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SCC Expands the Duty of Honest Performance: Silence or Non-Disclosure Can Now Also Constitute a Breach

This past Friday, the Supreme Court of Canada released its much-anticipated decision in *C.M. Callow Inc v Tammy Zollinger* (“*Callow*”), the first of two appeals heard in December 2019 seeking clarification on the scope of the organizing principle of good faith recognized in *Bhasin v Hrynew* (“*Bhasin*”).

Many had hoped that the decision would shed light on the scope of the duty of good faith and honest performance recognized in *Bhasin*, and provide clear guidance to lower courts and commercial parties on their contractual obligations.

However, the decision which resulted in a 5-3-1 split across the court (Kasirer J writing for the majority, Brown J concurring, and Côté J in dissent) may add further uncertainty to the jurisprudence around obligations of good faith.

While the majority of the Court agreed that the respondent, a group of condominium corporations known as Baycrest (“Baycrest”), had breached its duty of honest performance in its contract with the appellant Mr. Christopher Callow (“Mr. Callow”), there was significant disagreement on the correct approach to both liability and damages on the appeal.

In addition, the majority’s articulation of the duty of honest performance and reference to the civil law doctrine of abuse of right may, as suggested by Brown J, raise more questions than it claims to answer.

Background:

The appeal in *Callow* centred on a term in Baycrest’s contract (the “Contract”) with the appellant Mr. Callow for winter maintenance. The Contract allowed Baycrest to terminate its agreement with Mr. Callow, without cause, upon giving Mr. Callow 10 days’ notice.

In the spring of 2013, Baycrest decided that it would not renew the Contract and instead terminate it before the following winter. However, Baycrest chose not to communicate its decision to Mr. Callow until several months later in September 2013, when it gave Mr. Callow 10 days’ notice.

Notwithstanding the 10-day notice period, Mr. Callow sued Baycrest for breach of contract on the basis that Baycrest breached its duty of good faith and honest performance. Mr. Callow submitted that:

- Baycrest knowingly misled him about the possibility of renewing the Contract despite having already made its decision to terminate; and
- Baycrest further accepted free services from Mr. Callow over the summer of 2013, which it knew were provided by Mr. Callow as an incentive for Baycrest to renew the winter maintenance agreement and despite knowing that the termination was already a foregone conclusion.

Baycrest argued that it was under no duty to disclose its decision and that its silence did not constitute dishonesty. The termination clause on its face did not require it to give more than 10 days' notice.

The trial judge held that Baycrest breached its duty of honest performance. The Court of Appeal for Ontario reversed the trial judge's decision, holding that the duty of honest performance did not impose a positive duty to disclose its intention to terminate the winter maintenance contract before the 10-day notice period required under the Contract.

The Decision:

Kasirer J for a majority of the Court restored the trial judge's decision, holding that Baycrest knowingly misled Mr. Callow and breached its duty of honest performance of the winter maintenance contract. The Court held that while Baycrest did not have a free-standing obligation to disclose its intention to terminate before the notice period, it was required not to knowingly mislead Mr. Callow in exercising the termination clause. Brown J, concurring in the result, agreed.

Both Kasirer J and Brown J highlighted the trial judge's findings that Baycrest engaged in "active communications" and actions that deceived Mr. Callow about its intentions with respect to the winter contract and violated the duty of honest performance. The majority held "[o]ne can mislead through action, for example, by saying something directly to its counterparty, or through inaction, by failing to correct a misapprehension caused by one's own misleading conduct".

In dissent, Côté J rejected the idea that silence could be considered a breach of the duty of honest performance as outlined in *Bhasin*. Absent a duty of disclosure, Côté J stated that "a party to a contract has no obligation to correct a counterparty's mistaken belief unless the party's active conduct

has materially contributed to it.” Côté J found that Baycrest’s conduct did not rise to this level.

Côté J also noted the practical difficulties that the majority’s statement of the law created for commercial parties, who will now have to try to assess how a counterparty will construe their silence and draw distinctions between different types of silence.

Parties may also face significant uncertainty when trying to navigate conversations that are forced on them by counterparties seeking information on issues or decisions they may wish not to disclose.

The Abuse of Rights

In its reasons, the majority further clarified that to trigger the duty of honest performance, the impugned dishonesty must be directly linked to the performance of a contract. In its analysis, the majority turned to the doctrine of abuse of right that exists in the Quebec civil law context to demonstrate this point.

Kasirer J discussed the required direct link between dishonesty and performance of the contract from *Bhasin* by comparing it to how the framework for abuse of rights in Quebec connects the manner in which a contractual right is exercised to the requirements of good faith. While Baycrest had the right to terminate the contract, it exercised that right in a manner that transgressed the core expectations of honesty required by good faith in the performance of contracts.

Brown J raised significant concerns about the uncertainty and confusion that Kasirer J’s reference to the abuse of rights doctrine would inject in the law.

According to Brown J, not only was the abuse of rights doctrine unnecessary to deal with the appeal, a position echoed by Côté J, but the majority’s discussion of the abuse of rights doctrine expanded and confused the law set forth in *Bhasin*.

Moreover, invoking the civil law concept conflated, or at least obscured, the distinction between the duty of honest performance and the duty to exercise discretionary powers in good faith at common law and sacrificed analytical clarity. Justice Brown stated:

“The gravamen of a claim in honest performance is that a party made dishonest representations concerning contractual performance that caused its counterparty to suffer loss. It is not that a right was exercised in a way that was wrongful, abusive, or even dishonest. Here, for example, the complaint hinges on Baycrest’s deceptive conduct preceding the exercise of the termination clause... The exercise of the termination clause is

relevant only in the sense that it was the subject of the misrepresentation.”

Finally, Brown J raised serious concerns about the practical implications of importing Quebec civil law concepts such as the abuse of rights into the common law duty of good faith analysis, which is grounded in vastly different theories around laws and the rights at play.

Damages

The majority held that damages for breach of the duty of honest performance are to be assessed according to the ordinary contractual principles of a party's expectation damages, rather than reliance damages, which are the ordinary measure of damages in tort.

Interestingly, both the majority and concurrence distinguished the long-standing principle in *Hamilton v Open Window Bakery Ltd* that damages should be assessed according to the least burdensome form of performance.

Kasirer J upheld the trial judge's award of damages by addressing Mr. Callow's contractual expectations, while noting that while being conceptually distinct, reliance damages and expectation damages are often the same in reality.

In this vein, Brown J reached the same result as Kasirer J on the issue of damages but approached the calculation from the perspective of reliance. Brown J concluded that reliance damages should be awarded as the issue was not that Baycrest failed to perform the contract but that Mr. Callow relied on Baycrest's dishonest misrepresentation to his detriment.

Callow marks the first of two appeals heard by the Supreme Court of Canada in December of last year on the scope of good faith as an organizing principle in Canadian contract law. The second, *Wastech Services Ltd v Greater Vancouver Sewerage and Drainage District* ("*Wastech*"), is expected to be released next year.

Callow makes it clear that commercial parties should be on notice that in certain circumstances, courts may find that silence or omissions can now be considered as conduct that may knowingly mislead a counterparty, and fall afoul of the duty of honest performance.

Wastech calls on the Supreme Court to decide how much regard is the "appropriate regard" that a commercial party should have for its contracting partner's interests in the context of the duty of good faith.

It remains to be seen whether *Wastech* will respond to

concerns stemming from *Callow* about how much regard a party must have for what is in the mind of their counterparty. Will the Supreme Court continue to expand the duty of good faith in the next appeal or will it scale it back?