.

49. In the present case, the Monitor based his assessment of damages on the assumption that the Franchisor would terminate each of the Franchise Agreements three years from the opening of the pharmacy. I find that the Monitor was correct in doing so.

50. The Franchisees argue that the Franchisor would not in fact have terminated all of the Franchise Agreements after three years, absent its insolvency. That may well be true, but it is irrelevant to the quantification of the Franchisees' damages in contract.

51. The Supreme Court of Canada in *Open Window* specifically rejected a tort-like approach to damages pursuant to which a court would consider how the defendant would likely have performed its obligation under the contract:

> The trial judge erred in this case in engaging in a tort-like inquiry as to what would have happened if OWB had not breached its contractual obligations to Hamilton, and in concluding that OWB would not have terminated at the earliest opportunity.

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[9] *Open Window, supra*, at para. 11, quoting from *Cockburn v. Alexander* (1840), 6 C.B. 791.

> The assessment of damages required only a determination of the minimum performance the plaintiff was entitled to under the contract, i.e., the performance which was least burdensome for the defendant. The plaintiff agreed at the outset that she was entitled to no more by contracting for a contractual term that could be truncated with notice entirely at the discretion of the defendant.[10]

52. In other words, the correct approach is for the court to assume that the defaulting party would have performed the contract in the manner least burdensome to it, without considering any evidence as to the likelihood that this would actually have occurred.[11]

The Franchisee's Unconscionability Argument

53. The Franchisees do not disagree with the legal principles set out above. Rather, they argue that the principles do not apply in this case or, at a minimum, that I cannot determine whether they apply without hearing further evidence.

54. The Franchisees argue that there is a threshold question as to whether Section 12.1 of the Franchise Agreement is unconscionable and therefore unenforceable. They argue that, if the clause is unenforceable, then I ought not to assume that the Franchisor would have terminated the Franchise Agreement after three years when assessing the Franchisees' damages. Unconscionability is a question of fact. The Franchisees argue it is necessary to hear evidence to test the argument of unconscionability.

55. The Franchisees' unconscionability argument, in essence, is that:

(a) There was a disparity in bargaining power between the Franchisor and the Franchisees.

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[10] *Ibid*, at paras. 19 to 20.

[11] *Ibid.* See also *Purina, supra*, at paras. 48 to 49: "In my view, [*Open Window*] cannot be distinguished as the trial judge did, and should have been followed in assessing the breach of contract damages in this case, even if Purina did not act in good faith in breaching the contract. Had that been done, the trial judge would not have embarked on a hypothetical inquiry into how Purina would likely have performed its obligations under the contract if it had not breached the contract. That is the very sort of inquiry that [*Open Window*] says should not be done in approaching breach of contract damages where there are alternate modes of performing the contract."

(b) The terms of the Franchise Agreement were unfair, in that the Franchisees were contractually obligated to perform their obligations for a period of five (5) years whereas the Franchisor could terminate its obligations after three (3) years without cause.

(c) Moreover, if a franchise was profitable, the Franchisor could terminate the Franchise Agreement early under Section 12.1. The effect would be to confiscate the Franchisee's profitable business, including the valuable prescription files, without compensation.[12] In addition, in the event of such termination, the Franchisee would be subject to the non-compete clause for a period of a year.

56. Because Section 12.1 could be unenforceable by virtue of unconscionability, the Franchisees argue that I should distinguish the *Open Window* case and other cases relied upon by the Monitor. They argue that Section 12.1 is unlike the clauses considered in those other cases because it is unenforceable. For that reason, they say that I should consider that the three year termination provision would not be a valid means for determining the damages for the breach for the Franchise Agreements.

57. I do not accept this argument.

58. In *Agribrands Purina Canada Inc. v. Kasamekas*,[13] the Court of Appeal for Ontario had to determine what contractual damages flowed from the defendant's breach of a dealership agreement. The plaintiff argued that it would be unconscionable to allow the defendant to rely on a clause that allowed it to terminate the agreement upon sixty days' notice when calculating damages under the *Open Window* principle. The Court said:

> … I do not agree that unconscionability can be used in this way. In my view, that doctrine is applicable to determine whether the contract itself is unconscionable, given, for example, the circumstances in which it was made. The doctrine is not

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[12] It is worth noting that Section 12.1 of the Franchise Agreement requires the Franchisor to pay the Franchisee 2% of the gross sales for the previous twelve month fiscal period in exchange for a release. As a result, it is not accurate to say that the Franchisor could confiscate the Franchisor's business "without compensation".

[13] *Purina, supra*.

> applicable to determine how damages should be assessed in light of the circumstances of a particular breach.[14]

59. In this case, the Franchisees do not seek to set aside the Franchise Agreement. Indeed, they rely upon it in asserting their claims. Given that the Franchisees are not arguing that the Franchise Agreements were unconscionable, the claim that reliance upon Section 12.1 would have been unconscionable can have no effect on the calculation of damages in this case. In my view, the *Purina* case is a complete answer to the unconscionability argument.

60. Finally, I note that the Franchisees have in any event failed to point to any evidence that they might call that could lead to me to conclude that Section 12.1 is unenforceable because of unconscionability. While the Franchisees allude to the fact that they expected that the relationship would last for a period of five years, and that they conducted their affairs on that basis, this would constitute evidence of the Franchisees' subjective intentions. It seems doubtful that one party's subjective intention could be relevant to the unconscionability of a contract. Moreover, even if the proposed evidence that the Franchisees expected that the relationship would last for a period of five years, and that they conducted their affairs on that basis, were admissible, it would not, in my view, render Section 12.1 unenforceable on the basis of unconscionability.

Evidence of Surrounding Circumstances

61. The Franchisees argue that in order to properly interpret the Franchise Agreement, including Section 12.1, I must consider evidence of the surrounding circumstances, even if there is no ambiguity in the provisions of the contract. Thus, they argue that I should hear evidence from the Franchisees about the surrounding circumstances before I interpret Section 12.1 in the manner proposed by the Monitor. I agree that I should hear all the evidence of surrounding circumstances that could possibly assist me in interpreting Section 12.1. The question is whether there is any relevant evidence, in addition to what is already in the record.

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[14] *Ibid*., at para. 52.

62. I start by noting that the Franchisees do not suggest an alternative interpretation for Section 12.1 other than that set out in the clear language.[15]

63. As I noted earlier, the provisions of Section 2.2 and 12.1 of the Franchise Agreement are clearly worded. Moreover, the Franchise Agreement includes an "Entire Agreement" clause and a "No Representations or Warranties" clause that, collectively, limit the parties' rights to those enumerated in the Franchise Agreement and require any amendments to those rights to be executed in writing.

64. In cases of clearly worded provisions, the Supreme Court of Canada has said that,

> …to interpret a plainly worded document in accordance with the true contractual intent of the parties is not difficult, if it is presumed that the parties intended the legal consequences of their words.[16]

65. The Supreme Court of Canada has held that courts should reject a contractual interpretation that would render one or more of its terms ineffective.[17] As put more simply by the British Columbia Court of Appeal, "Words in a contract are presumed to have meaning."[18] Here, the Franchisees' position would render Section 12.1 ineffective. The Franchisees have given no indication of what evidence of the surrounding circumstances could overcome the effect of the clearly worded provisions of the Franchise Agreements.

66. I agree with the statement of Geoff Hall in his *Canadian Contractual Interpretation Law* text about the paramountcy of the words of an unambiguous contractual provision over the factual matrix:

> Given the paramount importance of the words, being the very language agreed upon by the parties to govern their legal obligations, in cases of conflict the words will always prevail over the context. Thus while the factual matrix can be used to clarify the parties' intentions as expressed in a written agreement, it cannot be

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[15] The sole exception to this concerns the Effective Immediately Issue, which I discuss below,

[16] *Eli Lilly & Co. v. Novopharm Ltd.*, [1998] 2 S.C.R. 129 [*Eli Lilly*] at para 56. See also, *Canadian Premier Holdings Ltd. v. Winterthur Canada Financial Corp.*, [2000] O.J. No. 1619 at para. 12 (CA).

[17] *National Trust Co. v. Mead*, [1990] 2 S.C.R. 410 at para. 26.

[18] *Pass Creek Enterprises Ltd. v. Kootenay Custom Log Sort Ltd.*, [2003] B.C.J. No. 2508 at para. 17 (C.A.).

> used to contradict that intention, create an ambiguity which otherwise does not exist in the written document, or have the effect of making a new agreement.
>
> …
>
> [I]t must not be forgotten that the words themselves are paramount and the role of the factual matrix is to assist in fixing their meaning, not to provide a new meaning inconsistent with the words.[19]

67. Moreover, here the record already contains substantial evidence of the surrounding circumstances relating to the formation of the Franchise Agreements. The Disclosure Documents that were presented to the Franchisees at the time they entered into the Franchise Agreements paint a thorough picture of the surrounding circumstances at the time. The Franchisees do not assert that these Disclosure Documents failed to comply with the appropriate regulatory requirements nor do they argue that they misrepresent what was involved in the prospective relationship.[20]

68. In addition, the Franchise Agreements are contracts of adhesion or at a minimum very similar to contracts of adhesion. While there were some amendments to approximately 30 of them, the basic terms with which I am concerned were the same throughout. The use of surrounding circumstances as an interpretive aid in the case of contracts of adhesion is limited.[21]

69. The Franchisees suggest that they could call evidence from the Franchisees that they expected that they would have a longstanding relationship under the Franchise Agreement and that they "understood" the Franchisor was making a five year commitment. They acted accordingly.

70. Although the proposed evidence of surrounding circumstances was only described in oral argument and understandably is somewhat imprecise, I am satisfied that all of the proposed

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[19] Geoff Hall, *Canadian Contractual Interpretation Law*, 2d. ed. (Markham, Ontario: LexisNexis Canada, 2012) at pp. 31-32.

[20] Again, I leave to one side for the moment, the Effective Immediately Issue.

[21] *Fairview Donut Inc. v. TDL Group Corp.*, 2012 ONSC 1252 [*Fairview Donut*] at paras. 413-416, affirmed 2012 ONCA 867.

evidence would either be evidence of subjective intention and therefore inadmissible, [22] or would contradict the clear wording of Section 12.1 and therefore be of no assistance in interpreting the language of the contract. It would not, even if accepted, cause me to read out Section 12.1 of the Franchise Agreements or to interpret the section in a manner inconsistent with its clear language. That is the effect of what the Franchisees ask me to conclude.

71. Thus, I do not find that in this case any further evidence of surrounding circumstances would be of assistance to me in interpreting paragraphs 2.2 and 12.1 of the Franchise Agreements.[23]

The Franchisees' Contract of Adhesion Argument

72. The Franchisees further argue that the Franchise Agreements are contracts of adhesion and, as such, I should interpret Section 12.1 with special care. In *Fairview Donut*, Justice Strathy (as he then was) accepted that Franchise Agreements are contracts of adhesion. He said:

> … Where there is ambiguity, they should be interpreted *contra proferentem*. Exclusionary clauses should be subjected to particular scrutiny see *Shelanu Inc. v. Print Three Franchising Corp …*[24]

73. The Franchisees say that the principles in *Fairview Donut* and *Shelanu* require me to hear further evidence before I interpret Section 12.1 as limiting the losses that flow from the breaches of the Franchise Agreements.

74. I do not accept that further evidence is required to interpret Section 12.1 for these reasons. Accepting for the purposes of the argument, that the Franchise Agreements in this case are contracts of adhesion, the cases do not go so far as to say that the normal rules of contractual interpretation are to be ignored.[25]

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[22] *Eli Lilly, supra*, at paras. 54-56, *Dumbrell v. The Regional Group of Companies Inc.*, 2007 ONCA 59 at paras. 51-56, and *Ventas Inc. v. Sunrise Senior Living Real Estate Investment Trust*, 2007 ONCA 205 at para. 24.

[23] Aside from the Effective Immediately Issue.

[24] *Fairview Donut, supra*, at para. 415, citing: *Shelanu Inc. v. Print Three Franchising Corp*. (2003), 64 OR (3d) 533, (CA) [*Shelanu*] at para 58.

[25] *Fairview Donut, supra*, at paras. 413 to 416.

75. As discussed above, the language of Section 12.1 is absolutely clear.[26] I doubt very much that it should be characterized as "an exclusion clause" (a finding that would be inconsistent with the approach taken by the Supreme Court of Canada to an analogous clause in *Open Window*) but even if it is, I do not consider that further evidence, even if examined with care, could possibly make a difference to this interpretation. Certainly, the Franchisees have not pointed to any admissible evidence that could have that effect.

76. Finally, I note that the Ontario Court of Appeal has observed that the factual matrix (or surrounding circumstances) is of little assistance in interpreting and assessing contracts of adhesion.[27]

<u>The Alleged Franchisor Promises</u>

77. The Franchisees also argue that, if given the opportunity, the Franchisees will present evidence of their reliance on promises allegedly made by Target Corporation to the Franchisees, after the Franchise Agreements were signed, including a promise made in June 2014 to continue to make EBIT Support Program payments for a further period of five years. They say this evidence could be of assistance in interpreting Section 12.1.

78. I recognize that, in some circumstances, the evidence of parties' conduct after the execution of an agreement may assist with the interpretation of contractual provisions.[28] That said, I do not find that further evidence about the EBIT Support Program or its extension could possibly assist me in interpreting the provisions of the Franchise Agreement. The parties' conduct cannot override the clear and unequivocal wording of a contractual provision.[29]

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[26] Aside from the Effective Immediately Issue, which I address below.

[27] *Fontaine v. Canada (Attorney General)*, 2016 ONCA 241 [*Fontaine*] at para 90.

[28] *Fairview Donut, supra.*, 2012 ONSC 1252 at paras. 413-416.

[29] "First, the words of the contract must be analyzed 'in its factual matrix', and a conclusion arrived at that there are two possible interpretations of the contract. Then, and only then, may the trial judge look at other facts, including facts leading up to the making of the agreement, circumstances existing at the time the agreement was made, and evidence of subsequent conduct of the parties to the agreement." *Arthur Andersen Inc. v. Toronto-Dominion Bank*, [1994] O.J. No. 427 (C.A.) at para. 18, leave refused, [1994] SCCA No. 189.

79. When I address Common Issues #2 and #3 below, I will address what occurred with respect to the EBIT Support Programs and what impact that evidence may have on the Franchisor's ability to rely on Section 12.1 in the damage assessment exercise because of a possible breach of the duty of good faith.

The Effective Immediately Issue

80. For the reasons set out above, I am satisfied that the language of Section 12.1 is clear and capable of only one interpretation, with the possible exception of what I refer to as the Effective Immediately Issue.

81. I repeat Section 12.1 for convenience:

> At any time following the third anniversary of the opening date of the Pharmacy, Franchisor may, at its option, terminate this Agreement without cause and all rights granted herein **effective immediately**, upon sixty (60) days prior written notice.
>
> [Emphasis added]

82. The question arises whether Section 12.1 should be interpreted so that notice could only be delivered after the third anniversary of the opening of the franchise, with the sixty day period running from that date (the Franchisees' argument), or whether it could be delivered 60 days before the anniversary, so that the termination would occur on the third anniversary of the pharmacy's opening (the Monitor's and the Applicant's argument).

83. The difference is that on the Franchisees' interpretation, the relevant period for calculating their lost profits would be 60 days longer than that assessed by the Monitor.

84. I have discussed the principles of contractual interpretation above, and decided that with respect to the balance of Section 12.1, the language is so clear that no further evidence of surrounding circumstances is needed or would be of assistance in the interpretation exercise. Importantly, the Franchisees have not put forward an alternative interpretation of Section 12.1 (other than with respect to the Effective Immediately Issue). Instead, they seek to avoid its

effects entirely. There is, therefore, no prospect of evidence of surrounding circumstances assisting me in choosing between competing interpretations.

85. I reach a different conclusion with respect to the Effective Immediately Issue. On this narrow point, the parties have put forward competing interpretations, and I must decide which of them is correct. Therefore, I propose to give the Franchisees an opportunity to call evidence relating to the interpretation of this clause. I reach the conclusion for the following reasons:

(a) First, the language is less clear than the rest of Section 2.1. Either of the two interpretations is possible.

(b) Second, there is some evidence in the record before me that raises a question about this issue. In referring to Section 12.1 in the Disclosure Documents, the Franchisor left out the words, "effective immediately". I recognize that the Disclosure Documents direct the reader to the actual section of the Franchise Agreement and say that the actual section supersedes the language in the Disclosure Document. Nevertheless, the Disclosure Documents form part of the surrounding circumstances and they are relevant to the interpretative exercise. The language used in the Disclosure Documents supports the Franchisee's position on this issue. By the same token, Mr. Mark J. Wong, General Counsel and Secretary for TCC, in an affidavit filed on behalf of the Applicants in the CCAA proceedings observed that the Franchisor would have the right at any time after the third anniversary of the opening date of the pharmacy to terminate the Franchise Agreement on 60 days' notice.[30]

(c) The parties have agreed that the threshold for me to decline to hear evidence is a high one. While cognizant of the "Entire Agreement" and the "No Representations or Warranties" clauses in the Franchise Agreements, I am not prepared at this stage to conclude that evidence of the surrounding circumstances could not assist me in interpreting Section 12.1, insofar as it relates to the Effective Immediately Issue.

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[30] Affidavit of Mark J. Wong, sworn February 10, 2015, and filed in Court File No. CV-15-10832-00CL, in response to a motion by the Pharmacy Franchisee Association of Canada, at paragraph 65: "As I described above, at any time after the third anniversary of the opening date of the pharmacy, TCC would have the right to terminate the franchise agreement for any reason on 60 days' notice."

86. In making this ruling, I am aware of the Ontario Court of Appeal's finding in *Fontaine v. Canada (Attorney General)* that surrounding circumstances have a limited role in interpreting a contract of adhesion.[31] But as the Monitor accepted, the threshold for refusing the Franchisees an opportunity to call evidence is a high one – could evidence of surrounding circumstances make a difference to the interpretive exercise?

87. I do not know what, if any, evidence could be called by the Franchisees on this issue. If there is none, I will proceed to rule on the basis of the record before me.

88. If the Franchisees propose to call evidence, the evidence should be focused on this issue only and it should not include evidence of subjective intentions.

89. I propose that any such evidence be called by way of affidavit and cross-examination outside the hearing room. I also propose that the Monitor and the Applicant shall have the opportunity to introduce responding evidence should they wish to do so. These are simply proposals. The parties may make submissions about the process if they wish. In addition, I may be spoken to about a schedule for such evidence if the parties are unable to agree.

Conclusion

90. In summary, I am satisfied that, with the exception of the Effective Immediately Issue, the language of Section 12.1 is clear and capable of only one interpretation. The Franchisees do not suggest a meaning different than that set out in the clear language. Moreover, the Franchisees do not point to any evidence that could possibly make a difference to the interpretation of the section.

91. Thus, for the above reasons, with the exception of the Effective Immediately Issue, my answer to Question 1 is, Yes. I am satisfied that the legal principles that limit the damages and the recovery of damages to the method of performance least burdensome to the defendant apply

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[31] *Fontaine, supra*, at par. 90.

to the Franchise Agreements. The Franchisees have not pointed to any further evidence that could assist further with the interpretation of the section.

92. With respect to the Effective Immediately Issue only I am prepared to consider evidence, on the basis set out above.

93. My ruling with respect to the use of Section 12.1 of the Franchise Agreements to calculate damages is subject to my findings with respect to the good faith arguments that the Franchisees have made, which I address under Issues 2 and 3, below.

(b) Issue # 2: If the answer to Issue 1 is yes, does the common law duty of good faith and/or the statutory duty of good faith and fair dealing under applicable franchise legislation[32] in the Regulated Provinces[33] impact TCC Pharmacy's ability to rely on such provision to limit the recoverable losses of Franchisees? Can the question be answered 'No' without further evidence?

Issue #3: If the answer to Issue 1 is yes, does the common law duty of honest performance impact TCC Pharmacy's ability to rely on Section 12.1 of the Franchise Agreement to limit the recoverable losses of Franchisees? Can the question be answered 'No' without further evidence?

Introduction

94. I will deal with questions 2 and 3 together. In oral argument, it became clear that the parties considered that the same principles and factors apply to both. As I have decided above, the answer to Question 1 is in the affirmative. Thus, these two questions are engaged.

95. To simplify the discussion, I will refer to the common law duty of good faith as the operative duty throughout. The parties accept, for purposes of these arguments, that the statutory duties of fair dealing in the applicable franchise legislation such as the *Arthur Wishart Act* and the common law duty of honest performance discussed by the Supreme Court of Canada in

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[32] Specifically, *Arthur Wishart Act (Franchise Disclosure), 2000*, SO 2000, c 3; *Franchises Act*, RSA 2000, c F-23, *Franchises Act*, RSPEI 1988, c F-14.1; *Franchises Act*, SNB 2014, c; *The Franchises Act*, CCSM c F156.

[33] Specifically, Ontario, Alberta, New Brunswick, Prince Edward Island and Manitoba (collectively, the "Regulated Provinces").

Bhasin v. Hrynew[34] are, for purposes of this case, the same and indistinguishable. Thus, if I answer questions 2 and 3 with regard to the application of the common law duty of good faith, the same answer would apply to the other duties referred to above.

96. The Franchisees' argument, as I understand it, is that:

(a) The Franchisor owed a duty of good faith that prevented it from relying upon its early termination rights under Section 12.1 of the Franchise Agreements;

(b) Because the Franchisor could not, in good faith, have relied upon its Section 12.1 rights, that section cannot be used as the "most beneficial" means of performing the Franchise Agreements; and

(c) In order to establish that the duty of good faith would have prevented the Franchisor from relying on Section 12.1, the Franchisees should be permitted to lead evidence of the surrounding circumstances.

97. In analysing the good faith argument, I consider it important to distinguish between: (i) the argument that the duty of good faith rendered Section 12.1 void or unenforceable ab initio; and (ii) the argument that reliance on the clause in particular circumstances would have constituted a breach of a duty of good faith.

<u>Good Faith and the Validity of the Early Termination Clause</u>

98. I find that the duty of good faith cannot be used in the first way (*i.e.* to render Section 12.1 void from the outset). The duty of good faith relates to the manner in which a contract is performed. It is not a concept that is used to strike or render unenforceable a provision in a contract. The doctrine cannot be used to change the parties' contractual rights, only to review the manner in which those rights are exercised. As the Ontario Court of Appeal held in *Transamerica Life Canada Inc. v. ING Canada Inc.*:

> The implication of a duty of good faith has not gone so far as to create new,

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[34] *Bhasin v. Hrynew*, 2014 SCC 71 [*Bhasin*].

> unbargained-for rights and obligations. Nor has it been used to alter the express terms of the contract reached by the parties. Rather, courts have implied a duty of good faith with a view to securing the performance and enforcement of the contract made by the parties, or as it is sometimes put, to ensure that parties do not act in a way that eviscerates or defeats the objectives of the agreement that they have entered into.[35]

99. In *Purina*, the defendant breached a dealership agreement. The plaintiff argued that, because the defendant owed an implied duty of good faith, the Court should not assume, for the purposes of determining damages, that the defendant would otherwise have performed the contract by exercising its contractual termination right.[36] This argument was accepted by the trial judge, but overturned by the Ontario Court of Appeal:

> Moreover, by finding an implied duty of good faith on Purina not to act in a way that defeats the very purpose of the contract and then finding that Purina could not rely on Article V(B) because it breached that implied duty, the trial judge erred by using the implied duty of good faith to alter the express terms of the contract, including the right to terminate on notice. In *Transamerica Life Canada Inc. v. ING Canada Inc* … this court made clear that Canadian courts have not accorded this power to an implied duty of good faith.[37]

100. In this case, relying upon the duty of good faith to "read out" Section 12.1(a) of the Franchise Agreement would amount to altering the express terms of a contract. As a result, the duty of good faith does not provide a basis for ignoring the Franchisor's early termination right, when applying the principle in *Open Window*.

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[35] *Transamerica Life Canada Inc. v. ING Canada Inc*., 2003 CanLII 9923 (CA) [*Transamerica*] at para. 53. See also paras. 88 to 89.

[36] It should be noted that, in *Purina*, the defendant was alleged to have actually breached a duty of good faith in the way that it in fact performed the contract. The plaintiffs did not argue that it would have been a breach of a duty of good faith for the defendant to have relied on the early termination clause. In other words, the duty of good faith was raised in respect of the defendant's actual contractual performance not the hypothetical least burdensome performance. In that sense, *Purina* was the opposite of the current case, in which there is no argument that the defendant actually acted in bad faith, but rather the Franchisees argue that the hypothetical least burdensome performance (reliance on the early termination clause) would have entailed a breach of a duty of good faith.

[37] *Purina, supra*, at para. 51.

Good Faith and the Exercise of the Early Termination Clause

101. I turn next to the question of the effect of a duty of good faith on the exercise of an early termination right. The thrust of the Franchisee's position on this issue is that it is necessary for me to hear evidence to determine whether and in what circumstances the Franchisor's decision to terminate could be an acceptable mode of performance. Absent such evidence, it would be an error to interpret Section 12.1 as a limit on the amount of damages recoverable for a breach.

102. In the real world, it is possible that if the Franchisor terminated a Franchise Agreement under Section 12.1(a) the Franchisee could argue that the Franchisor exercised its discretion in bad faith. Whether such an argument would succeed would depend on the circumstances surrounding the termination. If successful, such an argument would not lead to striking Section 12 from the Franchise Agreement, but only to a decision that the particular exercise of the power was done in the circumstances that breached the duty of good faith.

103. That, however, is not this case. This is not a case where I am asked to determine whether the Franchisor has acted in good faith under Section 12.1. I am concerned only with the proper approach to assessing damages under the principles in *Open Window*.

104. As I have said above, I am satisfied that, where there are different ways in which the Franchisor could meet its obligations under the Franchise Agreement, I should assume when determining the damages flowing from the breach that the Franchisor would have performed the Franchise Agreement in the manner least burdensome to the Franchisor. When the duty of good faith is layered onto that analysis, the hypothetical comparator, in my view, becomes: the least burdensome manner in which the Franchisor could have performed the Franchise Agreements, while acting in good faith.

105. As discussed earlier in this ruling, when applying the *Open Window* analysis, my task is not to consider how the defendant would most likely have performed the contract. Instead, I must ask, "What was the least burdensome way in which it could have done so?" When I apply this approach to Section 12.1, I find that, in assessing damages, I must assume that the Franchisor would have exercised the termination right under Section 12.1 at the earliest

opportunity, unless I find that it would have been impossible for the Franchisor to have done so in good faith. Put another way, if it was open to the Franchisor to terminate the Franchise Agreements under Section 12.1, while acting in good faith, then the only damages the Franchisees can claim are those required to place them in the position they would have occupied as a result of such a termination. I consider this approach to be consistent with the principle in *Open Window*, which requires me to assume the least burdensome performance of a contract, and not to perform a factual investigation into the most likely mode of performance.[38]

106. I do not accept that the exercise of the right under Section 12.1 would, in all circumstances, breach a duty of good faith. The parties agreed to the right. Moreover, they specifically agreed that the Franchisor could exercise the right "without cause". In other words, the Franchisees agreed that the Franchisor was not required to have any particular reason to exercise its right of termination. To say that it could never be exercised in good faith would be to read Section 12.1 out of the Franchise Agreement. The cases are clear that the implied duty of good faith cannot be used to amend or rewrite a contract. That is not what the duty is intended to do.[39] The duty is imposed in order to secure the contract that parties have made. It is not intended to replace or rewrite the contract. It is not intended to amend the contract or alter its express terms.[40]

107. The Franchisees argue that there could be situations in which the Franchisor's reliance on Section 12.1 could constitute bad faith. They present as a hypothetical example a case in which the Franchisee was profitable and the Franchisor nonetheless exercised the right under Section 12.1 to expropriate the Franchisee's property with no compensation. There is a good argument that this would not constitute bad faith. First, I note that Section 12.1 requires the Franchisor to make certain payments, such that it is not correct to say that Franchisor could use the clause to expropriate the Franchisee's property "without compensation", although the Franchisees might view the required payment as inadequate. Second, it is important to remember that it is not bad faith for a party to exercise its contractual rights for its own advantage.

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[38] *Open Window, supra*, paras, 19 and 20, *Purina, supra*, at paras. 48 to 49.

[39] *Transamerica, supra*, at para.53. *Purina, supra*, at para. 51.

[40] *Fairview Donut, supra.*

108. Fundamentally, good faith requires parties to perform their contracts honestly. In *Bhasin v. Hrynew*, the Supreme Court of Canada held that a duty of good faith performances applies to all contracts. The Court described the nature of that duty as follows:

> I would hold that there is a general duty of honesty in contractual performance. This means simply that parties must not lie or otherwise knowingly mislead each other about matters directly linked to the performance of the contract. This does not impose a duty of loyalty or of disclosure or require a party to forego advantages flowing from the contract; it is a simple requirement not to lie or mislead the other party about one's contractual performance.[41]

109. Without more, I do not see how it would be in any way dishonest or misleading for the Franchisor to exercise its rights under Section 12.1, even if the Franchisee was profitable, and the Franchisor was motivated by the desire to acquire it. Again, this was explicitly contemplated by the contract the parties made.

110. Even if this example could constitute bad faith, that would not render Section 12.1 unenforceable in <u>all</u> situations. Rather, it could arguably lead to a conclusion that in the particular circumstances, the Franchisor breached a duty of good faith. In entering into a Franchise Agreement including Section 12.1, the parties must be taken to have agreed that in at least some circumstances the Franchisor could exercise the right.

111. I do not accept, therefore, that the exercise of the termination right would always be a breach of the duty of good faith. Importantly, with one possible exception, the Franchisees have not pointed to any proposed evidence that could possibly lead me to determine that Section 12.1 could never be exercised in good faith.[42] The one matter that the Franchisees raise, where a duty of good faith could conceivably arise, concerns the EBIT Support Program, which I discuss below.

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[41] *Bhasin, supra*, at para. 73.

[42] This statement is subject to what I say below about evidence relating to the EBIT Support Program. It is worth noting that the triggering breach of contract in this case was the disclaimer of the Franchise Agreements. Clearly, the issuance of the Notices of Disclaimers did not breach a duty of good faith. The Disclaimers were issued pursuant to Section 32(2) of the CCAA and are part of a Court supervised process pursuant to which the Franchisees claims are being assessed. In any event, whether or not the defendant did, in fact, act in good faith is irrelevant to the application of the *Open Window* principle, which requires the Court to assume that, had the breach not occurred, the defendant would have performed the contract in the manner least burdensome to it. *Purina, supra*, at para 47.

EBIT Support Program

112. The EBIT Support Program, which arose in the course of oral argument, is the one matter on which I would provide the Franchisees with the opportunity to call evidence. In contrast to the circumstances surrounding the negotiation and implementation of the Franchise Agreements, the events relating to the EBIT Support Program occurred after the Franchise Agreements were in place and the Franchisees were operating their businesses.

113. The Franchisor first introduced the EBIT Support Program after the Franchisees had begun operating under the Franchise Agreements. Subsequently, because the Franchises were not as profitable as the parties had hoped, the Franchisor enhanced that program and extended it to cover a five year term. This was a voluntary program, in the sense that the Franchisor was not contractually obligated to deliver it.

114. There is material in the record relating to the introduction of this program and the subsequent enhancement, but it is not clear to me that I have the full record with regard to this matter.

115. The Franchisees provided me with a copy of a letter relating to the enhancement of the EBIT Support Program and sent from the Franchisor to the Franchisees, dated June 13, 2014, which I have marked as Exhibit "2". In that letter, the Franchisor says:

> We feel this extension and enhancement of financial support over the first five year term of your franchise agreement shows our commitment to the sustainability of this franchised pharmacy business. We want you to feel confident to invest in resources and local marketing to continue to focus on growing your business.

116. The Franchisees argue that this letter, and perhaps other potential evidence, could lead to a conclusion that it would have been a breach of the Franchisor's duty of good faith to exercise the early termination provision in Section 12.1. As such, they say I should disregard Section 12.1 in the damage calculation exercise.

117. The Franchisees say that there is at least enough information here that I should provide them with the opportunity to call further evidence that would be relevant to this argument. As I pointed out earlier, the threshold for ruling that I will not provide the Franchisees with an opportunity to call evidence on issues raised as Common Issues is a high one. I must be satisfied that the proposed evidence could not make a difference to the outcome.

118. I am not prepared to make that finding with respect to this issue. I am not confident that I have all of the relevant evidence or documents relating to the EBIT Support Program. There may be more that is relevant and admissible.

119. I conclude that the Franchisees should be given the opportunity to call evidence if they see fit. The evidence should be directed solely at the issue as to whether or not the Franchisor's exercise of its rights under Section 12.1 of the Franchise Agreements was fettered by a duty of good faith**.** To be clear, I would not use this evidence to amend Section 12.1, or to read it out of the Franchise Agreement. This evidence would apply only to events that occurred after the parties entered into the Franchise Agreement.

120. As indicated above, for a Franchisee to succeed in its good faith argument, it will have to prove that, as a result of the interactions between the Franchisor and the Franchisee in respect of the EBIT Support Program introduced after the Franchisees were operating under the Franchise Agreements, the Franchisor could not possibly have relied on Section 12.1 during the initial five year period, while acting in good faith. Under the *Open Window* principle, if there was any way for a Franchisor to exercise its right under Section 12.1 in good faith, I must assume that it would have done so.

121. Because of the prospect that I will decide this issue in the future with additional evidence I will say no more about it at this time. If the parties require clarity about the scope of this direction, they may speak to me. But, to be clear, I intend that any evidence be limited to the EBIT Support Program. The evidence should be focused, relevant and admissible. Again, I suggest the evidence be introduced by way of affidavits and that there be an opportunity for the monitor and the applicants to respond. Cross-examinations, if necessary, could take place outside the hearing room.

(c) Issue #5: Are the Franchisees also entitled to any recovery on account of any of the following:

- **(i) any amounts paid for employees' salaries, fees, expenses, notices of termination, payment to employees in lieu of notice and severance pay?**
- **(ii) any amounts paid to contractors during shut down?**
- **(iii) any costs of complying with regulatory requirements to shut down and/or to continue operation as an independent pharmacy?**
- **(iv) any loss in value of inventory and other assets?**
- **(v) any costs incurred in respect of relocation of its pharmacy?**

Introduction

122. The Franchisees argue that they are entitled to recovery in respect of the types of expenses listed in Issue 5. For purposes of this argument, I assume that one or more of the Franchisees has incurred or will incur such expenses.

123. In general terms, those are expenses that arise from the termination and from the relocation of the franchise businesses after termination. For ease of reference, I refer to all of the types of expenses listed in Issue 5 collectively as, "Termination Expenses". To decide this Issue, it is not necessary for me to hear this type of evidence. I assume it exists.

124. For the reasons set out earlier in these reasons, I have concluded that damages are to be assessed assuming the Franchisor would terminate the Franchise Agreements pursuant to Section 12.1 at the earliest date possible.[43] If the Franchisor had terminated the Franchise Agreements under Section 12.1, the Franchisees would, for the most part, have been faced with the same Termination Expenses.

125. Applying the principles I developed earlier in this Ruling, I find that the proper approach to determining whether any of the Franchisees are entitled to recovery in respect of Termination Expenses is to ask whether they would have incurred such expenses if the Franchisor had terminated the Franchise Agreements after three years, pursuant to Section 12.1.

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[43] My findings with respect to issue 5 are subject to whatever findings I may make with respect to the Effective Immediately Issue, and the question of whether a duty of good faith might have prevented the Franchisor from relying on the early termination clause in any particular case.

126. The starting point in a contractual damages analysis is that the plaintiff is entitled to receive only the benefits arising from the contract. As held by the Supreme Court of Canada in *Open Window*:

> Contractual obligations are voluntarily assumed by parties and given effect to by the courts. The failure to perform certain promised positive contractual obligations in contract law is conceptually distinct from the breach of unpromised negative obligations to not harm another's interests in tort law …[44]

127. In other words, under the *Open Window* principle, it is for the Franchisees to point to positive contractual obligations on the part of the Franchisor that would have required the Franchisor to pay the Termination Expenses, in the event of a Section 12.1 termination. In a contractual damages analysis, the Franchisor is not required to point to clauses that prevent the Franchisees from recovering in respect of harm that they may have sustained. The latter would be the type of tort-like analysis that the Supreme Court of Canada rejected in *Open Window*. For the reasons set out below, I find that the Franchisees have failed, for the most part, to demonstrate a contractual entitlement to Termination Expenses.

<u>Section 12.8 of the Franchise Agreement and the Disclosure Document</u>

128. Section 12.8 of the Franchise Agreement ("Payments upon Termination or Expiration") sets out the parties' contractual entitlements if the Franchise Agreement is terminated, either in accordance with its terms, or upon its expiration. Section 12.8(b) provides the following:

> If the Franchisee does not exercise its first right of renewal and the Agreement expires at the end of the Initial Term, or if this Agreement is terminated without cause by Franchisor prior to the expiration of the Initial Term, in consideration for the termination of this Agreement and Franchisee's right hereunder, Franchisee will be paid two percent (2%) of the previous twelve fiscal month period's Gross Sales provided that Franchisee and Pharmacist have delivered to Franchisor a complete release, in a form provided by Franchisor, of Franchisor and its Affiliates, and their respective shareholders, directors and officers from all obligations of and claims against any such persons under or in connection with the Agreement.

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[44] *Open Window, supra*, at para. 15.

129. The language of the Disclosure Document tracks the language of this provision almost *verbatim*:

> If the Franchisee does not exercise its first right of renewal and the Franchise Agreement expires at the end of the Initial Term, or the Franchise Agreement is terminated without cause by the Franchisor prior to the expiration of the Initial Term, the Franchisee will be paid two percent (2%) of the previous twelve fiscal month period's Gross Sales, provided that the Franchisee and Pharmacist have delivered to the Franchisor a complete release of the Franchisor and its Affiliates, and their respective shareholders, directors and officers from all liability in connection with the Franchise Agreement.

130. Thus, the Franchise Agreements explicitly address the amounts payable on termination by the Franchisor: 2% of the gross sales for the previous twelve fiscal month period. The Franchise Agreements do not provide for payment of any other costs or expenses. In this regard, I find it significant that Section 12.8(b) draws no distinction in the Franchisees' rights as between an early termination of the Franchise Agreement under Section 12.1, and the situation where the Franchise Agreement expires at the end of the Initial Term (and the Franchisee has not exercised its first right of renewal). One would not expect the Franchisees to be entitled to Termination Expenses where the Franchise Agreement has run its course. Section 12.8(b) provides no basis for suggesting that a different result should obtain where the Franchisor has exercised its right of early termination. Presumably, the sixty day notice period required by Section 12.1 was intended to alleviate, at least in part, the impact upon the Franchisee of any Termination Expenses.

131. Far from setting out a right to compensation for Termination Expenses, the Franchise Agreement and Disclosure Document contemplate that the Franchisee will deliver a complete release to the Franchisor in exchange for the Gross Sales Payout payment.[45]

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[45] While not advanced before me, I have considered the argument that the fact that Section 12.8(b) requires the Franchisee to grant a full and final release in return for the 2% Payment suggests that, absent such a release, the Franchisee might be entitled to advance a claim for Termination Expenses. I draw no such inference. It is entirely reasonable to conclude that the contemplated release could have been intended to cover any number of potential claims unrelated to the Termination Expenses that may have arisen over the course of the Franchise Agreement. The purpose of the section appears to be to effect a "clean break" between the parties. From the Franchisor's perspective, the intent is to ensure that the 2% Payment will be the last payment it has to make to the Franchisee, and that it is not exposed to any further claims.

132. The scheme of the Franchise Agreements with respect to termination by the Franchisor is as follows:

(a) The Franchisor may terminate without cause after three years from the date of the opening of the pharmacy upon giving 60 days' notice; (S. 12.1);

(b) The Franchisor shall pay the Franchisee 2% of the gross sales for the previous twelve month fiscal period (the "2% Payment") in exchange for a release; and

(c) There is no provision or obligation to the Franchisor to make any additional payments including for costs, arising from termination and relocation.

133. The Franchise Agreement explicitly addresses the issue of payment for termination without cause. I am satisfied that this scheme sets out the bargain in the contract as to what would occur on termination. It is the least burdensome method of performance for the Franchisor. Thus, the parties have expressly addressed the issue of termination and the financial consequences of a termination.

134. For this reason, applying the least burdensome test in *Open Window* leads me to conclude that for purposes of determining what damages are available to the Franchisees, I should proceed on the basis that the Franchisors would terminate without cause and pay the amounts contemplated by Section 12.8. It is worth noting the Monitor has included Section 12.8 payments in his response to the Files claims.[46]

<u>The Franchise Agreement as a Whole</u>

135. My interpretation of Section 12.8(b) receives further support when the section is read within the context of the Franchise Agreement as a whole.

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[46] In passing, I observe that regardless of what the Franchise Agreements may provide, the applicants have transferred all of the patient lists to the Franchisees. There is no issue remaining with respect to those lists.

136. Throughout the Franchise Agreement, the Franchisees are treated consistently as independent contractors. Thus, Section 13.1 of the Franchise Agreement provides:

> 13.1 Independent Parties
>
> Franchisee and Phramacist are and will at all times remain independent contractors with Franchisor and are not and shall not represent themselves to be the agent, joint venturer, co-employer, fiduciary trustee, partner or employee of Franchisor, or to be related to Franchisor other than as its independent franchisee or the shareholder of Franchisee. Neither Franchisee nor Pharmacist shall make any representations or take any acts which could establish any apparent relationship of agency, joint venture, co-employer, fiduciary, trust, partnership, dependent contractor or employment, and Franchisor shall not be bound in any manner whatsoever by any agreements, warranties or representations made by Franchisee or Pharmacist to any other person nor with respect to any other action of Franchisee or Pharmacist. Neither Franchisee nor Pharmacist shall establish any bank account, make any purchase, apply for any loan or credit, or incur or permit any obligation to be incurred in the name or on the credit of Franchisor. No acts of assistance given by Franchisor to Franchisee or Pharmacist shall be construed so as to alter this relationship.
>
> Franchisee must conspicuously identify itself at the Licensed Space of the Pharmacy and in all dealings with customer, contractors, suppliers, public officials, employees, regulators, and other as the owner of the independent business under a franchise agreement from Franchisor, and must place other notices of independent ownership on signs, forms, stationery, advertising and other materials as Franchisor requires and as required by applicable law.

137. Section 5.9 of the Franchise Agreement specifically addresses the Franchisees' status as independent contractors. It reads, in part:

> Franchisee is, and shall continue to operate, an independent business and have sole authority and control over its employees. All persons employed in and about or in connection with the Pharmacy shall be, and herby are, recognized to be employees of the Franchisee. Franchisee shall deliver to each of its employees a notice stating that Franchisee but not Franchisor is such employee's employer. Franchisee shall be solely responsible for all aspects of the employment relationship with its employees, including without limitation, all decisions relating to the hiring, dismissal, promotion, demotion, transfer and lay-off of such employees. **Franchisee shall be solely responsible for all employment-related obligations to its employees, including without limitation, in respect of wages, salaries, benefits notice of termination, pay in lieu of notice, severance pay, and any other obligation under contract, statute, common law or otherwise.**
>
> …

> **Franchisee shall be solely responsible for all liabilities arising in respect of its agents, employees and independent contractors** and shall take all reasonable steps to ensure that its agents, employees and independent contractors do not make any representations or engage in any acts that could establish an apparent relationship of agency, joint-venture, partnership or employment with Franchisor, which relationships Franchisee and Franchisor agree do not exist. For greater certainty, Franchisor shall not be bound by any agreement, contract, representation or warranty made by any agent, employee or independent contractor retained or hired by Franchisee, except where Franchisee has first obtained the prior written consent of the Franchisor. Franchisee shall indemnify and hold harmless Franchisor in respect of any claims by any of its agents, employees or independent contractors that Franchisor is their employer or otherwise liable for any amounts or benefits owing or potentially owing to them in connection with providing services to Franchisee, whether under contract, statute, common or civil law or otherwise.
>
> [Emphasis added]

138. It is inherent in the Franchisees' status as independent contractors that the Franchisees be responsible for their own costs and expenses. Indeed, the portions of Section 5.9 that I have emphasized above expressly provide that the Franchisees shall be solely responsible for all costs associated with its employees and contractors. Thus, items (i) and (ii) of the Termination Expenses are expressly addressed in the Franchise Agreement. The remaining Termination Expenses, in my view, are addressed implicitly by virtue of the Franchisees' status as independent contractors.

139. In any event, as I noted earlier, the question I must answer is whether there is anything in the Franchise Agreement that would entitle the Franchisees to recover the Termination Expenses, not whether there are sections that expressly preclude such recovery. I find that nothing in the Franchise Agreement would have entitled the Franchisees to recover any portion of the Termination Expenses, in the event that the Franchise Agreements had been terminated pursuant to Section 12.1 of the Franchise Agreements.

Surrounding Circumstances

140. I have considered whether further evidence of surrounding circumstances could assist me in interpreting the Franchise Agreement as it relates to the Franchisees' entitlement to claim Termination Expenses. I have concluded that it could not.

141. While the Franchisees clearly seek the opportunity to lead evidence about the types of Termination Expenses they have incurred, they have not pointed to any potential evidence of surrounding circumstances that could assist me in interpreting the Franchise Agreements. Evidence of what Termination Expenses the Franchisees have incurred would not assist in determining whether such losses would be recoverable under the contracts.

142. I should note as well that I already have before me evidence of the surrounding circumstances, in the form of the Disclosure Documents. As set out above, the Disclosure Documents accurately and thoroughly describe the Franchisees' rights on termination, in complete conformity with Section 12.8 of the Franchise Agreement. There is no suggestion anywhere in the Disclosure Documents that Franchisees would be entitled to receive anything on termination, apart from the 2% Payment. Neither the Franchise Agreements nor the Disclosure Documents suggest that the Franchisees could claim any additional amounts, even if the 2% Payment were not made (for example, if a Franchisee had refused to sign a release).

Section 32(7) of the CCAA

143. I have considered the Franchisees' argument that Section 32(7) of the CCAA supports their claims for the amounts set out in Issue 5. I do not accept this argument.

144. Section 32(7) provides:

> If an agreement is disclaimed or resiliated, a party to the agreement who suffers a loss in relation to the disclaimer or resiliation is considered to have a provable claim.

145. I am satisfied that Section 32(7) is not intended to create new heads of damages or new causes of action that are not otherwise available to the party suffering a loss. It says only that the party suffering a loss has a provable claim, nothing more.

146. A CCAA filing does not entitle creditors to payment of amounts they could not otherwise expect to recover under their agreements with the debtor company. Were it otherwise, the CCAA process itself would become the basis for new claims that did not exist or arise except by virtue of the CCAA itself. The CCAA process is intended to address claims of creditors against the debtor company that existed at law, and to fairly address those claims among the creditors. It is not intended to create a new set of liabilities for the debtor company.

Conclusion

147. Taking in their totality all of the matters discussed above, I conclude that there was no contractual bargain between the parties that the Franchisees would receive upon termination anything other than the 2% Payment. I am satisfied that the overall intent of the Franchise Agreements was that the Franchisees, as independent contractors, should bear their own costs of doing business, including any costs associated with the termination of the Franchise Agreements, whether that be at the end of the five-year term, or after three years, pursuant to Section 12.1.

148. The Monitor's position, as I understand it, is that all of the Termination Expenses constitute costs that that the Franchisees would have incurred had the Franchisor performed the Franchise Agreements in the least burdensome way, meaning that the Franchisor had terminated by giving sixty days' notice, pursuant to Section 12.1 of the Franchise Agreement. If this is factually correct, then I find that none of the Termination Expenses are recoverable, and there is no need for further submissions or evidence on this point.

149. I have considered, however, the possibility that some of the Franchisees, as a result of the disclaimers, may have had to incur expenses falling within the broader category of Termination Expenses that they would not have incurred if the Franchisor had terminated by giving sixty days' notice, pursuant to Section 12.1 of the Franchise Agreement ("Non-Section 12.1 Expenses").

150. I believe I can best illustrate the difference between what I mean by "Non-Section 12.1 Expenses" and other Termination Expenses through the use of two hypothetical examples:

(a) Example 1: Suppose that a Franchisee has incurred costs as a result of having had to notify a regulator of the closing of its pharmacy, as a result of the disclaimer. The Franchisor would still have incurred these costs if the Franchisor had given notice pursuant to Section 12.1 of the Franchise Agreement after three years. If the Franchisee were compensated for these costs, the Franchisee would be better off than the Franchisee would have been, had the Franchisor performed the contract by terminating it under Section 12.1. As a result, these costs would not be recoverable. I expect that the majority of the Termination Expenses fall within this category.

(b) Example 2: Now, suppose that a Franchisee was a party to a three year fixed-term agreement with a sub-contractor, pursuant to which the Franchisee was required to pay a $10,000 penalty to the subcontractor if the Franchisee terminated the agreement prior to the three-year mark. As a result of the disclaimer, the Franchisee has actually had to pay the $10,000 penalty. Had the Franchisor terminated the Franchise Agreement pursuant to Section 12.1 of the Franchise Agreement, the Franchisee would not have been required to pay this penalty (since the Franchisee would not have had to terminate its agreement with the sub-contractor). This would be an example of a Non-Section 12.1 Expense.

151. The question of whether Non-Section 12.1 Expenses should be recoverable was not fully argued before me. I also do not know whether any of the Franchisees have, in fact, incurred any Non-Section 12.1 Expenses. That said, and without deciding this question at the present time, there would seem to be a live issue as to whether or not Non-Section 12.1 Expenses ought to be recoverable.

152. Returning to first principles, I find to be quite helpful Prof. Cassels and Prof. Adjin-Tettey's formulation of the principle on which contractual damages are to be calculated, as set out in their text *Remedies: The Law of Damages*. That formulation is as follows:

> Expectation damages are designed to secure for the plaintiff the benefit of the contract. Most generally, they can be calculated by determining *the difference*

> *between the position that the plaintiff would have occupied, had the contract between performed, and the position that the plaintiff is actually in as a result of breach or non-performance of the contract.*
>
> [Emphasis in original][47]

153. Again, without deciding the question, it appears to me at least arguable that if the Franchisees have, in fact, incurred Non-Section 12.1 Expenses, the Franchisees would need to be compensated for such expenses, in order to be placed in the position they would have occupied if the Franchisor had performed the Franchise Agreement in the least burdensome manner, subject to normal contractual principles of remoteness and mitigation.

154. As a result of the above, if the Franchisees take the position that they have incurred Non-Section 12.1 Expenses, I am prepared to hear oral submissions from the parties as to whether or not such Non-Section 12.1 Expenses should be recoverable. For the purposes of this argument, it is not necessary for the Franchisees to adduce evidence of the Non-Section 12.1 Expenses that they have in fact incurred. Rather, I will consider the arguments as to whether or not such expenses should be recoverable on the assumption that such costs exist, and will provide a direction to the Monitor to deal with such amounts, based upon the determination I ultimately make.

155. This direction is not intended to open the door for the Franchisees to argue whether the Termination Expenses, as a whole, should be recoverable. Instead, the argument is to concern only the relatively narrow category of Non-Section 12.1 Expenses. To be clear, Non-Section 12.1 Expenses are only those expenses that:

(a) The Franchisees have actually incurred as a result of the disclaimers;

(b) The Franchisees would not have incurred if the Franchisor had terminated the Franchise Agreements after three years, in accordance with Section 12.1; and

(c) Are not unrecoverable under remoteness or duty to mitigate principles.

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[47] Jamie Cassels & Elizabeth Adjin-Tettey, *Remedies: The Law of Damages*, 3d ed (Toronto: Irwin Law, 2014) at 18 ["*Cassells*"].

156. Aside from these Non-Section 12.1 Expenses, I conclude that the Franchise Agreements do not provide for payment of Termination Expenses and that there is no other legal obligation arising from the relationship of the parties for payment of these expenses. All other Termination Expenses would have been a consequence of an early termination of the Franchise Agreement under Section 12.1 and are not recoverable.

157. Finally, with respect to Issue 5, I note that the claims of certain Franchisees (pharmacists) for relocating to other communities after the disclaimer will be addressed when I am considering Issue 7 relating to mitigation.

(d) Issue #8(a): Are the Franchisees entitled to any revenues received by the Franchisor or its Affiliates before or after the Initial Order based on the sale of products and services to the Franchisees other than as provided for in the Franchise Agreement? Can this question be answered "No" without further evidence?

Introduction

158. The core of the dispute relating to this Issue is the Franchisees' request for more information about Rebates.

159. Under the Franchise Agreements, Franchisees are required to purchase their products, particularly generic drugs, directly from McKeeson. This constituted the large majority of the Franchisees' drug purchases.

160. The Franchisees argue that without the information about Rebates, they are unable to assess whether the Franchisor acted fairly and in a commercially reasonable way with respect to the sharing of Rebates.

Section 5.3 of the Franchise Agreement

161. Section 5.3 of the Franchise Agreement deals with the issue of Rebates. It provides as follows:

> **5.3 Rebates**
>
> Franchisor and/or its Affiliates may and are entitled to earn revenue from and **Franchisor and/or its Affiliates may and are entitled to receive and retain for its and/or their own credit, without accounting to or sharing with Franchisee**, all payments, profits, rebates, discounts, advantages, goods, commissions, incentives, or other allowances or benefits (collectively "Rebates"), which Franchisor and/or its Affiliates may earn or be granted by suppliers related, directly or indirectly, to the sale of products and services to Franchisee.
>
> Franchisee shall participate, on the same basis as other Target Pharmacy Franchisees, in group purchasing programs for Approved Products, the Computer System, Equipment, inventory signs, furnishings and forms, supplies, services and other items which Franchisor may from time to time require pursuant to Section 5.2 or otherwise. Franchisee acknowledges that Franchisor and/or its Affiliates may and are entitled to earn revenue from purchases made by Franchisee under such programs and that Franchisor and/or its Affiliates may and are entitled to receive Rebates, from sources or suppliers in respect of such programs for its and/or their own credit without accounting to or sharing with Franchisee.
>
> **Notwithstanding the foregoing, and where such payments are not prohibited by law, any Rebates which Franchisor may earn or be granted directly or indirectly from manufacturers of Generic Prescription Drug Products, listed on the Approved Generic Product Formulary List, shall be shared with Franchisee based upon a percentage of Franchisee's purchases of such Generic Prescription Drug Products, subject to applicable laws and as set forth in the Manual.**
>
> Franchisee acknowledges that Franchisor and its Affiliates owe no fiduciary, trust or other duty to Franchisee and are under no such duty to account or disclose to Franchisee for such revenues or Rebates, **and may retain such revenue and Rebates entirely for its and/or their own account.**
>
> [Emphasis added]

162. I am satisfied that the language of Section 5.3 of the Franchise Agreements is clear. The first and fourth paragraphs indicate that the Franchisor is entitled to receive and retain Rebates for its own use without accounting or sharing with the Franchisees. There is no duty to account or to disclose to Franchisees the amount of such Rebates.

163. The third paragraph is an exception to the general approach found in the first and fourth paragraphs. It applies only to GPDPs and contemplates a sharing based on a percentage of the Franchisees purchase of such products. It does not specify the amount of that percentage.

164. Viewed objectively, the language provides for a scheme where there is no contractual obligation on the part of the Franchisor to share or to account Rebates. The third paragraph is simply an exception to the general approach with respect to GPDPs.

165. I am also satisfied that the language of the section is fairly and accurately described in the Disclosure Documents. As indicated previously, the Disclosure Documents constitute surrounding circumstances for purposes of the interpretative exercise. There is nothing in the Disclosure Documents that would lead me to conclude that Section 5.3 should be interpreted in a manner other than that arising from the language used.

166. The Franchisees have not pointed to any further evidence that would assist in the interpretative exercise. The only evidence that they seek is evidence of Rebates, in order to make a determination as to whether or not the approach that was followed was fair and commercially reasonable. Even assuming for the moment that such evidence was to be produced, there is nothing in that evidence which would assist in interpreting the language used in the Franchise Agreements.

167. Thus I am satisfied that, for purposes of interpreting the language in Section 5.3, I do not need further evidence, nor would further evidence that the Franchisees seek assist me in interpreting Section 5.3.

<u>The Disclosure Documents</u>

168. In addressing GPDPs, Section 5.3 imposes an obligation upon the Franchisor to share Rebates with the Franchisees based on a percentage of the Franchisee's purchase of such products subject to applicable laws and as set forth in the Manual.

169. Section 5.3 does not spell out what percentage of the Franchisee's purchase of such products will be shared. However, the Disclosure Documents which were delivered to the Franchisees before they entered into the Franchise Agreements specifically address the arrangement for sharing with respect to GPDPs.

170. The relevant part of the Disclosure Documents reads as follows:

> However, where such payments are not prohibited by law, any Rebates which the Franchisor may earn or be granted directly or indirectly from manufacturers of Generic Prescription Drug Products, as listed on the Approved Generic Product Formulary List, will be shared with the Franchisee based upon a percentage of the Franchisee's Generic Prescription Drug Product purchases, subject to applicable laws and as set forth in the Manual from time to time. **In provinces other than Ontario, the Franchisor, directly or indirectly through its suppliers, currently intends to share with the Franchisee a minimum of twenty-five percent (25%) of the Franchisee's acquisition cost for purchases of primary Generic Prescription Drug Products, and a minimum of fifteen percent (15%) of the Franchisee's acquisition cost for purchases of secondary Generic Prescription Drug Products.** The specific percentage of the Franchisee's acquisition cost that will be used to determine how the Franchisor shares the Rebates it earns from manufacturers of Generic Prescription Drugs, including the minimum percentage, may change from time to time and may vary from province to province at the Franchisor's discretion. **In Ontario, the Franchisor has negotiated terms with its preferred supplier that will allow the Franchisor to, directly or indirectly through its supplier, pass through a four and one quarter percent (4.25%) volume discount to franchisees. The volume discount is comprised of a two percent (2%) prompt pay discount and a two and one quarter percent (2.25%) ordinary commercial terms discount, and is subject to change from time to time at the Franchisor's discretion.**
>
> …
>
> **The Franchisor and its affiliates owe no fiduciary, trust or other duty to the Franchisee and are under no such duty to account or disclose to the Franchisee for such revenues or Rebates, and may retain such revenue and Rebates entirely for their own account.**
>
> [Emphasis added]

171. Thus, the Disclosure Documents indicate that, in provinces other than Ontario, the Franchisor intended to share with the Franchisees a minimum of 25% of the Franchisee's acquisition costs for purchases of primary GPDPs and a minimum of 15% for secondary ones.

172. In Ontario, the Franchisor had negotiated terms which would allow the Franchisor to directly or indirectly pass through a form 4.25% volume discount to Franchisees.

173. As a result, to the extent that the Franchisor had a discretion with respect to sharing Rebates in relation to GPDPs, it had exercised that discretion before each Franchisee entered into a Franchise Agreement and it had fully disclosed the basis on which it proposed to share Rebates.

174. Significantly, the Franchisor did not change the arrangements for Franchisees receiving Rebates with respect to GPDP after the parties had entered into the Franchise Agreements. To the contrary, the arrangement set out in the Disclosure Documents remained the same throughout. In addressing the Claimants' claims in the CCAA proceedings, the Monitor has allowed for Rebates based on the above formulae.

The Franchisees' Request for Further Information

175. The Franchisees argue that the Franchisor may have exercised its discretion with respect to Rebates in a manner that breached a duty of good faith, fair dealing or commercial reasonableness. They say that they can only assess whether this is the case if they are provided with further information about the Rebate programs and, in particular, details about the amounts of Rebates paid directly or indirectly to the Franchisor as a result of sales to the Franchisees.

176. I conclude that the Franchisees are not entitled to production of the information they request. I reach this conclusion for two reasons. First, the terms of section 5.3 are clear. Other than with respect to GPDPs, the Franchisor has no obligation to share Rebates with the Franchisees. Thus, there is no need for production of information with respect to those Rebates.

177. Moreover, with respect to GPDPs, the Franchisor set out explicitly in the Disclosure Documents the basis upon which the sharing would occur. That information was provided to each prospective Franchisee before it entered into the Franchise Agreement. The basis for the sharing was not changed after the Franchise Agreements were executed. It remained the arrangement throughout. I do not accept that, acting in accordance with this arrangement, which

was fully and accurately disclosed in the Disclosure Documents before the parties entered into the Franchise Agreement, could constitute a breach of a duty of good faith.

178. The Franchisees are able to calculate precisely the amount that they are entitled to receive as a result of the sharing exercise, because the percentage is based on the amount of their own purchases. They have the information necessary to determine if they received Rebates in accordance with the formulae set out in the Disclosure Documents. There is no need to have the information relating to the Rebates to make this calculation.

179. Moreover, any argument that the Franchisor breached a duty of good faith or otherwise in exercising its discretion as to how to share Rebates relating to GPDPs is answered by the fact that the discretion, if there was one, was exercised before the Franchisees entered into the Franchise Agreement and was fully disclosed to the Franchisee at that time.

180. As I have indicated above, a duty of good faith relates only to the performance of the contract by the Franchisor. The Franchisor had done everything that it was required to do in connection with the sharing of Rebates prior to the Franchisees entering into the Franchise Agreement and it had fully and fairly disclosed what it intended to do. It did not change that course of action after the Franchise Agreements were executed.

181. In the result, I deny the Franchisees' request for further information with respect to Issue 8(a).

DATED: June 28, 2016

The Honourable Dennis R. O'Connor, Q.C.

Schedule "A"

Court File No. CV-15-10832-00CL

ONTARIO
SUPERIOR COURT OF JUSTICE
COMMERCIAL LIST

THE HONOURABLE DENNIS O'CONNOR,	)	WEDNESDAY, THE 3RD
	)	
CLAIMS OFFICER	)	DAY OF MAY, 2016

IN THE MATTER OF THE *COMPANIES' CREDITORS ARRANGEMENT ACT*, R.S.C. 1985, c. C-36, AS AMENDED

AND IN THE MATTER OF A PLAN OF COMPROMISE OR ARRANGEMENT OF TARGET CANADA CO., TARGET CANADA HEALTH CO., TARGET CANADA MOBILE GP CO., TARGET CANADA PHARMACY (BC) CORP., TARGET CANADA PHARMACY (ONTARIO) CORP., TARGET CANADA PHARMACY CORP., TARGET CANADA PHARMACY (SK) CORP., and TARGET CANADA PROPERTY LLC (the "**Applicants**")

ORDER

(Pharmacist Claims Dispute Common Issues List and Timetable)

THIS HEARING, pursuant to the *Companies' Creditors Arrangement Act*, R.S.C. 1985, c. C-36 and the Order of Regional Senior Justice Morawetz dated February 12, 2016 in the above-referenced proceedings was heard this day at 333 Bay Street, Suite 3400, Toronto, Ontario.

ON READING the materials filed by the Monitor and by Sutts, Strosberg LLP in its capacity as Pharmacist Representative Counsel with respect to the Pharmacy Franchisees' claims and on hearing the submissions of counsel for the Monitor, counsel for the Target Canada Entities, and Pharmacist Representative Counsel:

1. THE CLAIMS OFFICER ORDERS that the Common Issues List applicable to the determination of the Pharmacy Franchisees' claims shall be as set out at Schedule "A" hereto (the "Common Issues List")

2. THE CLAIMS OFFICER ORDERS that Issues 1, 2, 3, 5, and 8(a) on the Common Issues List shall be heard at the hearing scheduled for the week of June 6, 2016.

3. THE CLAIMS OFFICER ORDERS that the parties shall comply with the procedural timetable set out at Schedule "B" hereto in connection with the hearing in June.

Dennis O'Connor
Claims Officer

SCHEDULE "A"

(see next page)

Court File No. CV-15-10832-00CL

ONTARIO
SUPERIOR COURT OF JUSTICE
COMMERCIAL LIST

IN THE MATTER OF THE *COMPANIES' CREDITORS ARRANGEMENT ACT*, R.S.C. 1985, c. C-36, AS AMENDED

AND IN THE MATTER OF A PLAN OF COMPROMISE OR ARRANGEMENT OF TARGET CANADA CO., TARGET CANADA HEALTH CO., TARGET CANADA MOBILE GP CO., TARGET CANADA PHARMACY (BC) CORP., TARGET CANADA PHARMACY (ONTARIO) CORP., TARGET CANADA PHARMACY CORP., TARGET CANADA PHARMACY (SK) CORP., and TARGET CANADA PROPERTY LLC (the "**Applicants**")

FINAL LIST OF COMMON ISSUES

AS DETERMINED MAY 3, 2016

Target Canada Pharmacy Franchising LP ("**TCC Pharmacy**"), was franchisor to 94 separate franchisees (individually a "**Franchisee**", and collectively, the "**Franchisees**") operating in-store Target-branded pharmacies across Canada, outside of Quebec. The in-store pharmacies were operated pursuant to franchise agreements between each Franchisee and TCC Pharmacy, as franchisor, and related documents and agreements. Each Target Canada Pharmacy Franchise Agreement (each, a "**Franchise Agreement**"), each Target Pharmacy Franchise Disclosure Document (including any applicable Statements of Material Change), franchise amending agreements entered into by certain of the Franchisees (for example, conversion bonus agreements), and the Financial Support Package 2014 as amended by the letter from Jeff May dated June 13, 2014 outlining the details of the EBIT Top Up Support Program are collectively, and as applicable to each Franchisee, referred to herein with the Franchise Agreement as the

"Franchise Documents"[1] The Franchise Agreement granted each Franchisee a license to operate the Target-branded pharmacy using certain Target Pharmacy trade-marks. The Franchisees were typically independent corporations which, in the majority of cases, were wholly-owned by a licensed pharmacist (individually, a "**Pharmacist**", and collectively, the "**Pharmacists**"). Both the Franchisee and the Pharmacist is a party to the Franchise Agreement because, among other things, in order to operate a pharmacy franchise, a licensed pharmacist is required under applicable regulations to be present at the premises during operating hours. The Franchisees and Pharmacists are hereinafter collectively referred to as the "**Pharmacist Franchisees**". In addition to the entitlements set out in the express terms of the Franchise Agreement, TCC Pharmacy introduced and implemented the EBIT Top Up Support Program in February 2014 to provide financial support to eligible Franchisees, which support program was modified and enhanced for the benefit of eligible Franchisees in June 2014.

The Monitor and Pharmacist Representative Counsel agree that the appropriate measure of the damages arising from the disclaimer of each Franchise Agreement is that the Franchisee should be put in the same position in which it would have been had the Franchise Agreement been performed by TCC Pharmacy.

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[1] Unless otherwise stated, references to a particular section of the Franchise Agreement herein shall refer to the Target Canada Pharmacy Franchise Agreement among each Pharmacist Franchisee and TCC Pharmacy.

The common issues of the Pharmacist Franchisees are as follows:

DISCLAIMER OF FRANCHISE AGREEMENTS

1. Based on ordinary contractual interpretation and damages assessment principles, does Section 12.1 of the Franchise Agreement operate to limit the Franchisee's recoverable losses under the Franchise Agreement to a period of three years from the opening of such Franchisee's pharmacy? Can the question be answered 'Yes' without further evidence?

2. If the answer to Issue 1 is yes, does the common law duty of good faith and/or the statutory duty of good faith and fair dealing under applicable franchise legislation[2] in the Regulated Provinces[3] impact TCC Pharmacy's ability to rely on such provision to limit the recoverable losses of Franchisees? Can the question be answered 'No' without further evidence?

3. If the answer to Issue 1 is yes, does the common law duty of honest performance impact TCC Pharmacy's ability to rely on Section 12.1 of the Franchise Agreement to limit the recoverable losses of Franchisees? Can the question be answered 'No' without further evidence?

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[2] Specifically, *Arthur Wishart Act (Franchise Disclosure), 2000*, SO 2000, c 3; *Franchises Act*, RSA 2000, c F-23; *Franchises Act*, RSPEI 1988, c F-14.1; *Franchises Act*, SNB 2014, c; *The Franchises Act*, CCSM c F156.

[3] Specifically, Ontario, Alberta, New Brunswick, Prince Edward Island and Manitoba (collectively, the "**Regulated Provinces**").

4. Is the methodology set out in each Notice of Revision or Disallowance issued by the Monitor to each Franchisee a correct approach to measure:

   (i) loss of future profits (including treatment of the OTC Royalty Payment and EBIT Top Up Support Program) in connection with the Franchise Agreement; and

   (ii) Gross Sales Payout, as set out in section 12.8(b) of the Franchise Agreement?

With respect to Common Issue #4, it is agreed that the Monitor will justify its approach to the determination of damages with evidence. The Monitor will not assert its methodology is entitled to deference.

5. Are the Franchisees also entitled to any recovery on account of any of the following:

   (i) Any amounts paid for employees' salaries, fees, expenses, notices of termination, payment to employees in lieu of notice, and severance pay?

   (ii) Any amounts paid to contractors during shut down?

   (iii) Any costs of complying with regulatory requirements to shut down and/or to continue operation as an independent pharmacy?

   (iv) Any loss in value of inventory and other assets?

   (v) Any costs incurred in respect of relocation of its pharmacy?

(vi) Any other obligations upon shut down? **[NTD: To be identified by Pharmacist Representative Counsel by May 24, otherwise to be removed.]**

Can the question be answered 'No' for any of these categories without further evidence?

6. If the answer to any of the items under Issue 5 is yes:

(i) Does the aggregate amount of such entitlements exceed the $25,000 amount allowed by the Monitor "to compensate [each Franchisee] for certain costs incurred and other miscellaneous items"?

(ii) If the answer to Issue 6(i) is yes, what additional amount would be reasonable?

MITIGATION

7. The claimants acknowledge that they had a duty to mitigate in the circumstances of this case. The common issue to be determined, if possible, is whether a uniform approach or approaches to mitigation should be adopted.

OTHER ISSUES

8. a) Are the Franchisees entitled to any revenues received by the Franchisor or its Affiliates before or after the Initial Order based on the sale of products and services to the

Franchisees other than as provided for in the Franchise Agreement? Can this question be answered 'No' without further evidence?

(k) (i) If the answer to 8 is 'Yes', should there be an accounting?

CONFIRMATION OF ISSUES

Pharmacist Representative Counsel hereby confirms that the above list is an exhaustive list of the common issues of the Pharmacist Franchisees.

ALL OF WHICH IS RESPECTFULLY SUBMITTED this 3rd day of May, 2016.

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SCHEDULE "B"

Procedural Schedule re: Threshold Issues Hearing

Item	Date
Joint Brief of Background Documents agreed to	May 11
Filing of Monitor's written submissions on Common Issues 1, 2, 3, 5, 8(a).	May 20
Filing of Pharmacist Representative Counsel written submissions on Common Issues 1, 2, 3, 5, 8(a)	May 27
Filing of Monitor's reply submissions (if necessary)	June 3
Oral argument on Common Issues 1, 2, 3, 5, 8(a)	June 6, 7, 8, 9 and 10

6560424

IN THE MATTER OF THE *COMPANIES' CREDITORS ARRANGEMENT ACT*, R.S.C. 1985, c. C-36, AS AMENDED
AND IN THE MATTER OF A PLAN OF COMPROMISE OR ARRANGEMENT OF TARGET CANADA CO., *et al*

Court File No. CV-15-10832-00CL

ONTARIO
SUPERIOR COURT OF JUSTICE
COMMERCIAL LIST

PROCEEDING COMMENCED AT
TORONTO

ORDER
(Pharmacist Claims Dispute Common Issues List and Timetable)

6540905

Court File No.: CV-15-10832-00CL

ONTARIO
SUPERIOR COURT OF JUSTICE
COMMERCIAL LIST

IN THE MATTER OF THE *COMPANIES' CREDITORS ARRANGEMENT ACT*, R.S.C. 1985, c. C-36, AS AMENDED

AND IN THE MATTER OF A PLAN OF COMPROMISE OR ARRANGEMENT OF TARGET CANADA CO., TARGET CANADA HEALTH CO., TARGET CANADA MOBILE GP CO., TARGET CANADA PHARMACY (BC) CORP., TARGET CANADA PHARMACY (ONTARIO) CORP., TARGET CANADA PHARMACY CORP., TARGET CANADA PHARMACY (SK) CORP., AND TARGET CANADA PROPERTY LLC (THE "APPLICANTS")

RULING

Alan Mark, Francy Kussner, Jesse Mighton – Goodmans LLP (Counsel to the Monitor)

William V. Sasso, Sharon Strosberg – Sutts, Strosberg LLP (Pharmacist Representative Counsel)

Stephen Ferguson – Alvarez & Marsal Canada Inc. (the Monitor)

Christine Jackson, Jeremy Dacks – Osler Hoskin Harcourt LLP (counsel to the Target Canada Entities)

Stavros Gavrilidis – Pharmacist Franchisee Representative

1. This ruling addresses two issues.

   (a) Common Issue No. 7. This issue is as follows:

   7. The claimants acknowledge that they had a duty to mitigate in the circumstances of this case. The common issue to be determined, if possible, is whether a uniform approach or approaches to mitigate should be adopted.

   (b) Non-Section 12.1 Expenses

   Have the Franchisees incurred expenses as a result of the disclaimer that they would not have incurred if the Franchisor had terminated the Franchise Agreements after three years in accordance with Section 12.1. If so, are such expenses recoverable?

Mitigation

2. At the August 3rd hearing the Franchisees made three submissions with respect to Common Issue No. 7.

   (a) The Franchisees do not have a duty to mitigate any part of their claims;

   (b) If the Franchisees do have a duty to mitigate, it is not appropriate to use a uniform approach or approaches to estimate the reduction of their losses by way of mitigation. It is necessary to do an individual assessment of each of the Franchisee's mitigation efforts; and

   (c) If a Franchisee has a duty to mitigate, the wage earnings or estimate of wage earnings of the associated Pharmacist as an employee of a pharmacy other than the Franchisee are not properly included to reduce the losses incurred by the Franchisee.[1]

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[1] Pursuant to the Franchise Agreements, the Franchisees are corporations. The agreement requires each Franchisee be controlled by a Pharmacist and that the Pharmacist work full time for the Franchisee. For clarity, I will refer to the Pharmacist associated with a particular Franchisee as the "associated Pharmacist" although the Franchise Agreement does not use this term.

(a) The Duty to Mitigate

1. The Franchisees argue that they do not have a duty to mitigate their claims. Thus to the extent that their claims are otherwise accepted, I should not consider what steps they or the associated Pharmacists took after the disclaimer to earn other income so as to reduce their losses that formed the subject of their claims.

2. At the conclusion of the hearing on August 3rd, I ruled that the Franchisees did have a duty to mitigate and indicated that I would deliver my reasons later. These are my reasons.

3. It is worth noting that in agreeing to Common Issue No. 7, the Franchisees had acknowledged that they have a duty to mitigate. However they now make two arguments why there is no such duty.

4. First the Franchisees argue that by virtue of my ruling of June 28, 2016, the Franchisor has been deemed to exercise the early termination rights under Section 12.1. That being the case, the Franchisor is obligated to pay the Franchisees the amount set out in Section 12.8(b) of the Franchise Agreement, namely, two percent (2%) of a Franchisee's gross sales over the previous 12 months provided the Franchisee gives the Franchisor a complete release.

5. The Franchisees submit that mitigation is not required or applicable because their losses are limited by Section 12.1 of the Franchise Agreements and that the Franchisor is required by the Franchise Agreements to pay liquidated damages.

6. The Franchisees point out that the Ontario Court of Appeal has held that mitigation does not apply to liquidated damages or amounts owing under a contract. See *Bowes v. Goss Power Products Ltd.*, 2012 ONCA 425 (CanLII).

7. The problem with this argument is that in addressing the Franchisees' claims, the Monitor has not applied mitigation to the payments required under Section 12.8(b) of the Franchise Agreements. Those are liquidated payments and as such not subject to mitigation. The Monitor,

quite properly in my view, has allowed the two percent (2%) payment in full for each of the Franchisees with no reduction for mitigation.

8. In paragraph 17 of his Affidavit sworn July 22, 2016, Mr. Ferguson sets out the categories of claims by the Franchisees together with the Monitor's response to each of the claims. The Monitor proposes to apply the mitigation reduction only to the Franchisees' claims for future losses of profits, not to the payments under Section 12.8(b).

9. The claims for losses of future profits are not claims for liquidated damages nor are they provided for under the Franchise Agreements. Rather, they are based on the common law principles for awarding damages arising from a breach of contract. Clearly these types of damages are not liquidated nor have they been agreed to by contract. As such, they do not come within the principle that there is no duty to mitigate liquidated or contractually provided damages.

10. In oral argument, the Franchisees submitted that because one of their claims is for contractually provided liquidated amounts (the 2%) their loss of future profits claims should be subject to the same principle that mitigation does not apply to liquidated contractually provided for damages.

11. I do not accept this argument. The Franchisees did not provide any authority for this approach. I am not surprised. There does not appear to be any principled reason why because one claim is for a liquidated amount, other claims that are for non-liquidated damages should, for mitigation purposes, be treated as liquidated claims.

12. The Franchisees make a second argument why there is no duty to mitigate. They say that as a result of my ruling of June 28, 2016, the Franchise Agreements should be treated as fixed-term contracts. The fixed terms would be either 3 years or 5 years depending on my conclusion on two issues yet to be decided.

13. The Franchisees submit that two decisions of the Court of Appeal of Ontario support this position. They refer to *Bowes* (supra) and *Howard v. Benson Group Inc., carrying on business as The Benson Group Inc.*, 2016 ONCA 256.

14. I do not accept this submission. In *Bowes* at paragraph 34, the Court said that "... an employment agreement that stipulates a fixed term of notice or payment *in lieu* should be treated as fixing liquated damages or a contractual amount. It follows that, in such cases, there is no obligation on the employee to mitigate his or her damages."

15. In *Howard*, the Court found that an employer who terminates without cause a fixed term employment contract, is liable for wages and benefits for the unexpired term of the contract. The contract did not specify a notice period. The Court decided, relying on *Bowes*, that a contractually fixed term is distinguishable from common law reasonable notice. At paragraph 39 the Court said, "There is no reason to depart from the rule in *Bowes* that there is no duty to mitigate where the contract specifies the penalty for early termination. It does not matter whether the penalty is specified expressly, as in *Bowes*, or is by default the wages and benefits for the unexpired term of the contract, as in the case of fixed term contracts generally."

16. The underlying approach in these two cases, both employment situations, is that because the contracts specified, expressly (*Bowes*), or by way of default (*Howard*), that the payments owing should be treated as contractually required liquidated amounts, they are not subject to mitigation.

17. In both *Bowes* and *Howard*, the contract provided for a fixed and definable stream of payments from the employer to the employee. The Court of Appeal treated these streams of payment as liquidated damages contractually provided by the agreements.

18. The important difference in the present case is that the Franchise Agreements make no provision, either expressly or by way of default, for payment of liquidated amounts during the unexpired portion of the fixed term of the Franchise Agreements after the breach (the disclaimer). Instead, as I said above, the Franchisees' claims for damages during the unexpired period of the Franchise Agreements are claims for loss of future earnings. The damages claimed

are not payments that the Franchisor would have made to the Franchisees had the contracts been performed. Rather, they are amounts the Franchisees would have earned from the opportunity provided in the Franchise Agreements.

19. The amounts of damages for future loss of profits are general damages. They are determined pursuant to common law principles. They are not liquidated amounts agreed to by way of contract in the Franchise Agreements.

20. Thus I conclude the decisions in *Bowes* and *Howard* do not lead to a conclusion that the Franchisees' claims for losses of future profits should not be subject to mitigation.

21. For these reasons I conclude the Franchisees were under a duty to mitigate the damages resulting from their claims for future loss of profits.

(b) Uniform Approach or Individual Assessment

22. I have concluded that the Franchisees had a duty to mitigate their future loss of profits claims. The question arises as to how those mitigation efforts should be determined.

23. When filing their Proofs of Claim, the Franchisees did not include any offset to the amounts claimed to account for mitigation.

24. Faced with a large number of claimants and a lack of information, the Monitor considered three alternatives – individual assessments, a uniform approach or a hybrid approach which would apply different common mitigation factors to the Franchisees whose associated Pharmacists obtained subsequent employment as a pharmacist from those who reopened independent pharmacy operations.

25. The Monitor opted for a uniform approach. This resulted in an aggregate reduction of $5.3 million for future loss profit claims asserted by the 80 Franchisees whose claims are still in dispute.

26. The Monitor's uniform approach assumed a 6 months grace period during which no mitigation was applied. This was intended to represent a reasonable period for the Franchisees or the Pharmacists to make arrangements to generate new income.

27. Following the grace period, the Monitor applied a mitigation factor of $85,000 per annum to the end of the 3 year period referred to in Section 12.1 of the Franchise Agreement.

28. The Monitor's research revealed that the average salary range for a senior pharmacist is between $72,000 and $117,000. The Monitor selected an amount close to the bottom of the range.

29. Throughout, the Monitor has remained willing to consider other proposals for dealing with mitigation. The Monitor is concerned that dealing with mitigation on an individual assessment basis will result in cost and delay to both the Franchisees and to the Estate.

30. Significantly the Monitor is aware that the approach proposed is a type of rough justice. Some Franchisees would be winners because they or the associated Pharmacist earned more than the amount produced by the Monitor's approach. Others would be losers. Those Franchisees would recover less than if the Monitor had done individual assessments. For example, if a Franchisee or the associated Pharmacist did not earn anything despite reasonable efforts, the Monitor's approach would apply the uniform approach and reduce the claim by the same factor as that applied to all Franchisees including associated Pharmacists that obtained subsequent employment.

31. The Monitor argues that the CCAA provides the court and therefore me as a Claims Officer, sufficient latitude to fashion an approach that is appropriate so as to avoid excessive cost and delay.

32. The Franchisees argue that it can never be appropriate, without express instructions from the Court, for a Claims Officer to determine a claim on other than the information required to make an informed decision.

33. The Franchisees also argue that assessments should be based on what each Franchisee or Pharmacist actually did. Each Franchisee and Pharmacist's situation is different and the mitigation efforts should be considered individually. Concerns about delay and expense should not dictate an approach that creates winners and losers within the Franchisee group.

34. At the conclusion of the hearing on August 3rd, I indicated that I would not decide this issue at the present time. I think it would be useful to have more information about the actual mitigation activities of the Franchisees and the Pharmacists before addressing what is an appropriate approach.

35. With this in mind I asked the parties to prepare a questionnaire for the Franchisees and Pharmacists about what they had done insofar as employment, reopening pharmacies or other business activities to reduce their loss claims flowing from the disclaimer. I directed that the parties work out the contents of the questionnaire and a schedule to enable them to assemble the information for an appearance before me on October 6 and 7, 2016. I will be dealing with the other outstanding issues at that time.

(c) Pharmacists Mitigation Activities

36. The Monitor argues that in considering the mitigation efforts of the Franchisees, I should consider the efforts of the associated Pharmacists who control the Franchisee corporations and who, prior to the disclaimers, were fully employed by the Franchisee corporations.

37. The Franchisees respond saying I should not consider the efforts of the Pharmacists. They argue that to do so would constitute an impermissible piercing of the corporate veil. The Franchisees, all corporations, are the claimants in the CCAA proceedings. The loss of future profit claims relate to operations of the Franchisees and to their revenues and expenses. Thus, the Franchisees argue that the mitigation efforts should be only those of the Franchisee corporations not the individual Pharmacists.

38. I conclude that for the purpose of considering mitigation for the Franchisees' loss of profit claims, it is appropriate to consider the efforts of the individual Pharmacists who were associated with the Franchisees.

39. I start with the scheme of the Franchise Agreements. Those agreements require the Franchisee be a single purpose corporation with a purpose of operating the Target Franchise under the Franchise Agreement. The Franchise Agreement also requires that the Pharmacist, who is also a party to the agreement, be a central part of the Franchisee's business, both as the controlling shareholder and as the essential professional employee.

40. Under the agreement the Franchisee must ensure that the Pharmacist owns no less than 51% of the issued and voting shares of the Franchisee. Thus the Pharmacist must control the corporation (Section 3.1).

41. In addition, the Franchisee is required to employ the Pharmacist and to cause the Pharmacist to devote full time and attention to the management and operation of the pharmacy and subject to holidays to be present for a minimum of thirty-five (35) hours per week (Section 5.9).

42. I am told by the Monitor that in dealing with the loss of profits claims, the Monitor normalized earnings by including the amount of the salary paid to the Pharmacist as a return to owner and therefore part of the profit of the Franchisee. If one were to take the position that the salary of the Pharmacist from employment after the disclaimer is not to be considered as part of the mitigation, then it would make sense to remove the normalized calculation whereby payments to the Pharmacist were a return to owner in the loss of profit calculation. Assuming the two were the same, there would be a wash. While the two amounts would not necessarily be the same, the general principle nonetheless makes sense.

43. In addition, it seems to me sensible from a commercial standpoint that for the purposes of mitigation, the two – the Franchisee and the Pharmacist – be viewed in the same light. Indeed, were it otherwise in the scenario where the Pharmacist obtains new employment after the

disclaimer, it is unlikely that the Franchisee would be in a position without the assistance of the Pharmacist to take any steps to mitigate its losses.

44. In the present case, it was incumbent upon each Franchisee to take reasonable steps to mitigate its loss of future income. A central asset of the Franchisee was the employment and professional skill of the associated Pharmacist. In these circumstances it is reasonable to require the Franchisee, controlled by the Pharmacist, to take steps to use its assets and resources to reduce its losses. It is reasonable to conclude that the Franchisee was required to either seek another business opportunity or failing that, to require the Pharmacist to find other employment so as to put his or her professional skills to use. It would not fulfill the duty to mitigate to simply do nothing.

45. The Pharmacists point out that Section 10.2 of the Franchise Agreement distinguishes between the Pharmacists' and the Franchisees' rights and obligations after expiration or termination. Under Section 10.2, the Franchisees and Pharmacists are precluded from establishing or operating a competitive business in the Franchisee's territory for one year. They are also precluded from diverting any business opportunities. The section goes on to provide that notwithstanding those obligations, the Pharmacists shall be entitled to obtain positions as employees in a competitive business.

46. I do not consider that Section 10.2 affects the conclusion I reach above. To start it has no application to the circumstances of this case. After the disclaimer, there was no longer a Target Pharmacy and there was nothing for a competitive business to compete with. In any event, Section 10.2 was not enforceable in the face of the disclaimer.

47. Moreover, the fact that Section 10.2 treats the Pharmacists differently in permitting the Pharmacists to be employed is simply recognition of the fact that the Pharmacists have employable skills. The Franchisees' corporations do not. That fact does not change my conclusion that one way for the Franchisees to mitigate their losses was to permit or require the associated Pharmacists who were the core of the Franchisees' businesses to seek other employment.

Non-Section 12.1 Expenses

48. In my ruling of June 28, 2016 I found that the proper approach to determining whether the Franchisees are entitled to recover "termination expenses" under Common Issue No. 5 is to ask whether a Franchisee "would have incurred such expenses if the Franchisor had terminated the Franchise Agreement after 3 years, pursuant to Section 12.1". If so, the expenses are not recoverable.

49. Accordingly, I ruled against recoverability of the Termination Expenses set out in Common Issue No. 5 on the basis that they would have been incurred in a Section 12.1 Termination.

50. I directed that the parties may make submissions on the recoverability of Non-Section 12.1 Expenses if the Franchisees had in fact incurred such expenses.

51. In response, Mr. Gavrilidis filed an affidavit on behalf of the Franchisees. In that affidavit he takes the position that after the disclaimer, the Franchisees did not wish to relocate their pharmacies and continue in business. He says that had the Franchise Agreements been terminated in accordance with Section 12.1, the Franchisees would have liquidated their assets and collected on their receivables.

52. Mr. Gavrilidis goes on to say that because the Franchisor forced the Franchisees to accept ownership of the patient files (also described as the prescription databases) after the disclaimer, the Franchisees had no choice but to continue on in business to serve their clients. In doing so they incurred the costs of relocation, payments for new licences, expenses related to pharmacy libraries, insurance costs and everything necessary to open a new pharmacy.

53. Mr. Gavrilidis asserts that it was only because the Franchisor breached Section 12.1 and 12.11 of the Franchise Agreement by foisting the patient files on the Franchisees in the aftermath of the disclaimer that the expenses referred to were incurred.

54. I don't accept this submission.

55. The underlying premise of Mr. Gavrilidis' affidavit that the Franchisors forced the Franchisees and the associated Pharmacists to do something that they otherwise would not have done is unsupported by the evidence. There is no evidence that other Franchisees or Pharmacists share Mr. Gavrildis' view that the patient files were foisted on them and resulted in unwelcomed expenses. Mr. Gavrilidis' affidavit which was sworn on July 18, 2016 was the first time that any Pharmacist or Franchisee had taken this position.

56. In previous submissions in the CCAA proceedings, the Pharmacists and Franchisees had taken the position that they owned the patient files and that they should be free to deal with them as they saw fit.

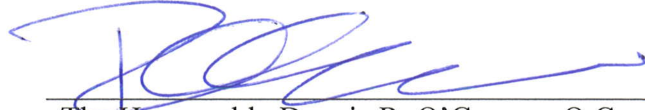
57. On January 21, 2015, the Franchisor wrote the Pharmacists and Franchisees saying that the patient files belonged to the Pharmacist Franchisees. The Franchisor indicated that the Franchisor would not be directing the Pharmacist Franchisees to transfer the files to itself or to a designee pursuant to Section 12.11 of the Franchise Agreement. The Franchisor indicated that the Pharmacist Franchisees had a number of options with regard to the patient files including moving the files to another pharmacy that they operate or selling the files to another pharmacy.

58. It appears in the record that there would have been no difficulty transferring or selling the files to other pharmacies if the Franchisees or Pharmacists had chosen to do so. At no time before Mr. Gavrilidis' affidavit had any Franchisee or Pharmacist indicated to the Monitor that ownership of the patient files was a hardship. In fact several of the Franchisees required confirmation from the Franchisor that patient files would be retained by the Pharmacist Franchisees.

59. In his Second Report, the Monitor indicated that transfers of patients' files had been completed or were underway for 25 of the pharmacies.

60. I do not accept the underlying premise of the Franchisees' arguments that the patient files were foisted on the Franchisees or Pharmacists in breach of the Franchise Agreement resulting in costs that would not have been incurred on a Section 12.1 termination.

61. Thus I conclude that the Franchisees have not established any claim for Non-Section 12.1 Expenses.



DATED: August 19, 2016

The Honourable Dennis R. O'Connor, Q.C.

Court File No.: CV-15-10832-00CL

ONTARIO
SUPERIOR COURT OF JUSTICE
COMMERCIAL LIST

IN THE MATTER OF THE *COMPANIES' CREDITORS ARRANGEMENT ACT*, R.S.C. 1985, c. C-36, AS AMENDED

AND IN THE MATTER OF A PLAN OF COMPROMISE OR ARRANGEMENT OF TARGET CANADA CO., TARGET CANADA HEALTH CO., TARGET CANADA MOBILE GP CO., TARGET CANADA PHARMACY (BC) CORP., TARGET CANADA PHARMACY (ONTARIO) CORP., TARGET CANADA PHARMACY CORP., TARGET CANADA PHARMACY (SK) CORP., AND TARGET CANADA PROPERTY LLC (THE "APPLICANTS")

RULING (EFFECTIVE IMMEDIATELY, GOOD FAITH AND UNIFORM MITIGATION ISSUES)

Alan Mark, Francy Kussner, Jesse Mighton – Goodmans LLP (Counsel to the Monitor)

William V. Sasso, Sharon Strosberg – Sutts, Strosberg LLP (Pharmacist Representative Counsel)

Stephen Ferguson – Alvarez & Marsal Canada Inc. (the Monitor)

Christine Jackson, Jeremy Dacks – Osler Hoskin Harcourt LLP (counsel to the Target Canada Entities)

Stavros Gavrilidis – Pharmacist Franchisee Representative

OVERVIEW

1. On June 28, 2016, I issued a ruling in this case (the "Previous Ruling") with respect to the Pharmacy Franchisee Claims under the Claims Procedure Order that Morawetz J. made in this proceeding.[1] This ruling should be read in conjunction with my Previous Ruling.

2. My Previous Ruling addressed Common Issues 1, 2, 3, 5 and 8(a), as defined in my Order of May 3, 2016 and attached as Schedule A to my Previous Ruling. My Previous Ruling permitted the parties to adduce additional evidence, and make additional submissions, with respect to three points:

(a) The correct interpretation of the words "effective immediately", as used in Section 12.1 of the Franchise Agreements (the "Effective Immediately Issue". This was the one aspect of Common Issue 1 that I did not decide in my Previous Ruling.

(b) Whether or not the Franchisor's exercise of its rights under the early termination clause of the Franchise Agreements was fettered by a duty of good faith, as a result of interactions between the parties in respect of the EBIT Support Program that was introduced after the Franchisees were operating under the Franchise Agreements (the "Good Faith Issue"). This was the one aspect of Common Issues 2 and 3 that I did not decide in my Previous Ruling.

(c) Whether a uniform approach or approaches to mitigation should be adopted (the "Uniform Mitigation Issue"). This is Common Issue 7.

---

[1] Capitalized terms and abbreviations herein have the meaning referred to in the Common Issues List that was attached as Schedule A to my Previous Ruling, or as defined in the body of my Previous Ruling. As in my Previous Ruling, for readability, I will sometimes refer to TCC Pharmacy as the Franchisor and the Pharmacist Franchisees as the Franchisees. Where reference is made to the *Company's Creditor's Arrangement Act*, R.S.C., 1985, c. C-36 ("CCAA") proceedings, capitalized terms shall be the meanings as defined in the Initial Order dated January 15, 2015, the Claims Procedure Order, or other orders or documents referenced in the proceedings unless otherwise defined.

3. This ruling sets out my findings with respect to the Effective Immediately Issue, the Good Faith Issue and the Uniform Mitigation Issue. For the reasons set out below, I have the following determinations:

(a) Effective Immediately Issue: Section 12.1 of the Franchise Agreements permitted the Franchisor to deliver a notice of termination 60 days before the three-year anniversary of the relevant Franchise Agreement, such that the termination would occur on the third anniversary of the pharmacy's opening.

(b) Good Faith Issue: The Franchisor was not limited in the exercise of its rights under Section 12.1 by a duty of good faith as a result of any interactions between the parties in respect of the EBIT Support Program.

(c) Uniform Mitigation Issue: The Supervising Judge in this proceeding is in a better position than I am to decide whether concerns about the costs and delay associated with deciding the mitigation issue on a case-by-case basis warrant an order that the Monitor shall use a uniform approach. Absent such an order from the Supervising Judge, I am not prepared to order a uniform approach and the issue of mitigation will have to be addressed through individual assessments.

4. I address each of these issues separately, below.

The Effective Immediately Issue

(a) Introduction

5. One of the Issues I addressed in my Previous Ruling concerned the interpretation of Section 12.1 of the Franchise Agreements. Issue 1 reads as follows:

> Based on ordinary contractual interpretation and damages assessment principles, does Section 12.1 of the Franchise Agreement operate to limit the Franchisees' recoverable losses under the Franchise Agreement to a period of three years from the opening of such Franchisee's Pharmacy? Can the question be answered, 'Yes' without further evidence?

6. Section 12.1 of the Franchise Agreements provides:

> At any time following the third anniversary of the opening date of the Pharmacy, Franchisor may, at its option, terminate the Agreement without cause and all rights granted herein effective immediately, upon sixty (60) days prior written notice.

7. In my Previous Ruling, I held that the language of Section 12.1 was clear and capable of only one interpretation. Specifically, I found that the effect of this section was to limit each Franchisee's recoverable losses under the Franchise Agreements to a period of three years from the opening of such Franchisee's pharmacy.

8. My finding in this regard was subject to one *caveat*. This related to the interpretation of the words "effective immediately", as used in Section 12.1. The Franchisees argued that these words should be interpreted so that the Franchisor could only deliver notice after the third anniversary of the opening of the franchise, with the sixty day period running from that date. The Monitor and the Applicant argued that the Franchisor could deliver notice 60 days before the anniversary, so that the termination would occur on the third anniversary of the pharmacy's opening. The difference is that on the Franchisees' interpretation, the relevant period for calculating their lost profits would be 60 days longer than that assessed by the Monitor.[2]

9. Significantly, other than with respect to the Effective Immediately Issue, the Franchisees did not put forward a competing interpretation to that found in the clear language of Section 12.1 and applied by the Monitor. Thus, I concluded that evidence of surrounding circumstances was not needed and would not be helpful in interpreting Section 12.1. The only exception was that evidence of the surrounding circumstances might be relevant to the Effective Immediately Issue.

10. In my Previous Ruling,[3] I pointed out that the parties had put forward competing interpretations of the Effective Immediately Issue and that, as a result, I must decide which one is correct. I concluded that the Franchisees should have an opportunity to call evidence of

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[2] See my Previous Ruling, paras. 82 and 83.

[3] *Ibid.*, para. 84.

surrounding circumstances with respect to the interpretation of that issue only.[4] In my Previous Ruling, I gave the following direction concerning the Effective Immediately Issue:

> 85. I reach a different conclusion with respect to the Effective Immediately Issue. On this narrow point, the parties have put forward competing interpretations, and I must decide which of them is correct. Therefore, I propose to give the Franchisees an opportunity to call evidence relating to the interpretation of this clause …
>
> 87. I do not know what, if any, evidence could be called by the Franchisees on this issue. If there is none, I will proceed to rule on the basis of the record before me.
>
> 88. If the Franchisees propose to call evidence, the evidence should be focused on this issue only and it should not include evidence of subjective intentions.
>
> 89. I propose that any such evidence be called by way of affidavit and cross examination outside the hearing room. I also propose that the Monitor and the Applicant shall have the opportunity to introduce responding evidence should they wish to do so. These are simply proposals. The parties may make submissions about the process if they wish. In addition, I may be spoken to about a schedule for such evidence if the parties are unable to agree.

11. Subsequent to my Previous Ruling, the Franchisees filed the affidavit of Stavros Gavrilidis, sworn July 18, 2016 (the "Gavrilidis Affidavit"). They did not produce any documents relevant to the Effective Immediately Issue. The Monitor and the Applicant conducted an extensive search of the documents in the TCC files for evidence relevant to the Effective Immediately Issue. They did not find any. They did not cross-examine Mr. Gavrilidis on his affidavit.

(b) The Evidence

12. At the time of My Previous Ruling, the only extrinsic evidence relating to the Effective Immediately Issue that was before me consisted of the Disclosure Documents provided to

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[4] As set out in greater detail in paragraph 85 of my Previous Ruling, I decided that the Franchisees should have an opportunity to call evidence relating to the Effective Immediately Issue because: (i) The language of Section 12.1 on the Effective Immediately issue was less clear than the rest of Section 12.1, such that either of the two interpretations put forward by the parties was possible; (ii) there was some evidence in the Record that raised a question about the issue; and (iii) the threshold to decline to hear evidence of surrounding circumstances was a high one.

Franchisees, and the affidavit of Mr. Mark J. Wong, General Counsel and Secretary for TCC, sworn February 10, 2015 in the CCAA proceedings (the "Wong Affidavit"). The Wong Affidavit contained the following statement:

> As I described above, at any time after the third anniversary of the opening date of the pharmacy, TCC would have the right to terminate the franchise agreement for any reason on 60 days' notice.[5]

13. In their Submissions dated October 4, 2016, The Pharmacist Representative Counsel relied upon this statement.[6] They then took the position that, "There is no further relevant evidence from any party that informs this contract interpretation issue."[7]

14. I will discuss the content and significance of the Disclosure Documents later in this ruling.

15. The one piece of additional evidence that I have considered is found in the Gavrilidis Affidavit that the Pharmacy Representative Counsel filed after my Previous Ruling. Mr. Gavrilidis states:

> After this e-mail [of September 30, 2012], I spoke by phone with [a TC Pharmacy representative] on the telephone. I asked him why section 12.1 was in the Franchise Agreement and what would happen if it the early termination provision was exercised by the Franchisor. I understood from my conversation with him that, "protecting the brand and the guest experience" meant that if they had franchisees that Target was simply not happy with for whatever reason and even [sic] those did not breach the agreement in any way, they could simply terminate their agreement. Over and above "protecting the brand and the guest experience." I also understood that the Franchisor wanted the early termination option to be able to take over the pharmacy and run it as a corporate pharmacy if it exceeded their expectations; that at any time <u>after</u> the three year mark, they could take over the pharmacy after giving me 60 days' notice.[8]

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[5] Affidavit of Mark J. Wong, sworn February 10, 2015, and filed in Court File No. CV-15-10832-00CL, in response to a motion by the Pharmacy Franchisee Association of Canada, at para. 65.

[6] Submissions and Compendium of Pharmacist Representative Counsel on Effective Immediately and EBIT Support Program Issues, October 4, 2016, para.10 ("Franchisee's Submissions").

[7] *Ibid.*, para. 11.

[8] Gavrilidis Affidavit, para. 6. Underlining in original, entire paragraph *sic.*

(c) Analysis

16. The Franchisees argue that:

(a) In my Previous Ruling, I found that the language concerning the Effective Immediately Issue was less clear than the remainder of Section 12.1 and that both parties' interpretations were possible;[9]

(b) The Franchise Agreements are therefore ambiguous with respect to the Effective Immediately Issue;[10]

(c) The Franchise Agreement are, "at a minimum very similar to contracts of adhesion";[11] and

(d) I should therefore interpret the Franchise Agreement *contra proferentem* in a manner against the party who drafted the Franchise Agreement (the Monitor or the Franchisor) and in a manner favourable to the Franchisees.

17. As set out above, the Pharmacist Representative Counsel's submissions were premised upon the assumption that I had concluded that the contractual language relating to the Effective Immediately Issue was ambiguous. I do not agree that I made any such finding.

18. At issue in my Previous Ruling was whether or not I should allow the Franchisees the opportunity to call evidence of surrounding circumstances to assist me in interpreting Section 12.1. In my Previous Ruling, I drew a distinction between the Effective Immediately Issue and the balance of Section 12.1.

19. Specifically, I found that:

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[9] Franchisee Submissions, para. 9, referring to paragraph 85(a) of my Previous Ruling.

[10] Franchisee Submissions, para. 13.

[11] *Ibid.*

(a) With the exception of the Effective Immediately Issue, the Franchisees had not put forward an alternative interpretation of Section 12.1 and that, accordingly, further evidence of the surrounding circumstances could be of no assistance to the contractual interpretation exercise. The fact that I was presented with only one possible interpretation rendered moot the issue of whether I should hear evidence of surrounding circumstances.[12]

(b) With respect to the Effective Immediately Issue, by contrast, the parties had put forward competing interpretations. In light of the very low threshold for me to hear additional evidence,[13] I was not prepared to conclude that evidence of the surrounding circumstances could not assist me in interpreting Section 12.1, in so far as it related to the Effective Immediately Issue.[14]

20. My previous acknowledgment that the Franchisees had advanced a competing interpretation with respect to the Effective Immediately Issue, and my willingness to hear evidence on this issue, does not equate to a finding of contractual ambiguity. The fact that opposing parties can come up with alternative readings of a contractual clause is not, of itself, sufficient to demonstrate that the clause is ambiguous. Moreover, the law of Ontario is clear that evidence of surrounding circumstances is always admissible to assist in the interpretation of a contract, even in the absence of an ambiguity.[15] In reaching the conclusion that I would hear evidence of surrounding circumstances, I did not conclude that the language standing alone was ambiguous. It remains to be determined, therefore, whether the *contra proferentem* rule is applicable to this case.

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[12] Previous Ruling, para. 84.

[13] Or, to put it another way, the very high burden that the Monitor had to meet in order to obtain an order that the Franchisees not be entitled to call evidence.

[14] Previous Ruling, para. 85.

[15] See, for example, *Hi-Tech Group Inc. v. Sears Canada Inc.*, [2001] OJ No. 33 (CA) at para. 23: "Indeed, because words always take their meaning from their context, evidence of the circumstances surrounding the making of a contract has been regarded as admissible in every case." See, also *Primo Poloniato Grandchildren's Trust (Trustee of) v. Browne*, 2012 ONCA 862, leave denied [2013] SCCA 68, at para. 67: "It is well established that in interpreting a contract, the court may consider the 'factual matrix' surrounding the contract, even where there is no ambiguity."

21. In this regard, it is important to note that resort is to be had to the *contra proferentem* rule "only when all other rules of construction fail to enable the Court of construction to ascertain the meaning of a document".[16] As a result, I must first consider whether I am able to interpret the "effective immediately" portion of Section 12.1 by applying other contractual interpretation principles.

22. I begin with the language of Section 12.1, keeping in mind the admonition that the words themselves are paramount and the role of the factual matrix is to assist in fixing their meaning, not to provide a new meaning inconsistent with the words.[17] Section 12.1 reads:

> At any time following the third anniversary of the opening date of the Pharmacy, Franchisor may, at its option, **terminate the Agreement** without cause and all rights granted herein **effective immediately**, upon sixty (60) days prior written notice.
>
> [Emphasis added]

23. In my view the correct interpretation based on the language is the one urged by the Monitor. I reach this conclusion on the basis of the wording of Section 12.1. In particular, I find that the words "effective immediately" can only have been intended to refer to "any time following the third anniversary of the opening date of the Pharmacy". Termination of the Franchise Agreement could only be "effective immediately" following the three year mark, if written notice were provided in advance of that date.

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[16] *Reliance Petroleum Ltd. v. Stevenson*, [1956] SCR 936 at p. 953. See also, *Consolidated-Bathurst Export Ltd. v. Mutual Boiler & Machinery Insurance Co.*, [1980] 1 SCR 888 at p. 901, Monitor's Brief of Authorities, Tab 7, and *Scanlon v. Castlepoint Development Corp.* [1992] OJ No. 2692 (CA).

[17] Geoff Hall, *Canadian Contractual Interpretation Law*, 2d. ed. (Markham, Ontario: LexisNexis Canada, 2012) at pp. 31-32.

24. It is well established that "a contract, like a statute, ought to be so construed that, if it can be prevented, no clause, sentence or word shall be superfluous, void, or insignificant."[18] As I stated in my Previous Ruling:

> The Supreme Court of Canada has held that courts should reject a contractual interpretation that would render one or more of its terms ineffective. As put more simply by the British Columbia Court of Appeal, "Words in a contract are presumed to have meaning."[19]

25. The interpretation proposed by the Franchisees would render the phrase "effective immediately" in Section 12.1 superfluous and of no effect. Had the intention been to grant the Franchisor the right to give notice after three years and then terminate the agreement sixty days thereafter, the words "effective immediately" would have been unnecessary, and the clause could have read simply:

> At any time following the third anniversary of the opening date of the Pharmacy, Franchisor may, at its option, terminate the Agreement without cause and all rights granted herein, upon sixty (60) days prior written notice.

26. Without the words "effective immediately", Section 12.1 would have had precisely the meaning advanced by the Franchisees. The inclusion in the clause of the words "effective immediately" must be presumed to have been intended to give the clause a meaning different from the meaning it would have had without those words.

27. Moreover, if the words "effective immediately" were intended to refer to the notice being effective immediately upon expiration of the sixty (60) day notice period (as opposed to the termination being effectively immediately), there would not be a comma after the phrase "effective immediately".

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[18] *Elliot v Billings (Township) Board of Education*, [1960] OR 583 at para 7 (CA), Monitor's Brief of Authorities, Tab 6.

[19] Paragraph 65 of my Previous Ruling, citing *National Trust Co. v. Mead*, [1990] 2 SCR 410 at para. 26, and *Pass Creek Enterprises Ltd. v. Kootenay Custom Log Sort Ltd.*, [2003] BCJ No. 2508 at para. 17 (CA).

28. Thus, the plain and ordinary meaning of the words used is that notice of termination can be provided so as to make it "effective immediately" following the third anniversary of the opening date of the Pharmacy.

29. I have considered the evidence of surrounding circumstances, and have concluded that it does not affect my interpretation of Section 12.1. Specifically I find that:

(a) The statement made by Mr. Wong in his affidavit, quoted at paragraph 10, above, was, at best, an ambiguous statement, made after the fact, as to how Mr. Wong understood Section 12.1 to operate. It is not properly part of the surrounding circumstances with respect to the signing of the Franchise Agreements and is of no assistance in interpreting those agreements.

(b) Mr. Gavrilidis' evidence relating to his belief arising from a conversation with a representative of TCC is equally unhelpful. The conversation was not specific as to whether the sixty (60) day notice could be given before or after the three year mark. Moreover, the language referred to in the conversation arises from a conversation with only one Franchisee, which occurred after the Franchise Agreement had been entered into, and relates to the interpretation of what is in fact a contract of adhesion.[20] I do not consider the conversation helpful in determining, from an objective standpoint, the intent of the language used in Section 12.1.

(c) By the same token, the language of the Disclosure Documents cannot override the wording in the Franchise Agreements. At paragraph 85(b) of my Previous Ruling, I pointed out that the description of Section 12.1 in the Franchise Disclosure Documents does not contain the words "effective immediately". Accepting that the Disclosure Documents are part of the surrounding circumstances, I do not consider that they operate to change the plain and ordinary meaning of the language in Section 12.1. The language in the Disclosure

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[20] As I noted in my Previous Ruling at paragraph 86, surrounding circumstances have a limited role in interpreting a contract of adhesion. *Fontaine v. Canada (Attorney General)*, 2016 ONCA 241 at para. 90.

Documents is intended only to be a summary of Section 12.1. By its own terms the Disclosure Documents is not a contract and is subordinate to the Franchise Agreements. Each Disclosure Document includes the following section 24: "This Disclosure Document outlines and summarizes some contractual obligations of both the Franchisor, the Franchisee, and the Pharmacist that are found in the Franchise Agreement and other agreements. For ease of reference and understanding, there obligations may be paraphrased or described in general terms in this document. **Such outlines or summaries do not supersede, replace or modify the actual text of the obligation contained in the relevant agreement.**"[21] As a result of this clause, it cannot be said that there is any inconsistency between the Franchise Agreements and the Disclosure Documents or that the Disclosure Agreements undermine the plain and obvious meaning of Section 12.1 of the Franchise Agreements.

(d) Conclusion

30. In summary, I am satisfied that the plain and ordinary meaning of the language of Section 12.1 must prevail. As I was able to interpret Section 12.1 on the basis of ordinary principles of contractual interpretation, it is neither necessary nor appropriate for me to resort to the *contra proferentem* principle.

31. I conclude that for purposes of assessing damages, the Monitor was correct in using a termination date on the third anniversary of the Franchise Agreements and not sixty (60) days thereafter.

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[21] Emphasis in original. Joint Brief of Documents, Tab 12, page 490.

The Good Faith Issue

(a) Introduction

32. The Good Faith Issue relates to Common Issues 2 and 3, which provide as follows:

> Issue No. 2: If the answer to Issue 1 is yes, does the common law duty of good faith and/or the statutory duty of good faith and fair dealing under applicable franchise legislation in the Regulated Provinces impact TCC Pharmacy's ability to rely on such provision to limit the recoverable losses of Franchisees? Can the question be answered 'No' without further evidence?
>
> Issue No. 3: If the answer to Issue 1 is yes, does the common law duty of honest performance impact TCC Pharmacy's ability to rely on Section 12.1 of the Franchise Agreement to limit the recoverable losses of Franchisees? Can the question be answered 'No' without further evidence?

33. The parties agreed that I could deal with these two issues together.

34. In my Previous Ruling, I concluded that the answer to Common Issues 2 and 3 was "No", with one exception. Specifically, I found that:

(a) For the purposes of calculating damages pursuant to the principles articulated by the Supreme Court of Canada in *Hamilton v. Open Window Bakery Ltd.*,[22] I was required to assume that the Franchisor would have performed the Franchise Agreement in the manner least burdensome to the Franchisor, while acting in good faith.[23]

(b) The exercise of the early termination right under Section 12.1 of the Franchise Agreements would not breach a duty of good faith in all circumstances.[24]

(c) With one exception, the Franchisees had not pointed to any proposed evidence that could possibly lead me to determine that section 12.1 could not be exercised

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[22] *Hamilton v. Open Window Bakery Ltd.*, 2004 SCC 9 [*Open Window*], at paras. 17 and 20.

[23] My Previous Ruling, para. 105.

[24] My Previous Ruling, para. 106.

in good faith. The only matter that the Franchisees had raised, where a duty of good faith could conceivably arise concerned the EBIT Support Program.[25]

(d) I was not prepared to find that further evidence about the EBIT Support Program could not make a difference to the outcome of Issues 2 and 3. Accordingly, I concluded that I should give the Franchisees the opportunity to call evidence directed solely at the issue as to whether or not the Franchisor's exercise of its rights under Section 12.1 of the Franchise Agreements was fettered by a duty of good faith.[26]

(e) For a Franchisee to succeed in its good faith argument, it would have to prove that, as a result of the interactions between the Franchisor and the Franchisee in respect of the EBIT Support Program introduced after the Franchisees were operating under the Franchise Agreements, the Franchisor could not possibly have relied on Section 12.1 during the initial five year period, while acting in good faith. Under the *Open Window* principle, if there was any way for a Franchisor to exercise its right under Section 12.1 in good faith, I must assume that it would have done so.

(b) The Evidence

35. The Franchisees availed themselves of the opportunity to adduce additional evidence about the EBIT Support Program by filing the Gavrilidis Affidavit. The Monitor and the Applicant conducted a thorough and extensive search of the records of TCC and produced any documents which could potentially be relevant to this issue. There were only a few.

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[25] *Ibid.*, para. 111.

[26] I set out the facts relating to the EBIT Support Program and the reasons why I afforded the Franchisees the opportunity to call additional evidence at paragraphs 112 to 199 of my Previous Ruling. By contrast, I held, at paragraphs 175 to 181, that the Franchisees were not entitled to production of further information about the Rebate programs and, in particular details about the amounts of Rebates paid directly or indirectly to the Franchisor as a result of sales to the Franchisees, because the basis on which Rebates would be shared could not constitute a breach of any duty of good faith.

36. Before turning to a consideration of the Gavrilidis Affidavit and the Applicant's documents, I note that the following facts do not appear to be in dispute:

(a) The documents surrounding the EBIT Support Program were referenced in the versions of the Franchise Agreement and Disclosure Documents that were created after the program was put in place.[27]

(b) The EBIT Support Program was introduced in 2014 and enhanced a few months later, in June 2014. At that point, its term was extended to cover the initial term under the Franchise Agreements.[28]

The Gavrilidis Affidavit

37. In his affidavit, Mr. Gavrilidis gives the following evidence:

(a) There was a teleconference of the Franchise Advisory Board On May 23, 2014. During that teleconference, Jeff May, a representative of the Franchisor, made the following statements (as recorded in the minutes of the call):

> - We are currently planning for 2015, 2016, 2017, 2018 expenditures, part of this includes looking at the continuation of the EBIT support program and potential adjustments.
> - One decision that has been made is that the OTC top-up program will now run the full term of your franchise agreement.
> - We would like to receive input that helps us best understand franchise thoughts around EBIT support.
> - We understand the importance of support to some and that franchises need certainty of any future support; because of this we will work towards having this finalized and communicated over the next few months.[29]

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[27] Franchisees' Submissions, at para. 28.

[28] Franchisees' Submissions, at para. 29.

[29] Gavrilidis Affidavit, para. 11 and Exhibit "A".

(b) There was a further conference call involving Mr. May and most of the Franchisees on June 10, 2014. During that call, Mr. May announced that Target's senior leadership had approved an enhanced and extended support program for certain Franchisees who were in dire financial straits.[30]

(c) In a letter dated June 13, 2014, Jeff May wrote on behalf of the Franchisor:

> As announced on the teleconference on June 10, 2014, Target Healthcare has secured approval from Target senior leadership for an enhanced and extended support program for eligible franchisees in the first five year term of their franchise agreement. The details of the program are as follows:
>
> ...
>
> - EBIT Support program is extended to cover the first five year term of the franchise agreement for new franchisees, and the remainder of the first five year term for existing franchisees.
>
> ...
>
> In addition to this financial support program enhancement, the OTC Royalty guarantee has also been extended to cover the remainder of the first five year term of the franchise agreement.
>
> ...
>
> We feel this extension and enhancement of financial support over the first five year term of your franchise agreement shows our commitment to the sustainability of this franchised pharmacy business. We want you to feel confident to invest in resources and local marketing to continue to focus on growing your business.
>
> ...
>
> Our future is full of opportunities, and we have many great things to look forward to in the months and years ahead. Please continue to be passionate about the profession and active in providing outstanding healthcare services to your Target Pharmacy guests.[31]

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[30] *Ibid.*, para. 12.

[31] Gavrilidis Affidavit, para. 12 and Exhibit "B". The June 13, 2014 letter was before me at the time of my Previous Ruling and I quoted from it at para. 115 of that ruling.

(d) Mr. Gavrilidis and "many Pharmacy Franchisees continued to invest heavily into operations including wages, advertising and marketing", "[b]ecause of the statements and guarantees made by Target".[32]

(e) Mr. Gavrilidis expected business to increase in the fall of 2014 and invested in hiring nurses to provide free flu shots and to upgrade his computer systems to improve automation. Despite a "huge financial deficit" at his January 31, 2014 year end, he continued to employ two full time pharmacy technicians to provide superior service to customers and fulfil in-store marketing initiatives that Target had asked the Franchisees to carry out. At the time, he felt that "Target was turning the corner towards success after two years of extreme difficulty." In September 2014, he hired an additional relief pharmacist. In October 2014, he purchased hundreds of calendars to distribute to customers.[33] This evidence does not relate to the EBIT Support Program and, as such, does not fall within the scope of evidence that my Previous Ruling permitted the parties to produce.

(f) Mr. Gavrilidis met with a Target representative in December 2014 to discuss his business plan. The representative encouraged him to pay his insurance invoice for the coming year as soon as possible.[34] As noted in the Monitor's Submissions, this discussion and the subsequent e-mail do not relate to the EBIT Support Program and they do not fall within the scope of my direction as to the additional information that the parties were permitted to adduce.[35]

(g) The Franchisor circulated the Financial Support Package 2014 for the EBIT Support Program to all of the Franchisees and posted it on its online portal. The Package included the following statements:

1. Increase EBIT support to $110,000 effective June 1, 2014.

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[32] Gavrilidis Affidavit, paragraph 13.

[33] *Ibid.*, at paras. 13 to 21.

[34] Gavrilidis Affidavit, para. 21 and Exhibit "C".

[35] Monitor's Submissions, para. 38.

> 2. Extend the EBIT support through to the end of the first 5 year Franchise Agreement term.
>
> ...
>
> In addition, we have also put in place the OTC Royalty Guarantee to the end of the first 5 year Franchise Agreement term.
>
> ...
>
> Program is in place for the *first 5 year term* of your franchise agreement, all other components of the program remain as is including eligibility criteria and expense model (labour allowances, fees and operating expenses).
>
> ...
>
> Franchisees will be eligible for support after 6 fiscal periods of operation, and the support will continue for the *first 5 year term* of your Franchise Agreement.[36]

(h) The Disclosure Documents were amended following the June 23, 2014 letter, to include express references to the enhanced EBIT Support Program. For example, the August 25, 2014 Disclosure Document included the following statements:

> (b) Franchisee Support Package
>
> In February 2014, Franchisor introduced a financial support package for eligible franchisees based on an annualized *earnings before interest and tax* calculation (the "EBIT Top-Up Program"). In June 2014, Franchisor revised the EBIT Top-up Program to, among other things, increase the annual EBIT threshold from $75,000 to $110,000 (the "EBIT Threshold").
>
> ...
>
> If the Franchisee is eligible for the EBIT Top-Up Program, it will receive an EBIT Top-Up of up to the total amount of the annualized EBIT Gap. The Franchisee will receive the EBIT Top-Up for up to the remainder of the Initial Term of their Franchise Agreement and provided the Franchisee continues to have a negative EBIT Gap ...[37]

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[36] Gavrilidis Affidavit, para. 22 and Exhibit "D", pgs. 3 to 5 (emphasis in original).

[37] Gavrilidis Affidavit, para. 23 and Exhibit "E", pgs. 46 to 47 (emphasis in original).

(i) Mr. Gavrilidis had personal interactions with the Target executives between January / February 2013 and July 2014 that led him to believe that Target "would be in business in Canada in the long term" and "was committed to operating [its] stores through the Initial Term of the Franchise Agreement."[38] Again, I agree with the Monitor that these discussions and the subsequent e-mail do not relate to the EBIT Support Program and they do not fall within the scope of my direction as to the additional information that the parties were permitted to adduce.[39]

The Applicant's Documents

38. As described in the Memorandum of Steps Completed to Identify Relevant Documents Arising from Claims Officer's Ruling, dated June 28, 2016, the Monitor and the Applicant conducted an extensive search to locate additional documents relating to the EBIT Support Program.[40] I am satisfied that this process was reasonably designed so as to be likely to uncover any relevant materials.

39. In the end, there were only two relevant documents, beyond those discussed in the Gavrilidis Affidavit:

(a) The Minutes of an April 14, 2014 meeting of the Franchise Advisory Board, which including the following passages:

> ➤ Jeff May... emphasized that much has been accomplished in the short period of time that Target Healthcare has partnered with franchisees through either sub committees and/or the FAB. This successes [sic] need to be shared across the franchisee network; some highlights include:
>
> ➤ The EBIT program and the BDF program were built through partnership with the FAB and sub committees.
>
> ...

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[38] Gavrilidis Affidavit, paras. 24 to 28.

[39] Monitor's Submissions, para. 41.

[40] *Ibid.*, paras. 30 to 32.

> ➤ Discussions are ongoing around additional strategies for locations where growth is lagging and what financial requirements may exist after the current EBIT Support program ends.

...

➤ The FAB noted their previous discussions on the Termination rights issue: these discussions resulted in consensus that the franchise agreement is very clear and that all franchisees were provided the appropriate opportunity to review and seek advice.

...

➤ EBIT Support Program: Clarifying communication required regarding the use of projections in EBIT calculation.

...

TGT Action items(s) [sic]

...

➤ Re-communicate the eligibility criteria for the EBIT Support Program, specifically forecasting and actual results methodology.[41]

(b) Notes from a conference call held on May 23, 2014 about the EBIT program sub-committee of the FAB, and an accompanying e-mail. The covering e-mail repeats the following statement from the notes, which was attributed to Jeff May:

One decision that has been made is that the OTC top-up program will now run the full term of your franchise agreement.[42]

The notes also record the following:

OTC top-up running the full term of franchise agreements needs to be communicated to all franchisees. Jeff May – wanted to share

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[41] Memorandum of Steps Completed to Identify Relevant Documents Arising from Claims Officer's Ruling Dated June 28, 2016, dated August 31, 2016 ("Monitor's Additional Documents"), Tab A1.

[42] *Ibid.*, Tab A2.

with FAB first and will share with FAB first and will share with all shortly.[43]

(c) Analysis

40. The Franchisees argue that "the Franchisor made clear and unequivocal commitments to the Pharmacist Franchisees to provide extended and enhanced benefits for the entire Initial Term of the Franchise Agreement" and that, accordingly, it would have been a breach of the duty of good faith for the Franchisor to exercise its right of early termination under Section 12.1 of the Franchise Agreement.[44]

41. I find, as a matter of fact, that the evidence does not establish the "clear and unequivocal commitments" upon which the Franchisees' argument is premised. There can be no dispute that the Franchisor's representations and the various documents surrounding the EBIT Support Program demonstrated a clear intention, on the part of the Franchisor, to continue EBIT Support payments during the "initial 5 year term" of each Franchise Agreement. The issue, however, is whether those comments could reasonably be read as superseding the Franchisor's right to terminate the Franchise Agreements under Section 12.1. I find that they cannot. In my view, the only reasonable way to interpret the various statements and documents is that the Franchisor undertook to make EBIT Support payments during the initial 5 year term, under those Franchise agreements that remained in effect during that period. As explained in My Previous Ruling, under the *Open Window* principle, I am required to assume that none of the Franchise Agreements would have remained in effect past the earliest date on which the Franchisor could have terminated them pursuant to Section 12.1.

42. My conclusion is based upon the following specific findings:

(a) There can be no dispute that, prior to the implementation of the EBIT Support Program, the Franchisor had an unfettered right to terminate the Franchise Agreements on their three-year anniversary. Mr. Gavrilidis himself admits that he

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[43] *Ibid.*

[44] Franchisees' Submissions, at para. 3(b).

understood "that if they had franchisees that Target was simply not happy with for whatever reason and even [sic] those did not breach the agreement in any way, [the Franchisor] could simply terminate their agreement."[45]

(b) The EBIT Support Program was a gratuitous program, as was its extension. There is nothing in the evidence to indicate that by implementing the program or the extension, the Franchisor intended to forego its right to terminate any franchise under Section 12.1 of the Franchise Agreement.

(c) The evidence introduced fails to establish that TCC Pharmacy could not have relied on Section 12.1 during the initial term while acting in good faith. Nowhere in the evidence is there any statement, on the part of the Franchisor, that it would not invoke its right of early termination under Section 12.1, nor is there any evidence that any Franchisee took any action in reliance upon such a representation (had it been made).

(d) There is no evidence that could possibly be characterized as dishonest conduct on the part of the Franchisor; there is no evidence of lying or misleading the Franchisees into believing that the EBIT Support Program amended the terms of the Franchise Agreement. None of the evidence relating to the EBIT Support Program indicates there was an intention or expectation that the Franchise Agreements would be amended so as to preclude TCC from exercising the 12.1 right.

(e) The Franchise Disclosure Documents referred to in the Gavrilidis Affidavit contain a clear and concise summary of the termination provision including, specifically, that the Franchisor had the right to terminate after three years. I recognize that the Disclosure Documents that were issued after the June 13, 2014 Letter, in the normal course, would not have been provided to existing Franchisees. However, continuing to issue Disclosure Documents making it clear that the termination right had not been foregone undermines an argument that the

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[45] Gavrilidis Affidavit, para. 6.

Franchisor, necessarily would have been acting in bad faith in relying upon that right.[46]

(f) None of the evidence filed indicates that if TCC Pharmacy were to have exercised the Section 12.1 right, such exercise would have been arbitrary or capricious or contrary to the parties' expectations.

(g) Mr. Gavrilidis is the only Franchisee to have given evidence about reliance on the EBIT Support Program. While he claims to have relied upon certain statements and documents, this claim is undermined by his admission that he: "understood that the Franchisor wanted the early termination option to be able to take over the pharmacy and run it as a corporate pharmacy if it exceeded their expectations; that in any time after the three year mark, they could take over the pharmacy after giving me sixty days' notice".[47] In light of this understanding, it would not have been reasonable for Mr. Gavrilidis to assume that the Franchisor had waived the right to terminate the Franchise Agreements under Section 12.1 by implementing the EBIT Support Program.

(h) Mr. Gavrilidis' evidence that he relied on the June 13, 2014 letter by incurring additional expenses is undermined by the fact that such expenses were largely incurred before the letter was sent.[48]

43. In summary, I conclude that the Franchisees have failed to establish that there were no circumstances under which the Franchisor could have exercised its right of early termination under Section 12.1 of the Franchise Agreements while acting in good faith. As a result, I am required by the principle in *Open Window* to assume when calculating damages that the

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[46] As I noted above, the Disclosure Documents also include, in Section 24, an express statement the contents of the Disclosure Documents do not supersede, replace or modify the actual text in the Franchise Agreements.

[47] Gavrilidis Affidavit, para. 6.

[48] For example, he describes the purchase of a delivery vehicle and affixing logos to it. The vehicle, however, was purchased in July 2013 and the logos affixed in April 2014. *cf.* Gavrilidis Affidavit, para. 17. .

Franchisor was entitled to exercise the right of early termination on the earliest possible date. The answer to Common Issues 2 and 3 therefore remains, "no".[49]

The Uniform Mitigation Issue

(a) Introduction

44. The Uniform Mitigation Issue arises out of Common Issue 7, which reads:

> 7. The Claimants acknowledge that they had a duty to mitigate in the circumstances of this case. The common issue to be determined, if possible, is whether a uniform approach or approaches to mitigation should be adopted.

45. In my ruling of August 19, 2016, I found that the Franchisees had a duty to mitigate their losses. I also concluded that, for the purposes of considering the reasonableness of mitigation, it would be appropriate to consider the efforts of the individual pharmacists who were associated with the Franchisees (the "Pharmacist Franchisees").

46. At the time of my ruling, there were eighty (80) Franchisee claimants whose claims were in dispute. The Monitor considered several options for addressing the issue of mitigation. The Monitor concluded that a uniform approach (the "Proposed Uniform Method") should be adopted. Under that approach, a mitigation factor of $85,000 per annum would be applied to each claimant's recovery. In addition, there would be a six month grace period before the mitigation factor began. In other words, the Monitor argued that, for mitigation purposes, the Monitor should assume that each Pharmacist Franchisee would have earned $85,000 per annum (after the initial six month grace period) for the time period between when their franchise operations ceased and the earliest date upon which the Franchisor could have effected the termination of their franchises, pursuant to Section 12.1 of the Franchise Agreements. That amount would then be deducted from the Franchisee's claim for lost earnings. Under this approach, individual assessments would not be necessary.

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[49] I should add that even if I were to consider the evidence in Mr. Gavrilidis' affidavit referred to in paragraphs 37 (e), (f) and (i), that evidence is not sufficient to support a conclusion that TCC Pharmacy would breach a duty of good faith if it terminated the Franchise Agreement under S. 12.1. My reasons for this conclusion are essentially the same as those set out in paragraph 42 hereof.

47. The Proposed Uniform Method has several advantages. It is straightforward and easy to apply. It would avoid both the costs to the claimants and the estate, and the delays, involved in individual assessments.

48. The difficulty with the Proposed Uniform Method is that it is a type of rough justice. Inevitably, some Franchisees would benefit from such an approach, because their Pharmacist Franchises earned more than the amount produced by the uniform approach. Others would be losers because they earned less than the mitigation factor under the Proposed Uniform Method.

49. The Monitor has been prepared throughout to consider proposals for another approach. However, the Franchisees have been consistent that individual assessments are required. Counsel for the Franchisees argued that each claimant's case should be assessed on its own facts and according to law. Further, he submitted that a Claims Officer does not have the authority, without direction from the Court, to decide individual claims on any other basis than that of individual assessments.

50. At the end of the hearing on August 3, 2016, I indicated that I would not decide whether to adopt the Proposed Uniform Method at that time. I wanted more information about what had occurred with the Franchisees after the disclaimers. Accordingly, I asked the parties to prepare a questionnaire to be forwarded to all eighty (80) Franchisees.

51. The Monitor has filed evidence as to the responses to the questionnaire and subsequent settlements entered into between the Monitor and certain claimants. Both parties filed written submissions, and presented oral arguments as to how I should resolve the Uniform Mitigation Issue in light of this additional information. At the October 6, 2016 hearing, the Monitor continued to advocate for a uniform mitigation method. The twenty-seven Franchisees who had not settled argued for individual assessments. For the reasons set out below, I have concluded that, absent an order from the Supervising Judge, individual assessments will be required in order to decide the mitigation issue, and no uniform approach should be applied.

(b) The Evidence

The Questionnaire

52. The parties agreed upon a questionnaire and the Monitor reported a summary of the results for the hearing on October 6, 2016.[50]

53. Seventy nine (79) of the eight (80) claimants responded. The Monitor divided them into four (4) categories:

(a) Those who found subsequent employment as a pharmacist in a pharmacy not owned by that Pharmacist Franchisee (thirty three (33) claimants);

(b) Those who found employment as a pharmacist but later opened a new independent pharmacy (six (6) claimants);

(c) Those who established a new independently owned or franchised pharmacy (thirty six (36) claimants); or

(d) Those who are working in a non-pharmacist capacity or are not employed (four (4) claimants).[51]

54. A review of the information provided in the completed mitigation questionnaires discloses a wide range of outcomes. A number of Pharmacist Franchisees have gone on to new enterprises more successful than their former Target Canada pharmacy operations, in some cases achieving income of such a magnitude as would mitigate altogether any claim against the estate for lost profits. However, another group of Pharmacist Franchisees have fared more poorly relative to the common mitigation factor applied by the Monitor. Under the Proposed Uniform Method, those who have not done as well will have their recovery from the estate reduced by a mitigation factor that exceeds, in some cases by a large amount, the income they actually earned during the relevant time period.

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[50] Target Canada Co. claims Process-Pharmacist Franchisees; Report on Information Contained in the Mitigation Questionnaires, prepared by Alvarez & Marsal, September 20, 2016 (the "Questionnaire Report").

[51] Questionnaire Report, p. 2.

55. For each of the four (4) groups, the Questionnaire Report indicates the following ranges:

GROUP 1[52]		
HIGH, AVERAGE AND LOW	**YEAR 2015**	**YEAR 2016**
High	$140,002	$138,745
Average	$80,008	$92,749
Low	$18,415	$35,000
GROUP 2[53]		
HIGH, AVERAGE AND LOW	**YEAR 2015**	**YEAR 2016**
High	$122,179	$124,499
Average	$72,852	($124,427)
Low	$22,893	$28,586
GROUP 3[54]		
HIGH, AVERAGE AND LOW	**YEAR 2015**	**YEAR 2016**
High	$636,348	$953,393
Average	$110,228	$147,048
Low	($73,952)	($267,262)
GROUP 4[55]		
HIGH, AVERAGE AND LOW	**YEAR 2015**	**YEAR 2016**
There was no useful information supplied.		

[52] Questionnaire Report, p. 3.

[53] *Ibid.*, p. 4.

[54] *Ibid.*, p. 5.

[55] *Ibid.*, p. 6.

56. The Questionnaire Report indicates that fifty three (53) of the seventy nine (79) questionnaires received are missing certain required information that would be necessary to complete a more thorough analysis.[56] I note that the numbers for 2016 involve an element of projection as the questionnaires were completed before the end of the year.

The Settlements

57. At the hearing on October 6, 2016, counsel for the Monitor advised that the Monitor had settled with fifty three (53) of the eighty (80) claimants whose claims had been in dispute. Thus there are twenty seven (27) remaining.

58. Counsel indicated that, in arriving at the settlement amounts, the Monitor's general approach involved the Proposed Uniform Method. At the point when the Monitor settled with the fifty three (53) Franchisees, I had not ruled on whether I would accept the Monitor's proposal for a uniform approach.

59. At the time of the settlements, the Franchisees and the Monitor did not have the benefit of this ruling on the Effective Immediately Issue, the Good Faith Issue and the Uniform Mitigation Issue. The uncertainty created by any of those issues could have affected their decisions to settle. I do not know on what basis the settlement amounts were calculated. In particular, I do not know what assumptions were made as to the outcome of the Effective Immediately Issue and the Good Faith Issue in calculating the settlement amounts.

60. Were it not for the Effective Immediately Issue and the Good Faith Issue, I would have been inclined to assume that any Franchisee who settled had a smaller (or at most, equal) mitigation amount deducted from their claim under the Proposed Uniform Method than would have been deducted if the extent of their mitigation had been calculated on an individual basis. Absent those other issues, there would have been no reason (aside from any issues as to what they could prove) for a Franchise to reduce its claim by an amount greater than the actual income they earned through their mitigation efforts.

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[56] *Ibid.*, Appendices.

61. I recognize that the Effective Immediately Issue and the Good Faith Issue cast some doubt on the basis for the settlements. Thus, for example, it is possible that the settlements were calculated on the assumption that I would accept the Monitor's arguments and would assume under the *Open Window* principle that the Franchise Agreements would have been in place for more than three years, but for Target's insolvency. While this is possible, I nonetheless consider it very likely that the reductions for mitigation that were applied when determining the settlement amounts were, at least on average (if not in all cases) lower than they would have been, had individual assessments been performed.

62. It is likely that this approach has resulted in the Monitor paying some claims, perhaps many, in excess of what would have been paid if there had been individual assessments. If I adopt the Monitor's proposal to apply the Proposed Uniform Method to the outstanding claims, the overpayments to the Franchisees who have settled would be offset, partially at least, by underpayments to those who have not settled.

(c) Analysis

63. The Monitor continues to propose that I should adopt the Proposed Uniform Method because of the following:

(a) Individual assessments will be lengthy and expensive;

(b) The costs of assessments to both the claimants and the estate will be very large in relation to any benefit to the claimants as a group and to some individually;

(c) The delay will be excessive and will prejudice both other creditors in these proceedings and some of the claimants;

(d) The Franchisees did not initially submit information regarding mitigation;[57] and

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[57] I note that, in my view, the Franchisees cannot be faulted for not addressing the issue of mitigation at an earlier stage. It was the role of the Monitor to propose a methodology. In response, the Franchisees were within their rights to maintain their position that individual assessments are required.

(e) The Franchisees have submitted no evidence that the results of applying a uniform mitigation factor would yield unacceptable results.

64. The Monitor argues that when considering whether to order the uniform approach for the remaining twenty seven (27) claimants I should disregard the settlements. I should, in effect, step back in time and consider the issue as it was initially proposed when there were eighty (80) Franchisees whose claims were in dispute. The Proposed Uniform Method recognized that there would be winners and losers. If, viewed at that point, I would have ordered the Proposed Uniform Method, then I should not order otherwise now because of the settlements. The integrity of the approach requires that it be applied to all eighty (80) claimants, not just to those who are likely to benefit from it.

65. I accept that if one is to apply a uniform approach, the terms of the Proposed Uniform Method are reasonable. The six (6) month grace period is ample and perhaps generous for many Pharmacists. $85,000 a year is lower than the average income that a senior Pharmacist might expect to earn from employment or from operating an independent business. If I were to adopt a uniform approach, I would be inclined to use the mitigation factor proposed by the Monitor and apply the Proposed Uniform Method.

66. However, I am not prepared to order a uniform approach for the reasons set out below.

67. In the normal course, claimants in a CCAA process are entitled to a distribution in proportion to the full amount of their legal enforceable claims. If some creditors are permitted to receive a recovery in excess of their legal entitlements, then other creditors will receive a reduced prorated distribution.

68. The Monitor's proposal departs from the normal approach in that some creditors would receive more and others less than a distribution based on their legal entitlements. The justification for this approach is primarily one of expediency. The Proposed Uniform Method would avoid excessive costs and delay and thereby avoid prejudice to both the claimants and to the other creditors of the estate.

69. At the October 6, 2016 hearing, I asked counsel whether there were any precedents for making this type of order in CCAA proceedings. With the exception of one case, which I will mention below, they indicated that they were not aware of any such authority. In addition, I asked counsel about the normal practice on the Commercial List of the Ontario Superior Court of Justice in addressing issues of this nature in CCAA proceedings. Again, they were not able to indicate any cases in which this type of approach had been adopted.

70. There is no explicit authority under the CCAA to make an order of the nature proposed. That said, I recognize that CCAA courts have a broad jurisdiction to make innovative orders for which there is no explicit authority.

71. The one case counsel referred me to is the 1997 case in *Re: T. Eaton Company Limited*[58], in which Justice Houlden said:

> 2. Mr. Sternberg contended that the adoption of a formula for ranking the claims of creditors was in error and that the claims of the landlords should be based on the damages actually suffered by them. With respect, I do not agree. If this procedure was followed, I do not believe that Eatons could make a successful plan of restructuring. It would take years to determine the value of claims and the uncertainty would make the plan unworkable.
>
> 3. The formula, as amended, is a fair one and permits landlords to be dealt with in a consistent and orderly manner. Accordingly, Mr. Sternberg's motion is dismissed.

72. The formula to which Justice Houlden was referring is that found in Section 65.2(4)(b)(i)(2) of the *Bankruptcy and Insolvency Act*.[59] At the time of the *Eaton* decision, this provision had been enacted by Parliament, though not yet proclaimed.

73. In my view, this case is not particularly helpful. To start with, in *Eaton* there was a statutory formula for addressing the landlord's claim. There is no similar provision in the case. Moreover, what seemed to underlie Justice Houlden's view was the need to proceed with the restructuring of Eaton's as quickly as possible. It is not clear to me that the circumstances are the

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[58] 1997 CarswellOnt 5959 (Gen. Div.) (*Eaton*).

[59] RSC 1985, c.B-3 (*BIA*).

same in this case. Here, the Franchisor filed for protection under the CCAA with the intent of affecting an orderly wind-down of the business affairs of TCC. As I point out below, I am not in the best position to decide whether, in the circumstances of this CCAA process, an order adopting a uniform approach is warranted in order to avoid expense and delay, when such an approach will result in some creditors receiving more than their legal entitlements and others less than theirs.

74. I am concerned about the unfairness that would be visited upon some or all of the remaining twenty seven (27) claimants who are requesting an individual assessment. This would be particularly unfortunate, given that this group is likely composed of those individuals who have fared most poorly in the aftermath of the disclaimers. To now have the claims they are legally entitled to make reduced because of a uniform approach that benefits those who, relatively speaking, have done better seems harsh. In effect, the losers would be subsidizing the winners.

75. I recognize that the information in the Questionnaire Report has not been verified. Thus, it would be unwise to attach too much importance to that information. However, one would expect that the information about Group 1 (the Pharmacists who obtained employment after the disclaimer) would be relatively accurate.

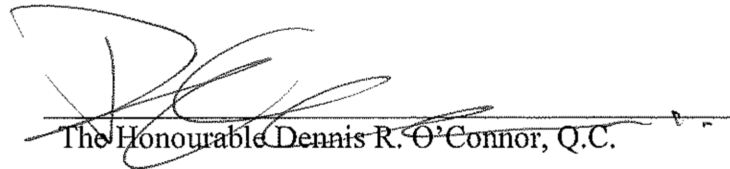
76. The range of reported incomes for Group 1 is very wide. The highest income reported for 2015 was at $140,000 per year, the lowest was $18,415. Assuming the highest earner settled with the uniform mitigation factor of $85,000, he or she has benefited to the extent of $55,000. If the lowest income earner is required to accept a mitigation factor of $85,000, he or she will suffer a shortfall of about $66,000.

77. As the Monitor fairly recognized, there will be winners and losers if the uniform approach is adopted.

78. In the result, I am not prepared to order a uniform approach. That said, I recognize that there could be circumstances in which a Court might decide to do so. In my view, the Supervising Judge in this CCAA proceeding is in a much better position than I am to decide

whether the concerns about costs and delay are sufficiently significant to warrant making an order of this nature. Absent such an order from the Supervising Judge, it will be necessary to proceed with the remaining twenty seven (27) claims on the basis of individual assessments.

79. I am optimistic, perhaps unduly, that some of those claims, particularly where the Pharmacist has obtained subsequent employment, could be dealt with expeditiously.



DATED: October 25, 2016

The Honourable Dennis R. O'Connor, Q.C.

IN THE MATTER OF THE *COMPANIES' CREDITORS ARRANGEMENT ACT*, R.S.C. 1985, c. C-36, AS AMENDED
AND IN THE MATTER OF A PLAN OF COMPROMISE OR ARRANGEMENT OF TARGET CANADA CO., *et al*

Court File No. CV-15-10832-00CL

ONTARIO
SUPERIOR COURT OF JUSTICE
COMMERCIAL LIST

PROCEEDING COMMENCED AT
TORONTO

PART II OF II
MOTION RECORD OF
PHARMACIST REPRESENTATIVE COUNSEL
(motion returnable Wednesday, September 13, 2017 at 11:15 a.m.)

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