

Avoiding Disputes: The Duties of Good Faith and Honesty in Contractual Performance

Prepared for: Legal Education Society of Alberta
Business Disputes

Presented by:
Leah Tolton
Dentons Canada LLP
Edmonton, Alberta

For presentation in:
Lake Louise, May 5, 2018

AVOIDING DISPUTES: THE DUTIES OF GOOD FAITH AND HONESTY IN CONTRACTUAL PERFORMANCE

Principles to Guide Contract Drafting 2

- 1. Do Not Lie 2
- 2. You Don't Have to be Fair 3
- 3. A Court Will Uphold Express Contract Terms and Will be Slow to Imply Terms 4

Defining Contractual Obligations: Say What You Mean and Mean What You Say 4

A Word About Implied Terms 5

Include a Limitation of Liability Clause 5

Include an Entire Agreement Clause 7

The Final Check: Things That Cause Interpretation Problems 8

PowerPoint – Avoiding Disputes: The Duties of Good Faith and Honesty

PRINCIPLES TO GUIDE CONTRACT DRAFTING

The Supreme Court of Canada rendered its decision in *Bhasin v Hrynew*¹ just over three years ago. In *Bhasin*, Justice Cromwell noted that Anglo-Canadian common law had resisted acknowledging any generalized and independent doctrine of good faith. This had resulted in an “unsettled and incoherent body of law” that had developed “piecemeal” and which was “difficult to analyze.”² From this, it was apparent that it was necessary to provide some predictability to the Canadian common law. Despite this lack of certainty at the time of the decision, *Bhasin* has not precipitated a flood of decisions that have dramatically changed Courts’ interpretations of contracts.

Three general principles of contracting flow from *Bhasin* that will assist practitioners to successfully draft agreements and enhance the likelihood that the agreements will be enforced:

1. Do Not Lie.

The main issue in *Bhasin* was that Canadian American Financial Corp. (“Can-Am”) repeatedly misled Mr. Bhasin regarding Mr. Hrynew’s appointment as Provincial Trading Officer. Further, Can-Am repeatedly denied a rumoured merger between Mr. Bhasin’s and Mr. Hrynew’s books of business in response to Mr. Bhasin’s enquiries. Can-Am’s dishonesty was linked directly to its agreement with Mr. Bhasin and Mr. Bhasin’s ability to exercise the non-renewal provisions of his contract with Can-Am. Had Mr. Bhasin been made aware of Can-Am’s intentions, he could have acted to retain the value of his dealership business that he had built up over the previous ten years.

Justice Cromwell noted in *Bhasin*:

“[C]ommercial parties reasonably expect a basic level of honesty and good faith in contractual dealings. While they remain at arm’s length and are not subject to the duties of a fiduciary, a basic level of honest conduct is necessary to the proper functioning of commerce.”³

So what does this mean for contracting parties?

- (a) They must perform their contractual duties honestly and reasonably and not capriciously or arbitrarily;
- (b) They must not lie or knowingly mislead each other about matters directly linked to the performance of the contract;

¹ *Bhasin v Hrynew*, 2014 SCC 71

² *Ibid* para 32

³ *Ibid* para 60

- (c) They must be able to rely on a minimum standard of honesty from their contracting counterparty in performing the contract; and
- (d) They must be honest when asked questions in relation to the contract.

The duties of honesty and good faith in contractual performance do *not* mean that:

- (e) the parties owe each other a duty of disclosure. If a contract does not impose a positive obligation to disclose facts, silence as to those facts is neither dishonest nor a misrepresentation. That said, non-disclosure (i.e., silence) or selective disclosure of a material fact may be considered a breach the duty of honest performance if it has the same effect as a lie in the particular circumstances; or
- (f) parties are prevented from pursuing their individual self-interest.

Note that all of the foregoing obligations relate to *performance* of the contract, not to the terms of the contract itself. This obviously does not mean that parties can be dishonest in the statements that they agree to within a contract, but it does mean that they are still free to negotiate the deal that they want.

2. You Don't Have to be Fair.

The *Bhasin* decision does not create a requirement that terms of contracts be fair or that a contracting party be reasonable when exercising discretion granted to it by a contract. The Courts have been hesitant to extend the requirements of good faith beyond honesty for fear of causing undue judicial interference in contracts.⁴ Parties are free to pursue their individual self interests and to pursue advantages flowing from the contract. Lawyers can advocate for their clients without worry that lack of fairness when contract terms are applied will be breach the duty of good faith.

The Alberta Court of Appeal has held that even where parties to a contract have drafted their contract in clear and unambiguous terms, a court will not be permitted to review the contents of the arrangement on the basis of *Bhasin* principles to determine whether it is fair or not. It “does not invite the court to examine the terms of the contract and decide whether they are “honest”, “capricious” or negotiated in “good faith”, much less, whether they are “fair” or “reasonable.””⁵

Although there is no requirement of “fairness”, when drafting contracts, one should ensure the wording used is clear and unambiguous. Where there is inevitable one-sidedness to a provision, the

⁴ Ibid para 89

⁵ *Styles v Alberta*, 2017 ABCA 1 at para 51