

Damages in Lieu of Specific Performance: *Semelhago v Paramadevan*

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In *Semelhago v Paramadevan*¹ the Supreme Court dealt with two important matters of law. The main issue on appeal was the proper method of calculation of damages in lieu of specific performance. On this issue, the Court upheld an award of \$82,000 in a case in which it was manifest that the plaintiff had suffered little or no actual loss. However, as a result of the way in which the case was argued a key issue was not addressed. This Comment argues that the door remains open to a very different result in future cases if the issue of the duty to mitigate in the context of an action for specific performance is fully argued. The second issue was scarcely less important than the first and remarkably it was raised for the first time in the Court's decision, without argument from the parties. Reversing the long established rule that specific performance is routinely available to both parties in actions for the purchase and sale of land, the majority held that "Specific performance should . . . not be granted as a matter of course absent evidence that the property is unique..." This holding was very likely motivated by an understandable desire to minimize the future opportunity for windfall awards such that which was upheld in *Semelhago* itself. Of course the Court did not explicitly justify its holding on the availability of the remedy as a form of damage control, but it is difficult to see what else might have motivated the Court to alter the law on such a well-established point without argument. If the argument made in this Comment is correct and the duty to mitigate can be used to control the problem of windfall gains in an action for specific performance, then the holding on this point was unnecessary. The Comment will also argue that apart from the issue of windfall damages, the decision of the Court to limit the availability of specific performance was probably unfortunate as a matter of policy and it will lead to increased costs of litigation and settlement.

The facts in *Semelhago* are straightforward. In August 1986, the plaintiff agreed to buy a house in the Toronto area from the defendant for \$205,000, with a closing date of October 31, 1986. The vendor reneged and purchaser sued the vendor for specific performance or damages in lieu thereof. At trial, the purchaser elected damages in lieu of specific performance. The only question at the Supreme Court was the method of calculation of those damages. At the time of trial, the market value of the property to be purchased was \$325,000. The purchaser retained his old house when the

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¹[1996] 2 S.C.R. 415.

deal fell through and it was worth \$300,000 at the time of the trial.² At trial Corbett J. awarded damages of \$120,000, being the difference between the contract price and the value of the property assessed at the time of trial. She expressed her dissatisfaction with this award, noting that “There is no question that [the award] does result in a windfall to the plaintiff.”³ She also indicated that she would have been willing to consider alternative measures of damages except that she felt herself bound the decision of the Court of Appeal in *306793 Ontario Ltd. v. Rimes*, which held that the plaintiff’s true loss was the difference between the contract price and the value of the property at trial.⁴ The Court of Appeal found itself able to distinguish its decision in *Rimes* and made deductions which reduced the award to \$81,733.96.⁵

In dismissing the vendor’s appeal from that award Sopinka J., for the Court, held that “the appropriate date for the assessment of damages [in lieu of specific performance] is the date of trial”,⁶ or, for practical reasons, the date close to trial. He then continued to state that “The difference between the contract price and the value “given close to trial” as found by the trial judge is \$120,000. I would not deduct from this amount the increase in value of the respondent’s residence which he retained when the deal did not close.”⁷

This apparently clear endorsement of the method of calculation used by the trial judge is obscured by Sopinka J.’s remarks, in the final paragraphs of the decision, that he had “reservations about the propriety of [the] deductions [made by the Court of Appeal]”⁸ but he would not disturb them as there was no cross-appeal on this point and the matter was not in issue. This cannot be interpreted simply as indicating that the Court felt the deductions were inappropriate and that no adjustments at all should have been made to the trial judge’s award, as Sopinka J. further stated that “My reservations relate to the basis upon which the Court of Appeal distinguished *Rimes*. . . . On my reading of the reasons of MacKinnon A.C.J.O. in *Rimes*, the principal reason for deciding not to deduct the carrying charges was that to do so would be inconsistent with adopting the date of trial as the assessment date. I am not convinced that there is an inconsistency but would prefer not to express any further opinion on

²*Id.* at 419.

³Quoted in the decision of the Supreme Court *id.* at 421.

⁴(1979) 25 O.R. (2d) 79 at 84 leave to appeal refused [1979] 2 S.C.R. xi.

⁵19 O.R.(3d) 479 at 482.

⁶*Supra* note 1 at 427.

⁷*Id.*

⁸*Id.* at 430.

the question inasmuch as there is no cross-appeal and these matters are not in issue here.”⁹ The Court of Appeal’s attempt to distinguish *Rimes* was certainly unconvincing and its decision was a clear retrenchment from *Rimes* if not a first step towards confining *Rimes* to its facts.¹⁰ Sopinka J. is apparently suggesting that if on closer examination the deductions made by the Court of Appeal are consistent with adopting the date of trial as the assessment date then it may have been preferable to overrule *Rimes* rather than distinguish it. But while the Supreme Court has indicated that some deductions may be consistent with adopting the date of trial as the assessment date, it cannot be taken to have specifically approved the calculation of deductions made by the Court of Appeal. Thus the Supreme Court’s decision leaves the matter of these very significant deductions remains entirely open.

With this in mind, let us turn to a closer examination of the Supreme Court’s decision. There are two conflicting strands in the Court’s reasoning. The Court recognized that damages assessed as the difference between the contract price and the value of the property at trial “may appear to be overly generous to the respondent in this case and other like cases and may be seen as a windfall,” but it explained that “this criticism is valid if the property agreed to be purchased is not unique.”¹¹ Does the Court mean by this that the criticism is invalid if the property is unique because in that case there is no windfall? Or does it mean that the award is a windfall even if the property is unique, but the windfall is then somehow justified? While the ambiguity is never clearly resolved in the Court’s decision, I will argue that the latter interpretation is preferable. The award upheld in *Semelhago* is undoubtedly overcompensatory even if the property is unique, and such an award is not defensible in light of sound policy and legal principle. However, the award can be justified, not as a general matter, but on the narrow ground that in this particular case the duty to mitigate was not argued.

Much of the decision indicates that the Court felt its award was justified as being compensatory. The Court began its analysis by citing with approval the following passage from *Johnson v Agnew*:

⁹*Id.*

¹⁰The Court of Appeal distinguished *Rimes supra* note 4 on the basis that “[The facts in *Rimes*] are not the facts of the case now before the court. In this case, the purchaser is not a shell and the trial judge found that the evidence established what probably would have happened had the transaction closed.” While the Court in *Rimes* did refer to the lack of evidence on that point, this was only discussed in the penultimate paragraph and the central part of the Court’s reasoning was that in its view the true loss was the difference between the contract price and the value of the property at trial (as noted *supra* note 4). Note the irony that in distinguishing *Rimes* in this way the Court of Appeal would have treated a plaintiff which was a shell company buying for investment more generously than a plaintiff who was an individual buying for personal use.

¹¹*Id.* at 428.

(2) The general principle for the assessment of damages is compensatory, i.e., that the innocent party is to be placed, so far as money can do so, in the same position as if the contract had been performed. Where the contract is one of sale, this principle normally leads to assessment of damages as at the date of the breach -- a principle recognised and embodied in section 51 of the Sale of Goods Act 1893. But this is not an absolute rule: if to follow it would give rise to injustice, the court has power to fix such other date as may be appropriate in the circumstances.¹²

The Court then noted that if the innocent purchaser is compensated on the basis of the value of the goods as of the date of breach “the purchaser can turn around and purchase identical or equivalent goods. The purchaser is therefore placed in the same financial situation as if the contract had been kept.”¹³

However, the Sopinka J. stated that “Different considerations apply where the thing which is to be purchased is unique.” In a case in which the plaintiff would be entitled to specific performance “the rationale that the innocent purchaser is fully compensated, if provided with the amount of money that would purchase an asset of the same value on the date of the breach, no longer applies. This disposition would not be a substitute for an order of specific performance. The order for specific performance may issue many months or even years after the breach. The value of the asset may have changed.”¹⁴ In main part for this reason “it is not inconsistent with the rules of the common law to assess damages as of the date of trial.”¹⁵

The most obvious reading of this passage is that in order to *adhere* to the principle of compensation the usual rule of damages assessed as at breach must be rejected in favour of damages assessed as of the date of trial. Certainly this was the view of Megarry J. in *Wroth v Tyler*¹⁶ which was relied upon by the Supreme Court. The facts in that case were very similar to those in *Semelhago*: the contract was for the purchase of land for £6,000, the value at the closing date was £7,500 and the value at trial was £11,500. Megarry J. stated that “On facts such as these, the general rule of assessing

¹²[1980] A.C. 367 at 400-401 quoted *supra* note 1 at 424.

¹³*Supra* note 1 at 424.

¹⁴*Id.* at 425.

¹⁵*Id.* at 426. The Court also made the formal argument, discussed in more detail below, that a claim for specific performance has the effect of postponing the date of breach.

¹⁶[1974] 1 Ch. 30.

damages as at the date of breach seems to defeat the general principle, rather than carry it out.”¹⁷

But this position does not withstand further consideration. It is obviously true that providing the purchaser, at the date of trial, with the difference between the contract price and the market value at the date of breach without pre-judgment interest would not provide full compensation. If the plaintiff were compensated in full at the time of breach she would be able to invest the money and earn a return or pay off debts and avoid further interest payments. But this is true whether or not the asset is unique and whether or not the plaintiff sues for specific performance and it is for this reason that the courts have the general power to award pre-judgment interest. If the problem is that pre-judgment interest is not fixed at realistic rates, this is a general problem which should be addressed directly. Certainly it provides no basis for distinguishing between damages in lieu of specific performance and damages at law.

Assuming a reasonable award of pre-judgment interest on the damages assessed at the time of breach, Megarry J.’s point is not generally correct. The plaintiff’s contract money plus damages at breach are by definition sufficient to purchase a similar asset at the time of breach. The amount needed to allow the plaintiff to buy a similar asset at the time of trial is this same amount plus an additional amount to allow for the appreciation in value of the asset. The plaintiff receives at least some part of this additional amount in two forms. Pre-judgment interest arguments the award of damages. At the same time, the plaintiff has the contract money available as a result of the breach which he would not otherwise have had. He must do something with that money, and in general we can expect that some return will be earned; the plaintiff in *Semelhago* for example, kept the money in the form of a house, which made a good return. If the rate of interest on the damages and the rate of return which the plaintiff earns on her contract money are equal to the rate of appreciation of the asset in question, an award of damages assessed as of breach plus interest will indeed allow the plaintiff at the time of trial to “turn around and purchase identical or equivalent goods.”

This is not to say that damages plus interest will necessarily provide compensation in fact, but rather that it may very well do so. We cannot know without knowing the rate of appreciation of the asset in question as compared with the rate of return on the plaintiff’s use of her contract money. A failure to grasp this point was clearly at the heart of the decision of in *Wroth v Tyler* where Megarry J. stated said that “In the case before me, I cannot see how £1,500 damages would constitute any true substitute for a decree of specific performance of the contract to convey land which at the time of the decree is worth £5,500 more than the contract price.”¹⁸ With respect, what Megarry J. failed to see is that the purchaser either had £6,000 available to invest which he would not have had but for the breach, or he was saving himself interest on the same amount. When the investment income or

¹⁷*Id.* at 57.

¹⁸*Id.* at 58, quoted by the Supreme Court in *Semelhago supra.* note 1 at 426-27.

foregone costs are added to damages at breach plus interest it is perfectly likely that the purchaser will be fully compensated.

This may not have been apparent in *Wroth v Tyler* where it was not clear on the facts what steps the purchaser took when the deal did not close. In *Semelhago*, in contrast, the point is inescapable because we know what the purchaser in fact did with the money which was freed up by the failure of the transaction; he kept his old house, which he would not have had if the deal had closed. If we ignore the increase in value of this asset, then the plaintiff will receive a windfall. Consider the facts more closely. As noted, the contract price for the vendor's house was \$205,000 and the trial judge found that "[i]n order to finance the purchase, the purchaser was going to put up \$75,000 cash, plus \$130,000 which he was going to raise by putting a mortgage on his old house. The mortgage was in fact taken out. It was for six months and was open so that he could close the deal on the new house and then sell the old one at an appropriate time in the six months following the closing. . ."¹⁹ As noted earlier, when the deal did not go through the purchaser kept his old house, which was worth \$300,000 at the time of trial, while the vendor's house had value market value of \$325,000 at the time of trial.

In view of these facts, consider, apart from what the law is or should be, what award would have taken the purchaser from the monetary position he was in at trial and put him as nearly as possible in to the position he would have been in had the transaction closed on the closing date. The trial judge found as a fact that the purchaser would have sold his old house, which had a value of \$190,000 at the closing date, in order to finance the purchase.²⁰ No doubt he would have used \$130,000 of the proceeds to pay off the mortgage on the old house on selling it, which would have left him with \$60,000 in cash. Now, it may be that the \$130,000 mortgage was a second mortgage and some part of that extra \$60,000 would have been used to pay off a remaining first mortgage. But if the purchaser had wished, he could earlier have used some part of the \$75,000 cash which he used to finance the new house to pay off any first mortgage on his old house. The only change attributable to the failure of the deal itself is that the plaintiff had \$15,000 more cash available and his old house rather than the new one.²¹

¹⁹*Supra* note 1 at 419.

²⁰Quoted by the Supreme Court, *supra* note 1 at 420.

²¹To recap in more detail, near the time set for closing, and in particular immediately after selling his old house, the *net* change in the plaintiff's position from before entering into the agreement would be that he would have the new house instead of the old and \$21,716 less cash (the \$15,000 difference in price of the house plus the carrying charge) that he would otherwise have had. Because the deal did not go through he had the old house and \$6,716 less cash at the same point in time. If "X" is the total amount of cash which the plaintiff had before entering into the agreement, and *i* is the interest rate earned on investments of cash, then we know that if the deal had gone through, at the time of trial the

To determine the net difference in the purchaser's position by the time of trial we must take into account both the relative change in value of the two houses and the rate of return on the extra cash which the purchaser had available. We know the rate of return on both the old and new house on the facts, but we need to make some assumptions regarding the plaintiff's rate of return on his cash. In so doing we must assume that the rate of return on the extra cash is the same whether or not the deal had gone through, since the plaintiff's decision as to how to use his extra cash is not causally related to the house purchase. What *is* causally related to the house purchase is the amount of cash which the purchaser has to invest. At the very worst the plaintiff's cash investments could have been disastrous and lost all their value. In that case the plaintiff would have been better off by \$25,000 had the contract been fulfilled; or, put another way, if the plaintiff had been awarded \$25,000 at the time of trial he would have been able to sell his old house, as he had planned to do, and then turn around and purchase the house which was the subject of the contract. On any less disastrous investment, the plaintiff's loss would be much smaller. A bad investment, such the stock market, which returned only 2% over the entire period in question, would have resulted in an actual loss of \$9,671; a better investment, such as medium term government bonds would have resulted in an actual loss of approximately \$3,100; a presumed investment in three month money market paper gives an actual loss of \$2 600.²²

I should emphasize that I am not advocating compensation in fact with a full inquiry as to what the purchaser did do with his money after the breach and what he might have done had the contract been performed. The point is simply a negative one: the principle of compensation does *not* require or justify an award of the difference between the contract price and the value of the asset at trial. The

purchaser would have had a house worth \$325,000 plus investments worth $(1+i)(X-\$21,716)$. Since the deal did not go through, the purchaser had a house worth \$300,000 plus investments worth $(1+i)(X-\$6,000)$ at time of trial. The net difference is $(\$25,000 - (1+i)\$15,000)$. That is, had the deal gone through, the plaintiff would have been ahead \$25,000 from the increased value of the house, but behind by the amount of the return on \$15,000 because he would have had that much less cash to invest in other things.

²²The return to an investment in the stock market is calculated as the increase in the average of the weekly TSE values reported by *The Economist* for November 1990 over November 1986. The return to medium term government bonds is calculated from the average return to 1 to 3 year Government of Canada marketable bonds reported in the Bank of Canada's *Selected Canadian and International Interest Rates Including Bond Yields and Interest Arbitrage*, p.13-14, assuming one year bonds reinvested annually over the period in question, for a total return of 1.456 or an average of 11% annually. An investment in the 3 month money market, reinvested every 3 months for the four years from Nov 1986 to Nov 1990 would bring a total return of 1.492, or an average annual yield of 10.52%: calculated from 3 month money market rates as reported in *The Economist* Economic and Financial Indicators, from Nov 1986 to Nov. 1990.

award in *Wroth v Tyler* was almost certainly highly overcompensatory and the result in *Semelhago* is undoubtedly so. The justification for the above lengthy discussion of this basic point is the continued influence of the argument of Megarry J. in *Wroth v Tyler*.²³ It is time that fallacy in *Wroth v Tyler* is laid to rest.

The general principle that the assessment of damages is compensatory is by no means sacrosanct. The principle that the plaintiff should be put in the position she would have been in had the defendant not breached is a starting point in the calculation of damages. Many other considerations, such as the principles of mitigation and foreseeability, are then taken into account in arriving at a final award, so that compensation in fact is the exception rather than the rule.²⁴

Accordingly, a second strand of the Court's argument suggests that even if a windfall has been granted, it is justified if the property is unique. The reason is that if the property is unique specific performance would be available and "the damages that are awarded [in lieu] must be a true substitute for specific performance."²⁵ Certainly an award of specific performance without adjustment to the contract price would have granted a windfall to the plaintiff in *Semelhago* as it would have allowed him to buy a house worth \$320,000 for only \$205,000. The implication is that if the purchaser would have gained a windfall from an order of specific performance he should also gain one from an order of

²³The influence of this fallacy is also seen in the Court of Appeal's discussion of the vendor's proposal that the purchaser be awarded the difference between the increase in value of the new house and the increase in value of the hold house, that is, \$10,000 (*supra* note 1 at 422). The Court of Appeal dismissed this with the comment (*supra* note 5 at 482) that the vendor's proposed assessment of damages "would achieve little, if any" of the objective of putting the plaintiff in the position he would have been in had the deal closed. But the effect of the vendor's proposal would be to provide full compensation in fact on the assumption that the purchaser held the extra \$15,000 in cash which was available because the deal did not close in a non-interest bearing form. If this were the case, the true loss would have been \$10,000. The vendor's proposed approach thus makes a very conservative implicit assumption about what the plaintiff would have done with his extra cash and is therefore most almost certainly *overcompensatory*. If compensation in fact were the goal, the vendor's proposal would be defensible as a rough and ready calculation. However, it is not consistent with the mitigation principle, discussed below, as it takes into account the actual increase in value of the house which the purchaser retained, rather than a notional return on the purchase price.

²⁴The most obvious general justification for overcompensation is punitive or exemplary damages. Such awards are recognized as extraordinary and justified only in unusual circumstances and are particularly rare in cases of breach of contract: see S.M. Waddams, *The Law of Damages*, 2nd ed. (Canada Law Book, 1991) ¶ 11.210 and ¶ 11.250. Certainly the vendor on the facts in *Semelhago* is not deserving of punishment on any accepted theory of exemplary damages.

²⁵*Supra* note 1 at 426.

damages in lieu of specific performance. In other words, the principle of compensation is overridden by the competing principle that an award of damages in lieu of specific performance must be equivalent to an award of specific performance.

The point that damages in lieu of specific performance must be a true substitute for specific performance is compelling, but to conclude from this that a windfall award of damages in lieu of specific performance is justified begs the question of why the purchaser should gain a windfall from an order for specific performance. The Court did not address this issue in its reasons, undoubtedly because in argument the vendor conceded the crucial point that the purchaser would have been entitled to the windfall had he obtained a decree for specific performance as opposed to damages in lieu.²⁶ Given this concession it is no wonder that the Court refused to draw an arbitrary distinction between an award of specific performance and an award of damages in lieu.

I suggest that the vendor's concession was unnecessary. It is true that traditionally no adjustment was made to the purchase price as the vendor's benefit from continued occupation was considered to roughly offset the purchaser's benefit from continued use of the purchase money. This rough and ready calculation was adequate in day so stable property prices and low inflation, but it does not allow for increases in property values which result either from a boom in the property market or from general inflation. These issues became increasingly pressing because of the general inflation of the 1970s and 80s and it was at this time that the courts began to wrestle with the issue. It is true that the weight of authority, in particular the Ontario Court of Appeal decision in *Rimes*, was against any adjustments, but as we have seen in *Semelhago* itself the Ontario Court of Appeal had begun a

²⁶The old tradition of reporting the argument of counsel as well as the decision of the Court could be very illuminating. While this tradition has been abandoned, videotapes of argument before the Supreme Court are now available (from International Duplication Services Inc., Ottawa), and the tapes of argument in *Semelhago* reveal the following exchanges between John Swan, counsel for the vendor, and members of the Court:

(At 21 minutes) Swan "Had he not abandoned the...his claim for specific performance, had he sought specific performance and continued with it, then it is perfectly possible that he could have appropriated the whole gain and kept the gain on his own house."

Gonthier J. "But why should it be different, that's my problem, because damages are normally granted, I would think, as being a substitute for, in other words the equivalent of."

(At 24 minutes) Swan "But you see, if the plaintiff [sic] through his fault delays so there is no need for the plaintiff to sell his house and let's suppose that the plaintiff had persisted at trial and got a decree of specific performance and had carried it through, then we can't possibly argue that it is improper for him to then sell his own house, let's say at 300,000, buy the plaintiff's house at 205,000..."

Sopinka J. "He would have sold his house but at the higher price..."

retrenchment from its position in *Rimes* and the case law was not so well established or consistent that the matter could be considered settled even today.²⁷

In justifying its method of calculation of damages in lieu of specific performance the Court noted that when an action for specific performance is commenced the contract continues in force and neither party is relieved of their obligations under the agreement. The Court presented this as a purely formal point without inquiring into the rationale under the rule, but it does suggest two more substantial arguments.

The first is that since neither party is relieved of their obligations, the party who seeks specific performance must be ready willing and able to close. If the purchaser were required to close at any instant of the day or night or face losing his or her entitlement to specific performance, then it might be reasonable for the purchaser to put the purchase money in a shoe box under the bed in order to have it ready for closing. And indeed, the method of calculation approved by the Court in *Semelhago* would result in compensation in fact to a purchaser who kept his purchase money in a shoe box or in some other non-interest bearing form between the date of breach and the date of trial.²⁸

This in itself does not justify an award of \$120,000. In the first place, if the law were that a purchaser seeking specific performance must be ready to close at any instant, the plaintiff in *Semelhago* clearly did not satisfy this requirement and should therefore have been disqualified from pursuing specific performance or damages in lieu. And in any event the law does not impose such a requirement. Time is not of the essence in equity and if the closing has been delayed by the fault of the vendor he will not be able to raise the time provision to defeat the claim of the purchaser.²⁹ If this were not the case a claim for specific performance would never succeed, since contracts for the sale of land routinely

²⁷See *Ribic v Weinstein* (1982) 140 D.L.R.(3d) 258 (Ont. H.C.J.) affd 10 D.L.R.(4th) 717 (Ont. C.A.); *Metropolitan Trust Co. of Canada v. Pressure Concrete Services Ltd.* (1976), 9 O.R. (2d) 375 (C.A.) and *Morgan v Lucky Dog Ltd.* (1987) 45 R.P.R. 263 (Ont. H.C.J.), refusing to make adjustments; contrast *Skariah v. Praxl* (1990) 73 O.R.(2d) 1 (H.C.J.) and *Tanu v Ray* (1981) 20 R.P.R. 22 (B.C.S.C.) ordering specific performance with an adjustment. See also the discussion in Robert J. Sharpe, *Injunctions and Specific Performance*, 2nd ed. (Canada Law Book 1992) ¶11.280-11.360, which was relied on in *Skariah v. Praxl*. In *Dynamic Transport Ltd. v. O.K. Detailing Ltd.*, [1978] 2 S.C.R. 1072, 4 R.P.R. 208, 85 D.L.R. (3d) 19, the Supreme Court upheld an award calculated on the basis of the rule in *Wroth v Tyler*, but the calculation of damages was not the main issue on appeal and the point does not appear to have been argued.

²⁸If the purchaser in *Semelhago* had put \$205,000 in a shoe box at the date of breach, then at the time of trial his net worth would have been \$205,000 plus investments worth $(1+i)(X - \$21,716)$. The difference between this amount the purchaser's wealth had the deal closed (see *supra* note 22) is \$120,000.

²⁹*Stickney v Keeble* [1915] A.C. 386 (H.L.).

provide that time is of the essence. The purchaser will have to have the purchase money available on some reasonable notice, but there are wide range of arrangements, from relatively liquid investments to a pre-approved mortgage backed by longer term investments, which would allow the purchaser to close within a reasonable time while still earning a positive return on his or her purchase money.

The second point, then, relates to the duty to mitigate. If there is no duty to mitigate when an order of specific performance is sought, then a plaintiff who kept the purchaser money in a showbox and so lost interest on it, would be entitled to claim that loss. But I suggest that there is a duty to mitigate even when an order of specific performance is sought, although the precise contours of that duty are different than in a case where the plaintiff has no legitimate claim to specific performance. The leading discussion of this point is found in the decision of the Supreme Court in *Asamera Oil Corp. Ltd. v Sea Oil & General Corp.*³⁰ and the main support for the proposition that there is no duty to mitigate when an order for specific performance is sought is the statement therein of Estey J. that “Before a plaintiff can rely on a claim to specific performance so as to insulate himself from the consequences of failing to procure alternate property in mitigation of his losses, some fair, real, and substantial justification for his claim to performance must be found.”³¹

But we should not be too quick to read this negative statement to stand for the converse positive statement that a plaintiff who does have a real claim to performance can entirely insulate themselves from the duty to mitigate. The statement must be read in context. Specific performance was denied on the facts and the decision in *Asamera* was motivated by an awareness of and a hostility to the windfall which an order of specific performance might generate. The trial judge in *Asamera* had relied upon English authorities which allowed an award of damages assessed at breach or at trial at the election of the plaintiff, as is the effect of allowing the plaintiff to pursue elect legal damages or damages in lieu of specific performance in the context of real property. The Supreme Court held that these cases ought not to be followed, in part because “they ignore the all-important and overriding considerations which have led to the judicial recognition of the desirability and indeed the necessity that a plaintiff mitigate his losses arising on a breach of contract.”³² Because the goods in question in *Asamera*, stocks, were fungible and had a value which is readily ascertained, the Court was able simply to hold that specific performance was not be available, so it was not necessary to directly address the possibility of making monetary adjustments to an award of specific performance.

The reason for imposing a duty to mitigate is readily apparent from the facts in *Semelhago*. In the absence of such a duty the windfall resulting from an order of specific performance or damages in

³⁰[1979] 1 S.C.R. 633, 89 D.L.R.(3d) 1 (S.C.C.), hereinafter cited to the D.L.R.

³¹*Id.* at 26.

³²*Id.* at 13.

lieu would encourage purely speculative litigation. Consider a case in which there is general inflation which affects land and other goods equally. For concreteness, assume that the contract price is \$200,000, the market price is the same, and the inflation rate is 10%. If the vendor breaches damages are clearly only the purchaser's out of pocket expenses and if the vendor offers to settle for this amount the plaintiff will agree rather than sue for damages at breach plus interest. But even if actual damages are minimal, the purchaser will have a strong incentive to sue for specific performance if no monetary adjustment accompanies the decree of specific performance, since if the matter takes four years to come to trial the purchaser can anticipate becoming the owner of a house then worth \$293,000 for a payment of only \$200,000. Seeking an order of specific performance is a one way bet which allows the purchaser to generate a solid return equal to the property inflation rate without tying up any of his or her own money.

The statements of principle in *Asamera* do not support the view that there is no duty to mitigate when specific performance is sought and neither do the more specific remarks with regard to specific performance. The statement that the plaintiff may not insulate himself from the duty to mitigate without a substantial claim to performance is found in a paragraph which began with the pronouncement that "On principle it is clear that a plaintiff may not merely by instituting proceedings in which a request is made for specific performance and/or damages, thereby shield himself and block the court from taking into account the accumulation of losses which the plaintiff by acting with reasonable promptness in processing his claim could have avoided."³³ The Court further that when the plaintiff does have a legitimate claim for specific performance, "the action for performance must be instituted and carried on with due diligence. This is *but another application of the ordinary rule of mitigation* which insists that the injured party act reasonably in all of the circumstances."³⁴ This is a direct statement that there is a duty to mitigate when an order of specific performance is sought, although in contrast to a case in which there is no legitimate claim for specific performance, that duty does imply that the purchaser must mitigate by purchasing equivalent goods at the date of breach. Note further that the Court's statement that the action for specific performance must be carried out with due diligence cannot be considered an exhaustive statement of the plaintiff's duty to mitigate in the context of seeking an order for specific performance. Rather, as the Court states, it is simply an application of the ordinary rule of reasonable avoid of losses to a hypothetical set of facts. When interest rates are low and delay in going to trial is minimal, then instituting the action for specific performance with due diligence might well satisfy the plaintiff's duty to act reasonably in the circumstances. This does not necessarily imply that diligence in instituting the action will suffice when asset values are fluctuating and delays are lengthy.

³³*Id.* at 26.

³⁴*Id.*, emphasis added.

Further, while the plaintiff in *Asamera* was not entitled to specific performance, we should note that it did have the benefit of an injunction restraining the defendant from disposing of the assets in question. If an action for specific performance would insulate a plaintiff from a duty to mitigate, it is reasonable to suppose that reliance on an injunction, which in effect is judicial assurance that a claim for specific performance will not be defeated by the actions of the defendant, should do the same. So the plaintiff argued, but the Court held that it was “under the general duty to mitigate its losses and may not escape this duty by relying on the 1960 injunction interminably.”³⁵ Thus the decision in *Asamera* illustrates that the plaintiff is under a duty to mitigate even when he has a legally recognizable expectation of performance.

The Court in *Asamera* did not hold the plaintiff to a strict duty to mitigate as of the day of breach. Rather, the Court recognized that in view of the injunction the plaintiff had obtained and other peculiar facts of the case, reasonable mitigation entailed purchase of shares at a time somewhat after the breach. The decision in *Asamera* supports a similar rule in cases in which the plaintiff is pursuing a legitimate claim to specific performance: the plaintiff is not relieved of the duty to act reasonably in mitigation of its losses, but the definition of reasonable behaviour must take into account the legitimate expectation of performance and so is more flexible than a strict requirement that the plaintiff purchase similar goods at the time of breach.

One consequence of the duty to mitigate is that the plaintiff will not necessarily be compensated for all losses in fact suffered. The duty to mitigate crystallizes the plaintiff’s losses at a certain point in time. The actions of the plaintiff in the short term and the losses suffered in fact as a result, before the loss is considered to have crystallized, are relevant and nice questions arise as to how what is reasonable in the circumstances.³⁶ But in the longer term, losses or gains which the plaintiff suffers are considered, in law if not strictly in fact, to be caused by the plaintiff’s investment decisions rather than by the breach. This is consistent with the Supreme Court’s statement in *Semelhago* that in calculating damages no allowance should be made for the increase in value of the plaintiff’s residence which he retained when the deal did not close. While it is true that the proximate cause of the plaintiff remaining in his house in the short term is that the deal did not close, but he was under no legal obligation to do so. The plaintiff might have sold his house and moved into an apartment, or bought a much smaller house and invested the difference, wisely or poorly; but once the law considers the damages to have crystallized, the consequences of any of these decisions by the plaintiff are irrelevant. This central to the

³⁵*Id.* at 30.

³⁶See generally *Asamera, id.* and for a discussion of the issue in American law see the Annotation, Specific Performance: Compensation or Damages Awarded Purchaser for Delay in Conveyance of Land, 7 A.L.R.2d 1204.

mitigation principle; if the plaintiff were compensated for all losses in fact suffered, he or she would have no incentive to take reasonable steps to avoid those losses.

Thus, while it is not appropriate to take into account the increased value of the purchaser's house which was retained as a result of the breach, neither is it appropriate to ignore entirely the fact that the vendor's breach freed up the purchase money for alternative investment by the purchaser. Rather, if the Court had considered the issue of mitigation on the facts in *Semelhago*, it would have been appropriate to deduct from the \$120,000 the notional return on the \$205,000 purchase price, without regard to what the purchaser in fact did with the purchase money. So, if the appropriate notional interest rate is 10% allowance for mitigation would have resulted in a deduction of \$95,000 from the damages assessed at trial.

This brings us to the question of the deductions made by the Court of Appeal. From the \$120,000 difference between the contract price and the value of the property in question at trial, the Court of Appeal deducted legal expenses and carrying charges on the 6 month mortgage, and, more importantly, it also deducted from this the notional return on the \$75,000 which the plaintiff would have spent on the purchase, for a net award of \$80,810.21.

There are several problems with this calculation. First, the deductions are clearly not sufficient to allow for the duty to mitigate, since notional interest was deducted only \$75,000 rather than on the entire purchase price.

Further, the Court of Appeal explained that its method of calculation "attempts to track the events as the trial judge found they would have unfolded, and attempts to put the purchaser, to the extent that money can do it, in the position he would have been had the sale closed."³⁷ If the mitigation approach discussed above is correct, then the Court of Appeal's attempt to provide compensation in fact was inappropriate.

Nor are the Court of Appeal's calculations appropriate even in light of its stated aim. The calculation fails to put the plaintiff in the position he would have been in had the trial closed for two reasons. First, the Court used a notional interest rate of 10% in calculating the return on the \$75,000 in cash. This correctly recognizes that since the transaction did not close the purchaser had this money free for investment elsewhere and this offsetting benefit to the plaintiff must be taken into account. But, as discussed above we know that the net result of the purchaser's actions after the breach was that \$60,000 of this was invested in retaining the old house, which made a return of just over 12%. The notional rate of 10% should have been applied to the extra \$15,000 alone. Further, an even more obvious cost of earning the \$120,000 is the carrying cost of the \$130,000 mortgage which was needed in addition to the \$75,000 cash to finance the house purchase. Deducting the notional interest on the cash while failing to deduct the carrying cost of the mortgage is inexplicable except as a mistake.

³⁷*Supra* note 5 at 482.

Thus the Supreme Court's reservations regarding the deductions made by the Court of Appeal are well warranted, even apart from the difficulty of distinguishing *Rimes*. In view of this, the Court's statement that damages in lieu of specific performance are to be calculated as the difference between the contract price and the value at trial is best interpreted as a statement this amount is appropriate absent any argument regarding deductions to be made to account for the duty to mitigate. When argued, deductions from this amount to allow for notional interest earned by the plaintiff on the purchaser money in compliance with its duty to mitigate are not precluded. It might be objected that this interpretation robs the Supreme Court's decision of any substance. But even without full analysis of important deductions, the holding that the starting point for assessing damages is the difference between contract price and the value of the asset at trial is very important in itself. To start with with damages assessed at the time of trial and then deducting notional interest which would have been earned from reasonable effort to mitigate is significantly different from the approach adopted in *Asamera*, for example, which was to determine the date at which the loss should be considered to have crystallized and award damages calculated as at date, plus interest. The difference is that if the former method is used the plaintiff enjoys the benefit of any unusual appreciation of the asset in question, while if the latter method is used he does not.

It might be suggested that if the disappointed purchaser has a legitimate claim to specific performance she should get the benefit of the increased value of the property, since it was that particular property she wanted. A full response to this point requires an analysis of the rationale for specific performance, which also allows a discussion of the Court's holding that specific performance should no longer be granted routinely in the sale of land.

In restricting the availability of specific performance the Court noted that specific performance is justified only when the asset is unique and "While at one time the common law regarded every piece of real estate to be unique, with the progress of modern real estate development this is no longer the case."³⁸ This reasoning is incomplete, since uniqueness of the asset is by no means the only justification for an award of specific performance.

Specific performance has two main advantages over an award of damages.³⁹ First, it results in more accurate compensation for the innocent party. An order for specific performance does not necessarily mean that the contract will be specifically performed since the plaintiff may agree not to enforce the order in return for compensation. If the cost to the defendant of performance is more than

³⁸*Id.*

³⁹See generally Robert .J. Sharpe, *Injunctions and Specific Performance*, 2nd ed. (Canada Law Book 1992) ¶7.50 -- 7.110; Alan Schwartz, *The Case for Specific Performance* (1979) 89 *Yale L. J.* 271.

performance is worth to the plaintiff, the defendant will prefer to offer the plaintiff acceptable compensation rather than perform. Conversely, if performance is worth more to the plaintiff than it costs the defendant, both parties will prefer performance to compensation. The compensation which the plaintiff will demand in order to excuse performance more accurately values the true loss than any award which could be made by a court, for two reasons. The plaintiff will not accept any offer for money offer which does not fully compensate her for any special subjective value which the asset has to her, since in that case she would prefer the asset to the compensation and she has the right to demand it. At the same time, she has no incentive to reject any offer which is at least sufficient to compensate her for that unique subjective value. This means that bargaining over an order of specific performance gives the parties an incentive to reveal (through the compensation agreed upon) their true subjective valuations of performance. This is not the case in damage assessment by the court, in which the plaintiff has every incentive to claim that the asset as a much higher unique value to her than is in fact the case. Further, even “objective” losses are costly and difficult to quantify and as a result this any award of damages by a court must be approximate at best. Again, in bargaining the parties will take into account their own best valuation of the costs and benefits performance, based on all their information, not just that which is readily provable in court. This leads to the second advantage of specific performance, which is that it eliminates the need for time consuming and expensive discovery and litigation related to the judicial quantification of damages.

The main disadvantage of specific performance is the need for judicial supervision of the remedy. Many aspects of the agreement may be only imperfectly specified in the written document because of the difficulty of quantification and the parties may be relying largely on the good faith engendered by an ongoing relationship to fill in the details, in which case strict performance of the contractual terms will be an inadequate remedy. Even where the contract is sufficiently specific, if performance is complex supervision of recalcitrant parties may be practically infeasible.

The overall case in favour of specific performance depends on how all of these factors play out in a particular context. The argument favouring specific performance is certainly strengthened when the asset is unique so that the difference between the subjective value of performance and objective damages awarded by a court may be large, but this is only one factor. When uniqueness is not an issue, the argument turns on the cost of damage assessment by the court as compared with the cost of supervision of the remedies, with an additional tilt in favour of specific performance because it leads to more accurate valuation of objective factors. In the case of contracts for the sale of land, supervision and enforcement of an order of specific performance is straightforward, while quantification of damages is costly, requiring as it does the evidence of expert assessors and resolution of the inevitable differences between them. Thus the previously well-established rule that specific performance is available to either the vendor or purchaser as a matter of course in the sale of land is strongly supported as a matter of policy. The fact that specific performance remains available when the property is unique

will improve valuation in the case of unique assets, but will further increase costs generally because of the potential for a mini-trial over whether the land is in fact unique.

So, one conclusion of this analysis is that apart from concerns with granting a windfall in allowing an order for specific performance, the holding in *Semelhago* that specific performance should no longer be routinely available is unfortunate because it can be expected to result in more expensive settlement and litigation and less accurate compensation.

The analysis also offers more support for the view that a plaintiff with a legitimate claim for specific performance should nonetheless be under a duty to mitigate. The rationale for ordering specific performance in contracts for the sale of unique assets is compensatory and any windfall awarded to the plaintiff under an order for specific performance is as badly in need of justification as it would be in the context of damages. The windfall nature of the award is not changed if the property in question is in fact unique in the sense that it has some special value to the plaintiff. It is true that in such a case an ordinary award of damages will be undercompensatory. But damages assessed at the date of trial without allowance for mitigation will no more reflect the asset's unique value to the purchaser than will damages awarded at the date of breach, since the degree of overcompensation would depend on the rate of inflation of house prices and the length of time from breach to trial. Neither of these factors has the remotest connection with the idiosyncratic value which the purchaser may place on the property. Specific performance responds to the problem of valuation of unique assets by requiring the parties to bargain *between themselves* thus providing incentives for the revelation of the true subjective value of the asset. The functional nature of SP is such that it elicits the subjective value of the property: the functional nature of monetary damages is such that the court must attempt to objectively measure the damages. It is impossible for a judicially determined monetary award to achieve this end.

But the more difficult question is whether a plaintiff seeking specific performance subject to the duty to mitigate should be entitled to any unusual return on the asset in question. So, on the facts in *Semelhago* property prices were rising at approximately 12% per year while a safe invest returned about 10%. Should the purchaser be entitled to the extra 2% return?⁴⁰ The foregoing analysis of specific performance suggests that we should distinguish between the unusual subjective value of the property and the unusual objective returns. The two are not related. A purchaser might place a very high subjective value on a property even though the property receives no unusual returns, and vice versa. It therefore does not follow that an award intended to compensate for subjective value should

⁴⁰It is striking that the extra return to real estate was only 2%, particularly in view of the Court of Appeal's comment that the litigation occurred during "a time of rapidly escalating real estate prices in the Toronto area" (*supra* note 5 at 481). Most of the rapid escalation was evidently due to inflation, which suggests that the real issue in this case from the plaintiff's point of view was to benefit from general inflation rather than from the unusual returns to real estate.

also compensate for unusual objective returns. As noted above, it is not possible for a monetary award, whether “in lieu” of specific performance or not, to compensate for the subjective value. Unusually high returns are available only for extra risk. If the purchaser has a preference for a riskier investment then mitigation at the time of breach is entirely possible, as there will be many available investment which have the same investment riskiness as the property in question even if they do not have the same subjective value to the purchaser.

From a policy perspective the disadvantage with compensating the plaintiff for the unusual returns to the property is that it provides an incentive for speculative litigation, albeit a much smaller incentive than if no deductions are made to account for the duty to mitigate. The reason is that on this approach a purchaser who has suffered no damages at the date of breach will nonetheless benefit by suing for specific performance since damages in lieu will be positive if the rate of appreciation of the property is greater than the notional interest rate. Of course, if the rate of appreciation of the property is less than the notional interest rate, the plaintiff suing for specific performance will not be awarded any damages in lieu, but if the market has declined by the trial date she will simply choose to drop the suit. In other words, allowing the purchaser the benefit of an unusual appreciation in the value of the asset gives the purchaser an option which she exercises by suing.⁴¹ In practice, the price of the option is the cost of litigation including the possibility of bearing the defendant’s costs of the action is unsuccessful, so a disappointed purchaser who has suffered no actual damages will not always choose to sue. But in the case of valuable properties in a volatile market, speculative suits might occur. Even with the relatively small sums at stake in *Semelhago* and modest returns to real estate of 2% more than a safe investment, the net gain from that higher returns would be \$25,000.

While I have argued that on the whole it is undesirable to allow the disappointed purchaser to benefit from any unusual returns to the property subject to an action for specific performance, the point can be reasonably debated. More to the point, the decision of the Supreme Court in *Semelhago* establishes that the plaintiff *is* entitled to any such unusual returns. However, to return to the main point, this is *all* that the decision can be taken to have settled with respect to the calculation of damages. Precedent, sound policy and legal principle all indicate that a plaintiff who seeks specific performance is

⁴¹So in *Asamera Oil* supra note 30 at 20 Estey J. remarked that “It is inappropriate in my view simply to extend the old principles applied in the detinue and conversion authorities to the non-return of shares with the result that a party whose property has not been returned to him, could sit by and await an opportune moment to institute legal proceedings, all the while imposing on a defendant the substantial risk of market fluctuations between breach and trial. . .” See the passage to the same effect from *Jamal v Moolla Dawood, Sons & Co.* [1916] 1 A.C. 175 (J.C.P.C.) at 179, quoted with approval in *100 Main Street Ltd. v W.B. Sullivan Construction Ltd.* (1978) 20 O.R.(2d) 401 (C.A.) at 418. The problem is not as severe in the context of real estate as property prices are not as volatile as stock prices, but this is only a matter of degree. At certain period even real estate prices may be very volatile.

under a duty to act reasonably in mitigation of his or her losses, although the precise nature of what is considered reasonable must take into account the reasonable expectation of performance. The Court in *Semelhago* expressly left open the question of the deductions made by the Court of Appeal and the issue of mitigation was not argued, or more precisely, the vendor's concession that the purchaser would be entitled to a windfall if specific performance were sought amounts to a concession that no adjustments to account for mitigation need be made. The law cannot be determined by incautious concessions of the parties and the issue of the duty to mitigate in the context of an order for specific performance cannot be considered to have been settled in *Semelhago*. The Supreme Court's decision stands only for the proposition that when damages are awarded in lieu of specific performance the calculation must begin with the difference between the contract price and the value at trial. The door remains open to substantial deductions to account for the duty to mitigate, if these are argued.