COURT OF APPEAL FOR BRITISH COLUMBIA

Citation: *Peace River Partnership v. Cardero Coal Ltd.,* 2023 BCCA 351

Date: 20230911
Dockets: CA48174, CA48177
Docket: CA48174

2023 BCCA 351 (CanLII)

Between:

Peace River Partnership

Appellant/
Respondent on Cross Appeal
(Plaintiff)

And

Cardero Coal Ltd.

Respondent/
Appellant on Cross Appeal
(Defendant)

\- and -

Docket: CA48177

Between:

Carbon Creek Partnership

Appellant/
Respondent on Cross Appeal
(Defendant/Plaintiff by Counterclaim)

And

Cardero Coal Ltd.

Respondent/
Appellant on Cross Appeal
(Plaintiff/Defendant by Counterclaim)

Before: The Honourable Mr. Justice Harris
The Honourable Mr. Justice Fitch
The Honourable Justice Skolrood

On appeal from: Orders of the Supreme Court of British Columbia, dated February 17, 2022 (*Cardero Coal Ltd. v. Carbon Creek Partnership*, 2022 BCSC 253, Vancouver Dockets S159680, S160477) and June 30, 2022 (*Cardero Coal Ltd. v. Carbon Creek Partnership*, 2022 BCSC 1103, Vancouver Dockets S159680, S160477).

Counsel for the Appellants:	P.T Linder, K.C.
Counsel for the Respondent:	S. Stephens
Place and Date of Hearing:	Vancouver, British Columbia March 29–30, 2023
Place and Date of Judgment:	Vancouver, British Columbia September 11, 2023

Written Reasons by:
The Honourable Mr. Justice Harris
The Honourable Justice Skolrood

Concurred in by:
The Honourable Mr. Justice Fitch

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Summary:

These appeals arise out of two actions that were brought concerning alleged breaches of agreements relating to a coal mining development project in northern British Columbia. The appellants, Carbon Creek Partnership ("CCP") and Peace River Partnership ("PRP"), signed a joint venture agreement ("JVA") and a lease agreement ("Lease") with the respondent, Cardero Coal Ltd. ("Cardero"). Following a decline in the price of coal, progress on the mining project was stalled and Cardero surrendered the land it had agreed to lease. In the fallout, both parties claimed the other breached both the JVA and the Lease. The trial judge found CCP had breached the JVA; that Cardero had not breached the JVA by surrendering the land; and that Cardero had breached the Lease by not paying a $500,000 advance royalty fee. CCP and PRP allege the judge erred in concluding: (1) that Cardero did not breach the JVA; (2) that Cardero's surrender notice was effective; and (3) that CCP breached the JVA. Cardero cross appeals the judge's award of costs.

Held: Appeal dismissed, cross appeal allowed in part. The judge did not make any of the errors CCP and PRP allege. The judge read the language of the JVA and the Lease as a whole, giving the words used their ordinary and grammatical meaning, consistent with the surrounding circumstances known to the parties at the time of the formation of the contract. He was alive to the evidence of the surrounding circumstances, and appropriately weighed that evidence in his analysis. Cardero's cross appeal is allowed in part. The judge erred in finding he was precluded from considering Cardero's settlement offer simply because the prospect of such an offer was not contemplated in the indemnity clause. The judge's cost order is varied to provide that PRP is entitled to be indemnified for its costs in advancing the Lease action, pursuant to the terms of the Lease, up until August 19, 2021, with the parties to bear their own costs thereafter.

Reasons for Judgment of the Honourable Mr. Justice Harris and the Honourable Justice Skolrood:

Introduction

[1] These appeals arise out of two actions relating to agreements pertaining to a coal mining development project (the "Project") in Carbon Creek, an area in northeastern British Columbia known to have substantial coal deposits. The parties made competing claims against one another alleging breach of the two agreements at the centre of the dispute.

[2] The Project and the agreements have a lengthy history as detailed by the trial judge in reasons indexed at 2022 BCSC 253 ("RFJ"). For the purpose of these appeals, it is not necessary to provide an extensive recounting of the facts.

Background

[3] Prior to the disputes arising, the Project comprised three contiguous parcels of land in the Carbon Creek area — the Freehold parcel, the Burns parcel and the Johnson parcel. Exploration of these parcels reported a significant volume of coal reserves. Historically, ownership of the parcels was disputed, which, at the outset, prevented the development of the Project. Ultimately, the competing interests were resolved and the agreements under consideration executed.

[4] Carbon Creek Partnership ("CCP") and Peace River Partnership ("PRP"), entities controlled by P. Burns Resources, were created for purpose of moving forward with the Project. The judge referred to these entities collectively as the "Partnerships". The initial party to the agreements with the Partnerships was Coalhunter Ltd. Coalhunter later became Cardero Coal Ltd. ("Cardero"). For convenience, we will refer to Cardero even when referring to its predecessor, Coalhunter.

[5] On June 15, 2010, the Partnerships and Cardero executed two agreements. Larry Horan represented the Partnerships and Michael Hunter represented Cardero.

[6] The first agreement created a joint venture between Cardero and CCP (the "JVA"). Essentially, Cardero "agreed to assume 100% of the costs of exploration, development, mining, and marketing in return for a 75% interest in the Project". CCP carried a 25% interest. Cardero was appointed Manager of the Project and was obligated to carry out the operation of the Project in "accordance with sound mining and engineering practices": JVA Article 8.2.

[7] At the time the agreements were executed, the Freehold did not form part of the Project. Cardero was granted a future option to enter into a lease for the Freehold. This formed the basis of the second agreement, which we will describe below.

[8] Article 4.13 of the JVA provided that "if and when" the Freehold is granted to Cardero, it "shall form part of the Premises and the interest … shall be held … in

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trust for the benefit of the … Joint Venture for so long as the … Joint Venture remains in effect" (the "trust clause"). Similar terms were established for licenses in relation to the Burns and the Johnson parcels (Articles 4.10 to 4.12), which formed part of the Project at the time the JVA was executed.

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[9] Article 5.10 gave Cardero (in its position as Manager) the option to "abandon … any of the Coal Tenures comprised in the Premises" (the "abandonment clause"). Withdrawal from the joint venture was permitted and governed by Article 11.1.

[10] The second agreement granted Cardero "an option to enter into a coal lease for the Freehold with PRP": RFJ at para. 26. We will refer to this agreement as the "Coal Lease Option Agreement", and the underlying lease as the "Lease".

[11] If the option was exercised, the Lease granted Cardero the exclusive right to mine the Freehold. To maintain the option, Cardero was obligated to pay PRP $6 million as well as a 5% royalty on any production.

[12] In the event Cardero failed to obtain the necessary permits by June 15, 2013, and commence production by June 15, 2017, PRP had the right to terminate the Lease: Lease Article 20.1.

[13] Article 23.1 provided Cardero the right to surrender the lands under the Lease, "upon giving [PRP] sixty (60) days prior written notice…" (the "surrender clause").

[14] In 2011 and 2012, Cardero conducted drilling, economic assessments and a pre-feasibility study of the Project. On November 7, 2012, satisfied with the economic potential of the Project, Cardero exercised its option on the Freehold by executing the Lease.

[15] Following the execution of the agreements, the price of coal began declining. This made the Project unattractive to investors. As a result, Cardero was unable to secure financing for the Project, and determined it was unlikely to meet the June 15, 2013 permitting deadline under the Lease.

[16] On May 1, 2013, the parties created an amended lease (the "Amended Lease") which replaced the permitting deadline with a new obligation on Cardero to pay the following advance royalties to PRP: June 2, 2013 — $500,000, June 2, 2014 — $2.5 million, (then $2.5 million in 2016 and 2017, and $3.5 million annually from 2018 onward). The Amended Lease also permitted Cardero to elect to defer the payment "due on June 2, 2013 … by notice in writing … to anytime between June 2, 2013 and June 2, 2014": Amended Lease Article 4.2(e)(i).

[17] On May 31, 2013, Cardero executed the amended agreements and elected to defer the payment of the $500,000 advance royalty due June 2, 2013 until June 2, 2014.

[18] Some months later, Cardero determined it would not be able to meet the June 15, 2017 production deadline. By operation of Article 20.1 of the Lease, this would result in the Freehold reverting to PRP. This was an unattractive risk to investors, and left Cardero unable to secure financing for the Project. Cardero sought an extension on the production deadline to 2022, on the basis of a projected rebound in the coal market. It also sought a five-year moratorium on the advance payments as set out in the Amended Lease.

[19] The parties did not reach an agreement and, on April 30, 2014, Cardero issued a surrender notice and a notice of abandonment. As the parties had previously agreed Cardero could deliver a surrender notice on 30 days' notice, both notices were stated to be effective May 30, 2014.

[20] Cardero did not make the advance royalty payment of $500,000 to PRP on June 2, 2014. On July 17, 2014, Mr. Horan, on behalf of PRP, sent a letter to Cardero requesting performance of the obligations that arose from Cardero's surrender. It also demanded payment of the $500,000 advance royalty.

[21] Cardero continued to perform actions required to maintain the joint venture's remaining coal tenures, and also sought to acquire additional interests for the joint venture.

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[22] The JVA established a Management Committee which was constituted to make decisions in respect of the common operations of the Project. The Management Committee held a meeting in September 2014 where it was decided: (1) CCP would prepare an authorization letter to the B.C. Ministry of Energy and Mines (the “Ministry”); (2) CCP would review and approve the insurance policy; (3) CCP would review certain amendments to the JVA; (4) CCP would review a proposed resolution; and (5) the parties would execute a resolution relating to the 2014 work plan.

[23] Mr. Horan signed the work plan resolution but did not action the remaining items. Following the meeting, Mr. Horan, on behalf of CCP, advised Cardero it would not be cooperating in relation to the joint venture until payment of the outstanding $500,000 royalty was addressed.

[24] On August 24, 2015, Cardero delivered a notice of default under the JVA to CCP based on CCP’s alleged failure to action the remaining items from the September 2014 meeting.

[25] The next steps are summarized by the judge:

> [104] Cardero then took steps to schedule a Management Committee meeting for September 3, 2015. However, since CCP refused to attend, no quorum was achieved. The meeting was therefore adjourned and reconvened in Vancouver on September 15, 2015. Again, CCP failed to attend. However, pursuant to fallback terms in the JVA, quorum was achieved this time even without CCP. The Management Committee passed various resolutions in connection with the 2015 work plan and other outstanding matters. All items of business at the meeting passed unanimously, including approval of the insurance policy for the Joint Venture, approving amendments to the JVA to modify the Manager’s accounting responsibilities, and approving the minutes of the September 16, 2014 Management Committee meeting. In relation to the letter to the Ministry, the Minutes note that “unless the CCP provided authorization for the Manager to act on their behalf, there was in fact nothing that the Manager could do to change that situation”.

[26] On November 20, 2015, Cardero delivered a notice to CCP indicating it was electing to acquire CCP’s interest in the joint venture (as per Article 12.1 of the JVA). Cardero filed its notice of civil claim on the same date.

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[27] On January 18, 2016, CCP delivered a formal notice of default to Cardero under Article 12.1 of the JVA. The default identified in the letter was "Cardero's decision to irrevocably surrender its interest and terminate the Lease with PRP": RFJ at para. 107. CCP filed its notice of civil claim on the same date.

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[28] On August 19, 2021, Cardero made a formal settlement offer. Broadly, Cardero offered: (1) to settle the JVA Action by consent order that would grant Cardero the right to purchase CCP's joint venture interest; and (2) to settle the Lease Action by paying $500,000 to PRP with contractual interest, after which the parties would enter a consent order dismissing the action with no costs payable to either party. The Partnerships did not accept the offer.

At Trial

[29] The two actions were heard together in a trial that lasted 11 days.

[30] In the first action, Cardero asserted CCP breached the JVA by refusing to participate or cooperate in the joint venture, and by failing to comply with decisions of the Management Committee (the "JVA Action"). CCP filed a counterclaim (the "JVA Counterclaim") alleging Cardero breached the JVA "by abandoning the Freehold contrary to its obligation to maintain the property in trust for the Joint Venture": RFJ at para. 130.

[31] In the second action, PRP alleged that Cardero's surrender notice was ineffective, thus resulting in Cardero being in breach of its obligations under the Lease. PRP sought damages for the breach, as well as payment of the $500,000 and $2 million advance royalties (the "Lease Action").

[32] The judge determined:

a) CCP breached the JVA by refusing to provide the letter and follow Management Committee decisions, and by asserting it would no longer cooperate with the joint venture;

b) Cardero's letter of August 24, 2015 was effective notice of default under the JVA;

c) Cardero's surrender notice was effective notice under the Lease;

d) Cardero did not breach the JVA by abandoning the Freehold and failing to maintain it in trust for the benefit of the joint venture; and

e) Cardero breached the Lease by not paying the $500,000 advance royalty.

[33] In the JVA Action, the judge made an order entitling Cardero to purchase CCP's interest in the joint venture. CCP's counterclaim was dismissed. In the Lease Action, the judge awarded PRP $500,000 plus interest, and "losses" as assessed by the Registrar. PRP's claim for $2 million was dismissed.

[34] In reasons indexed at 2022 BCSC 1103, the judge gave supplementary reasons on costs (the "Costs Reasons"). In the JVA Action, he found Cardero was entitled to be indemnified by CCP for its costs pursuant to the terms of the JVA. In the JVA Counterclaim, he found Cardero was entitled to costs as against CCP at Scale C, with double costs for all steps taken after the settlement offer date (August 19, 2021). In the Lease Action, He found PRP was entitled to be indemnified by Cardero for its costs in advancing the Lease Action pursuant to the terms of the Lease. He directed the allocation of trial costs as between the JVA Claim, the JVA Counterclaim, and the Lease Claim be divided equally.

<u>Issues on CCP and PRP's Appeals</u>

[35] CCP and PRP have each appealed. In addition, Cardero cross appeals the judge's award on costs in both actions. Cardero's cross appeal is addressed below.

[36] Depending on the issue, CCP and PRP allege the judge erred in concluding:

a) Cardero did not breach the JVA;

b) Cardero's surrender notice was effective; and

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c) CCP breached the JVA.

[37] We will consider each in turn. We observe, however, that the appellants raised a number of subsidiary issues. In our view, those issues are subsumed within the principal issues we have just described.

1. Did the judge err in concluding Cardero did not breach the JVA?

[38] In the JVA Action, CCP argues the judge erred in interpreting the agreements in a way that permitted Cardero to abandon the Freehold without triggering a breach of the JVA trust clause. Specifically, it says the judge erred by failing to read the contracts as a whole, giving the words used in the trust clause their ordinary and grammatical meaning, consistent with the surrounding circumstances known to the parties at the time of the formation of the contract. CCP claims the judge ignored the surrounding circumstances by failing to account for the parties' object and purpose in including the trust clause. CCP argues these failures led to an erroneous and unreasonable interpretation, resulting in a commercial absurdity that defeats the parties' bargain.

[39] CCP contends the judge committed extricable legal errors by rejecting the evidence of Mr. Hunter and Mr. Horan as to their intentions that the core properties be held in trust for the duration of the joint venture, and by failing to give meaning to the following words in the trust clause: "for so long as the … Joint Venture remains in effect". It says had the judge properly given effect to those words and the surrounding circumstances, he would have concluded Cardero was obligated to hold its interest in the Freehold in trust for the duration of the joint venture.

[40] At times, during oral submissions, it appeared CCP was asserting the Freehold was not capable of being abandoned. However, we understand its settled position to be that set out in its written materials:

> Respectfully, the trial judge misapprehended the arguments made at trial. At paragraph 146 of the RFJ, the trial judge says that "CCP argues that Article 4.13 of the JVA prohibits abandonment by requiring the Freehold to remain in trust. In fact, CCP's position was and is simply that 4.13 imposes a trust obligation to hold the [Freehold] in trust for so long as the joint venture

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> remains in effect. When Cardero chose to surrender the [Freehold], its breach of trust under 4.13 triggered a default under the JVA, which gave rise to the remedies on default prescribed under Article 12. That is, Cardero was not *prohibited* from abandoning the [Freehold] but, rather, in the event that it did so, CCP had the right to pursue the remedies provided for under the JVA. (Appellants Factum, para. 86).

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[41] The judge's interpretation of the agreements permitted Cardero to abandon the Freehold without triggering a breach of the trust clause. CCP says this results in a commercial absurdity, and undermines the entire purpose of the joint venture, which was to assemble the core properties in trust. By allowing the Manager to abandon any coal tenure, the properties could be broken up at any time, and then reacquired by Cardero outside the JVA, free of its obligation to fund the exploration and development costs. CCP asserts this result undermines the benefits flowing to it under the JVA and defeats the parties' bargain.

[42] Cardero says the judge did not make any extricable legal error in his interpretation of the agreements; he properly considered the surrounding circumstances and provided cogent reasons for rejecting the subjective evidence upon which CCP relied. Cardero cautions that CCP is urging this Court, as it did at trial, to reach an interpretation that overwhelms the words in the contract and creates a new agreement between the parties.

[43] Cardero says that CCP's position — that Cardero could not abandon the Freehold *and* carry on with the joint venture — is inconsistent with the Article 5.10 of the JVA, which expressly permits abandonment while contemplating a continuation of the joint venture. It says it would be contrary to the plain meaning of the language in the JVA to conclude that an act of abandonment during the existence of the joint venture triggers a breach (and the consequent right of buyout by the non-defaulting party).

[44] Cardero also takes issue with CCP's assertion that assembling the core properties was fundamental to the joint venture. It points to the fact that, had Cardero not exercised the option, the Freehold may never have formed part of the

joint venture. This possibility contradicts the suggestion that combining the core properties was the entire purpose of the joint venture.

[45] Finally, it says CCP's submission mischaracterizes the parties' bargain. While Cardero was obligated to cover exploration and development costs, neither agreement imposed a positive obligation on Cardero to mine any property, including the Freehold. It also points out that Cardero paid $6 million to exercise the option, and that, in its role as Manager, it was contractually obligated to act "in a sound and miner-like manner in accordance with sound mining practices".

[46] Contractual interpretation is an exercise of mixed fact and law, which attracts a highly deferential standard of review, absent extricable error: *Sattva Capital Corp. v. Creston Moly Corp.*, 2014 SCC 53 at paras. 50, 53. Appellate intervention is permissible only where a judge has made a palpable and overriding error. In contrast, a correctness standard applies where a court has made an extricable legal error. Such errors will be uncommon and appellate courts should not strive to unearth extricable error. The applicable principles were summarized by the Supreme Court of Canada in *Corner Brook (City) v. Bailey*, 2021 SCC 29 at para. 44:

> In *Sattva*, this Court also explained that contractual interpretation is a fact specific exercise, and should be treated as a mixed question of fact and law for the purpose of appellate review, unless there is an "extricable question of law". The exception is standard form contracts, which is not relevant here: see *Ledcor Construction*. Extricable questions of law in the context of contractual interpretation include "the application of an incorrect principle, the failure to consider a required element of a legal test, or the failure to consider a relevant factor": *Sattva*, at para. 53, quoting *King v. Operating Engineers Training Institute of Manitoba Inc.*, 2011 MBCA 80, 270 Man. R. (2d) 63, at para. 21. The circumstances in which a question of law can be extracted will be uncommon. Whether something was or should have been within the common knowledge of the parties at the time the contract was entered into is a question of fact: *Sattva*, at paras. 49-55 and 58.

[47] It is necessary to begin by assessing how the judge undertook the task of interpreting the contract. We begin by observing he correctly set out the governing legal principles: RFJ at paras. 134–39. Specifically, the judge referred to the

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approach outlined by the Supreme Court of Canada in *Sattva* and recently clarified in *Corner Brook*, where the Court stated:

> [20] This Court set out the current approach to contractual interpretation in *Sattva*. *Sattva* directs courts to "read the contract as a whole, giving the words used their ordinary and grammatical meaning, consistent with the surrounding circumstances known to the parties at the time of formation of the contract": para. 47. This Court explained that "[t]he meaning of words is often derived from a number of contextual factors, including the purpose of the agreement and the nature of the relationship created by the agreement", but that the surrounding circumstances "must never be allowed to overwhelm the words of that agreement": paras. 48 and 57. "While the surrounding circumstances are relied upon in the interpretive process, courts cannot use them to deviate from the text such that the court effectively creates a new agreement": para. 57. This Court also clarified that the relevant surrounding circumstances "consist only of objective evidence of the background facts at the time of the execution of the contract … that is, knowledge that was or reasonably ought to have been within the knowledge of both parties at or before the date of contracting": para. 58.

[48] He acknowledged that consideration of the surrounding circumstances is aimed at giving meaning to the words the parties used. It does not permit an examination of the subjective intentions of the parties.

[49] The judge then referred to *1001790 BC Ltd. v. 0996530 BC Ltd.*, 2021 BCCA 321. As his reliance on this case grounds one aspect of the appeal, we will replicate this paragraph in full:

> [137] As the B.C. Court of Appeal explained in *1001790 BC Ltd. v. 0996530 BC Ltd.*, 2021 BCCA 321, surrounding circumstances are considered where there is some ambiguity:
>
>> [42] What the parties indicated to the outside world is to be determined within the four corners of the contract itself. What either party subjectively understood or misunderstood is irrelevant in the absence of fraud or misrepresentation (see, for instance, *Shaw Production Way Holdings Inc v Sunvault Energy, Inc*, 2018 BCSC 926 at paras 139 *et seq*, aff'd 2019 BCCA 72). Where there is some ambiguity in the terms, the court may have regard to the surrounding circumstances, but these must never be allowed to overwhelm the words of the agreement. The interpretation of a written contract "must always be grounded in the text and read in the light of the entire contract": see *Sattva* at para 57.

[50] CCP highlights this passage to support its claim that the judge neglected to interpret the agreements in light of the surrounding circumstances. It says the judge

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failed to engage in a consideration of the surrounding circumstances, as he found no ambiguity that would justify looking beyond the contracts themselves. With respect, we do not agree with this assertion.

[51] First, we do not read this Court's decision in *1001790 BC Ltd.* as suggesting that surrounding circumstances may only be referred to if there is ambiguity. The paragraph cited above must not be interpreted in isolation. *1001790 BC Ltd.* involved a consideration of whether there was an enforceable contract. In finding there was no contract, the trial judge considered subjective evidence of the parties' intentions, and then used this evidence to reach a result that contradicted the clear and unambiguous words of the agreement. Applying *Sattva,* this Court found that this approach was in error. However, we do not interpret this Court's reasoning in *1001790 BC Ltd.* as going so far as to depart from the general rules of contract interpretation by suggesting surrounding circumstances are only relevant where there is ambiguity.

[52] Second, we do not think the judge interpreted this paragraph to mean ambiguity was a prerequisite to considering surrounding circumstances. He had already acknowledged the role of surrounding circumstances as an aspect of interpretation. Further, immediately following his reference to *1001790 BC Ltd.*, the judge highlighted the need to consider surrounding circumstances even when interpreting contracts containing "entire agreement" clauses.

[53] We are satisfied the judge correctly set out the applicable legal principles. Accordingly, in order to ground a finding of extricable legal error, CCP is required to clearly demonstrate the judge failed to apply these principles. As we will explain, we can find no error in the judge's analysis.

[54] CCP takes issue with the fact the judge began his analysis by considering the wording of the critical language of the JVA, especially Article 5:10, the abandonment clause. In particular, it says this resulted in the judge giving undue paramountcy to the abandonment clause over the trust obligations, and created a basis to ignore or reject the surrounding circumstances.

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[55] We do not agree with this characterization. The judge was tasked with the goal of ascertaining what the parties "indicated to the outside world" by the terms of their contract: *1001790 BC Ltd.* at para. 86. This necessarily involves consideration of the written words. As expressed by the Supreme Court of Canada in *Sattva* at para. 57:

> … The goal of examining [surrounding circumstances] is to deepen a decision-maker's understanding of the mutual and objective intentions of the parties as expressed in the words of the contract. The interpretation of a written contractual provision must always be grounded in the text and read in light of the entire contract.
>
> [Emphasis added.]

[56] CCP advanced an interpretation whereby abandonment of the Freehold triggered a consequent breach of the trust clause. This required consideration of the interplay of three clauses in two agreements: (1) the JVA trust clause, which imposes an obligation to hold certain interests in trust for the duration of the joint venture (JVA, Article 4.13); (2) the JVA abandonment clause, which permits abandonment of certain tenures by the Manager (JVA, Article 5.10); and (3) the Lease surrender clause, which expressly permits surrender of the Freehold with proper notice (Lease, Article 23.1). Any viable interpretation of the agreements must integrate these provisions as harmoniously as possible.

[57] At trial, CCP did not suggest that Cardero's decision to surrender pursuant to Article 23.1 triggered a breach of Lease: RFJ at para. 140. It is also relevant that, when the JVA was agreed to, acquisition of the Freehold was simply an option and, therefore, would only potentially form part of the joint venture. Against this background, the judge was entitled to structure his analysis by first considering the scope and operation of the abandonment clause.

[58] Regardless, the overarching determination is whether the judge "read the contract as a whole, giving the words used their ordinary and grammatical meaning, consistent with the surrounding circumstances known to the parties at the time of formation of the contract": *Corner Brook* at para. 20.

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[59] Article 5.10 gave Cardero (in its position as Manager) the option to abandon as follows:

> If the Manager wishes to abandon or permit to lapse any of the Coal Tenures comprised in the Premises, it may, provided that it gives notice of its intention in writing to the Co-Owners and, if one or more of the Co-Owners shall so request in writing within fourteen (14) days of such notice, transfers such Coal Tenures to those Co-Owners as tenants in common in accordance with their respective Interests. All costs of such transfers shall be home by such Co-Owners, including transfer taxes or other taxes payable in respect thereof. Any Coal Tenures so abandoned or transferred shall cease to be subject to this Agreement, except with respect to obligations or liabilities theretofore accrued.

[60] The judge considered the words used in the abandonment clause (including the definition of Coal Tenures and Premises), and concluded that, on the face of the language alone, the Freehold "clearly fits within the scope of the properties that could be abandoned": RFJ at para. 143. He then went on to consider whether, "when viewed within the broader context of the other JVA terms, as well as with a consideration of the surrounding circumstances", the abandonment clause should be interpreted to exclude the Freehold: RFJ at para. 143.

[61] The judge specifically considered Articles 5.8 and 5.9 of the JVA, and found they did not support an interpretation of the abandonment clause that would exclude the Freehold: RFJ at paras. 144–45.

[62] He then turned to a consideration of the trust clause (Article 4.13), which provides:

> If and when the [Freehold] is granted to Coalhunter, the [Freehold] shall form part of the Premises and the interest of Coalhunter therein shall be held by Coalhunter in trust for the benefit of the … Joint Venture for so long as the … Joint Venture remains in effect.

[63] The judge concluded it did not prohibit abandonment of the Freehold: RFJ at paras. 146–49. Of particular importance was the judge's observation that the

abandonment clause (Article 5.10) was not expressly made subject to the trust clause (Article 4.13):

> [147] Further, interpreting the contract as a whole, it would be a strange thing for one clause to negate a right expressly provided by another clause, unless such was expressly set out. The JVA's terms illustrate that its drafters were well aware of the usual mechanism for making one clause subject to another (see e.g., Articles 5.4, 5.5, 5.7, and 5.8). But the authors did not make Article 5.10 subject to Article 4.13.

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[64] CCP says the judge failed to give meaning to the following words in the trust clause: "for so long as the … Joint Venture remains in effect". We do not agree. The judge explained the significance and operation of the trust provisions as follows:

> [149] … <u>These provisions were obviously required given that certain property interests were going to be held in the name of one party to the Joint Venture and not the other. In such circumstances, it makes sense to ensure that the other party's interests are protected in relation to the property held for the Joint Venture.</u> Article 5.10 then deals with how property can be removed from the properties held by the Joint Venture. Once a property is properly removed, there is no purpose to be served by the trust obligations. The removed property then comes under the exclusive control of the party who ends up with ownership, here being the Partnerships. There is no residual trust obligation controlling either the Partnerships or Cardero in relation to abandoned property.
>
> [Emphasis added.]

[65] It cannot be said that the judge failed to give meaning to the words in the trust clause. He recognized the need for, and importance of, the trust provisions while the property was being held by the joint venture. He just simply did not accept the interpretation advanced by CCP; namely, that the provision required the Freehold to remain in the joint venture until such time as the joint venture ceased to exist. In our view, CCP has not established that the judge failed to give meaning to the trust clause.

[66] The judge also specifically contemplated the interaction between the agreements in considering CCP's central position that, "[b]y design, the surrender of

the Coal Lease triggered defaults under the JVA": RFJ at para. 151. The judge observed:

> [152] I find that it would be very problematic to have an act expressly sanctioned by one agreement to constitute a breach of a related agreement. That would be an unusual and flawed design rendering harmonious interpretation impossible. I do not agree that this is an objectively reasonable interpretation of the agreements when read together.

[67] Also relevant to judge's analysis was the fact that Cardero was not obligated to mine the Freehold: Lease, Article 5.6. CCP acknowledged this, but maintained that the only way Cardero could properly avoid mining the Freehold was to completely withdraw from the joint venture: JVA, Article 11.1. The judge disagreed:

> [154] … I do not accept that this was the only alternative available to Cardero in these circumstances. The JVA contemplates that some, but not all, of the Coal Tenures might be kept within the Joint Venture while allowing the abandonment of others. A single property abandonment did not require complete withdrawal from the JVA.

[68] The judge then turned his attention to what he described as a "broader review" of the surrounding circumstances: RFJ at para. 155. He made specific mention of Mr. Horan and Mr. Hunter's evidence. In particular, he noted their explanation that the purpose of the trust clause was "to ensure that all of the properties, including the Freehold, were kept together", and noted Mr. Hunter's testimony that the right to abandon was only put in the agreements to enable Cardero to "avoid having to mine and process inferior coal": RFJ at para. 155.

[69] The judge rejected these contentions for several reasons: (1) they did not reflect the language of the agreements; (2) there was no ambiguity that would necessitate a need to consider surrounding circumstances; (3) they reflected inadmissible subjective intentions; (4) their purported interpretation would lead to illogical results; and (5) they were inconsistent with the possibility the Freehold would never form part of the joint venture: RFJ at para. 156. We agree with the judge's observation that the execution of an "option" agreement and the use of "if and when" in the trust clause did not reflect a fundamental intent to keep the core properties together.

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[70] We recognize the judge said that one reason he could not give effect to CCP's argument was because he had "not found the presence of an ambiguity that would drive a need to consider surrounding circumstances": RFJ at para. 156. We would agree this statement would be in error if the judge meant he could only consider surrounding circumstances if there was an ambiguity, but we do not read the judgment in that way. As we have already indicated, the judge correctly stated the law on the role of surrounding circumstances, set out the background facts to the agreements, and, as we see it, had regard to certain of the surrounding circumstances in any event. Judgments need to be read generously, and sentences should not be parsed in an assiduous search for error.

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[71] As we read the judgment, the judge concluded that the surrounding circumstances said to support CCP's interpretation were either not to be considered given their subjective nature, or had the effect of overwhelming or contradicting the language the parties used to record their agreement. This conclusion was open to the judge based on the evidence before him, and is a matter to which we should defer. As the Supreme Court of Canada noted in *Corner Brook*, whether something is or should have been within the common knowledge of the parties at the time the contract was entered into is a question of fact: at para. 47. We take this to indicate that a determination of the relevant objective circumstances is a matter of fact. Accordingly, an appellate court cannot interfere with these determinations absent palpable and overriding error. No such error has been demonstrated on this record.

[72] We will refer to one final argument. CCP says the judge's interpretation results in a commercial absurdity. This absurdity arises because Cardero, as Manager, could simply abandon the Freehold, and then reacquire it as an owner. We disagree. There were provisions in the agreement that operated to limit the extent to which the Manager could act in a dishonest or commercially unreasonable way. Cardero could not arbitrarily abandon tenures without breaching its obligations, as Manager, to conduct the joint venture "in a sound and miner-like manner in accordance with sound mining practices". In fact, Cardero tendered expert evidence that concluded, in part, that its actions were consistent with those of "a prudent

mining operator and were in the best interests of the Joint Venture": RFJ at para. 113. The judge accepted, on the basis of the evidence, that there was "a legitimate reason for the Manager to consider whether it was wise to hold onto the Freehold": RFJ at para. 161.

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[73] In conclusion, the judge did not commit an extricable legal error. He stated and applied the correct legal principles, made no error of principle, had regard for the plain and ordinary meaning of the language and considered the agreements as a whole. The judge evaluated the surrounding circumstances identified by CCP, and concluded they fell outside those objectively relevant circumstances he could rely on to inform his interpretation of the contracts. Further, he concluded that, if considered, those circumstances would overwhelm the clear language of the contracts and lead to an interpretation inconsistent with the wording of the agreements and an illogical result.

[74] Accordingly, we would dismiss this ground of appeal advanced by CCP.

2. Did the judge err in concluding Cardero's surrender notice was effective?

[75] The judge concluded that, in the Lease Action, PRP was owed $500,000 as a result of an advance royalty payment falling due before Cardero had terminated the Lease. He found that Cardero's election under the Amended Lease operated to defer the payment date, not the due date. That obligation is not a subject of appeal.

[76] The judge dismissed PRP's claim to a $2 million advance royalty payment because it did not become due until after the Lease was terminated. PRP appeals that conclusion. Specifically, it argues the judge erred in finding that the surrender notice provided by Cardero was effective to terminate the Lease. If this Court agrees, then, subject to certain other defences raised, the $2 million should have been paid by Cardero.

[77] Article 23.1 of the Lease granted Cardero a right to surrender and terminate on 60 days' notice:

> Notwithstanding anything herein contained, [Cardero] may, at any time, upon giving the [PRP] (60) days prior written notice thereof determine or surrender all of its right, title and interest in all of the Lands or in any legal section of the Lands whereupon this Lease shall terminate as to the part so surrendered.

[78] Pursuant to the Amended Lease, the advance royalty payment of $2 million was due on June 2, 2014. Following the collapse in coal prices, financing the development became problematic, and Cardero sought an extension on the production deadline and a moratorium on the advance payments. Discussions took place about how to proceed. In March 2014, the parties agreed to reduce the notice period from 60 days to 30 days.

[79] On April 30, 2014, Cardero delivered notice of termination of the Lease effective May 30, 2014. The letter first proposed amendments to the Lease, stating:

> If this proposal is acceptable, kindly advise so that we can prepare the required agreement to implement this prior to May 30, 2014 (which is the date set for termination of the Lease in accordance with our notice below) and avoid termination of the Lease.

[80] The termination language followed in the next paragraph. It read:

> However, in order to ensure the termination of the Lease if the foregoing proposal is not acceptable, in accordance with the provisions of Article 23 of the Lease and our agreement regarding notice of termination as set out in our letter to PRP of March 27, 2014 and acknowledged by Mr. Horan on behalf of PRP, Cardero Coal hereby provides formal notice to PRP that Cardero Coal is surrendering all of its right, title and interest in and to all of the Lands (as defined in the Lease), effective May 30, 2014. As such surrender is with respect to all of the Lands, the lease will accordingly terminate, effective May 30, 2014.

[81] At trial, PRP asserted that Cardero's surrender notice was ineffective for a number of reasons. First, it argued it was not effective until it was acknowledged by PRP.

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[82] The judge rejected that argument noting that:

> [193] Article 23.1 does not require that PRP acknowledge a surrender in order for it to become effective. Rather, the Lease simply provides that Cardero may "at any time, upon giving [PRP]… prior written notice… surrender all of its right, title and interest" in the identified lands. <u>In my view, the plain meaning of this provision is that the only condition necessary to give effect to the surrender is notice is given in writing.</u> Were that not the case, the Partnerships could have withheld their acknowledgment through to the due dates of future Advance Royalty Payments, which would make no sense. Under such an interpretation, Cardero's right to surrender lands under the Lease would only be effectively exercisable at the discretion of the Partnerships. In my view, this would render Cardero's right to surrender illusory at best.
>
> [Emphasis in original omitted; emphasis added.]

[83] PRP also alleged the notice was ineffective as it failed to surrender all of the lands, and because it was not clear, unambiguous and unconditional. As the judge explained:

> [214] The Partnerships argue that Cardero's Surrender Notice was ineffective because it failed to surrender all of Cardero's right, title, and interest in all of the lands.
>
> [215] The Partnerships also argue that, in order to be effective, a notice of termination must be clear, unambiguous and unconditional. Notices of termination under a lease must be strictly construed and effected in strict compliance with their provisions—a termination notice which contains conditions is ineffective: *Arnold v. 2261324 Manitoba Ltd.*, [1995] 1 W.W.R. 305 at paras. 30-36 (Man. C.A.).
>
> [216] The Partnerships argue that the Surrender Notice was conditional and therefore ineffective.

[84] The judge also rejected these arguments, and provided the following reasons for doing so:

> [217] …
>
> a) The Surrender Notice covered the entirety of the lands covered by the Lease.
>
> b) The mere fact that the letter also outlined a path whereby Cardero was prepared to agree to new terms under which its valid surrender would no longer be operative does not mean that the Surrender Notice was ineffective.
>
> c) Absent a new agreement between the parties, the Surrender Notice would have its intended legal force.

d) The Lease was always subject to possible amendment by the parties. It had been amended on one prior occasion. But on this point, the Partnerships declined to agree to new terms sought by Cardero, and vice versa.

e) The parties conducted themselves as though the Surrender Notice was effective thereafter. For example, in the draft letter attached to their July 27, 2015 correspondence, the Partnerships state, "[a]s you are aware, Cardero terminated the Lease effective May 30, 2014".

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[85] On appeal, PRP says the judge made a legal error when he concluded that the only condition necessary to give effect to the surrender was notice in writing. We have underlined this passage in para. 82 above. This submission is unfair to the judge, and is an example of parsing the judgment for error. The point was obviously made by the judge in response to an argument that the surrender was not effective until it was acknowledged by PRP. He was not directing his mind to any other reasons why a notice in writing might not be effective. The judge reserved his consideration of those questions to the part of the judgment where he addressed PRP's arguments set out above.

[86] PRP also complains that the judge did not engage in the proper legal analysis, which required him to consider whether the notice was conditional, clear and ambiguous, and effective to surrender all rights, title and interest in the lands surrendered.

[87] In our view, he did consider and reject these arguments for the reasons replicated above. We accept that the judge states his conclusions in a cursory form, and does not expressly state that the notice was clear, unambiguous and unconditional. But he must be taken to have reached that conclusion, given his stated awareness of the arguments being advanced.

[88] As we have previously stated, judgments need to be read generously. In substance, the judge found that the notice expressly terminated the Lease unless the parties could agree otherwise. This interpretation was open to the judge on the evidence before him and, in our respectful view, did not render the notice conditional in a sense capable of undermining its validity.

[89] In any event, these are findings of mixed fact and law, and we are only justified in interfering if the judge committed a palpable and overriding error. No such error has been demonstrated by PRP. Given this conclusion, it is unnecessary to consider the alternative arguments advanced by PRP on this issue.

[90] Accordingly, we would dismiss PRP's appeal.

3. Did the judge err in concluding CCP was in default of the JVA?

[91] The judge found CCP breached the JVA by: (1) refusing to provide a letter confirming Cardero's authority to deal with the Ministry in respect of various coal tenures; (2) refusing to follow Management Committee decisions; and (3) asserting it would no longer cooperate with the joint venture operations generally: RFJ at para. 200.

[92] These breaches were primarily rooted in the judge's interpretation of CCP's obligations under Article 21.1 of the JVA, which provides:

> Each party shall promptly do and provide all acts and things and shall promptly execute and deliver such deeds, bills of sale, assignments, endorsement and instruments and evidences of transfer and other documents and shall give such further assurances as shall be necessary or appropriate in connection with the performance of this Agreement. The parties agree to co-operate fully in applying for all necessary governmental approvals and permits. Each party shall give to the Manager from time to time such powers of attorney and other evidences of authority as shall be necessary to enable the Manager to perform its duties hereunder.

[93] The judge concluded that CCP's refusal to provide the letter amounted to a breach of this provision:

> [204] Article 21.1 sets out CCP's obligation to do all things and promptly execute all documents as necessary, and specifically obligates CCP to fully cooperate in applying for all government approvals and permits. Despite this contractual obligation, in October 2014, Mr. Horan advised that CCP would not cooperate or sign anything. Specifically, Mr. Horan refused to provide a letter to the Ministry authorizing Cardero, as Manager, to deal with government authorities to convert pending coal licence applications into coal licences. According to Mr. Henderson's evidence, which I find was credible, this letter was needed to maximize the prospects that the licences for drilling would be granted. Only CCP could effectively provide the necessary assurance as to CCP's position. CCP's failure to cooperate in providing this letter was a breach of Article 21.1 of the JVA.

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[94] He also referred to CCP's refusal to participate in any Management Committee meetings after September 16, 2014, and then observed:

> [207] … [B]ut CCP had an obligation to "do and provide all acts and things… as shall be necessary or appropriate in connection with the performance of this Agreement." I find that its decision to stop cooperating with its Joint Venture partner was a breach of this obligation. It was not "appropriate" to hinder the conduct of the Joint Venture through such a complete lack of cooperation and engagement.

[95] The judge also found that CCP breached Article 6.11(a) of the JVA, which required the parties to abide by decisions of the Management Committee. Specifically, he identified CCP's failure to address the following action items assigned to it at the September 2014 Management Committee meeting:

a) draft the letter to the Ministry;

b) review and approve the insurance policy;

c) review certain amendments to the JVA; and

d) review and execute the proposed resolution: RFJ at para. 206.

[96] CCP submits that the judge made palpable and overriding errors in his interpretation of CCP's obligations under the JVA. First, it argues the letter was not necessary and, in any event, was cured by the approved work plan. Second, it argues that, by operation of Article 8.2 of the JVA, obligations respecting items b), c) and d) were not CCP's to perform. It says these defaults were administrative matters that were delegated to Cardero, as Manager, under Articles 6.1 and 8.2. Third, even if they were properly characterized as CCP's obligations, the fact they were ultimately cured by resolutions passed at a subsequent Management Committee meeting (in the absence of CCP's attendance) negates a finding of breach.

[97] CCP also takes issue with the judge's conclusion that CCP's decision to stop cooperating amounted to a breach. CCP characterizes this finding as a "general duty to cooperate" and says no such duty exists under the JVA.

[98] These are the same arguments that were made by CCP at trial, and rejected by the judge. The judge accepted evidence that the letter to the Ministry was needed to maximize the prospect of receiving licenses. The judge also found that the work plan and subsequent resolutions did not negate or cure the breaches that had occurred. He characterized these efforts by Cardero and the Management Committee to keep the joint venture moving forward despite CCP's failure to cooperate as "limited mitigatory steps": RFJ at para. 210.

[99] CCP's argument calls for us to disagree with the judge's conclusions concerning the obligations CCP had under the JVA, and whether these obligations were breached. Both claims involve questions of mixed fact and law, and are subject to deference absent palpable and overriding error.

[100] In our opinion, it was open to the judge to make the findings he did, and to interpret the JVA in the manner he did. In interpreting the contract, he had regard for the plain and ordinary meaning of the language, and considered the agreement as a whole. While CCP advocated for a different interpretation of its obligations under the JVA, it has failed to demonstrate the existence of an error that would justify appellate intervention.

[101] Most importantly, it appears to us that the judge's conclusion — that CCP's refusal to provide the letter to the Ministry amounted to a breach of Article 21.1 — is unassailable. Article 21.1 obliged CCP "to do all … things … as shall be necessary or appropriate in connection with the performance of [the JVA]". Moreover, it required CCP "to co-operate fully in applying for all necessary governmental approvals … and to give the Manager … evidences of authority as shall be necessary to enable the Manager to perform its duties". Even accepting the letter was not strictly necessary, but would assist in the processing of the necessary approvals, based on the broad wording of Article 21.1, we can see no plausible basis on which this Court could interfere with the judge's conclusion.

[102] Given our conclusion concerning the effect of Cardero's default letter (which we explain below), it is not necessary for us to address the other specific breaches.

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However, we do wish to comment on CCP's suggestion that the judge erred in imposing a "general duty to cooperate".

[103] The judge found CCP's "decision to stop cooperating" a breach of Article 21.1. Specifically, he concluded it was "not *appropriate* to hinder the conduct of the joint venture through such a complete lack of cooperation and engagement": RFJ at para. 207 (emphasis added). Implicit in this statement is the judge's finding that CCP's actions hindered the conduct of the joint venture. CCP has not provided any basis to set this conclusion aside. Article 21.1 required CCP to facilitate — not hinder — performance of the JVA. Moreover, the judge's conclusion that CCP's refusal to cooperate was not "appropriate" is reasonable in light of his finding on the evidence that CCP's conduct was motivated by an attempt to leverage payment of the $500,000 advance royalty: RFJ at para. 211.

[104] Finally, it is important to note the judge recognized the breaches were "relatively minor", and the corresponding consequences to CCP were "somewhat severe". With respect to these matters, the judge observed:

> [212] The fact that CCP's breaches were relatively minor in the broader context of the Project's development does not change the analysis. Article 12.1 of the JVA does not distinguish between major and minor breaches—rather it refers to a breach of "any obligation". If there is a breach, the other party has to give notice and provide an opportunity to cure before any other rights are triggered. As such, the parties effectively managed the prospect of minor breaches by providing for the opportunity to cure such breaches. Presumably, in the normal course, once notified of a minor breach, the defaulting party would see the wisdom of simply curing the failing rather than risking further remedies being sought against it. But that is not what occurred here.
>
> [213] While the operation of Article 12.1 arguably leads to somewhat severe outcomes, the parties' agency in designing the effect of any breach through the terms of the JVA must be respected. Furthermore, it should be noted that the otherwise harsh effect of Article 12.1 is muted by the fact that the breaching party is still given a right to compensation for their interest in the JVA notwithstanding their breach.

[105] While the consequences flowing from the such a minor breach were seemingly harsh, the judge acknowledged this was the process and result contractually agreed to by the parties.

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[106] In conclusion, we can find no error in the judge's findings or analysis leading to his decision that CCP had breached the JVA.

[107] This leaves the issue of whether the notice of default was effective.

[108] For Cardero to be entitled to its fullest remedy, the JVA requires not only that CCP be in default, but also that it has not cured the default after being given effective notice in accordance with the JVA. CCP contended before the judge, and on appeal, that, even accepting it was in default, Cardero's August 24, 2015 notice of default letter to CCP was ineffective as it was protected by settlement privilege.

[109] The judge found that the reference to the letter being "Without Prejudice" did not vitiate its effectiveness, because it did not contain a settlement offer and no litigation was pending at the time: RFJ at para. 221. Moreover, the judge reviewed the letter and concluded "Cardero was unambiguously enforcing its legal rights without proposing settlement or concession": RFJ at para. 221. Specifically, he found the suggestion to meet for discussion did not undermine "the provision of contractual notice": RFJ at para. 223. The judge applied the correct legal test, and his conclusions are unassailable on the evidence.

[110] It is necessary then to consider CCP's argument concerning the adequacy of the notice. Specifically, it says that Cardero's August 24, 2015 letter failed to clearly communicate the nature of the alleged default.

[111] The contents of the letter were not set out in full in the judgment. A copy was included in the appeal materials. We do not propose to review it at length here. It is sufficient, in our view, to point out the following passages:

> …
>
> BREACH OF THE JOINT VENTURE BY CARBON CREEK PARTNERSHIP
>
> <u>We find that we must raise certain breaches of the JV Agreement by Carbon Creek Partnership</u>. In this regard we refer to you to section 4.8 and 5.4 of the JV Agreement… as well as Section 21.1…
>
> …
>
> … Carbon Creek Partnership was asked to cooperate with the Manager's efforts including, but not limited to <u>(a) drafting a letter to Mineral Titles,</u>

> providing its permission for the Manger to act on its behalf in moving the Application to Licences; …
>
> …
>
> Carbon Creek Partnership's refusal to cooperate with (a) above is in direct contravention of Section 4.8 as well as Section 21.1 of the JV Agreement.
>
> …
>
> NEXT STEPS
>
> In accordance with Section 12.1(a) of the JV Agreement, we hereby provide notices of a breach to Carbon Creek Partnership and require that such defaults be cured on or before October 23, 2015, failing which it is acknowledged that Cardero Coal as the non-defaulting partner, shall have the right pursuant to 12.1(e) of the JV Agreement to acquire the Interest of the Carbon Creek Partnership. ...
>
> [Emphasis added.]

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[112] In our view, the contents of the letter provided adequate notice of the alleged default concerning the refusal to provide the letter. As such, given our earlier conclusion upholding the judge's finding that this failure constituted a breach, it is not necessary to consider whether the letter gave adequate notice of the other alleged breaches.

[113] For the first time on appeal, CCP seeks a remedy of relief from forfeiture for its breach. Cardero opposes this relief on the basis of prejudice and concerns about the absence of a compete factual record. Consideration of new issues raised on appeal will be rare. In this case, we are not satisfied it is in the "interests of justice" to do so: see *Firestar Custom Home Builders Inc. v. 1099000 B.C. Ltd.*, 2022 BCCA 324 at paras. 31–32.

[114] Accordingly, we would dismiss this ground of appeal.

Cardero's Cross Appeals On Costs

[115] Cardero cross appeals the judge's award of costs in both actions:

a) In the Lease Action, Cardero submits that the judge erred in awarding PRP its costs on a contractual indemnity basis despite the fact that PRP

failed to achieve substantial success in its claim and because it unreasonably refused to accept Cardero's formal offer to settle; and

b) In the JVA Action, Cardero submits that the judge erred in denying it contractual indemnity costs for its successful defence of the JVA Counterclaim.

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The Contractual Indemnity Provisions

[116] Cardero's appeal of the judge's costs award in the Lease Action turns largely on the interpretation of the indemnification clause in the Lease:

> 30.2 Indemnification by Coalhunter
>
> Coalhunter shall indemnify and save harmless the Peace River Partnership and its Representatives (collectively the "Peace River Partnership Indemnified Parties") from and against any and all Losses of every kind whatsoever, whether direct or indirect, which at any time or from time to time are directly or indirectly incurred or suffered by any of the Peace River Partnership Indemnified Parties in connection with, as a result of or arising out of:
>
> …
>
> (b) any breach of this Lease by Coalhunter …

[117] "Losses" is defined in the Lease to mean "claims, losses, demands, judgments, liabilities, expenses, damages, fines, charges and costs including legal costs incurred on a solicitor and own client basis".

[118] Similarly, Cardero's appeal of the judge's costs award in the JVA Counterclaim turns on the interpretation of the indemnification provision found in Article 19.1 of the JVA:

> The Carbon Creek Partnership shall indemnify and save harmless Coalhunter and its Representatives (collectively the "Coalhunter Indemnified Parties") from and against any and all Losses of every kind whatsoever, whether direct or indirect, which at any time or from time to time are directly or indirectly incurred or suffered by any of the Coalhunter Indemnified Parties in connection with, as a result of or arising out of:
>
> …
>
> (b) any breach of this Agreement by the Carbon Creek Partnership.

[119] As it is in the Lease, the term “losses” is broadly defined in the JVA to include legal costs incurred on a solicitor and own client basis.

The Judge’s Reasons

[120] Paragraph references below are cited to the Costs Reasons.

[121] With respect to the Lease Action, Cardero argued that PRP should be denied its costs because it did not achieve substantial success on its claims. However, the judge held that the substantial success test was not applicable given the contractual indemnity language in the Lease: para. 36. He found that the contractual language was clear and unequivocal and did not require PRP to establish substantial success in order to entitle it to contractual costs: para. 38. The judge further held that, while the court has a discretion to override a contractual costs term, that discretion is limited to extraordinary circumstances such as misconduct or where the award of contractual costs would lead to an inequity, neither of which was established here: at paras. 41 and 44.

[122] The judge also considered a formal offer to settle served by Cardero on August 19, 2021, and found that it was one that ought reasonably to have been accepted by PRP given that it accurately predicted the outcome of the trial: at para. 76. However, he found that the offer to settle was not effective to deny PRP its contractual indemnity costs. The judge said, at para. 86:

> … these sophisticated parties had previously agreed to indemnify each other for any legal costs arising from breaches of the Lease. They did not provide for an exception in the case of any offer to settle. Further … the courts will enforce such contractual terms absent extraordinary circumstances. In my view, the circumstances do not warrant the Court intervening and exercising its discretion to override the parties’ contractual intent, notwithstanding the existence of the Cardero Offer.

[123] The judge clearly considered himself bound to apply the contractual costs indemnity. However, he indicated that if he were not so bound, he would have found that PRP did not achieve substantial success in the Lease Action given that it only established a right to receive the first advance royalty payment of $500,000, but

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failed on its claim to the second advance royalty payment of $2 million: at paras. 47–50.

[124] In the JVA Action, the judge granted Cardero its contractual indemnity costs in respect of its claim that CCP breached the JVA: at para. 17. We note that much of the judge's analysis on this issue was concerned with whether Cardero had adequately pled its claim for such costs: see paras. 18–25. Having concluded that the pleadings were adequate, the judge had little difficulty finding that Cardero was so entitled. However, he denied Cardero's claim for contractual indemnity costs for defending the JVA Counterclaim. The judge said that, but for the need to enforce the contractual indemnity, he would have found that the JVA Action and the JVA Counterclaim were sufficiently intertwined to be considered together for costs purposes: at para. 29. However, the existence of the indemnity demanded a different approach: at para. 30:

> … Cardero's indemnity in the JVA Action is applicable to the JVA Claim. Under the clause, Cardero is entitled to costs incurred because of breaches of the JVA by CCP. However, I agree that Cardero's costs in <u>defending</u> CCP's JVA Counterclaim are not captured by the language of the indemnity. As a matter of contractual interpretation, any costs incurred by Cardero in defending the JVA Counterclaim did not "aris[e] out of…any breach of" the JVA by CCP. Rather they arose because of <u>alleged</u> breaches of the JVA by Cardero. [Emphasis in original.]

[125] Despite rejecting Cardero's claim for contractual indemnity costs, the judge held that Cardero was substantially successful in defending the JVA Counterclaim, and was therefore entitled to its ordinary costs. The judge considered the factors identified in *Mort v. Board of School Trustees of School District No. 63 (Saanich)*, 2001 BCSC 1473 at para. 7, for assessing a matter's relative difficulty, and concluded that Cardero was entitled to costs at Scale C: at para. 67. Given his finding, referred to above, that Cardero's offer to settle ought reasonably to have been accepted, he awarded Cardero double costs from the date of the offer, August 19, 2021: at paras. 70 and 87.

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[126] The judge then determined that, for the purpose of assessing costs globally, the time spent at trial should be allocated equally between the Lease Action, the JVA Action and the JVA Counterclaim, i.e., one-third of the total time to each: at para. 91.

Standard of Review

[127] Both cross appeals involve issues of contractual interpretation concerning the Lease and the JVA and, as such, engage questions of mixed fact and law, which are subject to the deferential standard of review of palpable and overriding error: *Sattva* at para. 53.

[128] Costs awards are discretionary, and thus also subject to considerable deference. Appellate interference will only be justified where a judge makes a misdirection of law, an error in principle, a palpable and overriding error of fact, or, otherwise, the award is so clearly wrong as to amount to an injustice: *Gichuru v. Purewal*, 2021 BCCA 91 at paras. 13–14; *Hartshorne v. Hartshorne*, 2011 BCCA 29 at para. 23.

Contractual Cost Indemnities

[129] As both cross appeals turn largely on the interpretation of the cost indemnity clauses in the Lease and the JVA, it is useful to consider how such provisions have been interpreted and applied by the courts.

[130] The judge cited Justice Donegan's decision in *Eisler Estate v. GWR Resources Inc.*, 2020 BCSC 562 [*Eisler Estate (SC)*], where she discussed the difference between costs awarded pursuant to the *Supreme Court Civil Rules* and contractual costs:

> [28] Courts have recognized a distinction between costs and legal (and other) expenses. Costs are awarded pursuant to the *Supreme Court Civil Rules*, B.C. Reg. 168/2009 [*Civil Rules*], and a judge cannot impose costs sanctions that are not authorized by those rules: *Tanious v. The Empire Life Insurance Company*, 2019 BCCA 329 at para. 45, leave to appeal refused [2019] SCCA No. 417. Rule 14-1 allows two categories of costs – party and party costs and special costs. The *Civil Rules* do not provide for "full indemnity costs": *Tanious* at para. 45.

> [29] Party and party costs are the default option. As they are to be assessed on a tariff, party and party costs are recognized to only provide a partial indemnity to the successful party. In *Tanious*, the Court explained that the partial indemnity default option; that is, party and party costs, is intended to allocate the high cost of litigation fairly between the parties: *Tanious* at paras. 46-47. Special costs, however, serve a different function. They are not compensatory; they are punitive: *Smithies Holdings Inc. v. RCV Holdings Ltd.*, 2017 BCCA 177 at para. 56. The purpose of special costs is to censure and deter litigation misconduct, not to compensate the successful party. Special costs are also not a substitute for damages or to be conflated with damages for mental distress, punitive damages or contractual costs: *Tanious* at para. 51.
>
> [30] Contractual costs are different. Courts have recognized that in entering into a contract, the parties may agree that one party will reimburse the other for actual legal fees and other expenses in certain circumstances. When those circumstances arise, entitlement to recovery of those actual legal fees and other expenses is derived from the terms of the contract and not from the statutory costs regime in the *Civil Rules*: *Tanious* at para. 52.
>
> [31] Where such a contract exists, the right to be indemnified for actual legal fees and expenses must be “clearly and unequivocally expressed.” However, it is important to remember that no “magical incantation” is required in order for a party to be entitled to a specific order for costs: *Bakshi v. Shan*, 2013 BCSC 969 at para. 44.
>
> [32] Like all questions of a contractual interpretation, the reasonable intention of the parties falls to be determined on the basis of the language used: *Bakshi* at para. 44.

[131] Justice Donegan’s findings on the substantive issues were upheld by this Court in reasons indexed at 2021 BCCA 113. In supplementary reasons (2021 BCCA 247 [*Eisler Estate (CA)*]), also cited by the judge, the Court addressed the issue of costs. The respondent, as it had done before Donegan J., sought full indemnity costs based on the terms of the contract in issue. Justice Voith held:

> [4] The contract in question was a written contract drafted by the appellant pursuant to which the respondents were to provide services to the appellant. Its provisions addressed not only termination and the payment of severance, but also indemnity, as follows:
>
>> 6.03 The Company shall pay all legal fees and expenses incurred by Eisler in contesting or disputing any termination or in seeking to obtain or enforce any right or benefit provided by this Agreement, provided that Eisler is successful in any such action.
>
> [5] Before us, as they did before Justice Donegan, the respondents rely on this clause in seeking full indemnity for their legal fees and expenses incurred in relation to this appeal. Like Justice Donegan, we can see no reason not to make the order requested.

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> [6] The appellant does not raise any issue of contractual interpretation. Rather, it seeks to avoid its clear contractual obligation by relying on the contents of one of this Court's forms. It says that Form 10 stipulates that Part 4 of the factum "must include any special disposition that is desired with respect to costs", and it points out that the respondents did not make this claim for contractual indemnity in their factum. The appellant further points out that when the respondents sought an order for security for costs, they based the amount on tariff costs, not on an indemnity basis.
>
> [7] In our view, the appellant's obligation is entirely independent of this Court's rules, which govern costs within the discretion of the Court. Rather, it arises under contract. As Justice Donegan noted in her costs award:
>
>> [30] Contractual costs are different. Courts have recognized that in entering into a contract, the parties may agree that one party will reimburse the other for actual legal fees and other expenses in certain circumstances. When those circumstances arise, entitlement to recovery of those actual legal fees and other expenses is derived from the terms of the contract and not from the statutory costs regime in the *Civil Rules* [citation omitted].
>
> [8] Nothing in this Court's Rules purports to override any such obligation, nor is the appellant relieved of its contractual obligations by the application for security. A contract is a contract.

[132] In her reasons, Donegan J. cited *Tanious v. The Empire Life Insurance Company*, 2019 BCCA 329, where Justice Dickson provided a thorough summary of the law governing costs generally. With respect to contractual costs, Dickson J.A. said (at para. 52):

> ... As for contractual costs, in entering into a contract parties may agree that one party will reimburse the other for actual legal fees and other expenses incurred in certain circumstances. When those circumstances arise, entitlement to recovery of legal fees and expenses is derived from the terms of the contract, not from the statutory costs regime: [*Canadian Petcetera Limited Partnership v. 2876 R Holdings Ltd.*, 2010 BCCA 469] at para. 42.

[133] In *Canadian Petcetera*, referred to by Dickson J.A., Justice Tysoe stated (at para. 42) that:

> … it is open to the parties to a contract to include a provision for reimbursement by one party to the other party for its actual legal and other expenses in certain circumstances. These are sometimes referred to as indemnity costs or contractual costs.

[134] *Eisler Estate (CA)* was cited by this Court in *Stewart v. Lloyd's Underwriters*, 2022 BCCA 84, where Justice Abrioux observed that full indemnity costs were

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awarded there on the basis of a contractual clause requiring full indemnification: para. 92. There was no discussion of the specific circumstances of *Eisler Estate*, which differed significantly from those in *Stewart*.

[135] *Eisler Estate (CA)* was distinguished by this Court in *Prescott Strategic Investments Limited Partnership v. Flair Airlines Ltd*., 2022 BCCA 443, where this Court allowed an appeal from a judge's order granting full indemnity costs on an application for a sealing order and a publication ban in an oppression proceeding. The judge had relied on a provision of the governing shareholder's agreement, cl. 13.3(e), that provided for recovery of "attorney fees and costs for enforcement and/or any legal action" relating to breach of a confidentiality obligation.

[136] Justice Griffin held that, if this were the only provision in the shareholder's agreement dealing with costs, there would be no basis to interfere with the judge's costs award, as the result would be supported by *Eisler Estate (CA)*: at para. 57. However, Griffin J.A. noted that there was another term of the shareholder's agreement that specifically provided an indemnity for officers and directors, including for costs on a solicitor and own client basis. Reading the two clauses together, Griffin J.A. found that cl. 13.3(e) had to be interpreted as providing for something less than a full indemnity, but rather to costs at a scale ordinarily awarded under the applicable court rules: para. 55.

[137] The cases cited above from this Court support giving effect to contractual terms governing the award of costs, which typically provide for costs on a full indemnity basis. However, there is no analysis in those cases about whether the court retains a discretion to deviate from the contractual indemnity, and the circumstances that might justify doing so.

[138] Appellate courts in other jurisdictions have recognized such a discretion where circumstances warrant. For example, in *Schafer v. Schafer*, 2023 ABCA 117, the court upheld the trial judge's decision declining to award solicitor-client costs, despite a clause in the parties' arbitration agreement in a family law dispute providing for such costs.

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[139] After noting that costs awards are highly discretionary, and subject to appellate review only where the judge has made an error of principle or the award is wholly unreasonable (at para. 72), the court said:

> [73] Any contractual right to costs is always subject to the court's discretion: Mark M. Orkin, Robert G. Schipper, *Orkin on The Law of Costs*, 2nd ed (Toronto: Thomson Reuters Canada, 2019) (loose-leaf updated 2020) at 219.1.1. The circumstances when a court may exercise its discretion to award costs in a manner different than what was agreed upon between the parties was recently addressed in [*Driving Force Inc. v. I Spy Eagle Eyes Safety Inc.,* 2022 ABCA 25] paragraph 72:
>
> > Even if there is a binding covenant to pay solicitor and client costs, the trial judge has a discretion to depart from that covenant having regard to the way the litigation was conducted, the proportionality of the expense related to the amounts in issue, the degree of success achieved, and other relevant factors: [citations omitted].
>
> [74] Therefore, we do not accept that a court should only exercise its discretion to not award contractually-agreed upon solicitor client costs where there has been abusive forms of litigation or other misconduct, although that clearly may be a relevant factor. Proportionality of the expense and degree of success achieved may also be considered.

[140] The court held that the judge, in declining to award contractual costs, properly considered the principle of proportionality given the relatively small amount of money in issue, as well as the desire to avoid a special hearing which would be required to assess solicitor-client costs: paras. 75–76.

[141] As reflected in para. 74 of *Schafer*, the court rejected the notion that it was necessary to establish misconduct in order for the court to decline to enforce a contractual provision for full indemnity costs. That was the approach taken in earlier cases, for example, in *HSBC Bank Canada v. Lourenco*, 2012 ABQB 648 at para. 31, a case cited by the judge here.

[142] Similarly, in *Rozdilsky v. Kokanee Mortgage M.I.C. Ltd.*, 2020 SKCA 1, Justice Kalmakoff discussed the general principles governing costs of appeals (at paras. 6–8) and then said:

> [9] A different set of considerations is engaged when a contractual agreement requires one party to a proceeding to pay the costs of another party on a solicitor and client basis. As a general proposition, where there is a contractual right to costs, the court will exercise its discretion so as to reflect

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> that right. To put this in the context of a foreclosure proceeding, a mortgagee generally is entitled to solicitor-client costs if the obligation to pay those costs is included as a term of the mortgage …
>
> [10] This general proposition, however, is not an absolute rule; the court retains discretion to deprive a party of solicitor-client costs, even in the face of an express contractual obligation, where such costs are not appropriate in the circumstances: *Fidelity Trust Company v Hawrish*, *Ward and Ward* (1986), 1986 CanLII 3118 (SK CA), 55 Sask R 10 (CA); *1269917 Alberta Ltd. v FMI Developments Ltd.*, 2011 SKCA 94, 375 Sask R 175; *Karkoulas v Farm Credit Canada*, 2005 SKQB 535, 274 Sask R 152. An agreement between the parties does not supersede the court's discretion over costs. The court may refuse to enforce a contractual provision regarding recovery of solicitor-client costs where there is good reason for so doing. Such reasons may include vexatious, oppressive, fraudulent or otherwise inequitable conduct on the part of the mortgagee, or other circumstances particular to the case that render the imposition of solicitor-client costs unfair, excessive or unduly onerous: *Bossé* at para 65; *Ledoux* at para 19.

[143] The court awarded solicitor-client costs on the appeal to the respondent as provided for in the mortgage contract, because there was nothing in the record to suggest that the respondent had engaged in fraudulent, vexatious, oppressive or inequitable conduct or that the award of solicitor-client costs would be unfair, excessive or unduly onerous: para. 12.

[144] The *Bossé* decision referred to is the decision of the Ontario Court of Appeal in *Bossé v. Mastercraft Group Inc.*, [1995] O.J. No. 884, 1995 CanLII 931 (C.A.), leave to appeal ref'd 24702 (21 September 1995), where the court said:

> The costs of and incidental to a proceeding or a step in a proceeding are, subject to the provisions of a statute or the rules of court, in the discretion of the court and the court may determine by whom and to what extent the costs shall be paid: *Courts of Justice Act*, R.S.O. 1990 c.C-43, s.131(1); rule 57.01 of the Rules of Civil Procedure. As a general proposition, where there is a contractual right to costs the court will exercise its discretion so as to reflect that right. However, the agreement of the parties cannot exclude the court's discretion; it is open to the court to exercise its discretion contrary to the agreement. The court may refuse to enforce the contractual right where there is good reason for so doing - where, for instance, the successful mortgagee has engaged in inequitable conduct or where the case presents special circumstances which renders the imposition of solicitor and client costs unfair or unduly onerous in the particular circumstances. See, generally, *Orkin on Costs*, 2nd ed. 1993, p.2-111; *Collins v. Forest Hill Investment Corporation*, 1967 CanLII 291 (ON SC), [1967] 2 O.R. 351 (Cty. Ct.), *Ontario Potato Distributing Inc. v. Confederation Life Insurance Co.* (1991), 25 A.C.W.S. (3d) 809 (Ont. Ct. Gen. Div.), *Cabot Trust v.*

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> *D'Agostino* (1992) 1992 CanLII 7507 (ON SC), 11 O.R. (3d) 144 (Gen. Div.), *C.D.I.C. v. Canadian Commercial Bank* (1989), 1989 ABCA 150 (CanLII), 68 Alta. L.R. (2d) 194 (C.A.), p.203-4.

[145] The court set aside the order for solicitor-client costs, and substituted an order for party and party (ordinary) costs. It did so because the costs had been ordered payable on a joint and several basis between a number of parties, which would have permitted the successful respondents to recover their costs from a single party in an amount well in excess of that party's indebtedness. The court held that this would be onerous and unfair: at 34.

[146] As noted above, although this Court has generally favoured the enforcement of contractual cost indemnity provisions, we do not read the relevant authorities as precluding a residual discretion on the part of the court to depart from such provisions. Rather, we accept the principle espoused in *Orkin*, as endorsed by the Alberta Court of Appeal in *Schafer*, that any contractual right to costs is always subject to the court's discretion. In our view, this is consistent with the overriding authority, and responsibility, of the court to manage and supervise its own processes.

[147] That said, the existence of a contractual indemnity cannot be ignored. As this Court has held, it is open to the parties to agree that one will indemnify the other for actual legal fees and costs in certain circumstances: *Tanious* at para. 52. Quoting Voith J.A. in *Eisler Estate (CA)*, "a contract is a contract": para. 8.

[148] Thus, where a contractual indemnity provision meets the threshold test of "clearly and unequivocally" establishing the right to indemnification (*Eisler Estate (SC)* at para. 31), that provision will, in our view, be presumptively enforceable. The burden then shifts to the party opposing indemnification to establish why the court should exercise its discretion to depart from the terms of the contract.

[149] As to when that discretion should be exercised, we do not think it is helpful to enumerate a list of specific factors that would justify doing so. Each case will turn on

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its specific facts. We agree with the court in *Schafer* that the circumstances in which a court may decline to award contractual costs are not limited to cases in which there has been litigation misconduct, although that may be a relevant factor. Nor do we think "extraordinary" circumstances are necessarily required. Rather, the court must consider all relevant circumstances, including factors such as degree of success and proportionality in terms of expense, keeping in mind that the overriding objective of the *Supreme Court Civil Rules* is to secure a "just, speedy and inexpensive" determination of every proceeding on its merits: R. 1-3(1).

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Discussion

The Lease Action

[150] Cardero again submits that the judge erred in granting PRP its contractual indemnity costs because PRP failed to achieve substantial success in its claim. Cardero submits that substantial success is, in effect, a condition precedent to the award of costs, including contractual indemnity costs. Cardero cites this Court's decision in *Victory Motors (Abbotsford) Ltd. v. Actton Super-Save Gas Stations Ltd.*, 2021 BCCA 129 at para. 158, for the proposition that "substantial success" generally means success on 75% of the matters in dispute (citing *The Owners, Strata Plan LMS 3259 v. Sze Hang Holding Inc.*, 2017 BCCA 346 at paras. 90–92). The Court, in both *Victory Motors* and *Sze Hang Holdings*, observed that the "substantial success" test may apply in cases involving multiple causes of action: *Victory Motors* at para. 158; *Sze Hang Holdings* at para. 92.

[151] PRP submits that the judge did not err in holding that the "substantial success" test did not apply given the language of the contractual indemnity, which does not require that PRP achieve a specified level of success. Rather, the clause provides an indemnity for any and all losses directly or indirectly incurred in connection with, as a result of, or arising out of any breach of the Lease by Cardero: Costs Reasons at paras. 37–38.

[152] We agree with PRP that to impose a requirement of substantial success in order for PRP to take advantage of the contractual indemnity would be to ignore the clear terms of the clause and to, in effect, re-write it.

[153] As set out above, it is our view that contractual cost indemnities are not absolute, and the court retains the discretion to decline to enforce such clauses in appropriate circumstances. Relative success may be one such circumstance, depending on the facts of a specific case: *Schafer* at para. 73. This, however, is a different proposition from the argument that failure to achieve ”substantial” success operates as a bar to recovering contractual costs.

[154] In our view, Cardero has not demonstrated that the judge erred in declining to deny PRP its contractual costs for failing to achieve substantial success.

[155] That said, and as indicated, the parties' relative success is a factor that may be considered when determining whether to enforce a contractual costs provision. Here, PRP sought damages totalling $2.5 million, comprising the first two advance royalty payments required under the Lease. PRP succeeded in its claim for the first payment of $500,000 which, with interest, resulted in a total payment owing of over $800,000. Thus, PRP can fairly say that it achieved a reasonable degree of success on its claim.

[156] However, PRP failed in establishing its claim for the larger advance royalty payment of $2 million. The judge found that the same reasoning that led him to find that Cardero owed the $500,000, necessitated a conclusion that it did not owe the $2 million: RFJ at para. 192. On this claim, Cardero says that it was the successful party. It submits that success in the Lease Action was divided, and that PRP should, therefore, have been denied its costs.

[157] Cardero also relies on its formal offer to settle. Cardero submits that the judge erred in awarding PRP its contractual costs despite finding that Cardero's offer to settle, which "accurately predicted the outcome of the trial", should have been accepted: paras. 70, 76. The judge again found that these sophisticated parties had

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agreed to indemnify one another, and made no exception for offers to settle: para. 86.

[158] In our view, the judge erred in finding that he was precluded from considering Cardero's offer simply because the prospect of such an offer was not contemplated in the indemnity clause. The existence of a formal offer, and the recipient party's response, like the relative success of the parties, is a factor that may be considered as part of the court's determination of whether to apply or depart from a contractual indemnity. We would add that we find no merit in PRP's argument that the judge, in finding that Cardero's offer should have been accepted, erred by treating PRP and CCP as a single entity. That approach was open to the judge on the facts before him; in particular, the facts that PRP and CCP were jointly represented, that control of both parties rested with the same principals, and that there was no indication that their interests were not aligned: Costs Reasons at para. 81.

[159] When Cardero's offer to settle is considered along with the relative success of the parties, most notably PRP's lack of success on the largest part of its claim, it is our view that this is a case in which it would be unfair and inequitable to award PRP full solicitor-client costs for the entirety of its claim. It is apparent from the judge's reasons that he recognized this unfairness but felt that he was obligated to apply the contractual costs indemnity absent extraordinary circumstances. Respectfully, the requirement for extraordinary circumstances frames the test too narrowly and amounts to an error in principle — albeit, an understandable one given that this Court has not previously addressed the extent of the discretion to depart from a contractual costs indemnity.

[160] The question then becomes whether this Court should determine an appropriate costs award in the Lease Action or remit the matter to the judge. In our view, it is open to us to substitute a costs award based upon the judge's findings and the principles that we have articulated.

[161] As a starting point, this is not a case in which costs can or should be apportioned between the two claims on the advance royalty payments. It is open to

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courts to take that approach where success has been divided on separate and discrete issues in the litigation, and where the court can reasonably identify the amount of trial time attributable to the separate issues: *Sutherland v. The Attorney General of Canada*, 2008 BCCA 27 at para. 31. Here, the judge did not make any findings as to the apportionment of trial time spent on the two advance royalty claims.

[162] In our view, in assessing costs of the Lease Action, it must be recognized that PRP had a valid claim that Cardero breached the Lease by failing to pay the first advance royalty payment of $500,000. PRP was required to commence litigation in order to pursue that claim, and it is entitled to the benefit of the contractual costs indemnity for doing so. However, as we have found, recovery of full indemnity costs for the entirety of the Lease Action would be unfair and inequitable given the parties' relative success and the existence of Cardero's offer to settle.

[163] It was at the point of the settlement offer that PRP should have critically assessed its position and, as the judge found, should have accepted the offer. In the circumstances, it would be unreasonable for PRP to claim full contractual indemnity costs past August 19, 2021, the date of the offer.

[164] Instead, given the divided success of the parties in the Lease Action at trial, it is our view that they should each bear their own costs for all steps in the Lease Action after August 19, 2021.

[165] We would, therefore, allow Cardero's cross appeal in part, and would vary para. 1 of the judge's costs order dated June 30, 2022, to provide that PRP is entitled to be indemnified for its costs in advancing the Lease Action, pursuant to the terms of the Lease, up until August 19, 2021, with the parties to bear their own costs thereafter.

[166] Finally, we note that an argument might have been advanced that the indemnity clause in the Lease should not be so broadly interpreted as to permit PRP to recover its solicitor-client costs for the entire Lease Action, including the $2 million

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advance royalty payment, given that Cardero's failure to pay that amount was found not to be a breach of the Lease. However, this argument was not made below or before us, thus we decline to consider it. We would observe that the dispute over the interpretation and application of the indemnity clause in the Lease, as well as the clause in the JVA discussed below, underscores the importance, when drafting such clauses, to use language that clearly and unequivocally identifies the scope of what is covered by the clause.

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The JVA Counterclaim

[167] Cardero submits that the judge erred by adopting an overly narrow interpretation of the costs indemnity clause in the JVA, the material terms of which provide that Cardero will be indemnified for any losses, defined to include legal costs incurred "in connection with, as a result of or arising out of" any breach of the JVA by CCP. The judge again held that, in the JVA Counterclaim, CCP alleged breaches of the agreement by Cardero, thus it fell outside of the terms of the contractual indemnity.

[168] Cardero says that the judge's interpretation failed to give meaning to the terms "in connection with" and "arising out of" as used in the indemnity clause. Cardero cites *Amos v. Insurance Corp. of British Columbia*, [1995] 3 S.C.R. 405, where the Court held that the phrase "arising out of" is broader than "caused by", and must be interpreted in a more liberal manner. The Court then said:

> … the words "arising out of" have been viewed as words of much broader significance than "caused by", and have been said to mean "originating from", "having its origin in", "growing out of" or "flowing from", or, in short, "incident to" or "having connection with" …

[169] Cardero notes that the "factual basis" section of the JVA Counterclaim simply repeats the facts alleged in its response to civil claim, although the Counterclaim also adds a claim for damages resulting from Cardero's alleged breach of the JVA. Cardero submits that it had to address CCP's allegations of breach in order to obtain the remedy it sought. For this reason, Cardero argues the costs it incurred would have been the same regardless of whether CCP brought its Counterclaim.

[170] In these circumstances, Cardero submits that its costs of defending the Counterclaim were clearly incurred “as a result of” or “in connection with” CCP’s alleged breaches of the JVA. The costs indemnity therefore applies.

[171] CCP notes that the judge’s costs order on its Counterclaim formed part of his overall costs assessment in the three proceedings: the Lease Action, the JVA Action and the JVA Counterclaim. CCP submits that the determination of the various costs awards involved the exercise of discretion and, as such, is entitled to considerable deference.

[172] CCP submits further that Cardero’s claim and its Counterclaim differed significantly. Cardero alleged that CCP had failed to cooperate in carrying out the JVA and breached the JVA in several material ways. In contrast, CCP’s Counterclaim alleged that Cardero breached the JVA by surrendering its interest in the Freehold.

[173] In our view, Cardero has not demonstrated any error in the judge’s interpretation of the JVA indemnity clause that would warrant intervention by this Court. His finding that the clause is limited to costs incurred as a result of breaches of the JVA by CCP, but does not extend to costs incurred in defending allegations of its own breach, is one that was open to him on the language of the clause.

[174] Further, while Cardero accurately points out that the material facts alleged in CCP’s response to civil claim are simply repeated in the JVA Counterclaim, the essential facts alleged with respect to the allegations of breach by each of CCP and Cardero are different. The judge fairly found that the claims were intertwined, however, the question before him was whether the claims in the JVA Counterclaim fell within the meaning of the indemnity clause. He found that they did not.

[175] While the judge did not say so expressly, he effectively found that the clause did not meet the threshold requirement of “clearly and unequivocally” providing for an indemnity for Cardero on the JVA Counterclaim.

[176] We would therefore dismiss Cardero’s cross appeal.

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Disposition

[177] For these reasons, we would dismiss the appeals of CCP and PRP in the JVA Action and the Lease Action. We would further dismiss Cardero's cross appeal in the JVA Counterclaim. We would allow in part Cardero's cross appeal in the Lease Action, and would vary para. 1 of the judge's costs order dated June 30, 2022, to provide that PRP is entitled to be indemnified for its costs in advancing the Lease Action, pursuant to the terms of the Lease, up until August 19, 2021, with the parties to bear their own costs thereafter.

"The Honourable Mr. Justice Harris"

"The Honourable Justice Skolrood"

I agree:

"The Honourable Mr. Justice Fitch"

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