Can you ever advise a client to ignore foreign proceedings?

The effects of *Beals v. Saldanha*


J. Brian Casey

Your client, the owner of an electrical supply company in Gravenhurst Ontario, arrives with a claim issued out of the courts of Xanadu. The claim alleges damages of "at least $15,000" for failure to deliver electrical parts under a purported supply contract. Your client says he has never been to Xanadu and does not do business there. He does recall answering a general inquiry e-mail requesting information about high-voltage circuit breakers that the company advertises on its Web site. Your client recalls he e-mailed the price for the devices and possible delivery dates, but no contract was ever entered into.

The recent Supreme Court of Canada decision in *Beals vs. Saldanha* has settled many open issues with respect to the treatment of foreign claims and foreign judgments in Canada. While the Supreme Court may have settled the law, its decision has unsettling consequences for Canadian businesses wishing to sell products or do business in foreign jurisdictions, including your client from Gravenhurst.

In a 6-3 split decision, the *Beals vs. Saldanha* court upheld a default judgment for US$260,000 from a Florida state court, which arose out of an $8,000 real estate transaction. With interest and costs, by the time of the Supreme Court decision, the judgment was in excess of CDN$1million.

At its essence, the *Beals* case established the test that Canadian courts should apply in determining if a foreign court properly took jurisdiction over a Canadian defendant and the defences available to a defendant in Canada who wishes to dispute recognition and enforcement of a foreign judgment. This article will look at the practical consequences of the Court's decision and end with a short discussion as to how clients may avoid some of the pitfalls of doing business internationally.

In 1981 the Saldanhas and the Thivys, who had been friends for many years, bought a lot in a Florida subdivision for $4,000,[1] thinking that one day they might build a vacation home on it. They never visited the lot nor saw pictures of it.

In the summer of 1984, Rose Thivy was telephoned by a real estate agent in Florida, who said he had a prospective purchaser for the lot. After discussing the call with her co-owners, Mrs. Thivy advised they would sell the lot for U.S. $8,000. A written offer arrived in the mail. Mrs. Thivy noticed it referred to "Lot 1" in the subdivision while the lot owned by the Thivys and Saldanhas was "Lot 2." After discussions with the agent, she changed the figure from "1" to "2." The counteroffer was accepted and the transaction closed in late September, 1984, transferring Lot 2 to Mr. and Mrs. Beals.[2],

In January, 1985, Mr. Beals telephoned Mrs. Thivy and told her he had been sold the wrong lot. She told him of her discussion with the agent and suggested that Mr. Beals contact him.

In February, 1985, the purchasers commenced an action in Florida (the "first Florida action") against the Thivys, the Saldanhas, the agent and others. The Complaint alleged the purchasers and vendors had agreed to sell lot 1, but that after closing, and after commencement of construction of a model home on the property, the Beals learned they didn't own

Lot 1. The Complaint sought damages "which exceed $5,000."

The Saldanhas and Thivys did not hire a lawyer but collectively filed a defence setting out the facts as they knew them. In September, 1986, a Notice of Dismissal of the action was received and they thought that was the end of the matter.

In September, 1986, a second Florida Complaint was served. The claims were identical to the first action, but with the added claim that the defendants had represented they owned Lot 1, and that this representation was "knowingly and willfully false and fraudulent." Mrs. Thivy again filed a joint defence, exactly as had been done in the first action.[3]

Two Amended Complaints were subsequently received, but the amendments were directed against the other defendant, the agent and title insurer, with no new claims made against the Saldanhas or Thivys. The Saldanhas and Thivys did not deliver a defence to these Amended Complaints. Unknown to the defendants, under Florida procedural law, there was an obligation to deliver a defence to each and every amended Complaint even if no new allegations are made against you. Accordingly, default judgment was entered for failing to file a defence, with a jury trial directed to assess damages. The jury awarded the plaintiffs $210,000 for compensatory damages and US$50,000 for punitive damages.

An action was then commenced in Ontario to enforce the Florida judgment. In the course of the Ontario action it was determined that there was no transcript of the oral evidence at the Florida trial, but all of the exhibits filed were with respect to expenses claimed for preparing the lot for construction and a claim for lost profits related to a corporate entity owned by the plaintiffs. This corporation, which had been dissolved prior to the Florida judgment being obtained, was not a party to the Florida action.

The Ontario trial judge, Mr. Justice Jennings, dismissed the action on a number of grounds, including fraud in relation to the claim for damages and on the ground of public policy. In so doing he broadened the defence to include what he called a "judicial sniff test."

On appeal, the majority of the Court of Appeal overturned the decision. On the issue of fraud, in addition to disagreeing with the trial judge on his factual findings, the court held that while fraud which goes to the merits of the claim may be a ground for setting aside a foreign judgment, it is only applicable to cases where the fraud is revealed through newly discovered facts that could not have been discovered through the exercise of reasonable diligence. Since the Saldanhas had chosen to ignore the Florida proceedings, the majority held the trial judge erred in failing to limit the evidence to those facts that would not have been discovered if the defendants had appeared and defended the Florida action.

The majority of the Court of Appeal also disagreed with the trial judge's conclusions regarding public policy. They held the trial judge's reasoning was an unwarranted broadening of the doctrine.

The Supreme Court by a 6 to 3 majority dismissed the appeal. In so doing, the Court clarified the common law regarding the recognition and enforcement of judgments from foreign jurisdictions.

The real and substantial connection test

Although not necessary for the determination of the case, the Court took the opportunity to settle the question of whether the real and substantial connection test, as set out in the *Morguard* decision for inter-provincial cases, ought to be used in determining jurisdiction in foreign court proceedings.

The Court held that the "real and substantial connection" test is the appropriate test for both foreign and inter-provincial cases. The Court also clarified the meaning of the test to confirm that the "connection" may be a personal connection the defendant has with the jurisdiction, or it may be a connection with the subject matter of the action. Where a Plaintiff seeks to have the foreign court take jurisdiction based on the defendant's personal connection with the forum, a fleeting or relatively unimportant connection will not be sufficient. Personal connection would include circumstances where the defendant had a plant or office in the jurisdiction or was carrying on business there. Also, if the defendant, by contract or by conduct, has submitted to the jurisdiction, there is clearly a real and substantial personal connection between the forum and the defendant. In most cases, it will be sufficient to satisfy the real and substantial connection test if harm is occasioned in the jurisdiction by a defendant who "knew or ought to have known damage could occur in that foreign jurisdiction by reason of his actions" on the basis that there is a connection with the subject matter of the action.

In keeping with recent Ontario Court of Appeal decisions, the Supreme Court also held that reciprocity is part of the real and substantial connection test. The concept of reciprocity provides that if a Canadian Court would take jurisdiction over a foreign defendant in similar circumstances, then the Canadian Court should recognize the foreign court's jurisdiction over a Canadian defendant.

In our example, if the circuit breakers had been shipped to Xanadu and were faulty, the courts of Xanadu would have a real and substantial connection with the subject matter of the action, just as a Canadian court would do if the fact situation were reversed.

Difficulties arise under our example, where the claim is for damages for failure to deliver in Xanadu and your client states there never was a contract for delivery and, if there were, goods would not be shipped until paid for. In this case the plaintiff in Xanadu can say damages were suffered there, but there appears to be no other connection with that jurisdiction.

If the Canadian defendant decides not to appear in Xanadu the court there may well take jurisdiction, and it becomes difficult to determine what a Canadian court

would decide when the judgment is brought here for enforcement. Under the reciprocity theory, a Canadian court might well decide it had jurisdiction solely on the grounds that damages were suffered here, particularly where the defendant does not appear and where provincial rules of civil procedures permit service out of the jurisdiction based solely on damages having been suffered in that jurisdiction.

The impeachment defences

In our example, let's presume your client decides not to go to the time and expense of defending the action in Xanadu. Nothing is heard for two years until your client shows up with a Statement of Claim from the Ontario court claiming $100,000, based on a judgment from the High Court of Xanadu. The claim is based on a default judgment entered against your client and includes judgment for quadruple the amount of the contract, based on a Xanadu statute designed to prevent internet fraud.

In *Beals*, the Supreme Court confirmed that absent very extraordinary circumstances (which the court did not articulate) the defences to the enforcement of a foreign judgment are (1) fraud, (2) the denial of natural justice, and (3) public policy. It is clear from the Court's decision that the impeachment defences are to remain narrow in scope, notwithstanding the broadening of the real and substantial connection test for jurisdiction.

Fraud

The Supreme Court has clarified the issue of whether intrinsic or extrinsic fraud may be raised as an impeachment defence. The Court has done away with the distinction which had been applied in some provinces that only fraud going to the foreign court's jurisdiction (extrinsic fraud) could be raised as a defence in Canada.

In our Xanadu example, if your client was correct that no contract was ever entered into, yet the plaintiff fraudulently convinced the Xanadu court that a contract existed and goods which ought to have been delivered were not, then this would be considered fraud going to the foreign court's jurisdiction. In fact, there was no real and substantial connection to the court.

Intrinsic fraud, on the other hand, deals with the evidence actually led by the plaintiff during the hearing of the proceedings. In many cases, there is a concern that the failure of the defendant to defend the claim gives the plaintiff a licence to exaggerate or mislead the court during the proceedings. Henceforth either extrinsic or intrinsic fraud to the recognition or enforcement of a foreign judgment may be a defence. The restriction on raising the defence of intrinsic fraud, however, is that the allegation of fraud must be based on new and material facts, or newly discovered facts, which the defendant could not have discovered and brought to the attention of the foreign court through the exercise of reasonable diligence.

In the *Beals* case, the Supreme Court held the trial record did not disclose any new facts that could not have been discovered had the defendants appeared in the foreign court. Had the defendants appeared in the Florida action, they would have discovered the existence of the documents which appeared to show the losses were from a corporate entity and not the plaintiffs. By introducing the concept of discoverability of evidence and due diligence, the Court has determined that if the foreign court has properly taken jurisdiction, a Canadian defendant cannot raise allegations of fraud if the material facts upon which the defendant now wishes to rely could have been detected by the exercise of reasonable diligence using the foreign court's procedure.

In our example, if there had been a contract and the Xanadu court had jurisdiction, any fraudulent inflation of the damages claim in the Xanadu court would not be grounds for refusing enforceability in Canada, unless the evidence could not have been discovered at the time by reasonable diligence. A Canadian party cannot fail to appear in foreign legal proceedings that are properly constituted and then complain later of an excessive or fraudulent judgment. Once the Xanadu court had properly taken jurisdiction under the real and substantial connection test, the failure of the defendant to appear and defend would seem to preclude any allegation of fraud in Canada, as to do so would be an attempt to re-litigate the foreign decision. The Gravenhurst electrical contractor ignores the foreign proceeding at his peril.

Natural justice

The Supreme Court also held in the *Beals* decision that the defendants had sufficient notice of their jeopardy, notwithstanding that the claim contained less information than would be required in a Canadian pleadings. The Court stressed, however, that a Canadian court must be satisfied that the foreign court has followed and applied minimum standards of fairness. In Canada, it is fundamental that the judicial process is such that the defendant knows the case to be met and a fair opportunity to be heard.[4] The burden remains on the defendant to demonstrate, on the balance of probabilities, that these minimum standards were not met.

The domestic court must also be satisfied that the defendant was granted fair process by means of both judicial independence and fair ethical rules. In the *Beals* case, the fact that the Complaint simply claimed "an amount in excess of $5,000" was not a problem, as Florida's extensive discovery rules gave the defendants an opportunity to know the case against them. Similarly a reference

to "lost profits" in the Complaint was sufficient to inform them of their jeopardy that some amount under this head of damage was being claimed.

The Court also found that there was no evidence that the process used by the Florida Court could be considered unfair. The defendants were advised of the case they had to meet and were given a fair opportunity to defend under U.S. law. The fact they were noted in default by reason of their failure to understand Florida court procedure was their fault, as the Florida court clearly had jurisdiction over the subject matter of the action, namely the land.

The lesson is that so long as the pleading sets out the types of damages claimed by a plaintiff this would be sufficient notice to satisfy Canadian standards of natural justice. In addition, if the foreign court has a real and substantial connection with either the Canadian defendant or the subject matter of the action, the Canadian defendant is now responsible for understanding that foreign court's rules of procedure. Ignorance is no excuse.

In our example, if our Gravenhurst contractor had concerns about the court process, in Xanadu it would be up to him to show that the foreign court has not followed or applied minimum Canadian standards of fairness. The onus is on him. If there was a concern about judicial corruption, it is unclear whether it would be necessary to show that the particular judge in this particular case was corrupt, or whether it is sufficient to show that the judicial system generally is corrupt. The latter test is followed in the United States.

Public policy

With respect to the impeachment defence of public policy, the Supreme Court has confirmed that this defence is directed at the concept of repugnant laws, not repugnant facts. Public policy remains a very narrow ground of defence and will be used sparingly. There is no "judicial sniff test" under Canadian law. The Court has confirmed that substantial damages beyond that which a Canadian court might award is not, in and by itself, sufficient to raise a public policy defence.

In our Xanadu example, the fact that a local statute provided for quadruple damages may not be sufficient to raise a public policy defence. As Xanadu had jurisdiction over the defendant, the defendant cannot now complain about how it was treated, but rather must establish the Xanadu law regarding quadruple damages is somehow repugnant to Canadian public policy generally and ought not be enforced. It is doubtful a law purporting to deliver harsh penalties for internet fraud would be considered against Canadian public policy.

The lessons of *Beals v Saldanha*

As can be seen from this review of the impeachment defenses, there will be little for a Canadian defendant to argue if the foreign court has properly taken jurisdiction. The defenses of fraud, natural justice and public policy remain narrow in their application. Counsel faced with a client who has been sued in a foreign jurisdiction must be careful not to downplay the possibility of the foreign court's jurisdiction being upheld in Canada, or exaggerate the prospect that a Canadian court will apply one of the impeachment defenses to a resulting foreign judgment.

While most of the following points are self-evident, they bear repeating in light of the problems exemplified in *Beals* and the difficulties which may be encountered when advising a Canadian defendant who has been sued in a foreign jurisdiction.

1. Remind the client that you are only advising with respect to the law in the Canadian jurisdiction in which you are qualified. Any attempt to interpret the foreign proceeding or opine as to its reasonableness is dangerous, and would not be covered under the LawPRO liability policy.
2. Advise your client you can only give an opinion based on the material which is presently before you. The discovery process will likely turn up facts which could alter your opinion.

   Also, should your client receive further documentation from the court or the foreign plaintiff, your opinion may change. A full and complete inquiry of the facts known to your client must be undertaken so as to determine all the connections that might exist under the real and substantial connection test.
3. Initially, without the assistance of foreign counsel, your advice must be limited to an assessment, based on the facts as you have them, of whether a Canadian court will eventually take jurisdiction under the real and substantial connection test if your client decides not to appear in the foreign jurisdiction. While the impeachment defences can also be explained and discussed, it is almost impossible to determine whether any of the impeachment defences will be applicable. It is dangerous to provide any opinion with respect to the impeachment defences prior to the full extent of the foreign case and the foreign procedures being known.
4. You should urge the client to retain foreign counsel if for no other purpose than to provide an opinion as to whether the foreign court will take jurisdiction and what applicable procedural rules apply. It is only when the client is fully informed of the risks of attending in the foreign jurisdiction against the risks of waiting for the judgment to come to Canada to be enforced that he or she can make a reasoned decision. You can only provide an opinion respecting what a Canadian court might do with a foreign default judgment. You are not providing your client with the other half of the equation that he or she will need before deciding what course of action to take.

5. Paper the file and do a full report to the client. It may be years before a foreign judgment is brought to Canada for enforcement. It is also important to remind the client that if other documentation is received from the foreign court or new facts uncovered, this may well affect either your opinion, or that of foreign counsel who has been retained to assist.
6. Consider a declaratory application in Canada or the prospects for an anti-suit injunction. Foreign counsel should also be asked about conditional appearances to challenge the foreign jurisdiction.[5]

Avoiding foreign court proceedings

The example of a Gravenhurst electrical contractor being sued in a foreign court is no longer far-fetched. Canadian goods and services are sold worldwide and the number of Web-based transactions continues to grow. When advising a client with respect to carrying on business internationally, a lawyer should keep in mind that disputes will arise and that the client should do everything possible to avoid being sued in a foreign court.

While local businesses may be able to get away with a somewhat casual use of its commercial paper, uncertainty as to the details of an international commercial contract is dangerous. The more uncertainty as to the terms of the contract, the more likelihood there is the Canadian party will be a defendant in an unwelcome and unfriendly foreign jurisdiction.

The usual approach in international contracts has been to include a clause providing that the contract is to be interpreted under provincial and/or Canadian law with the exclusive jurisdiction of a provincial court. While this may be sufficient in many cases, there are a number of jurisdictions that will not enforce such a clause by reason of their local public policy. In other cases, the foreign party will refuse to accept such a clause but will instead either insist on its laws and its jurisdiction or, at the very least, a non-exclusive jurisdictional clause.

The most common method used by international business to avoid foreign court proceedings is by the use of a properly crafted arbitration agreement. International commercial arbitration is not mediation or conciliation. It is litigation, but the case is presented to a neutral arbitral tribunal. A property drafted arbitration clause is capable of having all disputes arising out of or in any way connected with a particular contract arbitrated rather than litigated. Claims sounding in contract, tort, equity, or statute, are all capable of being arbitrated. Legal and equitable relief can be granted including injunctions, specific performance and punitive damages.

New York Convention

One hundred and thirty four countries[6] have signed the United Nations Convention on the Reciprocal Enforcement and Recognition of Foreign Arbitral Awards, commonly referred to as the New York Convention.

Under this Convention, the courts of a signatory country must refer a matter to arbitration if the parties have entered into an international commercial arbitration agreement. The wording of the Convention is mandatory and the court must refer the parties to arbitration unless the arbitration agreement is null and void, inoperative, or incapable of being performed. The test as to whether the clause is null and void, inoperative or incapable of being performed will be determined under the law that the parties have agreed governs the arbitration agreement. Local law may have no application.

In Canada, each province has adopted the New York Convention either directly or through the adoption of the International Arbitration legislation[7].

Our Xanadu example also points out some of the additional problems which can occur with sales over the internet. By its nature, the internet is global and clients should be advised to make sure any sales over the internet require a purchaser to click and accept the terms of sale which includes a provision that the contract is governed by provincial and Canadian law, and that any dispute controversy or claim arising out of or in any way connected with the contract will be resolved by international commercial arbitration.

If Xanadu is a signatory to the New York convention, then the court will be faced with very strict limits on its jurisdiction. Should the plaintiff fail to disclose the arbitration clause, it can be argued the foreign court took jurisdiction by reason of the fraud of the plaintiff. As Xanadu has no personal jurisdiction over the defendant, there cannot be any real and substantial connection with the cause of action as the court was to refer the parties to arbitration under the New York Convention.

J. Brian Casey is a partner at Baker & McKenzie.

1 All amounts are in U.S. dollars

2 The agreement also involved another couple as purchasers, but they transferred their interest to the Beal's after judgment in Florida.

3 This was done without the consent or knowledge of the Saldanha's, but in the result nothing turned on this.

4 Rodaro v. Royal Bank of Canada (2002) 59 O.R. (3d) 74 (Ont. C.A.)

5 Amchem Products Inc. v. British Columbia Workers' Compensation Board [1993] 1 S.C.R. 897

6 Available at www.uncitral.org/en-index.htm

7 In Ontario, see the Ontario International Commercial Arbitration Act, R.S.O. 1990, c. I.9, which adopts the UNCITRAL Model Law.