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BRIEFING NOTE

SCC says buyer that waived its right to test goods is out of luck

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Introduction

In ***Earthco Soil Mixtures Inc. v. Pine Valley Enterprises Inc.*, 2024 SCC 20** ('*Earthco.*'), a buyer who was in a rush to purchase topsoil sued the seller for damages upon receiving sub-standard soil, despite having waived its rights to test the soil. The majority of the Supreme Court of Canada ('SCC') found that the exclusion clauses that the parties had expressly agreed upon exempted the seller from any statutory liability under section 14 of Ontario's *Sale of Goods Act* ('*SGA*'). This decision is significant to the interpretation of exclusion clauses within sale of goods contracts and contracts generally. If a dispute goes to court, the absence of "magic words" in a contract will not make or break a decision. Courts will look for a meeting of the minds which does not necessitate specific legal language.

In *Earthco,* The buyer had contracted with the seller to obtain topsoil with a specific composition. The seller provided the buyer with laboratory reports from different topsoil samples taken about six weeks prior, and warned the seller against going through with the purchase without obtaining updated test results. Having already missed project deadlines, the buyer waived its right to test the soil and insisted on immediate delivery.

The buyer and seller agreed to add two exclusion clauses to the standard purchase order, which stated that the buyer had the right to test and approve the material before it was shipped and, if the buyer waived those rights, the seller would not be responsible for the "quality" of the material once it left its facility.

After the topsoil was delivered and placed on the project site, testing revealed that there was substantially more clay in the topsoil than the laboratory reports had indicated and the buyer incurred the cost of removing and replacing the soil. The buyer sued the seller for damages, alleging that it did not received topsoil within the range of compositional properties that had been initially indicated.

The SGA

The SGA incorporates implied conditions and warranties into most contracts for the sale of goods. However, buyers and sellers are free to contract out of these statutory terms in many instances. Section 14 of the SGA sets out an implied condition that goods must correspond with their description and section 53 permits parties to vary or negative this, by way of an express agreement or usage (if the usage is such as to bind both parties to the contract).[1] It is important to note that there are no magic words required to contract out of the statutory terms. An agreement will be considered "express" for the purposes of these kinds of provisions if the parties have made their intention to override them unambiguous, using explicit language.

The SCC Analysis

In determining what qualifies as an "express agreement", courts look to principles of contractual interpretation and the law concerning exclusion clauses. In this case, the SCC emphasized that the paramount consideration must be the objective intention of the parties.[2] To find the intended meaning of words in a contract, courts will often look to the surrounding circumstances, often referred to as the "factual matrix". The word "quality" in exclusion clauses must be interpreted in a manner that is consistent with these contextual factors.

In Earthco, the objective intent of the parties' express agreement was that the buyer accepted the risk that the topsoil would not meet the previously supplied specifications regarding its composition if the buyer failed to test what it knew was an organic and changing substance. The buyer was a commercial purchaser with years of experience in buying large quantities of topsoil and deliberately assumed the risk, through its own conscious strategic decision, as it was free to do.

Enforceability of exclusion clauses

Exclusion clauses such as those under section 53 of the SGA are subject to their own set of legal rules because they raise distinct policy considerations. The SCC has directed that the factual matrix must be considered in order to determine the meaning of words in a contract and exclusion clauses ought to be analyzed in light of their purposes and commercial context.[3] To assess the

[1] Equivalent to sections 17 and 69 of BC's Sale of Goods Act, respectively.
[2] In Sattva Capital Corp. v. Creston Moly Corp., 2014 SCC 53 ('Sattva'), the Court stated how agreements should be interpreted and reviewed, and explained how the jurisprudence has shifted towards a more flexible, practical, and common-sense approach with a view to ascertain the objective intention of the parties.
[3] Sattva's direction to consider the surrounding circumstances when interpreting the terms of a contract means exclusion clauses must be analyzed in light of their purposes and commercial context.

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enforceability of an exclusion clause, courts will usually refer to a three-step test[4]:

1. Does an exclusion clause exist in the circumstances?
2. If an exclusion clause exists, was it unconscionable at the time the contract was made?
3. Even if the clause was not unconscionable, is there some overriding public policy consideration that outweighs the strong public interest in the enforcement of contracts?

The first step necessarily depends on an assessment of the intention of the parties and this is where a court should determine whether there is an express agreement that is sufficient to meet the requirements of a provision such as 53 of the *SGA.*

Conclusion

The SCC has confirmed that Sale of Goods statutes were never intended to be exhaustive or compressive codes and that they ought not to be applied too rigidly or to the exclusion of the freedom of parties to contract within the general limits of the law.[5]

The SCC's main task in *Earthco.* was to set out the proper way to interpret exclusion clauses in contracts for the sale of goods. The terms "quality" and "identity" have different legal meanings. Case law has distinguished between traits that go to the identity of goods (which pertains to description), and those which go to the quality of goods (which pertains to merchantability and fitness for purpose). The exclusion clauses in this case did not directly refer to any statutory conditions or to the identity of what was being sold. This was the main point of contention between the Court of Appeal ('CA') and the SCC.

The CA found that the reference to the quality of the good in the exclusion clauses was not sufficient to oust the liability implied by section 14. It emphasized that the implied condition in section 14 relates to the identity of goods. It found that the trial judge had erred when interpreting the exclusion clauses by failing to properly give effect to the requirement that explicit, clear and direct language be used to exclude a statutory conditions and as a result, did not recognize the exclusion clauses' failure to refer to the identity of the goods or to statutory conditions.

The SCC disagreed with the CA's strict interpretation and found that to expect parties to include proper legal language is a commercially impractical expectation and takes the focus away from where it should be: how the parties reasonably understood, or ought to have understood the words they used.

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[4] The test was set out in *Tercon Contractors Ltd. v. British Columbia (Transportation and Highways)*, 2010 SCC 4 ('*Tercon*').

[5] In particular, the principles in *Sattva*, and *Tercon*, which give priority to the parties' intentions, apply to the contracts subject to the *SGA.*

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