

## CASE NOTES AND COMMENTS

### Unilateral Assignment of Franchise Agreements in Bankruptcy: Economic Efficiency versus Freedom of Contract in *Ford Motor Company v. Welcome Ford Sales*

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#### INTRODUCTION

On May 27, 2011, the Alberta Court of Appeal released its reasons for judgment in *Ford Credit Canada Ltd. v. Welcome Ford Sales Ltd.*,<sup>1</sup> the first reported case to interpret s. 84.1 of the *Bankruptcy and Insolvency Act* (“BIA”).<sup>2</sup> Section 84.1 was enacted in 2009 as part of a package of amendments to the BIA, but the practical implications of this new provision were not yet clear. The decision in *Welcome Ford Sales*, however, erased any uncertainty: the Alberta Court of Appeal made clear that, upon bankruptcy, a trustee in bankruptcy may assign a long term performance agreement to a third party despite objections from the contractual counterparty.

Although decided in the context of a franchise agreement, *Welcome Ford Sales* contains a few important messages that are relevant to all businesses engaged in ongoing contractual relationships. First, businesses must be aware that if the other party to their agreement goes bankrupt, there is a risk that the trustee in bankruptcy will be able to assign the agreement to a third party without their consent. Second, even an agreement expressly referred to as a contract for “personal service” may be deemed a standard commercial agreement, capable of assignment. Finally, co-contracting parties wishing to oppose assignment on the basis of s. 84.1(4) must be prepared to marshal strong evidence to establish that the proposed assignee is not capable of performing the obligations under the agreement.

*Welcome Ford Sales* clarifies the law of bankruptcy by analyzing the conditions under which s. 84.1 will be applied, and provides guidance with respect to the factors that a court should take into account when assigning an agreement to a third party. The Court’s interpretation of s. 84.1 aligns nicely with the remedial goals of bankruptcy law as stated by the Standing Senate Committee when it recommended amendments to the BIA. When considering the factual matrix before the Court in this case, the decision is hardly surprising: Ford was unable to present a particularly

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<sup>1</sup> 2011 ABCA 158, 2011 CarswellAlta 883, [2011] A.J. No. 592, 505 A.R. 146, 77 C.B.R. (5th) 278, [2011] 8 W.W.R. 221, 44 Alta. L.R. (5th) 81, 522 W.A.C. 146 (Alta. C.A.) [*Welcome Ford Sales*].

<sup>2</sup> RSC 1985, c B-3 [*Bankruptcy and Insolvency Act*].

compelling case on the facts, and the result was very practical for the bankrupt estate.

However, the Alberta Court of Appeal's decision in *Welcome Ford Sales* also brings to light the conflict that exists between freedom of contract, on the one hand, and economic efficiency achieved by s. 84.1, on the other. Unilateral assignment without consent brings with it potential harms to co-contracting parties. This comment examines the application of s. 84.1 in *Welcome Ford Sales*, assesses the merits of the decision in light of conflicting public policy goals, and considers how parties can protect themselves from the prospect of unilateral assignment.

## 1. BACKGROUND

### (a) Section 84.1

Section 84.1 of the BIA was enacted following a comprehensive review of the federal legislation relating to debtors and creditors in Canada. In November 2003, the Standing Senate Committee on Banking, Trading and Commerce tabled a report<sup>3</sup> discussing the BIA and the *Companies' Creditors Arrangement Act*.<sup>4</sup> With respect to s. 84.1 of the BIA, the Senate Committee Report contains two passages of particular interest.

First, in a portion entitled "The Committee's Philosophy with respect to Insolvency Law", the report sets out the values underlying a "well-functioning insolvency system", including fairness, accessibility, efficiency, and effectiveness. The Committee acknowledged the social costs of bankruptcy, and stated that the system must ensure that these costs are minimized and shared appropriately.<sup>5</sup> The Committee concluded that the BIA should create a bankruptcy process that "allows assets to be re-allocated for use in an environment where profitability may exist".<sup>6</sup> This focus on preserving value for the bankruptcy estate sets the stage for the interpretation of the BIA in *Welcome Ford Sales*, where the Court takes as its starting point the notion that the BIA is fundamentally remedial legislation.

Second, the Senate Committee Report's section on executory contracts<sup>7</sup> contains its specific recommendations on assignment of a bankrupt's contractual rights and obligations.<sup>8</sup> The Committee began its analysis by acknowledging that altering private contracts results in negative implications: changing expectations, reducing predictability, and increasing risk. In spite of these drawbacks, however, the Com-

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<sup>3</sup> Standing Senate Committee on Banking, Trade and Commerce, *Debtors and Creditors Sharing the Burden: a Review of the Bankruptcy and Insolvency Act and the Companies' Creditors Arrangement Act and to make consequential amendments to other Acts*, 38th Parl., 1st Sess., received Royal Assent, 25 November 2005 [Senate Committee Report].

<sup>4</sup> RSC 1985, c C-36.

<sup>5</sup> *Senate Committee Report*, *supra*, n. 3 at 5-7.

<sup>6</sup> *Ibid.*, at 16.

<sup>7</sup> Defined as "contracts under which something remains to be done by one or more of the parties to the contract".

<sup>8</sup> *Ibid.*, at 131-138.

mittee made the following recommendation:

[T]rustees, Court-appointed receivers and monitors should be able to assign executory contracts where doing so would enhance the value of the assets and, thereby, moneys available for distribution to creditors. We recognize that while this circumstance would not permit the co-contracting party to choose its commercial partner, we feel that if the co-contracting party is no worse off financially, it would suffer no prejudice.<sup>9</sup>

The Committee's second recommendation lines up with its stated philosophy; it is designed with value preservation in mind, with the goal of ensuring that creditors are paid as much as possible in spite of the circumstances. With this recommendation, the Committee made a policy decision to prioritize creditors' rights to a bankrupt's assets over the contractual rights of the co-contracting party. The Committee's recommendations (and its policy priorities) were adopted in the BIA s. 84.1.

The relevant portions of s. 84.1 of the BIA read:

84.1 (1) On application by a trustee and on notice to every party to an agreement, a court may make an order assigning the rights and obligations of a bankrupt under the agreement to any person who is specified by the court and agrees to the assignment.

(3) Subsection (1) does not apply in respect of rights and obligations that are not assignable by reason of their nature . . .

(4) In deciding whether to make the order, the court is to consider, among other things,

(a) whether the person to whom the rights and obligations are to be assigned is able to perform the obligations; and

(b) whether it is appropriate to assign the rights and obligations to that person.<sup>10</sup>

### (b) The General Common Law of Assignment

At common law, a contract is "assigned" where the parties to the contract transfer all or some of the rights and burdens under the contract to a person who is a stranger to the original contract. If only rights or benefits under a contract are being assigned (and the assignor remains liable for the performance of its obligations), the consent of the remaining party to the contract is not required.<sup>11</sup> The consent of the remaining party to the contract *is* required where burdens or obligations of a party are assigned to a third party.<sup>12</sup>

<sup>9</sup> *Ibid.*, at 137-138.

<sup>10</sup> *Bankruptcy and Insolvency Act*, *supra*, n. 2, s. 84.1.

<sup>11</sup> *National Trust Co. v. Mead*, 1990 CarswellSask 165, 1990 CarswellSask 412, EYB 1990-67931, [1990] S.C.J. No. 76, [1990] 2 S.C.R. 410, 12 R.P.R. (2d) 165, 71 D.L.R. (4th) 488, 112 N.R. 1, [1990] 5 W.W.R. 459, 87 Sask. R. 161 (S.C.C.) [*National Trust* cited to QL].

<sup>12</sup> *National Trust Co. v. Mead*, 1990 CarswellSask 165, 1990 CarswellSask 412, EYB 1990-67931, [1990] S.C.J. No. 76, [1990] 2 S.C.R. 410, 12 R.P.R. (2d) 165, 71 D.L.R.

When drafting a contract, parties frequently include assignment provisions that provide for assignment of rights and obligations upon consent, which may not be unreasonably withheld. Moreover, certain statutes,<sup>13</sup> particularly those relating to leases of property, state that consent to assignment may not be unreasonably withheld. Further, the courts have set out factors to assist in determining whether consent to assignment has been unreasonably withheld:

1. The burden is on the party seeking consent to demonstrate that the refusal to consent was unreasonable. The question is whether a reasonable person could have withheld consent.
2. Information available to the refusing party *at the time of the refusal* is relevant to the determination of reasonableness, not any subsequent facts or reasons.
3. A refusal will be unreasonable if it was designed to achieve a collateral purpose that was wholly unconnected with the bargain reflected in the terms of the agreement.
4. A probability that the proposed assignee will default in its obligations may be a reasonable ground for withholding consent.
5. The financial position of the assignee may be a relevant consideration.
6. The question of reasonableness is essentially one of fact that must be determined on the circumstances of the particular case.<sup>14</sup>

The BIA differs from the common law and the aforementioned statutes in that it provides for assignment of rights and obligations without consent from the other party to the contract. The practical application of this difference will be discussed in Part 4.

### (c) The Facts

*Welcome Ford Sales* arose in January 2010, when Welcome Ford Sales (“Welcome Ford”), a franchised dealership of Ford Motor Company (“Ford”), was ordered into receivership on application of one of its creditors. Welcome Ford had recently ceased operations. As part of the receivership order, the court ordered that no agreements then in place (including the franchise agreement) could be terminated without consent of the court.

Ford made clear early on that it would not consent to the assignment or sale of

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(4th) 488, 112 N.R. 1, [1990] 5 W.W.R. 459, 87 Sask. R. 161 (S.C.C.) [*National Trust* cited to QL]. This is technically not an “assignment”, but rather “novation” — a new contract will be created between the assignee and the remaining party to the original contract. Strictly speaking, only rights or benefits may be “assigned”. See CED, *supra*, n. 10.

<sup>13</sup> See e.g., *Commercial Tenancies Act*, RSO 1990, c L.7, s. 23; *Residential Tenancies Act*, 2006, SO 2006, c 17, s. 98; *Landlord and Tenant Act*, CCSM c L70, s. 22.

<sup>14</sup> *1455202 Ontario Inc. v. Welbow Holdings Ltd.*, 2003 CarswellOnt 1761, [2003] O.J. No. 1785, 33 B.L.R. (3d) 163, 9 R.P.R. (4th) 103 (Ont. S.C.J.). This was upheld as “the applicable test” in *Tradedge Inc. v. Tri-Novo Group Inc.*, 2007 ONCA 562, 2007 CarswellOnt 5178 (Ont. C.A.). The factors are paraphrased from the original decision.

the dealership agreement to any third party. A few months later, however, a judge ordered that the receiver could nevertheless market the dealership agreement, and postponed Ford's request to terminate the dealership agreement. The receiver only marketed the dealership to existing Ford dealers, and the offer made by the ultimate purchaser (the highest bidder) produced sufficient funds to retire all debt to secured creditors, and produce a further \$570,000 to be distributed amongst the unsecured creditors.<sup>15</sup>

Welcome Ford was later assigned into bankruptcy. Pursuant to s. 84.1 of the BIA, the bankruptcy court approved the trustee's application to assign the dealership agreement to an existing Ford dealer, over Ford's objection. Ford appealed the approval of the assignment to the Alberta Court of Appeal.

## 2. JUDGMENTS OF THE ALBERTA COURTS

### (a) Alberta Court of Queen's Bench

#### (i) *Agreement Was Not Terminated Prior to Bankruptcy*

At trial,<sup>16</sup> Ford took the position that Welcome Ford had "fundamentally breached" the franchise agreement prior to bankruptcy. As a result, Ford argued, there was no agreement to assign under s. 84.1 of the BIA. The Alberta Court of Queen's Bench addressed the question of "fundamental breach" as a threshold issue, concluding that Welcome Ford had not fundamentally breached the agreement and thus that the agreement remained valid and assignable at the time of trial.

Ford suggested three "fundamental breaches" as the basis for termination of the franchise agreement: (a) the appointment of the Receiver; (b) the "shuttering" of the Welcome Ford premises; and (c) alleged "improper conduct" of senior employees of Welcome Ford leading up to the closure of the dealership in January 2010. The trial judge would not make findings of fundamental breach on any of those arguments.

With regard to the appointment of the Receiver, the trial judge found that at all times the Receiver had been able and willing to honour the franchise agreement and its commercial purpose, but Ford's conduct prevented it from doing so. Similarly, with regard to the second ground of alleged "fundamental breach", the trial judge held that while the Welcome Ford dealership was not operating after being "shuttered" in January, this was not for lack of effort on the part of the Receiver; Ford had at all times resisted any further operation of Welcome Ford as a franchise. Finally, the third ground, alleged improper conduct, was declined because it was not yet proven, and the allegations were made against a senior officer — not Welcome Ford itself or its principal shareholder.<sup>17</sup>

The trial judge concluded that Ford had effectively prevented the Receiver from operating Welcome Ford, and could not be allowed to benefit from that resistance. Ford could not, then, succeed with its argument that the agreement had en-

<sup>15</sup> *Welcome Ford Sales*, *supra*, n. 1 at paras. 3–7.

<sup>16</sup> *Ford Credit Canada Ltd. v. Welcome Ford Sales Ltd.*, 2010 ABQB 798 (Alta. Q.B.) [*Ford Credit*].

<sup>17</sup> *Ibid.*, at paras. 16–37.

ded and thus there was no agreement to assign. The possibility of success of such an argument under different facts will be discussed in Part 4.

*(ii) Agreement Can Be Assigned Pursuant to S. 84.1 of the BIA*

The trial judge held that the franchise agreement between Ford and Welcome Ford could be assigned under s. 84.1 of the BIA. This decision will be discussed in the context of the Alberta Court of Appeal's reasons, below.

**(b) Alberta Court of Appeal**

The Alberta Court of Appeal upheld the trial court's decision that the franchise agreement could be assigned under s. 84.1 of the BIA. The Court's reasoning was predicated upon three important propositions: (1) Section 84.1 must be interpreted in the context of the BIA's role as remedial legislation; (2) Agreements must be truly personal in nature to be insulated from assignment; and (3) Co-contracting parties must marshal strong evidence to establish that a proposed assignee is not capable of performing the assignment.

*(i) Section 84.1 is to be Interpreted in the Context of its Role as Remedial Legislation*

The Court considered Parliament's intent when interpreting the meaning of s. 84.1. As demonstrated by the *Senate Committee Report*,<sup>18</sup> Parliament's goal was to use s. 84.1 to protect and enhance the assets of a bankrupt's estate by permitting sale and assignment of existing agreements to third parties for value.<sup>19</sup> Prior to the implementation of s. 84.1, a bankrupt's estate was vulnerable to losing the benefit of a valuable contract, to the detriment of the estate and often third party creditors. In enacting s. 84.1, Parliament made a policy decision to address this vulnerability, giving courts the discretion to approve an assignment in spite of the objections of the counter-party — thus retaining the value of the contract for the estate and its creditors.<sup>20</sup>

*(ii) Agreements must be Truly Personal in Nature to be Insulated from Assignment*

Although Ford argued the franchise agreement could not be assigned because it was personal in nature (an exception under s. 84.1(3)), the Court held that it was not a "personal contract". The Court agreed with the finding of the chambers judge that it was "a rather standard commercial franchise which could be performed by virtually any business person and entity with some capital and experience in automotive retailing".<sup>21</sup>

The Court made clear that parties cannot insulate an agreement from the effect of s. 84.1 by simply including a clause describing the obligations as "personal". If

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<sup>18</sup> *Supra*, n. 3.

<sup>19</sup> *Welcome Ford Sales*, *supra*, n. 1 at para. 36.

<sup>20</sup> *Ibid.*, at para. 39.

<sup>21</sup> *Ibid.*, at para. 50.

an agreement is to be deemed unassignable by reason of its personal nature it must be “based on confidences, or considerations applicable to special personal characteristics, and so cannot be usefully performed by another”.<sup>22</sup> If counter-parties to an agreement are to argue that the agreement is not assignable on the basis of the exception under s. 84.1(3), they must present some evidence that the identity or skills of individual assignor was important to them.<sup>23</sup>

*(iii) Co-Contracting Parties must Marshal Strong Evidence to Establish that a Proposed Assignee is Not Capable of Performing the Agreement*

Section 84.1(4) directs a judge considering an order of assignment to consider whether the proposed assignee can perform those obligations in the same manner as the assignor. The court in *Welcome Ford* determined that the proposed assignee, who was already successfully operating another Ford dealership in the area, would be able to perform the obligations in question.<sup>24</sup> The chambers judge had relied on uncontradicted affidavit evidence that the proposed assignee had an excellent track record operating a profitable Ford dealership. Ford argued that there was insufficient evidence to make this conclusion, but in the absence of evidence from Ford showing some disability on the part of the proposed assignee, the chambers judge inferred that the proposed assignee had the capital, experience, and capacity to perform the obligations assigned to him. The Court of Appeal upheld this conclusion.<sup>25</sup>

The court’s decision in this respect suggests that counter-parties attempting to oppose an assignment under s. 84.1 must be prepared to marshal real evidence demonstrating that the proposed assignee is not up to the job.

*(iv) Alberta Court of Appeal’s Conclusion*

The Alberta Court of Appeal upheld the chambers judge’s decision to approve the assignment of the agreement. The major factors in its decision were the unreasonableness of Ford’s refusal to consent, the uncontradicted evidence that the proposed assignee was up to the job, the fact that the proposed assignment would substantially cure earlier breaches of the agreement, and the fact that Ford’s rights and remedies under the agreement would carry on unchanged.<sup>26</sup>

### 3. DISCUSSION

#### (a) Policy Considerations

The Alberta Court of Appeal’s application of s. 84.1 of the BIA accords with the overarching goal of bankruptcy law, as stated by the *Senate Committee Report*:

<sup>22</sup> *Ibid.*, at para. 55, citing *Black Hawk Mining Inc. v. Manitoba (Provincial Assessor)*, 2002 MBCA 51, 2002 CarswellMan 213, [2002] 7 W.W.R. 104, 163 Man. R. (2d) 215, 269 W.A.C. 215, 29 M.P.L.R. (3d) 163 (Man. C.A.) at para. 82.

<sup>23</sup> *Ibid.*, at paras. 57–59.

<sup>24</sup> *Ibid.*, at para. 61.

<sup>25</sup> *Ibid.*, at para. 62.

<sup>26</sup> *Ibid.*, at para. 72.

preserving maximum value for the bankruptcy estate.<sup>27</sup> The Court ensured that it was interpreting the BIA in its context as remedial legislation, and applied it in a manner that protected the remaining value of the estate. The result of the Court's approval of the assignment was that Welcome Ford's secured creditors could be paid in full, with a substantial sum left over for its unsecured creditors (in contrast, liquidation of the bankrupt's assets without the sale and assignment of the agreement would have left a debt of over \$1 million to its secured creditor and produced nothing for any other creditor).<sup>28</sup> The assignment also ensured that the franchise could continue to operate under different ownership, creating a situation where profitability and economic growth were possible. This application of s. 84.1 of the BIA was resoundingly successful with respect to economic efficiency.

Conflicting policy considerations, however, must also be considered. In particular, s. 84.1 of the BIA ignores the intention of co-contracting parties. Freedom of contract is a fundamental tenet of our law; the purpose of a contract is to effect, and make enforceable, the intentions of the parties to it. This does not solely include the party's intentions with respect to the substance of the rights and obligations — freedom of contract includes the freedom to choose *who* will be responsible for these obligations.

It can be assumed that it was the intention of Ford to contract specifically with Royce Smith, the initial owner and operator of the Welcome Ford dealership. If the parties did not specifically intend to contract with each other, they could have included an assignment clause in their agreement, as so many other commercial parties do. In the absence of such a provision, it can be concluded that the parties intended that their rights and obligations would be with respect to each other.

Section 84.1 of the BIA suggests that the contracting parties' intentions can be overridden in order to maximize value for the bankruptcy estate. As was the case in *Welcome Ford*, s. 84.1 has the power to effectively force a party to contract with someone against its will.

The *Senate Committee Report* recognized this deficiency in its proposal for amendments to the laws relating to executory contracts, stating, "...while this circumstance would not permit the co-contracting party to choose its commercial partner, we feel that if the co-contracting party is no worse off financially, it would suffer no prejudice".<sup>29</sup> The assertion that the co-contracting party would suffer *no* prejudice is perhaps an overstatement. It can be argued that a party's intentions in entering into a long term, complex contractual relationship with another specific party should be accorded more weight, regardless of the economic outcome. Although s. 84.1 may be a step forward for economic efficiency in the bankruptcy process, this comes at the expense of parties' freedom of contract.

The notion that there is more to a business relationship than what can be seen in the annual financial statements is particularly compelling in the franchise sector where the relationship between the contracting parties is the essence of the entire business model. In franchising relationships, the franchisor essentially entrusts its trademarks, business systems, know-how and, indeed, its brand, to its franchisees.

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<sup>27</sup> *Senate Committee Report*, *supra*, n. 3 at 5-7.

<sup>28</sup> *Welcome Ford Sales*, *supra*, n. 1 at para. 7.

<sup>29</sup> *Senate Committee Report*, *supra*, n. 4 at 138.

Franchisees are often the direct ‘face’ of the organization in the consumer market. For these reasons, franchisors must be particularly focused on the identities of their individual franchisees and their ability to comply with often quite sophisticated business systems and onerous contractual responsibilities.

Moreover, franchise agreements are often long term contracts that, out of necessity, are silent with respect to key aspects of the business relationship, leaving many aspects of the relationship to be addressed in policies that can be, and typically are, amended through negotiation and consultation. There is — simply put — a high degree of cooperation that is required between the parties to such an agreement. Finally, the parties to a franchise agreement owe obligations of fair dealing in the performance and enforcement of the contract.<sup>30</sup> That obligation includes a duty of good faith and a duty to act in accordance with reasonable commercial standards. In these circumstances, it is not surprising that the franchisor wants to know and approve the party with whom it must work.

### (b) Difficult Facts to Oppose Assignment

The facts of this case made Ford’s attempt to oppose the assignment of the franchise agreement an uphill battle. Under s. 84.1, a court must consider the appropriateness of the proposed assignment and whether the proposed assignee is “able to perform the obligations”.<sup>31</sup> These are factual questions, determined on the circumstances of a particular case. The facts of *Welcome Ford* did not help Ford make a compelling case, and the result was unsurprising.

The proposed assignee was an existing Ford franchisee with an excellent track record of operating a profitable Ford dealership. He had received many national awards from Ford over the years, and his existing dealership premises met Ford’s “Millennium Standards”.<sup>32</sup> Furthermore, the courts found that Ford had effectively prevented the Receiver from operating the Welcome Ford dealership; the Receiver had at all times been ready and willing to honour the agreement, but was unable to do because “Ford at all times resisted any further operation of Welcome Ford as a franchise”.<sup>33</sup>

Ford brought no evidence demonstrating how it could be prejudiced by the assignment. With the exception of their abstract right to choose with whom they wish to contract, it is unclear what Ford lost as a result of the assignment. Moreover, it is not clear what Ford would have gained if had they successfully prevented

<sup>30</sup> *Shelanu Inc. v. Print Three Franchising Corp.*, 2000 CarswellOnt 4040, [2000] O.J. No. 4129, 11 B.L.R. (3d) 69, [2000] O.T.C. 768 (Ont. S.C.J.) at para. 25; additional reasons at 2000 CarswellOnt 4407, 11 B.L.R. (3d) 100 (Ont. S.C.J.); additional reasons at 2001 CarswellOnt 1581, [2001] O.J. No. 1750 (Ont. S.C.J.); reversed in part 2003 CarswellOnt 2038, [2003] O.J. No. 1919, 64 O.R. (3d) 533, 172 O.A.C. 78, 226 D.L.R. (4th) 577, 38 B.L.R. (3d) 42 (Ont. C.A.); additional reasons at 2006 CarswellOnt 2627, 19 B.L.R. (4th) 19, 269 D.L.R. (4th) 152 (Ont. C.A.); *Arthur Wishart Act (Franchise Disclosure)*, 2000, SO 2000, c 3, s. 3; *Franchises Act*, RSA 2000, c F-23, s. 7; *Franchises Act*, RSPEI 1988, c F-14.1, s. 3; *Franchises Act*, SNB 2007, c F-23.5, s. 3.

<sup>31</sup> *Bankruptcy and Insolvency Act*, *supra*, n. 2, s. 84.1(4).

<sup>32</sup> *Ford Credit*, *supra*, n. 15 at para. 91.

<sup>33</sup> *Ibid.*, at para. 25.

the assignment. On all the evidence, the proposed assignee appeared to be a perfect fit.

Perhaps most importantly, the result on the facts promoted economic efficiency. The assignment was an extremely practical solution for the estate, and for its creditors. Coupled with an ideal assignee, the potential for better financial results for Ford, and a lack of evidence demonstrating potential prejudice, the result was predictable. It is less clear how s. 84.1 will apply in cases where the abilities of the proposed assignee and appropriateness of the assignment are not so obvious.

### (c) Deviation from the General Law of Assignment

*Welcome Ford* offers the first judicial interpretation of s. 84.1 of the BIA, and potentially has wide-ranging consequences. The decision invites the question: What would the result of the case have been in the absence of s. 84.1?

As stated above, the common law requires consent for the assignment of contractual obligations (also known as "novation"). As the Supreme Court stated in *National Trust Co. v. Mead*:

Because assent is the crux of novation it is obvious that novation may not be forced upon an unwilling creditor and, in the absence of express agreement, the court should be loath to find novation unless the circumstances are really compelling. . . the burden of establishing novation is not easily met.<sup>34</sup>

As such, without a statutory provision relating to assignment, the unilateral assignment that took place in *Welcome Ford* would have been difficult to achieve.

Various statutes provide for assignment of contractual rights and obligations upon the co-contracting party's consent, which may not be unreasonably withheld.<sup>35</sup> If the BIA included a provision of this sort, the result of *Welcome Ford* would likely have been the same. The ability to assign a bankrupt's rights and obligations under s. 84.1 of the BIA is not absolute — not only does s. 84.1(3) provide for exceptions for particular rights and obligations, but under s. 84.1(4) assignment will only be approved by a court where the assignee is able to perform the obligations, and where it is appropriate to assign the rights and obligations to that person. These limits correspond quite closely to the test for whether consent is unreasonably withheld.<sup>36</sup>

If *Welcome Ford* was determined on the basis of a statutory obligation not to unreasonably withhold consent to assignment, Ford would have likely been determined to have unreasonably withheld its consent because of the apparently strong financial position of the assignee, the unlikelihood that the assignee would default in its obligations, the finding that Ford's rights and remedies under the agreement would carry on unchanged, and the possibility (as alluded to in the trial decision) that Ford had refused to consent in order to achieve a collateral purpose.<sup>37</sup>

The Court's decision in *Welcome Ford* was fair and practical, and likely

<sup>34</sup> *National Trust*, *supra*, n. 11 at para. 32.

<sup>35</sup> *Supra*, n. 12.

<sup>36</sup> See Part 2(b), above.

<sup>37</sup> *Ford Credit*, *supra*, n. 15 at para. 37. ("Ford Motor has taken the position from the outset that it did not want a Ford dealership operating in the Fort Saskatchewan area.")

would have been the same under a statutory regime prohibiting the unreasonable withholding of consent (rather than permitting unilateral assignment). With this in mind, it is worth considering that perhaps an obligation to not unreasonably withhold consent to assignment would be more appropriate than the current iteration of s. 84.1 of the BIA. Such a law would continue to honour the stated purposes of bankruptcy law and promote economic efficiency, but would prevent unilateral assignment, which undermines freedom of contract. In such a scenario, the ultimate decision to approve an assignment would lie in the hands of the co-contracting party, rather than a court.

#### **(d) How Can Unilateral Assignment Be Avoided in Ongoing Contractual Relationships?**

Parties with rights and obligations that may become subject to the application of s. 84.1 of the BIA — such as franchise and distributorship agreements — ought to consider how to protect themselves from unilateral assignment against their wishes. The decisions of the Alberta courts in *Welcome Ford* suggest two ways a party may do so.

Ford attempted to avoid assignment by suggesting that the agreement had been “fundamentally breached” and thus terminated, so there was no agreement to assign. As discussed above, this argument failed because the courts held that the agreement had not been fundamentally breached. The idea, however, was not a bad one. If an agreement is drafted to provide the option to terminate in certain circumstances (including *prior* to bankruptcy or even insolvency), a co-contracting party who may be vulnerable to unilateral assignment under s. 84.1 may elect to terminate prior to the bankruptcy trustee’s application for assignment to the court. Such contractual draftsmanship may be able to provide parties with an “out” if they worry that an undesirable application for assignment under s. 84.1 may be successful.

The Court inferred that the proposed assignee had the capacity to fulfill the contractual obligations on the basis of unchallenged evidence to the effect that the proposed assignee had an excellent track record, and would be up to the job. Ford did not adduce any of its own evidence on this issue, and the Court rejected Ford’s argument that there was insufficient evidence to conclude the proposed assignee would be able to perform the obligations. It is quite possible, however, that a court considering the question of appropriateness of an assignment would decide the issue differently if the co-contracting party presents compelling evidence on this point. If a party wishing to oppose the assignment marshals strong evidence to establish that the proposed assignee is not capable of performing under the agreement, a court would likely decline to order the assignment in light of s. 84.1(4).

## **4. CONCLUSION**

The Court’s interpretation of s. 84.1 of the BIA in *Welcome Ford Sales* created a practical result for the bankrupt’s estate and its creditors, and aligns nicely with the overarching goal of bankruptcy law to preserve value for the estate in an economically efficient manner. The decision reminds businesses that if the other party to their agreement goes bankrupt, they are at risk of their agreement being assigned to a third party without their consent.

The factual matrix before the Court did not make for a particularly compelling case against assignment, but it is possible that in circumstances in which the proposed assignee is not an ideal candidate — and where the party opposing the assignment presents evidence to this effect — a court may not approve an assignment over the objections of the other party to the agreement. Moreover, parties may strive to protect themselves from the application of s. 84.1 by drafting their agreements to provide for the option to terminate prior to bankruptcy — meaning there would be no agreement left to assign.

The application of s. 84.1 in *Welcome Ford* may be criticized for circumventing the principle of freedom of contract by permitting assignment even against a co-contracting party's wishes. Countervailing policy considerations, however, should be taken into account; the assignment in this case protected the remaining value of the bankrupt's estate, ensured the estate could fulfill the bankrupt's commitments to both secured and unsecured creditors, and created a business situation with the potential to produce profits into the future. In light of this concern, however, a slightly different assignment regime may be more appropriate. A statutory obligation not to unreasonably withhold consent to an assignment — the norm in statutes relating to commercial and personal leases — may be a better fit for the BIA. Such a regime would place the decision to approve an assignment in the hands of the co-contracting party, and would thus better respect freedom of contract without compromising the economic efficiency promoted under s. 84.1 as it currently stands.