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Don't Lie to an Employee: The Dangers of an Employer's Dishonest Contract Negotiations

On November 13, 2014, the Supreme Court of Canada issued a landmark decision on the law of contract. In *Bhasin v. Hrynew*, 2014 SCC 71, per Cromwell J. ("*Bhasin*"), the Court recognized a new duty of honest contractual performance, as a branch of the "legal organizing principle" of good faith. In short, the new duty requires that parties to a contract must not lie or otherwise knowingly mislead each other about matters related to the contract.

The Court's decision in *Bhasin* led to many questions: how would the lower courts enforce such a duty between contractual parties? What kind of evidence is required to show that contractual parties have not acted honestly with one another? Would the new duty of honest contractual performance apply to contracts that already impose a requirement of good faith, such as insurance and employment agreements?

One year later, it is clear that Ontario Courts have embraced and willingly enforced the new duty of honest contractual performance. In the Ontario Superior Court's decision *Antunes v. Limen Structures Ltd.*, 2015 ONSC 2163, per C.J. Brown J. ("*Antunes*"), the Court applied the duty in *Bhasin* to an employment relationship. The Court used the reasoning in *Bhasin* to find that a defendant employer was in breach of its duty of honest performance and fair dealing owed to the employee. In so doing, the Court made two key rulings, namely that:

i. the defendant employer must adduce some evidence that it acted honestly and in good faith in the negotiation and performance of the employment contract; and

ii. the Court will consider the defendant employer's breach of honest contractual performance in quantifying the reasonable notice period owed to the employee.

The Duty of Honest Contractual Performance: A Summary

In *Bhasin*, the Court held that at common law, there exists an "organizing principle of good faith". Good faith requires that a party to a contract, in fulfilling her duties under the agreement, should have regard to the "legitimate contractual interests of the contracting partner". This does not mean that a contractual party has to serve the other party's interests in all cases. Rather, it simply means that a party to a contract must not seek to undermine the other party's interests to the contract in bad faith.

The idea of good faith underlies and manifests itself in more specific doctrines, such as the new duty of honest contractual performance. This duty requires parties to be honest with one another in performing their contractual obligations. As Justice Cromwell held:

> …I would hold that there is a general duty of honesty in contractual performance. This means simply that parties must not lie or otherwise knowingly mislead each other about matters directly linked to the performance of the contract. This does not impose a duty of loyalty or of disclosure or require a party to forego advantages flowing from a contract; it is a simple requirement not to lie or mislead the other party about one's contractual performance.

Because the duty of honest performance is a doctrine of law, the parties cannot exclude it, though they may, in certain contexts, be free to relax the requirements of the doctrine, "so long as they respect its minimum core requirements". Thus, any change by the parties to the duty of honest performance has to be in express terms.

Honest Contractual Performance and the Employment Relationship

In *Antunes*, the Court imposed a duty of honest contractual performance on an employment relationship. The decision engages two issues: (i) the nature of the evidence required to show a breach of the duty; and (ii) the effect of a breach of honest performance on damages for wrongful dismissal.

In *Antunes*, the plaintiff had left his position as an independent contractor in the construction industry to accept employment with the defendant. The plaintiff claimed that the principal of the defendant company (the "Principal") induced him to join the defendant as a senior project manager. The plaintiff signed an employment agreement. The plaintiff alleged that he was induced to accept a position with the defendant on the basis of the Principal's representations, namely that he would early a salary of $150,000, with an increase to $200,000 after the first year of employment. The plaintiff further alleged that the Principal represented that he would be awarded 5% of the company's shares, with the potential of an additional maximum of 5% of the shares of the company's residential division within one of year of starting employment.

Critically, the plaintiff alleged that the Principal represented to him that the company was thriving, that it was worth $10 million, and that, accordingly, the plaintiff's 5% shares in the company would be worth $500,000.

Ultimately, the plaintiff was never issued the shares. Rather than acting as a senior project manager, he was preparing delay claims instead. The plaintiff also discovered that the defendant company was not in as good a financial situation as the Principal had represented prior to employment. Moreover, it turned out that there never existed a "residential division" of the defendant company. The plaintiff was terminated without notice on November 9, 2012. He therefore brought an action for wrongful dismissal, breach of contact, and negligent misrepresentation against the defendant company.

The Ontario Superior Court allowed the action. The plaintiff was awarded eight months' notice and an additional $500,000, based on the Principal's misrepresentation regarding the value of the defendant company's shares when the plaintiff was hired.

i. Evidence Required to Show A Party Acted Honestly

Applying *Bhasin*, the Court held that a party to a contract had to be able to rely on a minimum standard of honesty from the contracting partner in relation to performing the contract. In employment law, the employer further has a duty to act in good faith, with a sense of "fair dealing" with respect to its employees. The Court held that in this case, the defendant did not act in good faith, nor did the employer deal fairly with the plaintiff in offering him employment and in his termination.

In particular, the Court held that the defendant did not deal honestly with the plaintiff during the negotiation of the employment contract. The plaintiff relied on a series of misrepresentations made by the defendant regarding: (i) the financial state of the defendant company; (ii) the fact that the company was allegedly worth $10 million, when there was no evidence to support this fact; (iii) the value of the initial 5% shareholding in the company, which was never issued; and (iv) the existence of a "residential division" of the defendant company, which turned out never to have existed.

Critically, the defendant company failed to call anyone to testify on its behalf, including the Principal. The Principal was the person who had negotiated the employment contract and would have had direct knowledge of the negotiations and discussions leading up to the formation of the employment contract. He would have been a key material witness. Moreover, the defendant company failed to answer undertakings requested at examinations for discovery regarding the Principal's knowledge of the negotiations leading up to the employment contract. Further, there was no documentary evidence introduced by the defendant regarding negotiations. Accordingly, the Court drew an adverse inference against the defendant company regarding its failure to produce the Principal as a witness.

In these circumstances, the Court accepted the evidence of the Plaintiff. That is, it accepted that representations were made to the Plaintiff that were inaccurate and untrue and that the Plaintiff relied on them in accepting employment.

The Court in *Antunes* has therefore made it clear that where a defendant fails to provide key evidence to refute allegations that it behaved dishonestly in the performance of a contract, the Court will accept the evidence of the plaintiff. While this ruling is hardly surprising, it shows the importance of advancing evidence on behalf of a defendant who is the object of a claim of dishonest contractual performance.

ii. Breach of Duty of Honest Performance Factors Into Wrongful Dismissal Damages

The Court in *Antunes* held that the plaintiff was entitled to eight months' reasonable notice for wrongful dismissal. In arriving at this conclusion, the Court took into consideration that the Principal's misrepresentations about a residential division of the defendant company, and the plaintiff's right to shares thereof, amounted to a breach of honest contractual performance, contrary to the ruling in *Bhasin*:

> I have also considered the misrepresentation as regards the potential for receiving up to 5% of the Residential Division. In that regard, I have taken into account, as regards the breach of the duty to contract in good faith, that upon entry into the employment contract, the president of the defendant corporation made it appear that there was another division in existence of which the plaintiff had the opportunity to obtain an additional 5% of shares. Such a Division did not exist, nor is there evidence that it was ever contemplated. Simply put, the defendant corporation's conduct is contrary to the requirement to execute contractual obligations in good faith: *Bhasin v. Hrynew, supra.*

Moreover, in arriving at an eight-month notice period, the Court considered the plaintiff's short period of employment with the defendant, his senior position, his supervisory duties, his age and the availability of similar employment, "as well as the defendant's misrepresentations and the defendant corporation's failure to abide by the rules of contractual conduct as set out in *Bhasin v. Hrynew*".

Antunes makes it clear, therefore, that a breach of the duty of honest contractual performance may have a direct impact on the Court's analysis of the plaintiff's entitlement to reasonable notice in an action for wrongful dismissal.

Conclusion

The Court's decision in *Antunes* is an excellent example of how the principles set out in *Bhasin* will apply in the context of an employment relationship. First, the case makes it clear that the defendant employer bears a minimal evidentiary onus when faced with allegations that it acted dishonestly in the negotiation and performance of the employment contract. Second, the case shows that Courts will be more than willing to consider the defendant's breach of honest performance in calculating the reasonable notice period owed to an employee upon a wrongful dismissal. Above all, the decision in *Antunes* shows that the duty of honest contractual performance is a flexible doctrine, unencumbered by rigid legal tests and applied freely by the Courts to impose notions of fairness and good faith in contracts, including employment agreements.

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