Cassels

Sweet Relief: British Columbia Court of Appeal Upholds Mutual Cancellation and Release Agreement Between Franchisor and Franchisee

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Franchisors can be reassured by a recent decision of the British Columbia Court of Appeal (*Dairy Queen Canada, Inc. v. M.Y. Sundae Inc.*) that affirmed the use of Mutual Cancellation and Release Agreements as a means to resolve franchise disputes while protecting franchisors against future claims.

In a May 2017 newsletter, we reported on a decision of the British Columbia Supreme Court that endorsed the use of a Mutual Cancellation and Release agreement as a means of terminating a franchise agreement. In that case, Dairy Queen Canada, Inc. (Dairy Queen), the franchisor, presented the Mutual Cancellation and Release Agreement to a franchisee that was in default of various obligations under its franchise agreement. In lieu of immediate termination, the Mutual Cancellation and Release Agreement gave the franchisee the opportunity to continue to operate for six months, during which it could sell its business, provided that the franchisee complied with the franchise agreement during the six month period. Importantly, and as its title would suggest, the Mutual Cancellation and Release Agreement contained a release of the franchisee's claims against the franchisor.

After signing the Mutual Cancellation and Release Agreement, the franchisee pursued claims against the franchisor for breach of contract, as well as various breaches of the *Arthur Wishart Act (Franchise Disclosure), 2000* (the Wishart Act), including breach of the duty of good faith and fair dealing.

In the original decision, the Supreme Court of British Columbia upheld the Mutual Cancellation and Release Agreement and found that it was a complete bar to the franchisee's claims. The Court rejected the franchisee's arguments that the Mutual Cancellation and Release Agreement had been signed under duress or should be disregarded on grounds of unconscionability.

The franchisee appealed this decision to the Court of Appeal for British Columbia, which upheld the lower court's decision.

As part of the appeal, the franchisee brought a motion to adduce fresh evidence from a hand-writing expert in support of a novel argument that the Mutual Cancellation and Release Agreement had not been signed at all. In dismissing the motion, the Court held that the proposed fresh evidence was "more than simply new evidence. This is a reversal of the entire case that [the franchisee] took to trial."

The Court also rejected the franchisee's argument that the Mutual Cancellation and Release Agreement had been entered into under duress, and endorsed the trial judge's finding that the offer to forbear enforcement in exchange for entering in the Mutual Cancellation and Release Agreement was nothing more than "legitimate commercial pressure." The Court explained:

In this case, Dairy Queen was asserting a contractual right to terminate the franchise agreement for failure to abide by its terms. The Mutual Cancellation and Release was presented as an alternative to immediate closure to provide time for Mr. Richards to wind up the business in an orderly fashion. The trial judge concluded that:

… the Cancellation and Release is more generous on its face than the [Franchise] Agreement itself, allowing the franchisee time to recoup its investment through the sale of an operating franchise rather than immediate termination of the Agreement and an accompanying demand to cease and desist.

The trial judge appears to have accepted that the proposal of Dairy Queen to provide additional time to the appellants in return for the Mutual Cancellation and Release fell within the range of legitimate commercial pressure. I can see no error in this conclusion.

The Court of Appeal also rejected the franchisee's argument that the timeline to review and sign the Mutual Cancellation and Release Agreement was insufficient and amounted to illegitimate pressure. Rather, the Court found that the ten-day period provided was ample time for the franchisee to explore its legal options. The Court explained:

[The franchisee] had known since April that Dairy Queen was taking the position that if he did not adhere to the standards required of the franchise, Dairy Queen could shut the business down. He had ample time to explore legal options before August 9. The trial judge determined that he had seen the document on July 31 and also that it was a document with which he was familiar. He could have refused to execute it, and defended any termination on the merits. This is not a case in which the demand was made without warning and without notice, leaving him with no option but to sign.

The Court of Appeal fully endorsed the trial decision below, holding that there was "no error in the trial judge's thorough analysis and certainly no palpable and overriding error."

The Court's decision confirms that mutual cancellation and release agreements can be valuable tools for franchisors looking to end unworkable franchise relationships while limiting their liability. In these circumstances, the agreement can also be beneficial to franchisees that would otherwise face immediate termination for breaches of the franchise agreement. Instead, the franchisee will hopefully be able to find a buyer and recoup some or all of its investment in the franchise. For these reasons, before effecting a termination, franchisors should consider whether a mutual cancellation and release agreement could provide a mutually beneficial way to end the relationship while (hopefully) avoiding conflict.

A copy of the trial decision is available here.

A copy of the appeal decision is available here.

Dairy Queen was represented by Colin Pendrith of Cassels at the summary trial and on appeal.
