Is It Permissible To Backdate The Effective Date Of A Contract?



Backdating is Generally Permissible

It is common for two parties, particularly in the commercial context, to enter into a contract at one time, but agree to have the contract come into effect at an earlier time. This practice is colloquially known as backdating. Courts respect the parties' decision to backdate since giving effect to backdating provisions respects the parties' intentions as well as their freedom of contract.[1]

The Supreme Court of Canada addressed the issue of backdating in *McClelland & Stewart Ltd v. Mutual Life Assurance Co. of Canada*[2] where the Court interpreted a life insurance policy to discern whether an exclusion clause started to run as of January 23rd, 1968 (the backdated date chosen by the agent for the calculation of premiums) or February 28th, 1968 (the date the contract was delivered to the insured). The Court considered the construction of the whole policy and held that the exclusion clause took effect on the backdated date chosen by the parties.

Backdating Must Not Be for the Purpose of Misleading Third Parties

Although backdating is generally permissible under the common law, a court will not give effect to backdating where the parties backdated the contract to mislead a third party. For example, in *Re Rovet,*[3] a company's employees were interested in unionizing. The company attempted to impede the unionization by hiring additional employees that were against the union. However, to the company's disappointment, these employees were not hired until **after** the company's current employees filed their application to unionize, making the new employees unable to participate. To cure this deficiency, the company, and their solicitor, backdated the contracts of the newly hired employees to a date **before** the application to unionize. The Law Society of Upper Canada Ontario Discipline Committee determined that backdating the employment contracts was for the purpose of misleading a third party, and suspended the solicitor for a period of twelve months.

Additionally, where the backdating of an agreement affects the taxes that are imposed (or not imposed) on one of the contracting parties, courts will generally only respect the backdating provisions as between the contracting parties. A court will generally not enforce the backdating provisions as between a taxpayer and the applicable tax enforcement agency (such as the Canada Revenue Agency).

Backdating Must Not Contravene Applicable Rules or Legislation

In addition to misleading a third party, backdating may also be impermissible where it contravenes applicable rules or legislation. For example, in *Research in Motion Ltd.*[4] the Ontario Securities Commission found that RIM engaged in improper backdating practices when certain high ranked individuals backdated options to a price that was "in the money". This practice contravened both the TSX Rules as well as RIM's stock option plan that required options "to be granted at an exercise price not less than the closing price of RIM's common shares on the TSX on the last trading day preceding the date on which the Options are approved for grant".[5]

The Bottom Line

In summary, backdating is generally permissible where it is done to alter the obligations of the contracting parties only. However, it is impermissible where the parties backdate either to unconscionably interfere with the rights of third parties (including the government's right to tax such parties) or where it contravenes applicable rules or legislation.

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