



Contracting parties beware: Court of Appeal implies duty of good faith

BY [MEREDITH HAYWARD](#), AFFLECK GREENE ORR LLP.

The Ontario Court of Appeal has recently held that, in certain circumstances, contracting parties owe a duty of good faith to one another and, further, that an "entire agreement" clause will not preclude the implication of a duty of good faith as a term of a contract.

In *Civicliffe.com Inc. v. Canada (Attorney General)*,¹ Industry Canada contracted with Civicliffe.com Inc. ("Civicliffe") and SmartSources.com Technologies Inc. ("SmartSources") to develop a portal to make all information and services of federal government ministries and agencies accessible on-line, called "Access.ca". The primary contractor for the creation of the portal was the plaintiff, Civicliffe. SmartSources was to provide two specific components for the portal: a search engine and a context information manager. It was Civicliffe's responsibility to integrate the components supplied by SmartSources and deliver a completed portal for implementation of pilot projects at up to twenty sites across Canada.

The development of the portal did not proceed as planned. SmartSources and Civicliffe did not work together as envisaged by the contracts. Eventually, Civicliffe's portal was approved by the independent software technology company retained by Industry Canada to evaluate it, but it did not include the components to be supplied by SmartSources. SmartSources, instead of supplying the two components it has agreed to provide, developed its own stand-alone portal using its search engine and context information manager. The two portals were each independently tested at only two pilot locations. Civicliffe was not involved in any further expansion of the Access.ca project and ultimately went into receivership.

The trial judge found that Roger Casselman, the Industry Canada representative responsible for the deliverables from Civicliffe and SmartSources, deliberately encouraged SmartSources to provide its own portal. The email exchanges between Casselman and SmartSources "paint a picture of deceit and sabotage".² SmartSources' "decision not to co-operate in the integration was promoted and encouraged by Industry Canada. Further, Industry Canada encouraged SmartSources to supply its stand-alone portal in direct breach of the terms of the agreement".³

After examining the express terms of the contract to determine the intentions of the parties, Weiler J.A. found that the overall intention of the parties was that Industry Canada would facilitate co-operation between Civicliffe and SmartSources. Industry Canada was required to act fairly and to take reasonable steps to meet the contractual goals. This included working together in the development, supply and commercialization of Civicliffe's portal. The actions of Industry Canada, particularly in its dealings with SmartSources, undermined the reasonable expectations of the parties, and undermined the very objectives of the contract. The business efficacy of the contract was seriously affected.

In Canada, the doctrine of good faith has been found to arise in cases which can be categorized in three types: (a) those imposing a duty to co-operate in achieving the objectives of the agreement; (b) those imposing limits on the exercise of discretionary powers provided for in the contract; and (c) those precluding parties from acting to evade contractual duties, by engaging in conduct not strictly prohibited by the letter of the

terms of the agreement, but which has the effect of defeating rights under the agreement. Given the findings of the trial judge, Industry Canada's conduct fell within all three of the categories that courts have recognized as giving rise to the imposition of a duty of good faith.

Further, Weiler J.A. rejected the Crown's submission that the inclusion of an "entire agreement" clause in the agreements precluded the trial judge from holding that Industry Canada breached its contracts with Civicliffe because the contracts did not expressly include a duty of good faith or a duty to exercise discretion fairly. According to Weiler J.A., an entire agreement clause will not preclude the implication of a term in a contract because an implied term is already part of the existing contract. In addition, the "entire agreement" clauses in the contracts at issue did not expressly preclude terms being implied into the contract. Finally, if the conduct at issue in this case was covered by the entire agreement clause, the court had the discretion to refuse to enforce it where to do so would be unconscionable, unfair, unreasonable or otherwise contrary to public policy.

Civicliffe was awarded \$1 million in damages. The punitive damage award of the trial judge was

overturned on appeal because there was no evidence to suggest that Casselman's misconduct was the general culture at Industry Canada or that Industry Canada profited from Casselman's misconduct. However, Casselman is still employed by Industry Canada.

The Court of Appeal's decision signals that the Ontario courts have adopted a conservative approach to the imposition of a duty of good faith in contractual relationships. Given the egregious conduct of Industry Canada in this case, it is clear that the contracts were breached and the result did not depend on the implication of a duty of good faith into these contracts. That said, individuals and corporations alike need to keep this recent development in mind when carrying out their obligations under their contracts, and be aware that conduct contrary to the reasonable expectations of the parties will not be protected by an "entire agreement" clause.



For more information contact:

Meredith Hayward, Affleck Greene Orr LLP
Tel: 416-360-0121
Email: mhayward@agolaw.com

¹ 2006 CanLII 20837 (ON C.A.)

² *Ibid* at para. 19

³ *Ibid.*