

**Uniform Law
Conference of Canada**

***Uniform Illegal
Contracts Act***

UNIFORM ILLEGAL CONTRACTS ACT

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Interpretation

1 In this Act:

“**contract**” includes

- (a) an agreement, a trust, a transaction and an arrangement,
- (b) any provision of an agreement, a trust, a transaction or an arrangement, including a provision transferring or otherwise disposing of property, and
- (c) if the context requires, the instrument recording the contract; (« contrat »)

“**court**” includes a tribunal, and an arbitrator, acting within its proper jurisdiction; (« tribunal »)

“**defect**”, in relation to a contract, means whichever of the following results in the contract becoming an illegal contract:

- (a) the formation, existence or performance of the contract does not comply with or is contrary to an enactment;
- (b) by virtue of a rule of equity or common law, the contract is contrary to public policy;
- (c) a party to the contract lacked status, capacity or power to enter into the contract;
- (d) the operation of an enactment, or of a rule of equity or common law, affects the enforceability of the contract other than in the manner contemplated by paragraph (a) or (b); (« vice »)

“**enactment**” means any primary or subordinate legislation passed by the legislative or executive branch of any level of government in Canada, including any legislation passed by any minister or other official of such a government that is passed in accordance with that person’s authority; (« texte »)

“**illegal contract**” means a contract that is null, void, voidable, illegal, unlawful, invalid, unenforceable or otherwise ineffective as a result of a defect; (« illégal »)

“**performance**” includes intended performance; (« exécution »)

Comment: The key definitions in section 1 are “contract,” “defect” and “illegal contract”. These cast a wide net to bring within the Act as many kinds of transactions as possible that may be vitiated for one reason or another. The repetition of the various synonyms for the concept of the vitiation of a contract is deliberate in the definition of “illegal contract.” The purpose is designed to track as many statutory formulations as possible and put beyond doubt the applicability of this Act where these words are used in another enactment. Section 2 adds a gloss to the definitions. Later in the Act, in section 3(3), certain kinds of illegal contracts are excluded from its operation.

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The approach that consists in defining a contract as including various legal instruments which are not contracts would not be consistent with civil law methodology. For the Act to be implemented in Québec, its substantive provisions, once redrafted in civilian form, should find their way into the *Civil Code* of Québec, within the existing provisions relating to the nullity of contracts (art. 1416 ff.). The result pursued by the definition of “contract” would then be achieved automatically, since the rules governing nullity of contracts may always be extended by analogy to other juridical acts, without its being necessary to provide an explicit definition to that effect.

The definitions of “defect” and “illegal contract” cover the full range of absolute or relative nullities in Québec law. There are two categories of rules which may bring about the absolute or relative nullity of a contract. The first are those which relate to the procedure of contract formation. The second are those which concern public order, either statutory or based on general moral or social imperatives recognized by the courts.

“**property**” means an obligation, power, interest, right or thing, of any type, that is the subject matter of an illegal contract. (« bien »)

Comment: The term “property” is used in section 4(2). The concern it addresses is where property is purported to be transferred under an illegal contract and the property is then the subject of a further transfer to a person who is not a party to the contract. If this transferee’s title is called into question the court can grant relief to the transferee.

Exception

2 Despite the definitions of “defect” and “illegal contract”, the fact that the formation, existence or performance of a contract does not comply with or is contrary to an enactment, or that a contract does not comply with a formality required by an enactment, does not render the contract null, void, voidable, illegal, unlawful, invalid, unenforceable or otherwise ineffective unless that result is clearly required

- (a) by the enactment, or
- (b) in order to further the enactment’s purpose.

Comment: Section 2 creates a benevolent rule of interpretation designed to ensure that contracts are not characterized as illegal owing to the violation of a feature of a statute that is not central to its operation.

The benevolent rule of interpretation is recognised by Québec courts and legal scholars. A codification of the rule in the *Civil Code* of Québec would be desirable.

Application

3(1) This Act applies to an illegal contract whether or not

- (a) subject to subsection (2), the contract was entered into before or after the coming into force of this Act, or
- (b) the defect is a provision of the contract and that provision is severable.

Comment: Subject to subsection (2), the Act applies retrospectively to existing contracts. The remedy of severance is provided in section 5(1)(g).

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(2) This Act does not apply to an illegal contract that was entered into before the coming into force of this Act if, within a proceeding commenced before the coming into force of this Act, the contract is challenged as being null, void, voidable, illegal, unlawful, invalid, unenforceable or otherwise ineffective as a result of the defect.

Comment: The Act applies retrospectively to existing contracts except where the illegality is the subject of litigation at the time the Act comes into force.

(3) Despite subsections (1) and (2) but subject to section 4(2), this Act does not apply to an illegal contract if

(a) the defect is that the formation, existence or performance of the contract does not comply with or is contrary to an enactment and the enactment expressly sets out the relief that may be granted in relation to such a contract, [the following are optional]

(b) the defect arises through the operation of [limitation statute of enacting province] or legal or equitable doctrines relating to delay,

(c) the defect is that the contract is not in writing or signed or witnessed as provided by an enactment,

(d) the defect is that the contract calls for the creation or vesting of a right and, under the contract, that creation or vesting will occur later than the time at or before which the creation or vesting must occur under an enactment or at common law,

(e) one or more parties to the contract are minors,

(f) the contract is avoided by frustration, or

(g) the defect is that the contract has not been filed or registered as required by an enactment.]

Comment: Enacting jurisdictions will wish to consider very carefully the interface between an *Illegal Contract Act* and their existing statute-base. There may be certain contracts that should be excluded from the operation of the Act. A particular kind of contract may be excluded for one of two reasons.

First, an enactment may render a contract unenforceable for reasons that are central to the system of justice. Many jurisdictions might regard their statute of limitations as falling into this category.

A second reason for excluding certain kinds of contracts is that specialized enactments may provide relief from the consequences of illegality that are more finely-tuned to the body of law involved than a law of general application. For example, some provinces have replaced their old *Statute of Frauds* legislation with a more modern statement of the principle that incorporates a benevolent version of the equitable doctrine of part performance and allowing a party to rely on a change of position. Supervening illegality may cause a contract to be frustrated in which case the position of the parties are best dealt with under local frustrated contracts legislation (if it exists). Some provinces will have moved to modernize their laws in relation to minors' contracts while others will not.

Individual jurisdictions must decide the precise types of contracts to be listed in section 2(3). This decision will be informed by local policy and statutes. The only element in the list that should be retained in all cases is paragraph (a).

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Claims for relief

- 4(1) Any party to an illegal contract may claim relief under section 5.
- (2) Without limiting subsection (1) but subject to subsection (3), if an illegal contract purported to transfer an interest in property to a person, a person who acquires or who purports to have acquired some or all of that interest in property from:
- (a) the first mentioned person; or
 - (b) any other person whose right to transfer that interest depends on the first mentioned person having acquired the interest under the illegal contract, may claim relief under section 5.
- (3) Subsection (2) does not apply if:
- (a) the relief sought by the person claiming relief under subsection (2) is expressly, or by necessary implication, prohibited by an enactment other than this Act; or
 - (b) an enactment, other than this Act, expressly provides for the relief that may be granted in those circumstances to the person claiming relief.

Comment: Even where specific legislation exists to define the legal position of, and provide relief in appropriate circumstances to, the parties to an illegal contract, that legislation may not address the question of relief for a non-party who has a claim to property passing under the contract. Section 4 permits enacting jurisdictions to fine-tune the applicability of the Act by filling that gap without doing violence to the legislative scheme for relief inter partes.

In the *Civil Code* of Québec, there already exist a number of provisions protecting both the true owner and a third party purchaser of property sold under an illegal contract (see art. 1454, 1455, 1701, 1707, 1713-1715).

Relief

- 5(1) A court may grant relief in relation to an illegal contract in one or more of the following ways:
- (a) restitution;
 - (b) compensation;
 - (c) apportionment of a loss arising from the formation, existence or performance of the contract;
 - (d) damages from a party at fault;
 - (e) a declaration;
 - (f) an order vesting property in any person or directing a person to assign or transfer property to another person;
 - (g) if the court is satisfied that:
 - (i) the contract would be reasonable and lawful if:
 - (A) one or more provisions of the contract were deleted; or
 - (B) the contract as a whole, or one or more of its provisions, were given limited effect only; and

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(ii) the deletion or limitation would not so alter the bargain between the parties that it would be unreasonable to give effect to the contract as modified, an order that the contract be modified to effect the severance or limitation and that the contract, as modified, be performed in a lawful manner specified by the court;

(h) any other relief the court could have granted under common law or equity had the contract not been an illegal contract.

Comment: Section 5(1) sets out a list of remedies that may be granted by the court when relief is sought from the consequences of an illegal contract. It gives the court a flexible set of tools necessary to fashion an outcome that will do justice between the parties.

Paragraphs (a), (b) and (c) parallel the remedies available under the *Uniform Frustrated Contracts Act*. A claim for damages under paragraph (d) will not arise often, but the kind of circumstances where damages might be properly claimed is where the validity of a contract hinges on getting the approval of a particular authority, and one of the parties is obliged by the terms of the contract to obtain it. If that party willfully or negligently fails to do so, damages would seem to be appropriate.

Paragraph (g) empowers the court to sever portions of an illegal contract and notional severance of the kind endorsed in the *New Solutions* case is expressly covered.

Paragraph (h) is intended to act as a backstop to the other remedies and does not constitute an invitation to the courts simply to enforce an illegal contract. Given the breadth of the other remedies, it is not likely to be invoked often. The kind of situation where it might be invoked is where restitution is made of a parcel of land and the conduct of the adverse party suggests that an injunction enjoining trespass on the parcel is necessary for the protection of the successful party. Paragraph (h) would allow the injunction to be joined with the other relief.

In the *Civil Code* of Québec as in paragraphs (a) and (b), taking into account section 5(2), the general rule is that the court must order restitution as between the parties to an illegal contract (art. 1422). Where restitution in kind has become impossible or is liable to affect third parties, the court must order restitution by monetary equivalence (art. 1700). For instance, if a service is performed under an illegal contract, the court will order restitution by equivalence, to the extent necessary to prevent unjust enrichment. Property purchased under an illegal contract may also be restituted by equivalence, where a third party has acquired rights in such property. The apportionment of losses incurred in relation to property or otherwise is governed by articles 1701 to 1706 of the *Civil Code*.

In the civil law as in paragraph (d), a party may obtain compensation by way of damages where wrongful conduct by the other party has caused him or her to suffer a loss, including a loss of profits (art. 1457, 1611).

As in paragraph (g), the *Civil Code* of Québec provides that an illegal clause may be deleted and the remainder of the contract upheld in appropriate cases (art. 1438). Notional severance, as set out in paragraph (g)(i)(B), is presently available in certain cases only, such as adhesion and consumer contracts (art. 1437). An even broader power to vary the terms of the contract is conferred upon the courts in the case of money loans (art. 2332). The adoption of notional severance as a general remedy would be desirable.

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(2) The amount to which a person is entitled by way of restitution, compensation or apportionment under subsection (1)(a), (b) or (c) must be determined in accordance with the following:

- (a) the amount must not include loss of profits; and
- (b) the amount must be reduced by the fair market value of:
 - (i) any benefits that remain in the hands of the claimant, and
 - (ii) any property that has been returned to the claimant within a reasonable time after the contract is challenged as being null, void, voidable, illegal, unlawful, invalid, unenforceable or otherwise ineffective; and
- (c) if and to the extent that the claim is for expenditures incurred in performing the contract, other than in performing an obligation under the contract to pay money, the amount must be limited to reasonable expenditures.

Comment: Section 5(2) provides guidance as to the way that restitutionary relief is to be assessed. It embodies the same policy as sections 7 and 8 of the *Uniform Frustrated Contracts Act*.

(3) A court making an order under this section may include, in that order, any terms and conditions it considers appropriate.

Discretionary Factors

6(1) In granting or refusing to grant relief under section 5, a court must consider the following:

- (a) the public interest;
- (b) the circumstances of the formation, existence or performance of the illegal contract, including the intent, knowledge, conduct and relationship of the parties;
- (c) whether a party to the illegal contract was, at a material time, acting under a mistake of fact or law;
- (d) the extent to which the illegal contract has been performed;
- (e) whether the contract was illegal from the time of its formation or whether the circumstances of its operation led to an illegal result;
- (f) if the defect arose out of an enactment, whether the enactment has been substantially complied with;
- (g) the consequences of refusing to grant relief;
- (h) any other factor the court considers relevant.

(2) In granting or refusing to grant relief in respect of an illegal contract that was entered into before the coming into force of this Act, a court, in addition to the factors set out in subsection (1), must consider whether or not:

- (a) a party to the contract has so altered that party's position that granting relief would, in the circumstances, be inequitable,
- (b) another proceeding has been commenced in respect of the contract, and
- (c) a party to the contract has settled a claim in respect of the contract.

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Comment: Section 6 sets out the factors to be considered by the court in granting or withholding relief. Additional factors may come into play if the contract predates the Act. These are set out in subsection (2).

In civil law jurisdictions, while restitution is the general rule, a court may refuse to order restitution in favour of a party who has acted fraudulently, immorally or by deliberately breaching the law. The factors underlying this exception to the general rule are identified at paragraphs (b) and (c). A codification of the exception in the *Civil Code* of Québec would be desirable.

In the *Civil Code* of Québec, a distinction is made between rules of public order which exist to protect a contracting party and rules of public order which exist in the interests of society as a whole (art. 1417, 1419). In the first instance, violation of the rule entails a relative nullity: only the party protected by the rule may have the contract annulled; he or she may also opt to affirm the contract (art. 1420). In the second instance, violation of the rule entails an absolute nullity: any person with sufficient legal interest may have the contract annulled (art. 1418).