

CANADA / JUDGMENT

Automaster Automotive Services Ltd. v. Kenco Enterprises Ltd.

2009 BCSC 1594

COURT

Supreme Court of British Columbia

DECIDED

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2009 BCSC 1594 Automaster Automotive Services Ltd. v. Kenco Enterprises Ltd.

IN THE SUPREME COURT OF BRITISH COLUMBIA

Citation:

Automaster Automotive Services Ltd. v. Kenco Enterprises Ltd.,

2009 BCSC 1594

Date: 20091120

Docket: S084963

Registry: Vancouver

Between:

Automaster Automotive Services Ltd. and

Litke Development Corporation

Plaintiffs

And

Kenco Enterprises Ltd.

Defendant

And

Automaster Automotive Services Ltd.

Defendant by Counterclaim

Before: The Honourable Mr. Justice Nathan Smith

Reasons for Judgment

Counsel for Plaintiff:

C. J. Watson

Counsel for Defendant:

H. MacDonald

Place and Date of Trial:

Vancouver, B.C.

June 18, October 14 and 15, 2009

Place and Date of Judgment:

Vancouver, B.C.

November 20, 2009

- [1] The plaintiff, Automaster Automotive Services Ltd. ("Automaster"), operates a transmission repair shop in leased premises in Nanaimo. A related company, the plaintiff, Litke Development Corporation ("Litke Development"), tried to exercise an option to buy the property, but the owner refused to sell. The plaintiffs now seek an order for specific performance of the option agreement.
- [2] The defendant, Kenco Enterprises Ltd. ("Kenco"), owns the property and says the lease gave only Automaster, not Litke Development, the option to purchase. Litke Development relies primarily on a separate agreement that predated the lease to support its position. Kenco also says that even if Litke Development had an option, it failed to comply with its terms.
- [3] The issues to be decided are whether Litke Development acquired an option to purchase and, if so, whether it did everything it was required to do before it could exercise the option. If Litke Development does not have the right to buy the property, Kenco counterclaims for unpaid rent.

Background

- [4] The property at issue is a two-unit commercial building that Kenco built in 1992. One unit has always been occupied by a transmission shop, although Automaster only became the operator in late 2004. Another automobile-related business leases the other unit.

- [5] When it took over the location, Automaster was wholly owned by Familiar Transmission Ltd., which in turn is wholly owned by Litke Development. A Mr. Russell, who manages the Nanaimo transmission shop, has subsequently acquired a 50 per cent interest in Automaster. Litke Development also owns, directly or through other subsidiaries, three more transmission shops. Robert Litke is the president of both Automaster and Litke Development. Kenneth Riddell is the president of Kenco.
- [6] Automaster occupies the property under a lease that is dated for reference December 1, 2004, but which was not actually signed until sometime in March 2005. Automaster is identified as the lessee and Kenco as the lessor. The lease was also signed by Litke Development, although there is nothing in the body of the document to define that company's role or interest in the transaction. Mr. Litke signed on behalf of both of his companies.
- [7] The lease included a term giving "the lessee or nominee" a right to purchase the property on the following terms:
45. RIGHT TO PURCHASE the said lands and improvements thereof, is hereby granted to the Lessee or nominee on the following terms and conditions:
- a) The Purchaser may exercise the option to purchase the property and lands known as 6430 Hammond Road including the space leased by Applecross Automotive, for a Purchase Price of \$985,000 Dollars on or before June 30, 2006 provided that the Lease is in good standing.
 - b) The Purchaser will make a non refundable deposit of \$12,500 towards the purchase price and the purchase of the Property and Lands
 - c) The Purchaser will use its best efforts to assume the existing first mortgage with CIBC or refinance with CIBC the existing first mortgage (@ 6.19%, Balance at March 1, 2005 approximately \$382,000 and maturity Dec 1, 2007)
 - d) The Purchaser will use its best efforts to complete the sale on or before November 31, 2005
 - e) The Pole Sign located at the corner (Hammond Bay Road & Island Highway) is included in the sale of the Property at an price to be determined based on the sign's condition and the status of the contracts with Devlin Electric.

(The pole sign referred to is located on a neighbouring property and is owned by Kenco, which contracted management of it to Devlin Electric.)

- [8] The terms of the purchase option had previously been set out in a letter from Mr. Litke to Mr. Riddell dated March 2, 2005 (the "letter agreement"). That document reads, in part:

Hi Ken:

Re: 6430 Hammond Bay Road as discussed this morning

Purchase of Building

2400 sq ft @\$16.50 = 39,600

Electrical Room 1,000

2952 @ \$13.00 = 38,376

Total 78,976

Less 5% Vacancy 3,948

Net 75,028

Cap @ 7.75%, 968,000 + \$17,000 Goodwill = \$985,000 Purchase Price

1. Purchaser to use best efforts to assume the existing first mortgage with CIBC or finance with CIBC (existing 1st @ 6.19%, Balance \$382,000 Maturity Dec 1, 07)
2. The Purchase price of the Pole Sign in additional to the building purchase price noted above, but will be set at a reasonable price to be determined based on condition once Ken has reconciled his arrangement with Devlin Electric Co. The sign purchase will be included in this purchase agreement as the terms are negotiated.
3. Purchaser may exercise the option to purchase at any time during the first 18 months of the Lease however the Purchaser will use its best efforts to complete within 12 months, provided that the lease is in good standing.
4. The Purchaser will make a \$12,500.00 deposit towards the purchase of the building which will be non-refundable.

Five Year Lease: (Automaster Automotive Services) in the Landlord's Standard Triple Net Lease, with standard waiver in favour of BMO and Leaseholds available to Tenant as BMO security

1st 6 mths @ \$13.00 per square foot triple net

Next 12 mths @ \$13.50

Next 24 mths @ \$14.00 Lease commencement date Dec 1/04

Last 18 mths @ \$15.00

Purchase of Equipment from BMO Business loan proceeds, \$12,500.00

"Rob Litke"

Litke Development Corporation

Accepted by

"Ken Riddell"

- [9] The letter agreement is signed by Mr. Litke on behalf of Litke Development. Mr. Riddell signed the letter indicating acceptance of its terms, but there is no reference to Kenco. Mr. Riddell testified that at the time of the letter agreement, he did not know which company would become a party to the lease. He said that he regarded the letter agreement as one that only set out the terms to be included in the lease, with the option to be acquired by whatever company became the lessee.
- [10] The lease that was subsequently signed contains an "entire contract" clause which reads as follows:

AND IT IS HEREBY AGREED:

22. THAT the whole contract and agreement between the parties hereto is set forth herein, that the Lessee has leased the premises after examining the same, that no representations, warranties or conditions have been made other than those expressed or implied herein, and that no agreement collateral hereto shall be binding upon the Lessor unless it be made in writing and signed by the Lessor[.]
- [11] Litke Development argues that it acquired the option to purchase either directly through the letter agreement or indirectly through the lease. Kenco argues that only Automaster, not Litke Development, held an option to purchase.
- [12] Both the letter agreement and the lease required the purchaser, whoever it was, to use its best efforts to complete within the first 12 months of the lease, that is by November 30, 2005. However, the option could be exercised up to May 31, 2006--18 months after commencement of the lease.
- [13] On May 24, 2006, one week before the option was to expire, Litke Development's solicitor wrote to Kenco's solicitor stating that Litke Development was giving notice of its exercise of the option under the letter agreement. The solicitor's letter enclosed a cheque for \$12,500 as the non-refundable deposit referred to in the agreement and proposed November 30, 2006 as a closing date for the transaction. On July 21, 2006, Kenco's solicitor returned the deposit cheque and stated in a letter that "my client is not prepared to proceed with the transaction at this time."
- [14] Mr. Riddell testified that during the first 12 months of the lease--the period during which "best efforts" were to be used--he received no indication that the option would be exercised. He said that time period coincided with another transaction he and Kenco were involved in and Kenco would have been in a position to complete if the option had been exercised before November 2005. However, the other transaction did not proceed and after that, Mr. Riddell said, he was "no longer interested" in selling the property because the continued rental income was important to him.

- [15] Mr. Litke said the option was not exercised earlier because Litke Development was also involved in another transaction--the sale of property it owned in Vancouver. He said that he was planning to apply the proceeds of sale from the Vancouver property to the purchase of the Nanaimo property. However, the deal to sell the Vancouver property collapsed and the property was not sold to another buyer until early 2006.
- [16] The rent that Automaster was to pay under the lease agreement was \$13 per square foot (\$3,198 per month) for the first six months and \$13.50 per square foot (\$3,321 per month) for the following year, plus a proportionate share of common area expenses. The lease also provided for two further increases in the base rent--to \$14 per square foot on May 31, 2006 and to \$15 per square foot on May 31, 2008. Automaster has refused to include those last two increases in the rent it is paying, arguing that it should have become the owner of the property before those increases took effect.

Did Litke Development Acquire an Option to Purchase?

- [17] The first issue is whether the letter agreement was in itself a binding contract. Kenco argues that it was not a party to the letter agreement, which in any event is unenforceable because of uncertainty and a lack of consideration, and because its operation is excluded by the "entire contract" clause in the subsequent lease.
- [18] The minimum essential requirements for an option agreement were defined in *Mason v. Vulcan Machinery* (1977), 4 B.C.L.R. 185 at 187 (S.C.):

An option is a continuing offer or contract by which the owner stipulates with another that the latter shall have the right to buy property at a fixed price within a certain time.

- [19] As with any contract, an option must be sufficiently certain in its terms to be capable of enforcement. As Baker J. said in *Hanley v. Anderegg* (1993), 33 R.P.R. (2d) 170 at para. 32 (B.C.S.C.):

Parties may, if they wish, compose and honour agreements which are oral or written on paper airplanes or scratched in the sand. They can only call upon the assistance of the courts to enforce those contracts if, in fact, the terms of the bargain are sufficiently certain and capable of determination and show a true meeting of the minds of the parties.

- [20] I cannot accept Kenco's submission that it was not a party to the letter agreement. In construing a contract, the court must determine what the parties intended by the language of the agreement, viewed objectively, in the circumstances in which the agreement was made: *Petty v. Telus Corp.*, 2002 BCCA 135 at para. 14, 164 B.C.A.C. 152.
- [21] Although Kenco's name did not appear in the letter agreement, the document identified the property, which all involved knew to be owned by Kenco, and was signed by Mr. Riddell, who was known by the parties to be the president of that company. Mr. Riddell had no right to deal with the property in his personal capacity and, in the circumstances, could only be signing the document on behalf of Kenco in his capacity as president of that company.

- [22] The alleged uncertainty in the letter agreement is that it leaves the price of the pole sign to be determined at a later date. Because that amount was to be included in the purchase price, Kenco argues that the total price to be paid is left uncertain and the letter agreement is merely an agreement to agree. If Kenco is correct, the same would apply to the option clause in the lease document.
- [23] Where one portion of a contract is unenforceable for uncertainty, that portion may be severed where it deals with matters that are incidental to the primary purpose of the contract and severance can be achieved without altering the main contract: *Boult Enterprises Ltd. v. Bissett* (1985), [1986] 1 W.W.R. 385, 67 B.C.L.R. 273 (C.A.).
- [24] I find that is the case here. The purchase of the pole sign is an incidental and minor addition to the contract, the primary purpose of which is the sale of the land and building. That distinguishes this case from one like *Baykey v. North West Office Furniture Ltd.*, (1992), 22 R.P.R. (2d) 67 (B.C.S.C.), relied upon by the defendant, where the entire option to purchase property was uncertain because it contained neither a price for the property nor a mechanism to determine the price.
- [25] Here, the letter agreement contains all elements necessary to form a binding contract for the purchase of the land and building. It identifies the property by its civic address, sets out a purchase price, and provides a time period during which the option can be exercised. The incidental reference to the purchase of a pole sign is easily and properly severable.
- [26] The defendant further argues that there was no consideration for the option agreement. An option to purchase land is enforceable only if there is some consideration "given by the optionee in any event" (*Hanley* at para. 33 quoting from *Murray McDermid Holdings Ltd. v. Thater* (1982), 42 B.C.L.R. 119 at 123).
- [27] In *Hanley*, which the defendant relies on, there was an option agreement to purchase land at a stated price, with the vendors also receiving a second mortgage on another property. The agreement stated that it was "for the sole benefit of the purchaser" and would expire at the stated date. Madam Justice Baker found there was no consideration to support the option.
- [28] In this case, I find that there clearly was consideration. The option agreement included a reference to a five-year lease to be entered into by Automaster and set out the rental rates that would apply. The consideration for the option was that Litke Development would cause its subsidiary to enter into a lease that would provide Kenco with rental income until the option was exercised, or for the full five years if the option was not exercised. That meets the test of consideration being given "in any event."

- [29] Kenco also relies on the entire agreement clause in para. 22 of the lease. The first obvious point is that such a clause is only binding on the parties to the agreement. The lease document is an agreement between Automaster as lessee and Kenco as lessor. Although Litke Development signed the document, it did not specifically assume any obligations or obtain any rights under the lease. I doubt that Litke Development can be considered a party to the lease in these circumstances.
- [30] However, even if Litke Development is a party to the lease, para. 22 does not exclude all other agreements. It says that no agreement collateral to the lease is binding on the lessor unless it is in writing and signed by the lessor. The letter agreement is in writing and I have already held that it was signed by the lessor.
- [31] For all of these reasons, I find that the letter agreement created binding contractual obligations as between Kenco and Litke Development and those obligations survived the subsequent execution of the lease document. Having found the letter agreement to be enforceable, I do not need to deal with the question of whether Litke Development could exercise the option under the lease agreement, either directly as a party to the lease or as nominee of Automaster.

Did Litke Development Comply with the Option?

- [32] Although Litke Development acquired an option to purchase under the letter agreement, its right to exercise that option was still subject to the terms of the agreement. A purchaser seeking to enforce an option agreement must show that its terms have been strictly observed and the owner is under no obligations to sell unless the conditions precedent are fulfilled or the purchaser is relieved from strict compliance on some equitable ground: *Pierce v. Empey*, [1939] S.C.R. 247 at 252.
- [33] The defendant alleges a number of failures to comply with the terms of the option but the only one of any substance, in my view, relates to the provision that, although the option was open for the first 18 months of the lease, the purchaser was required to use its best efforts to complete during the first 12 months.
- [34] The meaning of the term "best efforts" was reviewed by this court in *Atmospheric Diving Systems Inc. v. International Hard Suits Inc.*, [1994] 5 W.W.R. 719, 89 B.C.L.R. (2d) 356 at para. 71 (S.C.). The definition includes the following principles:
1. "Best efforts" imposes a higher obligation than a "reasonable effort".
 2. "Best efforts" means taking, in good faith, all reasonable steps to achieve the objective, carrying the process to its logical conclusion and leaving no stone unturned.
 3. "Best efforts" includes doing everything known to be usual, necessary and proper for ensuring the success of the endeavour.

4. The meaning of "best efforts" is, however, not boundless. It must be approached in the light of the particular contract, the parties to it and the contract's overall purpose as reflected in its language.
5. While "best efforts" of the defendant must be subject to such overriding obligations as honesty and fair dealing, it is not necessary for the plaintiff to prove that the defendant acted in bad faith.
6. Evidence of "inevitable failure" is relevant to the issue of causation of damage but not to the issue of liability. The onus to show that failure was inevitable regardless of whether the defendant made "best efforts" rests on the defendant.
7. Evidence that the defendant, had it acted diligently, could have satisfied the "best efforts" test is relevant evidence that the defendant did not use its best efforts.

[35] Madam Justice Dorgan added at para. 72:

- [72] The "no stone unturned" test has been applied to contracts relating to a wide variety of subject matter. Further, courts routinely imply a term in contracts that the parties will make reasonable efforts to fulfil their respective contractual obligations. Where the parties include a "best efforts" clause in a contract, as they did in the case at bar, they must surely intend that something more than "reasonable efforts" be used.
- [36] Mr. Litke testified that the option was not exercised before November 2005 because the sale of other property in Vancouver collapsed when the purchaser was unable to obtain financing. After that, his efforts to complete the Nanaimo purchase consisted of ongoing attempts to find another buyer for the Vancouver property.
- [37] However, there is nothing in the agreement that ties the exercise of the option solely to the proceeds of sale of the Vancouver property. In the absence of such a limitation, the "usual, necessary and proper" steps to complete the transaction had to include efforts to seek alternate financing. There is no evidence of any such efforts and when Mr. Litke was asked on cross-examination if it would have been possible to finance the Nanaimo purchase in some other way, he said he did not know.
- [38] While I am satisfied that, during the first 12 months of the option, Litke Development was making all reasonable efforts to sell the Vancouver property, the "best efforts" obligation required it to explore other sources of financing the Nanaimo purchase if the Vancouver sale proceeds were not forthcoming. As there is no evidence it did so, I must hold that Litke Development failed to fulfill the conditions of the option agreement.
- [39] The plaintiffs' claim for specific performance of the option agreement must therefore be dismissed.

The Counterclaim

- [40] The defendant counterclaims for arrears of rent. It is admitted that Automaster has refused to pay the rent increases that went into effect on May 31, 2006, and May 31, 2008. Kenco also alleges that rent remains unpaid for some months and claims that Automaster has underpaid the Goods and Services Tax on the common area expenses.
- [41] As I have found that Kenco was within its rights to refuse to sell the property, the lease remained in effect and Automaster was required to continuing paying the rent required by the lease, including the rent increases. Kenco is entitled to a judgment on its counterclaim for all arrears of rent, including the unpaid increases and the full rent for any months it has not been paid.
- [42] The alleged GST underpayment relates to an error in Kenco's own calculations that it says it discovered part-way through the lease. The evidence on that point came from Mr. Riddell, who relied on calculations prepared by his company bookkeeper and appeared to have a very limited understanding of them. The evidence does not satisfy me that Automaster owes any additional amount for GST.
- [43] In summary, the plaintiffs' claim for specific performance is dismissed and the counterclaim for arrears of rent is allowed against Automaster. Counsel may speak to the precise amount owing under the counterclaim if they are unable to agree on it.

N. Smith J.

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