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The Collapse of a House of Cards: Estoppel by Convention and the Need for a Shared Assumption

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In *Grasshopper Solar Corporation v Independent Electricity System Operator*,[1] the Court of Appeal agreed that a contractual party has a right to terminate a contract without paying damages if the other party does not achieve the performance to which it agreed in the contract. The Court also held that the Respondent was not estopped from terminating the contract despite an alleged shared assumption that it would not do so under the doctrine of estoppel by convention. This is because the shared assumption was found not to be between the parties but, rather, between the Respondent and third parties.

Factual Background

Grasshopper Solar Corporation, GSC Solar Fund I Inc., One Point Twenty One Gigawatts Inc., Egerton Polar Power LP, and MPI GM Solar 1 LP (collectively, the "**Solar Companies**") entered into contracts with the Independent Electricity System Operator ("**IESO**") in 2016 for the construction of solar facilities that would provide energy to the Ontario electricity grid ("**Supplier Contracts**"). The Supplier Contracts required the Solar Companies to achieve commercial operation for the facilities they were building by a specified date (called the Milestone Date for Commercial Operations ("**MDCO"**)), which was August or September 2019. The contracts also specified that:

- time was of the essence with respect to attaining commercial operations, and the parties agreed that commercial operation shall be achieved in a timely manner and by the MDCO;
- an event of default by the Solar Companies included a failure to perform any material covenant or obligation and the failure to remedy the event within 15 business days after written notice;
- an event of default *also* included the situation where the commercial operation date had not occurred on or before 18 months after the MDCO;
- the IESO may terminate the Supplier Contracts without paying damages if certain events of default occurred, including the two mentioned above. The IESO may also terminate the Supplier Contracts for other reasons, but then must compensate the Solar Companies for construction costs.

It was not disputed that the Solar Companies did not achieve commercial operations by the MDCO.

In June 2013, i.e. before the Solar Companies entered into the Supplier Contracts, the predecessor authority to the IESO dealing with new power generation contracts published a bulletin following questions raised by suppliers related to delays. The bulletin stated that for suppliers who failed to meet their MDCO, the IESO predecessor would send them a letter advising that it would not act upon its termination rights. The bulletin further stated that this was not a waiver and that the bulletin was being provided to suppliers for information purposes only.

In March 2019, the IESO sent a letter to suppliers, including the Solar Companies, reminding them of the MDCO and that a failure to

reach commercial operations by the MDCO was an event of default. The IESO also reminded the Solar Companies that the MDCO would not be extended and would be strictly enforced, with no indulgences granted. The risk of whether the MDCO was achieved was the suppliers' alone, and the IESO reserved all rights and remedies under the contract and at law.

Subsequent to this letter, in July 2019, the Solar Companies brought an application for a determination of their contractual rights under the Supplier Contracts.

The Application Judge's Decision

The application judge rejected the Solar Companies' submission that the failure to achieve commercial operations by the MDCO was not an event of default. The application judge interpreted the 18-month event of default provision as a "long-stop termination right" – a hard stop deadline with no cure period that applied if the IESO waived its right to terminate the contract for failing to meet the MDCO. The application judge concluded that this interpretation of the IESO's termination right was commercially reasonable, adding that there was no ambiguity to which the *contra proferentem* principle could be applied.

Further and importantly, the Solar Companies relied at first instance on the doctrine of estoppel by convention, arguing that there was a shared assumption that the IESO would not terminate the contract unless commercial operation was not achieved within 18 months of the MDCO. The application judge applied the test for the doctrine of estoppel by convention as set out in *Ryan* v. *Moore*, 2005 SCC 38 at para 59:

1. the parties' dealings must have been based on a shared assumption of fact or law: estoppel requires manifest representation by statement or conduct creating a mutual assumption. Nevertheless, estoppel can arise out of silence (which is implied);
2. a party must have conducted itself, i.e. acted, in reliance on such shared assumption, its actions resulting in a change of its legal position;
3. it must also be unjust or unfair to allow one of the parties to resile or depart from the common assumption. The party seeking to establish estoppel therefore has to prove that detriment will be suffered if the other party is allowed to resile from the assumption since there has been a change from the presumed position.

The application judge found that there was no shared assumption that the IESO would not terminate the Supplier Contracts for failure to achieve commercial operations by the MDCO. The 2013 bulletin was not evidence of a shared assumption and, in any event, the 2019 letter gave reasonable notice (six months) of the IESO's intention to terminate.

Court of Appeal's Decision

The Court of Appeal held that the Solar Companies' submissions failed to give effect to the time is of the essence clause, which was fatal to their argument. According to the Court, this clause makes it clear that the parties agreed that commercial operation was to be achieved in a timely manner and that time was of the essence. "Time is of the essence" provisions have a clearly defined meaning and are well understood. Having a cure period or notice period does not nullify a time is of the essence clause. Therefore, strict compliance with the MDCO was required.

Estoppel by Convention

The Court of Appeal further held that neither estoppel by convention nor promissory estoppel applied to this case. The doctrine of estoppel cannot vary the terms of a contract, but it may operate to prevent a party from relying on the terms of a contract to the extent necessary to protect the reasonable reliance of the other party. Given that the doctrine can undermine the certainty of contract, it must be applied with care, especially in the context of commercial relationships between sophisticated parties represented by lawyers.

The Court of Appeal further commented that estoppel by convention is a relatively rare form of estoppel that may arise when both parties to a contract act based on a shared assumption concerning circumstances relevant to their contract. If it would be unfair to allow a party to resile from the assumption, the doctrine operates to provide a remedy for detrimental reliance on the assumption by the other party. The Court further emphasized that estoppel by convention requires a "manifest representation" of a *shared* assumption, which may arise out of a statement or conduct, but may also arise from silence. The shared assumption must be "unambiguous and unequivocal". This requirement goes to the very purpose of the doctrine.

The Solar Companies argued that two of the three elements were present for estoppel. The Court of Appeal held that a shared assumption was not just a remaining element, but the crux of estoppel by convention that gave rise to the need for equitable relief. Without a shared assumption, there can be no reliance and no detriment, and therefore no equitable relief. The house of cards collapses.

In this case, the assumption arose out of dealings between the IESO and other suppliers, i.e. the IESO's past practice of not terminating suppliers for failing to achieve commercial operation by the MCOD, not between the IESO and the Solar Companies. The Court of Appeal held that there was no basis to interfere with the application judge's finding that the Solar Companies' assumption that the IESO would continue to follow its existing policy of not terminating contracts as a result of a supplier's failure to meet the MCOD was not shared by the IESO.

The same result follows if the claim is analyzed through the doctrine of promissory estoppel.

Promissory Estoppel

Promissory estoppel involves a promise by one party not to rely on its strict contractual rights. Where such a promise has been made with an intention that the other party will rely on it, and that party relies on the promise to his or her detriment, the party who made the promise is estopped from acting inconsistently with it. As with a shared assumption, although the promise does not vary the terms of the contract, the party who made the promise may be precluded from resiling from it to the extent necessary to protect the position of the party who has relied on the promise to his or her detriment.

The Solar Companies relied on the 2013 bulletin to argue that a promise was made not to enforce on the MDCO immediately. However, the bulletin was not a promise *to* the Solar Companies, but was directed to suppliers holding these types of contracts at the time.

While the Solar Companies may have assumed that time limits they contracted to meet did not really matter, the IESO did not share that assumption nor did it promise that it would not enforce the time limits. Detrimental reliance does not arise if there is no shared assumption nor a promise on which the Solar Companies could have relied to their detriment. In the absence of a finding that there was a shared assumption or a promise that was reasonably relied upon by the Appellants, the question of fairness did not arise. The Court of Appeal concluded that there was no basis to interfere with the contractual terms that the Solar Companies and IESO chose, and the consequences provided for in the contract for the breach of such terms.

Conclusion

This case provides clarification of the doctrine of estoppel by convention and promissory estoppel. While the law has not changed from 2005, this case provides clarity that the doctrine only applies when the conjunctive test is satisfied. The foundation of the conjunctive test is built on the relationship between the parties, how they have conducted themselves and what they represented to each other. If part of the conjunctive test is absent, the legal house of cards falls.

[1] *Grasshopper Solar Corporation v Independent Electricity System Operator*, 2020 ONCA 499.

The information and comments herein are for the general information of the reader and are not intended as advice or opinion to be relied upon in relation to any particular circumstances. For particular application of the law to specific situations, the reader should seek professional advice.

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