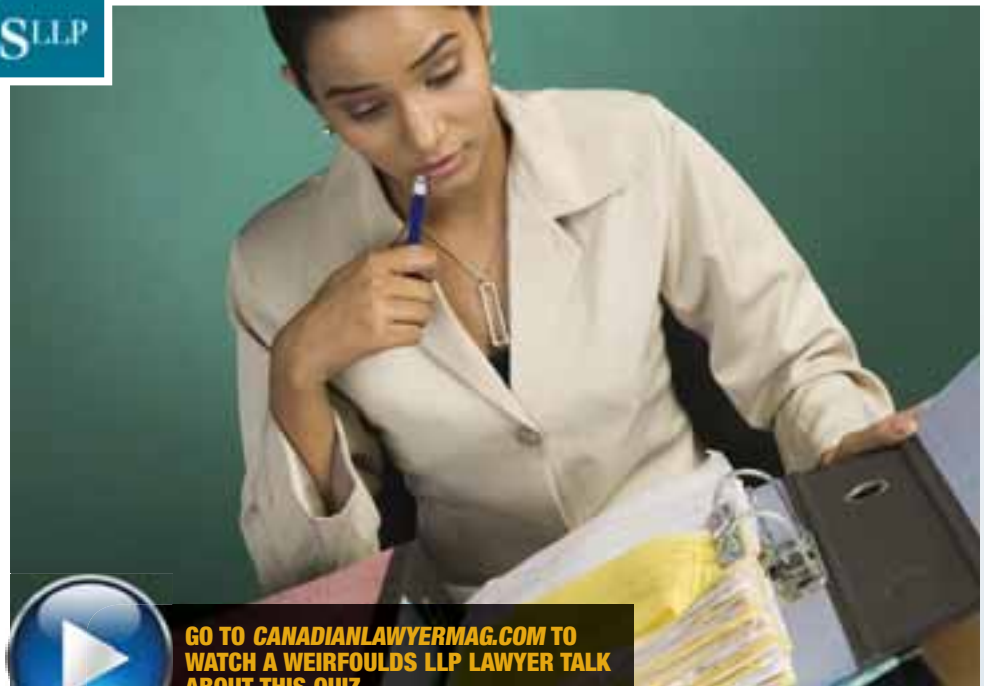


Good faith and honest contractual performance

In November 2014, the Supreme Court of Canada released a significant decision in *Bhasin v. Hrynew*, which recognized a new general duty of honesty in contractual performance. The court introduced “two incremental steps.” First, it acknowledged an “organizing principle” of good faith in contract law. Second, it recognized a new common law duty to act honestly in the performance of contractual obligations. In light of the potentially wide-ranging effects of this decision, parties will need to consider their performance obligations and behaviour.

Let’s explore the decision in greater depth by testing your knowledge of its possible implications.



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- 1** Is there a general duty of good faith in all contractual dealings?
(A) Yes
(B) No
(C) Maybe
- 2** Can parties contract out of the duty of honest contractual performance?
(A) Yes
(B) No
(C) Maybe
- 3** Is there an obligation to put the interests of a counter-party to a contract first? For example, a large grocery store chain has a contract with a small produce supplier for the purchase of fruits and vegetables. Is there any requirement for the grocery store to put the interests of the small produce supplier first when considering a change to the quantity of its order?
(A) Yes
(B) No
(C) Maybe
- 4** A landlord has a contract with a property management company for the management of its leased properties. The contract automatically renews, subject to a non-renewal clause. The landlord intended to renew the contract and communicated this to the property management company. However, one month later, the landlord changed its mind and exercised the non-renewal clause. Is this a breach of the duty of honest contractual performance?
(A) Yes
(B) No
(C) Maybe
- 5** Can a contracting party protect itself by limiting communications with the counter-party in the course of performing the contract?
(A) Yes
(B) No
(C) Maybe

1 (B) No. The court declined to adopt a general duty of good faith in all contractual dealings. Instead, the court recognized a more narrow common law duty of honest contractual performance, which it explained to mean “simply that parties must not lie or otherwise knowingly mislead each other about matters directly linked to the performance of the contract.” However, *Bhasin* and the court’s recent decision in *Sattva Capital Corp v. Creston Moly Corp* indicate that the court is prepared to introduce changes to long-standing principles of contract law and further changes in the future cannot be ruled out.

2 (B) No. Parties cannot contract out entirely of the duty of honest contractual performance. However, the court left open the possibility that parties can vary the “precise content of honest performance” in different contexts (presumably through drafting a contractual provision that establishes the standards the parties wish to live by). The court stated that modifications must be express, and that parties cannot contract out of the “minimum core requirements” of the duty. Since the parameters of the duty of honest performance, including its “minimum core requirements,” are yet to be determined, it remains to be seen what modifications the courts will permit.

3 (B) No. The court was clear that the duty of honest performance is not a fiduciary duty. A contracting party is under no obligation to put the interests of a counter-party first. However, at the very least, contracting parties should not engage in conduct that is actively misleading or otherwise deceitful. In defining the scope of the duty of honest performance, the court stated that it is similar to, but is not the same as or subsumed by, the law relating to civil fraud and estoppel.

4 (C) Maybe. The Supreme Court of Canada held that capricious and arbitrary behaviour was inconsistent with the duty of honest contractual performance. The landlord’s abrupt change in position might seem that way to the counter-party faced with an unexpected non-renewal, even though in many cases, exercising a non-renewal clause will be neither dishonest nor unreasonable. For example, there may be a change in market conditions or the landlord may decide to sell some of its properties. To protect itself, the landlord may wish to consider documenting its internal decision-making process so that it can readily explain its motivations and behaviour.

5 (C) Maybe. While the duty of honest contractual performance does not impose a duty of disclosure on contracting parties, overly circumspect communications may give rise to allegations of dishonesty by omission. If parties are concerned about violating (or appearing to violate) a new duty of honesty in contractual performance with which they are unfamiliar, they may well be tempted to say less to each other in general. Allegations of “dishonesty by omission” could lead to litigation. This risk would be heightened in situations where one contractual party poses a direct question to another.

YOUR RANKING?

- **One or Two correct:** *might be time to brush up*
- **Three correct:** *not bad, but some further work needed*
- **Four correct:** *very well done, but not perfect*
- **Five correct:** *excellent*

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