

# Liar Liar, Pants On Fire: Employers Require Employee Honesty – Does An Employer Have To Reciprocate?



The Supreme Court of Canada (SCC) recently handed down a ground breaking judgment in *Bhasin v Hrynew*. It held that there is an “organizing principle” of good faith in Canadian contract law which includes a duty to act honestly in the performance of contractual obligations.

The case did not involve an employment relationship but the decision will apply to employment contracts. The defendant and plaintiff were parties to a commercial dealership agreement. The defendant acted dishonestly by deliberately misleading the plaintiff about its intentions as well as the involvement of a competitor dealer.

The plaintiff lost the value of his business upon the agreement’s termination and started an action. The SCC found that the defendant had breached the contract by failing to adhere to this duty to act honestly.

## **WHAT THE NEW DUTY REQUIRES:**

The duty of honest performance requires parties not to lie to or knowingly mislead each other about matters directly linked to the performance of the contract. It does not impose a duty of loyalty or disclosure, and does not require one party to put the other party’s interests ahead of its own. Parties may still act in their own self-interest, as long as in doing so they do not lie to, mislead, or undermine the interests of the other party in bad faith. The Court distinguished between failure to disclose a material fact (such as an intention to terminate) and actively misleading the other party.

The SCC stressed that the principle of good faith should be applied in a way that allows parties to pursue their individual self-interest and recognized that

parties may cause loss to another (even intentionally) without running afoul of the principle if they do so in the legitimate pursuit of economic self-interest.

Parties cannot contract out of or exclude this duty. However, they may limit the scope of the duty by stipulating the standard of honesty required as long as the standard respects the minimum core requirement of honest conduct. The SCC did not set out what would constitute the minimum core requirement. This to be assessed in each situation and requires a highly context-specific analysis that gives proper regard to the legitimate interests of both parties.

### **IMPLICATIONS FOR EMPLOYERS:**

Until now, it was clear that an employer has a duty of good faith in the manner of termination. We can expect that lawyers acting for employees will argue that *Bhasin* extends the duty of good faith to all aspects of the employment relationship and that employers owe a duty of honesty to employees. The full extent or impact of the duty of honesty on employers is not clear. The precise impact of the decision on employers will depend on how courts shape this duty of good faith and the standard of honesty in future court cases. What can be expected, however, is that employee counsel will use *Bhasin* to claim additional damages for employees based on alleged breaches of the duty of good faith and honesty, just as we saw in the period following the SCC decision in *Wallace* many years ago.

The employer's conduct in all facets of the relationship could be subject to challenge and scrutiny including:

- the reasons for termination
- compensation discussions and negotiations;
- performance issues;
- the financial state of the business;
- security of employment;
- pre-hire representations
- the reasons or justification for change or maintaining status quo; and
- plans for restructuring or reorganizing the business (such as a future merger, acquisition of another business, or a sale of the business).

The SCC decision suggests that this duty does not require employers to actively disclose material facts where they have not been brought into issue. However, an employer that misleads an employee in answering a question or fails to correct an employee who expresses an incorrect belief related to the employment could face allegations that the employer's duty of honesty was breached. A key question will be what damages an employee can claim if the employer breaches this duty of honesty. For example, will an employee who makes a financial commitment on the strength of a statement from the employer that all is well be able to claim damages in addition to normal severance if that statement was misleading, the employee is terminated and the employee suffers additional damages as a result?

Until courts have further fleshed out the application of this new duty and provided greater certainty on its scope in the employment context, employers should exercise caution in discussions or negotiations with prospective and current employees. Employers should take care with any communications – active or passive – that could be construed as dishonest or misleading towards

employees on matters related to their employment.

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