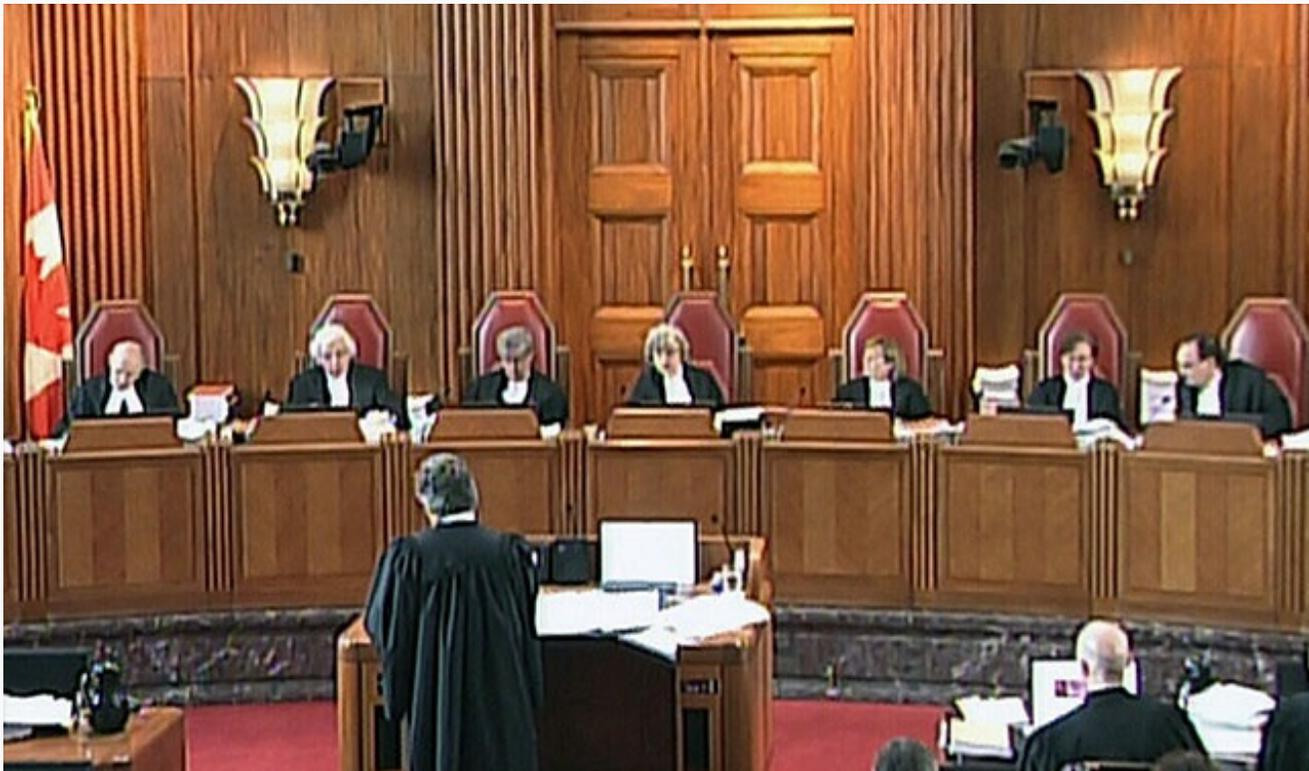


The Supreme Court of Canada moves the Law of Contract: The principle of good faith and duty to act honestly

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by Craig Ferris, *Western Canada Business Litigation Blog* | [see original article](#)



The Supreme Court of Canada has, for the first time, ruled that parties must not lie or mislead each other concerning matters linked to the performance of a contract in Canadian common law provinces.

On November 13, 2014, the Supreme Court of Canada released its much anticipated decision in [Bhasin v. Hrynew, 2014 SCC 71](#). In its decision, the Supreme Court of Canada for the first time expressly recognized “good faith” as an organizing principle in the operation of contract law in Canadian common law provinces. This is a significant alteration to the law of contracts in the common law jurisdictions of Canada. We expect that *Bhasin* will become known as one of the seminal decisions in Canada in relation to the performance of contractual obligations.

The Supreme Court of Canada’s alteration or what they called an “incremental step” to the law of contracts was to acknowledge good faith contractual performance as a general organizing principle of the common law of contract. This principle “underpins and informs” the various contractual doctrines which govern contracts in Canadian law. The Court differentiated an “organizing principle” from a specific legal doctrine. An organizing principle is a standard which underlies legal doctrines and which may be used to determine how those doctrines operate. It is flexible and may be given different weight in different situations. The Court found that good faith was a standard by which existing legal documents should be interpreted and also that by recognizing good faith as an organizing principle, it would allow the common

law of contract to be developed in a more coherent and principled manner.

The Court was careful to distinguish the organizing principle of good faith from a fiduciary obligation. It found that the organizing principle of good faith means that a contracting party should have “appropriate regard” to a contractual interest of the other contracting party. Appropriate regard will vary and depend on the circumstances of the specific contract, but it does not require the contracting party to subjugate its interests to the other party. **Rather, it obligates the party not to “undermine those interests in bad faith.”**

The Court went on to say that the organizing principle of good faith is recognized through existing contractual law doctrines, but that the categories of those doctrines are not closed. Instead, new doctrines can be recognized where the existing common law is found deficient and the organizing principle of good faith requires further development. In this case, good faith required the recognition of a general duty of honesty in contractual performance. **Simply put, the Court found that parties must not lie or mislead each other concerning matters linked to the performance of the contract.** On the facts of this case, the Court relied upon the findings of fact of the trial judge, who found that one party had misled the other party concerning the renewal of a dealership agreement and, if that party had not been misled, they would have taken steps to protect the value of their business. Having lost the value of the business, the Supreme Court of Canada awarded damages equal to the value of the business.

The Court did discuss whether parties could contract out of these obligations, but found that, like unconscionability, the overriding principle of good faith and the duty of honesty were core elements of contract law which could not be expressly excluded from the contract. Rather, the parties could influence the scope of the duty of honesty in a particular context and relax the requirements of the doctrine provided they recognize its minimum core requirements.

This decision was only released this morning. Nevertheless, it is important to note that the Supreme Court of Canada has for the first time expressly recognized good faith as an organizing principle of contractual law in the common law of Canada and manifested that organizing principle in a duty of honesty in the performance of contracts. It will take some time to understand fully understand the impact of this “incremental step” in the law.

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