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AGREEMENTS – THE TOP 10 LIST

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I. INTRODUCTION

This paper contains, with no attempt at "Lettermanesque" humour, a "top 10" list of points for consideration with respect to local government contracts. The list is in no particular order, nor does it purport to be exhaustive or particularly authoritative.

II. TO AGREE OR NOT TO AGREE?

Is the proposed 'agreement' intended to be contractually binding? Is the local government looking for a binding commitment from the other party, one that may be enforced using the courts? Alternatively, is the 'agreement' intended only as a statement of present intention or expectations, perhaps as a purely political commitment?

In order to avoid legal uncertainty, it is important that the document indicate, on its face, whether it is contractually binding. With most contracts, this will be abundantly clear from the wording and formal structure of the document. However, on occasion, a local government will be asked to sign a document that does not appear to be as formal as a typical contract, having a much friendlier, less intimidating name such as a 'memorandum of understanding', 'letter of intent' or 'agreement in principle'. The purpose of such a document is usually, but not always, to confirm a purely political (as opposed to legal) agreement or to confirm the parties' mutual intentions about a proposed transaction before drafting a formal contract.

An example of a political agreement is the B.C. Climate Action Charter, which has been signed by many BC local governments and purports to commit signatories to various greenhouse gas reduction measures. Importantly, subsection (9) of that documents states, "This Charter is not intended to be legally binding or impose legal obligations on any Party and will have no legal effect". Therefore, while a local government and its elected officials may conduct business as if they are bound by this Charter, a failure to comply with its terms does not give rise to the same kinds of legal repercussions as would be the case with a binding contract. In particular, a party to the Charter is not in a position to seek remedies to enforce the arrangement or obtain compensation for losses resulting from non-compliance by another party.

Importantly, even a document that appears to be a mere 'prelude' to a formal contract can give rise to contractual obligations. If the document includes the essential terms of a transaction, legal obligations may arise, if the wording of the document evidences an intention by the parties to be contractually bound. This may be the case even if the document contemplates the subsequent negotiation of more detailed legal agreements. An absence of a clear statement of intention can leave such a conclusion open to interpretation and give rise to legal uncertainty.

Accordingly, it is essential that MOUs, Letters of Intent and similar less formal documents expressly state whether they are to be contractually binding. If the document is not intended to be binding, wording such as the following should be included:

> "The parties do not intend to create contractual or other legal obligations by signing this MOU and no legal obligations whatsoever shall arise between the parties as a result of this MOU"

A failure to include this kind of wording may enable a party to the document to argue that the other party is contractually bound, and threaten legal action should the other party refuse to honour the terms. This kind of legal uncertainty and the potential for litigation may keep the local government 'at the table', even though it wishes to cease dealing with the other party on the particular matter.

III. HAS COUNCIL "BLESSED" THE AGREEMENT?

Is there a council resolution or bylaw authorizing the agreement?

1. The need for a council resolution

Generally speaking, only the council may exercise the powers of a municipality, except where council has properly delegated its powers. Council exercises its powers by passing resolutions and adopting bylaws. The power to enter most kinds of contracts is a 'natural person' power under section 8(1) of the *Community Charter*. Accordingly, a council may authorize most kinds of contracts by passing a resolution, without the need for a bylaw.

Where a municipality purports to enter into a contract, but council has not passed a resolution authorizing the contract, the contract is not likely to be binding on the municipality or the other party to the contract. In such circumstances, the municipality may be able to walk away from a purported contractual commitment. Similarly, the other party to the contract will not be bound. The other party may, however, have some recourse to compensation from the municipality, depending on the circumstances. For instance, if the municipality has benefitted from the other party's efforts, the municipality might be required to compensate for those efforts.

2. Closed v. Open Council Meeting

Unless there is a valid statutory basis for passing a contract authorizing resolution in a closed meeting, such a resolution must be passed in an open council meeting. A failure to do so may leave the resolution vulnerable, making it possible that the resulting contract could be set aside. Section 90 of the Charter lists the circumstances when a meeting may be closed to the public. If the consideration and even approval of a particular agreement fits within one of the listed circumstances, the resolution may be passed in a closed meeting. Otherwise, the matter must be dealt with at an open session.

For instance, a decision to enter a contract to purchase or sell land could be made in camera if council considers that "disclosure could reasonably be expected to harm the interests of the municipality" (section 90(1)(e) of the Charter). This might be the case if the municipality wishes

to make a competing offer to purchase a property or to accept an offer to purchase municipal land, but does not wish to publicly disclose the purchase price before the offer is actually accepted.

It is interesting to note that the circumstances where a council may, in a closed meeting, pass a resolution to award a contract for services, such as a construction contract following a tender process, appears to be quite limited. Perhaps such a decision might constitute the "acquisition of improvements" the disclosure of which "could reasonably be expected to harm the interests of the municipality". The meeting might be closed pursuant to section 90(1)(k), if the decision relates to "negotiations and related discussions respecting the proposed provision of a municipal service that are at their preliminary stages and that, in the view of the council, could reasonably be expected to harm the interests of the municipality if they were held in public". IT does, however, seem doubtful that the decision to actually award or enter into a contract would constitute "negotiations and related discussions". Where the municipality is receiving legal advice concerning its consideration of competing tenders, that portion of the meeting may be made in camera (s.90(1)(i)). Again, however, it may be difficult to stretch the consideration of legal advice to cover the ultimate contract award decision. Therefore, it appears that in most cases a decision to award a contract would have to be made in a meeting open to the public.

3. Delegation & Purchasing Policy

Because the power to enter into most contracts may be exercised by resolution, a council may, by bylaw pursuant to section 154 of the Charter, delegate that power to others.

Purchasing policies are typically adopted by council resolution, even though such policies often include some authority for staff to enter certain kinds of contracts. For instances, such policies sometimes purport to authorize staff to issue calls for tenders and other procurement processes that, as discussed further below, may give rise to contractual obligations in relation to the processes themselves.

The Courts have indicated that a separate council resolution is not required to authorize the purchase of every 'stock item' for the municipality. In this respect, authority under a purchasing policy to enter some contracts may be seen as a mere administrative function, as opposed to a delegation of a power. However, depending on the nature and significance of the particular contact, it may be the case that a council resolution is required to specifically authorize the contract. Alternatively, council could, by bylaw, delegate appropriate authority (and applicable parts of a purchasing policy could be incorporated into such a bylaw).

IV. EXTRA, EXTRA!!! READ ALL ABOUT IT!!!

Is a newspaper notice required with respect to the agreement?

1. The Notice Requirement

Unlike a private business, in some cases a municipality must publish a newspaper notice before it enters into certain kinds of agreements. In particular, section 26 of the Charter requires such a notice with respect to the disposition of land.

Under section 26, a municipality has a choice. It can offer land to the public for acquisition and give notice of that opportunity, or a municipality can deal directly with an interested purchaser and then give notice of the specific sale. Importantly, a notice of a specific sale to a specific purchaser must identify the intended purchaser and purchase price.

If a regional district intends to dispose of land, it must make the land available to the public generally. There are exceptions to this, including where the disposition is in exchange for other land, is for land consolidation purposes or is to a public authority or a non-profit corporation (sections 186 and187 of the Local Government Act).

The newspaper notice must be published in a newspaper in consecutive weeks. This likely means that the notices must be at least 1 week apart and that a municipality cannot rely on common understanding as to when a week begins (Sunday? Monday?). It is doubtful that notice Saturday and then Sunday would meet the consecutive weeks requirement.

If a municipality is making the property available for public acquisition, section 26 (2) requires that the notice set out the "process" by which the property may be acquired. Section 26 does not, however, impose any particular kind of process. It would therefore appear that a municipality may sell property by listing a property and waiting for an acceptable offer, as opposed to having go through a formal request for proposals process. Importantly, if a municipality provides such a notice and then wishes to accept an offer for the land, the municipality does not have to give a further notice with respect to the actual proposed sales transaction. This may be advantageous where the municipality does not wish the sale price for the land to be immediately known. For instance, if the sales transaction does not ultimately complete for one reason or another, the municipality may not want the sales price to be known to other prospective purchasers.

As noted above, if the municipality has not made the property available for public acquisition, the municipality will have to publish a more specific notice under section 26(3), which will have to identify both the purchaser and the sale price.

2. Notice of Dispositions of Lesser Interests

By virtue of the definitions of "dispose" and "land" under the *Interpretation Act*, the requirement for a notice extends beyond an outright sale of land and applies to grants by a municipality of other interests in land, such as leases, easements, section 218 statutory rights of way and section 219 covenants, options to purchaser, rights of first refusal and mortgages.

3. Notice of Assistance

If a proposed contract includes certain forms of assistance, the local government will have to give notice (section 24 of the Community Charter and section 185 of the Local Government Act). The forms of assistance for which a notice is required include disposing of land or an interest in or right with respect to land for less than market value, the provision of a loan, loan guarantee or security for a loan and assistance under a partnering agreement.

4. Timing of the Notice

The definition of "dispose" includes "to agree" to transfer, sell, grant etc. Therefore, a municipality must give notice before it has contractually agreed to the sale or other grant or disposition. In the case of a sale of land, this means that the notices must be published before the municipality signs the purchase and sale contract. On occasion, one sees contracts of purchase and sale that include a 'subject to statutory notice' condition, purportedly to enable the municipality to sign the contract before giving notice. It is doubtful that this practice complies with the legal requirement respecting notice. It may be acceptable for a municipality to sign a contract before publishing the notices if the contract is "subject to final approval of the sale by the council of the municipality, in its sole discretion". A contract, subject to such a condition, is really an option to sell in favour of the municipality

In *Coalition for a Safer Stronger Inner City Kelowna v. Kelowna (City)*, 2007 BCSC 605 (2007), a community group asked the B.C. Supreme Court to set aside a council resolution authorizing a lease, on the basis that the notice of disposition was published after council passed the resolution and that the City had breached its duty of procedural fairness by not providing an opportunity for public participation following the notice. The City passed a resolution to grant a lease to the Provincial Rental Housing Corporation for a proposed supportive housing project to provide housing for homeless persons with mental health and addiction problems. The City published the statutory notices after the resolution was passed and before execution of the lease. The court stated, "It is common ground that there is no specific duty contained in the Community Charter to hold a public hearing on the disposition of land. The petitioner says that when ss. 26 and 94 are considered together with s.24, all of the Community Charter, that by necessary implication, a public hearing or public consultation process is mandated". City council had, by resolution, adopted a "Healthy Community" policy that included a statement that "the City of Kelowna will ensure full community participation in matters relating to the overall health of the community and its citizens". The court stated, "It is this resolution to insure full community participation that the petitioner submits supports its position". The court held that the notices had to be published before the City entered the lease, but that they could be published after council passed the resolution authorizing the lease. The court noted that there had been public consultation leading up to the council resolution and that "To the extent that the "Healthy Community" policy adopted by the resolution of the council of the City contains at least an expectation of community participation, then, that expectation of community participation was fulfilled".

This decision clarifies that a notice of disposition may be published after council passes a resolution authorizing the disposition. The Court's reasoning indicates that to the extent that the City might have been subject to some procedural fairness requirement, that requirement arose because of council's policy, and not by virtue of the statutory notice requirement.

5. Purpose of the Notice – Public Input?

In *Doherty v. Southgate (Town)* (2006), the Ontario Court of Appeal clarified the rationale for requiring notice before a municipality binds itself to sell land:

> "the purpose of the notice is to inform the public of a proposed sale before a municipality binds itself to sell land. In this way, members of the public can, if they choose, make representations to their elected representatives that the land should not be sold because it is not surplus, or that the price being sought by the municipality is not sufficient. Publication of notice of a proposed sale prior to a municipality entering into an agreement of purchase and sale provides an opportunity for members of the public who object to the sale to use political suasion to register their objections, as opposed to the more costly and difficult remedy of a court action that would be required if a municipality has already legally committed itself to sell land. Admittedly, the statute does not provide for a specific hearing process to receive such objections. That, however, in my view, is not reason to dismiss what is otherwise a reasonable purpose for the notice requirement. The democratic process allows for political involvement by the public in both formal and informal ways. Moreover the requirement that a municipality give notice to the public prior to committing itself to a sale of land promotes, at least in a general sense, openness and transparency of municipal government, which can only be seen as a positive objective."

In some cases, the notice of disposition will be the first time the public becomes aware of the proposed disposition and the key terms set out in the notice. Accordingly, while there is no requirement for a public hearing or public consultation with respect to an agreement for which public notice is required, it is prudent for a municipality's land disposition process to allow council to gauge public response before an agreement is signed, such as by waiting a week following the second notice before signing the agreement.

V. DOES THE AGREEMENT OFFEND THE '5-YEAR RULE'?

With any proposed agreement, the following questions should be asked:

- Is the term of the agreement longer than 5 years, or could it exceed 5 years through exercise of any rights of renewal?

- Does the agreement contain any liabilities on the part of the local government that are of a 'capital nature', or is the local government providing a loan guarantee?

If the answer to both these questions is "yes", then the liability must receive the 'approval of the electors' before the local government signs the agreement.

1. The "5-Year Rule"

Section 175(2) of the *Community Charter* (which applies to regional districts by virtue of section 819 of the *Local Government* Act) provides that a municipality may not incur a liability under an agreement having a term greater than 5 years (including any rights of renewal or extension) unless the liability has received the approval of the electors.

Section 6 of the Municipal Liabilities Regulation (and section 2 of the Regional District Liabilities Regulation) provides that the elector approval requirement under section 175(2) only applies to "loan guaranties" and "liabilities of a capital nature". The Regulation significantly narrows the application of this '5 year rule'.

2. What is a capital liability?

Public sector accounting principles will guide the interpretation of both "capital" and "liability", at least for municipalities. In this respect, section 1(2) of the Municipal Liabilities Regulation provides, "Except as otherwise provided in this regulation, the terms used in this regulation are to be interpreted consistently with the recommendations and guidelines issued by the Public Sector Accounting Board as authorized by The Canadian Institute of Chartered Accountants". Curiously, the Regional District Liabilities Regulation does not contain a similar provision.

Prior to the Regulation, the BC courts had interpreted "liability" very broadly, to include local government obligations to "indemnify" the other party to the agreement and local government maintenance obligations, such as an obligation to maintain a municipal water system. The courts have yet to interpret the meaning of capital liability in the context of the Regulation.

The courts have considered the meaning of a capital expenditure in deciding whether an expense is 'operating' and therefore deductible from revenue for income tax purposes. These decisions are of assistance in distinguishing between capital and operating liabilities. In *Marklib Investments II-A Ltd. v. Canada* [1999] T.C.J. No. 716, the court stated:

> "The determination of whether the characterization of expenditures as current expenses or capital outlays depends, not upon the nature of the property acquired but upon the nature of the expenditure. The classic description of what constitutes a capital expenditure is in British Insulated and Helsby Cables Limited and Atherton, [1926] AC 205 (H.L.) at 213:

> "…when an expenditure is made, not only once and for all, but with a view to bringing into existence an asset or an advantage for the enduring benefit of a trade, I think that there is very good reason (in the absence of special circumstances leading to an opposite conclusion) for treating such an expenditure as properly attributable not to revenue but to capital."

An obligation to purchase or construct an improvement would likely constitute a capital liability. Whether an obligation to repair or replace part of a building is capital would appear to depend on whether the work is aimed at maintaining the building for its normally anticipated life or is aimed at expanding the building or extending the life of the building, such as with a major renovation project. In *Marklib*, the court considered the matter of building repairs and distinguished between repairs that result in a complete building reconstruction or renovation project, which would be capital in nature, and repairs aimed at maintaining a building. The court concluded that the repairs in question were not capital in nature, as the court did not consider that "the buildings in question were restored beyond their original condition" and referred to an earlier decision where the court stated "It would seem that if the repairs resulted in virtually the same old building as before the repairs were undertaken then such should be properly expensed, but if on finishing the repairs a virtually new building or at least quite a different building results then the repairs should be on capital account".

3. Term of the Liability or Term of the Agreement?

In some agreements, a local government may be required to make an initial capital expenditure, but have no capital liabilities after the first 5 years of the contract. Arguably, such a liability would be caught by section 175. That said, in some cases, such a liability would not offend the apparent intent of section 175, that is, to protect future taxpayers from long-term capital commitments made on behalf of current taxpayers. While the entire agreement must be examined in any given case, if the capital liability will be satisfied during the first 5 years of the agreement, there may be a strong argument that no elector approval is required.

4. Local Government Renewal Options

Similarly, where the term of the agreement will only exceed 5 years if the local government exercises a right of renewal, if that right of renewal is purely discretionary and there is no indirect loss to the local government from a decision to not exercise such a right, it seems unlikely that such an agreement would require elector approval. It could be argued that absent the renewal, the capital liability is under 5 years and that there is no further capital liability unless the local government exercises the right of renewal.

5. Operating versus Capital Leases

With respect to leases of property or other assets, the Public Sector Accounting Handbook distinguishes between operating leases and capital leases. Under the former, the local government pays rent for the use of the leased premises, but not with a view to acquiring the

leased premises. Under a capital lease, the local government is essentially acquiring the leased premises or asset. Under such an arrangement, 'rent' includes payment towards ownership of the asset, as opposed to only being payment for use of the asset. At the end of the lease term, the local government will typically have an option to acquire the asset, an option the local government is likely to exercise given its investment in the asset through periodic 'rent' payments. As a result, an obligation to pay rent under an operating lease is not a liability of a capital nature, whereas rent obligations under a capital lease are liabilities of a capital nature.

VI. IS THE AGREEMENT FOR MARKET VALUE?

Does the agreement contemplate a fair market value transaction?

Can the council or board justify this view?

1. Assistance to Business

Assistance includes providing financial grants and other advantages, loans and loan guarantees, tax exemptions and dispositions of land for less than market value. Based on the definition of 'assistance' under the Charter, assistance would include a transaction under which the local government does not receive fair market consideration in return for the performance by the local government of its obligations under the agreement.

Local governments are prohibited from providing assistance to a business, except under a partnering agreement where the business provides a service on behalf of the local government.

To date, when local governments have faced legal challenge on the basis that an arrangement amounts to assistance to a business, the Courts have been reluctant to second guess council decisions, showing great deference to council assessment of a transaction, provided there is no obvious intent to provide assistance and the council has not acted recklessly with respect to the arrangement.

2. Having a Basis for Market Value

The best way to ensure a contact is for market value, and not assistance to business, is to award or enter into the contract only after going through a public process for the contract. If land is sold to the highest bidder or a contract is awarded to the lowest satisfactory bid, it will be difficult to second guess the financial terms of the transaction.

Where a local government wishes to enter into a contract without first going through some kind of competitive process, the local government should have some basis for assessing that the contract is a market value transaction. The extent of such 'due diligence' will depend on the significance of the transaction. For instance, with a sale of land, there should be some basis for determining the value of the land. With a less significant transaction, one might rely on assessed value. In the case of the disposition of un-assessed road, one might rely on the value

of adjoining land, particularly if the road is to be consolidated with such land. With a more significant transaction, it will be prudent to obtain an appraisal.

VII. NO FETTERING!

A local government cannot agree to exercise its powers in a certain way.

A local government cannot agree to amend zoning or not to amend zoning.

A local government cannot agree to issue a permit.

A provision in a contract that obligates a local government to exercise its powers in a certain way is a fetter on the local government's powers and is unenforceable.

1. What is fettering?

Local governments have some powers in common with persons and other corporations, including the power to enter contracts. Local governments also have unique powers, including powers to regulate land use, to require permits for development and to impose taxation. These special powers must be exercised by public officials, in the public interest. A local government cannot lawfully make contracts with respect to how they will exercise such powers.

The inclusion in a contract of a requirement that the local government compensate the other party if the local government exercise its powers in a certain way may be unlawful, as such a clause may amount to an indirect fetter on the local government's statutory powers. For example, an obligation to compensate a landowner for loss of profits resulting from a downzoning has been held to be an indirect fetter and therefore unlawful and unenforceable.

However, In some circumstances, the courts may require that where a local government receives, under a contract, a benefit as a result of a rezoning, the local government may be forced to disgorge or compensate for that benefit should the local government subsequently downzone the subject property. Whether compensation is payable will depend on the particular circumstances.

2. Contracts Predicated on Regulatory Action

Where a transaction under a contract cannot proceed unless the local government first issues some permit or enacts some bylaw, the requirement for the permit or bylaw should be included as a "condition precedent" or "subject to" clause under the contract. The contract should, however, leave the local government to consider the issuance of the permit based on applicable bylaw requirements, or the enactment of a bylaw based on applicable planning or other considerations.

A contract that is conditional upon the enactment of a bylaw or issuance of a permit, may include financial consequences for the parties to the contract, including the local government. For instance, where a local government is selling land for redevelopment, it is common for the sale to be conditional upon rezoning and for the sale price to be based on the value of the land as rezoned. With such a transaction, the local government will benefit financially if the land is rezoned and then sold. There is nothing improper with such an arrangement. A local government is certainly free to rezone its own land and then sell that land. That said, the local government is wearing two hats, being both the vendor and the regulatory authority. Accordingly, the courts have held that in such circumstances, the local government must be meticulously fair in rezoning the property. Presumably, this means that the local government must satisfy the usual procedural fairness requirements and stick to planning considerations when evaluating the zoning amendment, and must also be up-front with the public respecting the proposed land sale and financial impact.

It may also be permissible for a contract to require that some compensation be paid by the local government as a result of a failed condition precedent, provided that such compensation reflects some benefit received by the local government, or address some shared risk between the local government and the other party (such as the sharing of costs incurred to date).

3. Contract Clauses

In order to avoid contractual uncertainty and potential compensation claims, it is important that local government contracts not include any obligations purporting to require a local government to exercise its powers in a certain way or to look favourably upon a permit application. Where a transaction under a contract is predicated on some local government regulatory action, this should be addressed as a condition under the contract. The contract should also include a clause stating that the council or board's discretion to adopt the bylaw or issue the permit is not affected (or 'fettered') by the terms of the agreement.

VIII. INDEMNITIES AND LIABILITY LIMITATIONS

A typical contract will include pure 'business terms' (price, term etc), as well as more technical legal clauses (such as default, termination and dispute resolution clauses). Of the latter variety, indemnities and liability limitations need to be considered very carefully. These kinds of clauses are often included in the 'fine print', reinforcing the need to carefully review all contract terms.

1. Indemnities

With a contractual indemnity, one party to the contract agrees to protect the other party from some potential liability.

In considering whether to include an indemnity in a contract, the first question is whether the requirement for an indemnity is appropriate. This will depend on the nature of the contract as well the circumstances surrounding the contract.

For instance, where a local government wishes to acquire a statutory right of way over private land for the purposes of operating a public trail, it is common for the right of way agreement to include an obligation for the local government to indemnify the land owner from liability associated with the use of the trail.

Similarly, if a local government is acquiring or selling land that may be contaminated, it is common for the purchase and sale contract to include an indemnity in favour of one of the parties, making the other responsible for contamination. Which party should take on such risk will depend on the circumstances, including the purchase price and the selling party's historical use of the property. In a case where a local government is seeking to acquire a key property for redevelopment or revitalization purposes, such as a former waterfront industrial property, the local government can expect that the vendor will require indemnification with respect to liability for contamination. Without such protection, the vendor will likely prefer to sit and hold the property, rather than sell and face potential exposure for contamination clean up costs.

A second consideration is the risk associated with giving the indemnity and whether the local government can manage that risk. With respect to liability for a public trail, the local government can try to manage that risk through appropriate trail inspection and maintenance practices and by maintaining appropriate liability insurance coverage. With respect to potential liability for land contamination, in acquiring a property that may be contaminated, the local government should, before purchasing the property, investigate the extent of contamination so that it has knowledge of the risk and costs in this regard.

The availability of insurance for each party will be a significant factor in determining whether an indemnity is appropriate and acceptable. Before giving an indemnity, the local government should review its insurance to ensure that any liability it assumes under the indemnity will be covered by insurance. Some policies may not provide coverage where a local government is to indemnify another party with respect to that other party's negligent acts.

It should be noted that to be effective, an indemnity needs to provide some protection against liability that would otherwise accrue to the party receiving the indemnity. In many cases, an indemnity has very little effect in shifting liability. For instance, if Party A indemnifies Party B for losses caused by A's negligence, but the indemnity also excludes liability for B's negligence, then the indemnity may not increase B's protection from what it would otherwise be at law – each party remains responsible for its own negligence.

2. Liability Limitations

Sometimes a contract will include a limitation on the other party's potential liability to the local government. This is fairly common in certain industry form consultant contracts, such as for architect and construction management services. The limitation may be to a stated amount. IN other cases, liability may be limited to the fees paid to the party for its services or to the extent of the party's insurance coverage.

The ability of a local government to negotiate over such a limitation may depend on the local government's leverage and ability to choose a different consultant, in any particular cause. Liability limitations can, however, represent a significant liability and risk shift to the local government and should be strongly resisted.

IX. SECTION 219 COVENANTS VERSUS CONTRACTS

If the agreement is a covenant under section 219 of the *Land Title Act* granted by a landowner to a local government, do the restrictions and requirements of the covenant fall within the scope of section 219?

Section 219 permits the inclusion of both positive and negative covenants providing that land or a building may only be used in accordance with the covenant, that land may not be built upon or must only be built upon in accordance with the covenant, that land may not be subdivided or that land may subdivided only in accordance with the covenant and that parcels subject to the covenant may not be sold separately.

What distinguishes such a covenant from a contract? If such a covenant is registered against title to the land in the land title office, its provisions will 'run with the land' to bind and restrict the land in the hands of the owner who grants the covenant, and also in the hands of future owners of the property. This is the case, even though a future owner never signs or agrees to the covenant.

However, in order for a provision in a covenant to run with the land, it must fall within the scope of section 219. The provision must relate to the use of land or a building on the land, to construction on the land or to subdivision of the land.

Obligations that do not fall within the scope of section 219 will not run with the land. For instance, an obligation to pay money is not a land use restriction and will not run with the land. An obligation on an owner to maintain works located on adjacent road will not run with the land, as the obligation is not in relation to the covenanted land. Similarly, an obligation not to apply for a building permit relates to building bylaw processes and individual rights under such a bylaw, and not to the use of the land (whereas a covenant not to build on the property would run with the land).

Section 219 covenants are powerful land use regulatory tools. However, they have their limits. It is nevertheless fairly common to see covenants that include provisions that go beyond the scope of section 219 and, as such, are not likely to run with the land to bind future owners. A covenant may still be used to secure these kinds of obligations. For instance, if the owner has promised to provide amenities to the local government in connection with a rezoning of the land, a covenant promise to pay money for amenities will not run with the land. However, such a promise might be secured by prohibiting construction on the land until that payment is made. Of course, the landowner may choose not to development and never make the amenity

payment. If the municipality's expectation is that the payment would be made at some point, regardless of the extent of development, then other security will be necessary (such as a letter of credit).

X. CONTRACTUAL OBLIGATIONS BEFORE THE CONTRACT (CONTRACT A AND CONTRACT B)

When a local government issues a tender call, requests for proposals or other procurement process, a local government may be entering a contractual realm associated with the procurement process itself - a realm rife with inadvertent financial exposure, lawyers, lawsuits and court decisions, not to mention headaches. Accordingly, before embarking on a procurement process, the local government should carefully consider its intended legal process and whether the documents it is using reflect that intent.

Briefly stated, where a local government is looking for bids or proposals for a contract (such as for the supply of a fire truck, for a road builder or for a recreation centre operator), contractual obligations can arise in relation to the procurement process itself, quite apart from the contract for the work or service. The sought after contract for the work or the service (the supply, construction or operating contract) is known as 'Contract B'. Depending on the terms of the tender or proposal call, it is also possible for 'Contract A' to arise between the local government and each bidder or proponent, governing the validity of bids or proposals and the local government's consideration of bids or proposals.

Whether Contract A arises depends whether the terms of the tender or proposal call evidence an intention by the local government to enter into contractual relations as part of the procurement process. The hallmark of such an intention is a requirement that bids or proposals be irrevocable for a period of time. Other factors may also suggest contractual intention, including wording that suggests a commitment on the part of the local government, such as promises to evaluate bids in a certain way. Contract A will typically obligate the local government to treat all tenderers fairly and in accordance with the commitments and terms set out in the tender documents.

Both Contract A and Contract B are present in a traditional tender call. An alternative process, without Contract A, would typically involve non-binding proposals, capable of being withdrawn or changed at the instance of the proponent. This is a traditional RFP process.

Selection of an appropriate process is a business and political decision of the local government (although consideration should be given to implications under trade agreements between BC and other provinces). A local government may receive more interest and more competitive pricing with a contractual process. A Contact A process may also give a greater assurance that the process is fair and open. The major downside is exposure to lawsuits alleging failure on the local government's part to comply with Contract A. With a contractual process, the local government must comply with its promises to bidders as disclosed in the procurement documents. A failure to comply with those promises, may leave the local government

vulnerable to claims from disgruntled bidders, who may feel that they should have been awarded the contract and wish to be compensated for the profits they would have earned on the contract.

On other hand, where the specifications for the project are less well-defined and subjective, making it more difficult to compare proposals, (such as where the local to government is looking for proposals as to design, as opposed to price only) a less formal process may be appropriate.

As noted above, it is the content of the procurement documents, and not the name of the process, that will be determinative - the Courts have found that a Contract A has arisen under a request for proposal processes.

Accordingly, a local government should first determine the process appropriate to its needs. If it does not wish to have contractual obligations in relation to the procurement process itself, procurement documents should clearly state that no contractual obligations shall arise as part of the procurement process. In order to avoid legal uncertainty, it is essential that the rest of the terms of the procurement documents are consistent with that intention. For instance, there should be no requirements for irrevocable offers or for bid security. It is common for the drafters of procurement documents to 'kitchen sink' the documents, by including a "No Contract A", but also requiring irrevocable bids, bid bonds and other clauses indicative of a contractual intentions. This kind of inconsistency gives rise to legal uncertainty that may compromise the proposal selection process.

If the local government wishes to use a more formal process, that gives rise to Contract A, the local government should may wish to include a clause limiting the local government`s liability in relation to the procurement process.

XI. AGREEMENT MONITORING

Does the agreement contain any important dates that should be monitored after signing?

After an agreement is signed, the agreement should be reviewed for key dates, such as closing dates, condition precedent dates, expiry dates and renewal dates. These dates should be noted with appropriate 'bring forward' systems, so as to ensure key dates are not missed and that necessary steps are conducted in advance of an applicable date.

A failure to meet a deadline or to respond appropriately to a missed deadline may result in an outright loss of legal rights or a breach of a contractual obligation. Such a failure may also give rise to an uncertain legal position. For instance, contracts for the sale of land will often include clauses making the transaction conditional upon some event, such as receipt by the purchaser of a satisfactory environmental investigation of the property. Where such a condition is for the benefit of local government, the local government cannot sit back and allow the condition to expire and then walk away from the agreement. The local government is under an obligation to try to satisfy the condition and would have to do some investigation into the environmental

condition of the land (or waive the condition). Similarly, where a land sale condition is for the benefit of the other party to the agreement and the local government has some role with respect to the condition (such as a rezoning condition), the local government needs to do what it can reasonably do in terms of processing and considering the rezoning or subdivision application. While the local government is not obligated to rezone, a lack of attention to the rezoning process on the part of the local government may affect its ability to treat the contract as at an end if the condition date passes. Also, if a key legal date under an agreement passes without formal communication between the parties, this may affect the legal rights of a party. For instance, if a condition precedent date passes (such as for rezoning), but the parties continue to pursue the transaction and rezoning, the status of the contract may be uncertain, making it unclear as to whether a party may treat the contract as at an end.

The bottom line is that it is important that a local government track key agreement dates, to help ensure that it upholds its end of the bargain in relation to such dates and that it does not inadvertently prejudice its rights under a contract.