Reimbursement clause for extrajudicial fees by a surety: valid or invalid?

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On April 6, 2021, the Court of Appeal, *per* Justice Mark Schrager, rendered an interesting decision in *Bank of Nova Scotia* c*. Davidovit* (2021 QCCA 551).

The Bank of Nova Scotia (the "**Bank**") had granted a commercial loan to a company, of which Aaron Davidovit ("**Davidovit**" or the "**Surety**") was the principal, for the operation of a gym. Under a clause contained in the personal guarantee (suretyship) signed by Davidovit, he was to reimburse all costs and expenses incurred by the Bank to collect amounts owed to it by the principal debtor or Surety, including, but not limited to, legal fees on a solicitor/client basis (the "**Clause**").

The Bank was claiming $31,145.22 in extrajudicial fees and legal costs from Davidovit, while the amount claimed from the Surety in capital and interest amounted to $35,004.49.

The trial judgment

The trial judge, the Honourable Frédéric Bachand, concluded that the contract of suretyship was a contract of adhesion within the meaning of article 1379 of the *Civil Code* of Québec (the "**C.C.Q.**") and agreed with Davidovit's arguments that the Clause was invalid because it was excessively and unreasonably detrimental to the adhering party and contrary to the requirements of good faith, in violation of article 1437 C.C.Q. Justice Bachand emphasizes two main problems with the Clause: (i) it was unilateral, thus giving a disproportionate advantage to the Bank while the Surety did not benefit from such an advantage; (ii) it could restrict access to justice in that it could deter the Surety (who was already vulnerable vis-a-vis his opponent) from contesting the Bank's claim, the Clause thus doing little to promote the rule of law.

Appeal decision

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The Court of Appeal reversed Justice Bachand's judgment on the invalidity of the Clause, but confirmed Davidovit's personal condemnation as Surety.

Firstly, the Court of Appeal pointed out that a unilateral clause is not in itself abusive. All of a borrower's obligations under a loan agreement or a surety's obligations under a contract of suretyship are unilateral, but that this fact alone cannot determine whether a clause is abusive. The logic applied by the trial judge would lead to the conclusion that the repayment of a balance due at the end of a loan is abusive, because it is unilateral.

Secondly, the fact that one party finds itself at a disadvantage is also not reason to conclude that a clause is abusive. Section 23 of the Quebec *Charter of Human Rights and Freedoms,* raised by Justice Bachand in dealing with equality of arms in a judicial process, did not apply in this case, despite the fact that a bank may appear to have more means to initiate legal proceedings than a surety does.

Thirdly, just because the law provides for a monetary sanction, such as payment of legal fees or other damages (e.g. in application of article 54 or 342 of the *Code of Civil Procedure*) for an abusive situation (e.g. a frivolous defence of a surety), this does not mean that contracting parties cannot agree to provide for such payment. The judges of the Court of Appeal held that, on the contrary, a clause for the reimbursement of extrajudicial costs and fees allows for legitimate claims to be pursued before the courts against principal debtors and sureties who refuse to pay.

Justice Schrager also took the liberty of commenting on the trial judge's conclusion regarding the qualification of the contract of suretyship as a contract of adhesion. However, considering that neither party questioned this qualification, the Court of Appeal did not formally rule on this aspect, but pointed out that the mere fact that the terms of a contract appear on a preprinted form does not necessarily mean that it constitutes a contract of adhesion, although a preprinted form may be an indication that the terms imposed are not negotiable.

The reasonableness of the amount claimed under the Clause

Although valid, the Clause must still be subject to control by the courts to ensure that the amount claimed for extrajudicial costs and fees is not abusive and is claimed in good faith. The Court found that the reimbursement of more than $31,000 in legal fees where the principal claim amounts to just over $35,000 is unreasonable and disproportionate. Given 1) the complexity of the case, 2) the amount of the claim against the Surety, 3) that the burden of demonstrating the reasonableness of the costs was on the Bank, 4) that claims for reimbursement of extrajudicial costs and fees must be exercised reasonably and in good faith (in accordance with articles, 6, 7 and 1375 C.C.Q.), the Court of Appeal reduced the claim and arbitrarily established it at $12,000.

Conclusion

Clauses for the reimbursement of extrajudicial fees have a certain acceptability in society, particularly in the commercial sphere. Even in a contract of adhesion, they are not necessarily abusive and invalid, but their application is subject to control by the courts so that they are exercised reasonably and in good faith.

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