

Cold cut for franchisees! Supreme Court of Canada denies designated supplier's duty of care for pure economic loss

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Introduction

Facts

Decisions

Comment

Introduction

In its recent five-to-four split decision in *1688782 Ontario Inc v Maple Leaf Foods Inc*,⁽¹⁾ the Supreme Court of Canada dismissed the proposed class action brought by Mr Sub franchisees against Maple Leaf Foods for damages resulting from a listeria outbreak linked to Maple Leaf cold cuts. By ruling in favour of the supplier, the majority of the court found that no duty of care is owed by an exclusive supplier for purely economic losses suffered by franchisees with which the supplier has no direct contractual relationship.

While the court confirmed that the supplier owed a duty of care to the franchisees' customers, who fortunately did not suffer any harm from the recalled products, it stopped short of finding that the supplier owed a duty of care to the franchisees given the lack of proximity between them and the fact that the damages were limited to pure economic losses due to reputational harm and an interruption in supply.

Facts

In 2005 Mr Sub (the franchisor) entered into an agreement pursuant to which it agreed to purchase specific menu items exclusively from Maple Leaf for three years. Despite the absence of a direct contractual relationship with Maple Leaf, Mr Sub franchisees were required by their franchisor to purchase 14 core meat products solely from Maple Leaf through the franchisor's distributors.

In 2008 Maple Leaf conducted a national recall of certain products, including cold cuts sold to Mr Sub franchisees, after a listeria outbreak at a meat plant in Toronto. The recall resulted in a shortage of products for six to eight weeks, affecting several menu offerings of Mr Sub franchisees.

The franchisees consequently launched a class action against Maple Leaf seeking damages for commercial losses from the interruption in product supply and reputational injury arising from being associated with Maple Leaf's recall for the listeria outbreak. The franchisees further alleged that Maple Leaf was negligent for supplying contaminated meat and claiming that such meat was safe for human consumption. Since there was no evidence that any customer of Mr Sub was harmed by the meat subject to the recall, the franchisees claimed damages resulting from:

- the disposal and destruction of contaminated meats; and
- loss of past and future sales and profits, goodwill and capital value of their franchise business.

Decisions

In response to the franchisees' claim, Maple Leaf brought a motion for summary judgment on the basis that it did not owe a duty of care to the franchisees. The motion judge disagreed and ruled that Maple Leaf did owe a duty of care to the franchisees in relation to the production, processing, sale and distribution of the meat supplied thereto, as well as a duty of care as to any representations made that the supplied meat and products were fit for human consumption and posed no risk of harm.⁽²⁾

The Ontario Court of Appeal reversed the motion judge's decision, finding that the judge had failed to consider the scope of the relationship between Maple Leaf and the franchisees and that Maple Leaf's duty to supply meat

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fit for human consumption was owed not to the franchisees, but rather to the end consumer. Moreover, the court concluded that in any event, if a duty of care were owed to the franchisees, it would not extend to a claim for purely economic loss.⁽³⁾

The Supreme Court of Canada narrowly upheld the Ontario Court of Appeal's decision and concluded that a duty of care must be based on the existence of a proximate relationship. The court found that the pure economic losses claimed by the franchisees did not fall within the scope of any existing category of proximity and, given the chain of contracts and established allocation of risk, could not be considered a reasonably foreseeable consequence of Maple Leaf's alleged negligence giving rise to a claim in tort.

The franchisees argued that the terms of their franchise agreement put them in a vulnerable position towards Maple Leaf and left them unable to protect themselves from its negligence. The franchisees also highlighted the operational disadvantages of operating a Mr Sub franchise, which left them vulnerable to interruptions in supply caused by the negligence of designated suppliers.

While the Supreme Court of Canada recognised that franchise agreements create a vulnerability with respect to franchisees, it was reluctant to establish a new duty of care on such basis. Rather, the majority of the court was of the view that franchisees are commercial entities whose vulnerability is the result of their choice to enter into a franchise agreement, with all of its terms and conditions, and that such a choice influences the expectations generated by such a relationship.

The court was therefore of the opinion that establishing a relationship of proximity between the franchisees and Maple Leaf would undermine the contractual framework and allocation of risks within which franchisees and franchisors choose to operate.

In addition, the court noted that, albeit conditional on their franchisor's approval, the franchisees could avoid an interruption of supply by seeking alternative supply sources. The franchisees' failure to exercise this option to mitigate the problem of the interrupted supply was viewed by the court as working against a finding of proximity.

While the majority decision viewed franchisees as commercial entities entering into franchise agreements with full awareness of the terms, conditions and consequences thereof, the dissenting judgment labelled the franchise agreement as a contract of adhesion in which the franchisees' bargaining and negotiating powers were illusory. While the dissent agreed with the majority decision that the franchisees' claim did not fall within an existing category of proximity, they were of the opinion that it would have been just and fair to establish a new duty of care. Pursuant to its analysis, the dissent concluded that a sufficient proximate relationship warranting a duty of care resulted from the fact that Maple Leaf:

- knew that it was (and had agreed to be) the exclusive supplier to the franchisees' business;
- had a direct line of communication with the franchisees; and
- provided sales support to the franchisees.

Comment

This decision addresses a number of issues relevant to franchisors and franchisees, as well as manufacturers, suppliers and other actors in commercial supply chains. Essentially, the court was clear that the duty of care owed by manufacturers and suppliers under common law is owed to end consumers and not other commercial parties in the supply chain, and that extra-contractual liability cannot be used by such commercial parties to circumvent a pre-established contractual allocation of risk.

While the Supreme Court of Canada did not expand the scope of existing categories of proximate relationships in respect of economic loss, the split of the court on this matter suggests that the common law duty of care may be broadened in future if warranted by proper factual circumstances, due largely to the imbalance of power in franchise relationships. From a franchisor's perspective, this decision should be a reminder to consider potential indemnity claims by franchisees when negotiating exclusive supply agreements for their franchise system. However, for the time being, this decision is a reminder for franchisees not to rely on extra-contractual claims as protection from risks that could have been allocated in the franchise agreement.

Interestingly, this decision has also exposed two contrasting views of the franchise relationship within the highest court of Canada. While the majority considered franchisees as independent commercial entities with full understanding of the terms and conditions of their franchise agreements and negotiating abilities in respect thereof, the dissent took the view that the franchisees were vulnerable parties and that the franchise agreement was a contract of adhesion in respect of which the franchisees' bargaining powers were illusory. In light of the dissenting view and opinion, it would be interesting to consider how similar matters would be decided by courts of the province of Quebec, where franchise agreements are commonly recognised as contracts of

adhesion. However, in this particular case, Quebec law expressly allows the legal warranty of quality to be invoked against a manufacturer by any party in the supply chain. As such, recourse by the franchisees against Maple Leaf would likely have succeeded on that basis alone, without consideration of the vulnerability resulting from contracts of adhesion.

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Endnotes

- (1) 1688782 Ontario Inc v Maple Leaf Foods Inc, 2020 SCC 35.
- (2) 1688782 Ontario Inc v Maple Leaf Foods Inc, 2016 ONSC 4233.
- (3) 1688782 Ontario Inc v Maple Leaf Foods Inc, 2018 ONCA 40.

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