Supreme Court of Canada to Hear Two New Cases on Good Faith in Contract

November 21, 2019

Five years after its landmark decision in *Bhasin v Hrynew*, 2014 SCC 71, the Supreme Court of Canada is scheduled on December 6, 2019 to hear two new cases on good faith in contract. The Supreme Court in *Bhasin* introduced to Canadian jurisprudence the general organizing principle of good faith in contract. This is not a "free-standing rule", but rather "a standard that underpins and is manifested in more specific legal doctrines", exemplifying the idea that a contracting party should have appropriate regard to its counterparty's legitimate interests.[1] Flowing from this is a common law duty of honest contractual performance. The Court held that this duty means parties may not lie to or mislead each other about the performance of the contract, but does not otherwise equate to a duty of loyalty or disclosure. *Bhasin* has been widely cited in case law and discussed in academic commentary. The two upcoming appeals provide a ripe opportunity for the Supreme Court to address further issues arising out of its earlier decision.[2]

Decisions under Appeal

The two appeals that bring the Supreme Court back to the notion of good faith in contract law are expected to clarify the parameters of good faith as a general organizing principle and the specific scope of the duty of honest contractual performance. Each of the cases under appeal deals with circumstances beyond those addressed by the Supreme Court in *Bhasin*, and raises important practical issues.

In *Wastech Services Ltd. v Greater Vancouver Sewerage and Drainage District*, 2019 BCCA 66, a decision from the British Columbia Court of Appeal, the question is whether a contractual duty of good faith applies to restrict a party's exercise of discretion in the absence of a contractual term. Wastech Services Ltd. ("Wastech") and the Greater Vancouver Sewerage and Drainage District ("Metro") were parties to a 20-year contract for the disposal of sewage waste from the Vancouver regional district. The contract gave Metro the discretion to allocate waste between certain disposal facilities, and contained detailed provisions for certain payment adjustments in specific circumstances.[3] In 2011, Metro exercised this discretion in a manner that reduced its costs, but also impacted Wastech's profits.

The dispute proceeded to arbitration. Wastech argued that there should be a term implied into the contract that limited Metro's power to re-direct waste between the facilities without adjusting the rates it paid to Wastech, or otherwise compensating Wastech. However, the evidence was that the parties had made the decision not to include such a term in the contract, and, as such, the arbitrator refused to imply the term Wastech sought. Despite making this finding, the arbitrator then held that Metro breached its duty of good faith because, in the exercise of its discretion for allocating waste, it did not have appropriate regard to Wastech's interests. The British Columbia Supreme Court overturned the arbitrator's decision as it improperly expanded the concept of good faith beyond its scope. The British Columbia Court of Appeal upheld the lower court's decision, stating:

> Since the arbitrator had rejected the implied term as something the parties had intentionally excluded… he erred here in failing to apply the right test – namely whether Wastech had a *legitimate expectation arising out of the Agreement* that Metro would not exercise its discretion in the way it did. The answer to that question had to lie not in the financial effect of the re-allocation on Wastech, but in the Agreement. Only then could an expectation to this effect be described as "contractual"[4].

The Court of Appeal held that "this fact substantially *took away* from the argument in support of a breach of the duty of good faith."[5]

The second decision on appeal is the Ontario Court of Appeal's decision in *C.M. Callow Inc. v Zollinger*, 2018 ONCA 896*.* In this case, the appellant condominium corporations formed a Joint Use Committee ("JUC") to make decisions relating to the condominium corporations' shared assets. C.M. Callow Inc. ("Callow") and the condominium corporations entered into two maintenance contracts, one for summer maintenance and one for winter maintenance, respectively. The winter maintenance contract provided for early termination by the condominium corporations on ten days' notice. In March or April of 2013, JUC decided to terminate the winter contract, but did not provide Callow with notice of termination until September 2013, so as to avoid jeopardizing Callow's work under the summer contract. Meanwhile, in the summer of 2013, Callow unilaterally performed free extra work, of which JUC was aware, with the hope that it would incentivize the condominium corporations to renew the two contracts upon their expiry. Nevertheless, in September of 2013, the condominium corporations terminated the winter maintenance contract on notice and Callow sued for breach of contract.

The trial judge found that the condominium corporations breached the contractual duty of honest performance. The Ontario Court of Appeal allowed the appeal on the basis that the trial judge had effectively modified the contractual right to terminate the contract and went beyond what the duty of honest performance requires or permits. The Court of Appeal held that there was no unilateral duty of disclosure, and that the duty of honest performance did not modify or otherwise limit the right to terminate the winter maintenance contract in accordance with its terms.

Implications

These important cases at the Supreme Court raise issues about the scope of good faith in contract post-*Bhasin*. The *Wastech* case raises the issue of how the general organizing principle of good faith manifests itself in the exercise of contractual discretion. The *Callow* case challenges the extent of any duty to disclose a decision to

terminate a contract. We anticipate that the Supreme Court's decisions in these cases will provide further clarity on the application of the principles outlined in *Bhasin* and the impact of good faith on Canadian contract law.

[1] *Bhasin v Hrynew*, 2014 SCC 71 at paras 64-65.

[2] *Wastech Services Ltd. v Greater Vancouver Sewerage and Drainage District*, Supreme Court of Canada File No. 38601 and *C. M. Callow Inc. v Zollinger*, Supreme Court of Canada File No. 38463.

[3] *Wastech Services Ltd. v Greater Vancouver Sewerage and Drainage District*, 2019 BCCA 66 [***Wastech***] at paras 20-29.

[4] *Wastech* at para 68 (emphasis in original).

[5] *Wastech* at para 69 (emphasis in original).

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