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SILENCE DOESN'T ALWAYS EQUAL A BREACH OF GOOD FAITH

Our March 26, 2021 News ReLease titled “Expanding *Bhasin*: Acting Honestly Includes Correcting False Impressions” reviewed the Supreme Court of Canada (“SCC”) decision, *CM Callow Inc v Zollinger* (“**Callow**”). In *Callow*, the SCC held that if a party to a contract remains silent while aware that it has caused its counterparty to operate under a misapprehension, that party may be liable for breach of the duty of good faith. Since then, two court rulings have taken a nuanced approach to the *Callow* holding.

Subway Franchise Restaurants of Canada Ltd. v BMO Life Assurance Co.

The Tenant entered into a lease for a ten-year term, with two 5-year renewal options. To exercise the first renewal option, the Tenant was required to give notice not less than 9 months and not more than 12 months before the expiry of the initial term.

Unfortunately, the lease did not provide a specific commencement or expiry date. The commencement date depended on the expiry of the pre-term fixturing period, which in turn depended on when possession of the leased premises was delivered to the Tenant. Neither party officially confirmed with the other the actual commencement date of the term.

An estoppel certificate was provided to the Tenant in connection with the acquisition of the property by the successor landlord. The estoppel certificate was the only document that specified the commencement and expiry dates of the term. The Tenant signed it without realizing that the dates in fact differed from its understanding of the initial term pursuant to its internal records. Relying

on inaccurate dates, the Tenant exercised its option to renew beyond the actual deadline. The Landlord rejected the Tenant’s renewal.

Prior to exercising its renewal, the Tenant made several attempts to confirm the commencement date with the Landlord. The Landlord did not respond. The Tenant sought relief from forfeiture, claiming that the Landlord breached its duty of good faith by ignoring its inquiries. It relied on *Callow*, arguing that the duty of honest performance - which flows directly from the organizing principle of good faith - requires parties not to knowingly mislead each other.

The trial judge found no evidence that the Landlord knowingly misled the Tenant, concluding that “the onus is on the tenant seeking relief from forfeiture to ... make a diligent effort to comply with the lease’s terms”.

The Ontario Court of Appeal upheld the lower court’s decision, concluding that a breach of the duty of good faith requires active deception. It held that “in the absence of the defendant’s false representations, the failure to disclose a material fact, without more, would not be contrary to the standard [of acting in good faith].” It found no evidence that the Landlord knowingly misled the Tenant or actively contributed to the Tenant’s misapprehension.

ARC Digital Canada Corp. v Amacon Alaska Development Partnership

The parties entered into a lease and, in exchange for financial assistance from the Landlord to fund the

Tenant's move to new premises, subsequently negotiated an amendment of the lease to provide for an early termination date of the term.

The Landlord sent the Tenant an amending agreement (the "**Agreement**") that called for payment of compensation by the Landlord in two instalments. The Tenant delayed signing the Agreement, while it firmed up its lease for the new premises.

After executing the new lease, the Tenant signed and returned the Agreement to the Landlord. At that point, the Landlord was no longer willing to honour the terms of the Agreement because the Tenant had not actually vacated the premises by the early termination date set out in the Agreement.

On the early termination date, the Tenant began to incur obligations under both leases. Shortly thereafter, the Landlord changed course and decided to proceed with the Agreement. The Landlord remitted the first instalment of the agreed compensation, but claimed that the Tenant had forfeited the second installment when it failed to vacate the premises by the stipulated date.

The Tenant claimed that the Landlord breached its duty of good faith, since it was well aware that the Tenant would only have the necessary funds to relocate to the new premises once it received the first instalment from the Landlord. In response, the Landlord argued that the Tenant

breached its obligation to vacate the premises on the negotiated terms.

The British Columbia Supreme Court ("**BCSC**") considered *Callow* and found that the Landlord's silence misled the Tenant. Presuming that the Tenant would rely on the Agreement to its detriment, the Landlord remained silent as the Tenant entered into a new lease. Only after the new lease was executed did the Landlord acknowledge the Agreement and pay the first instalment.

The BCSC found that the Landlord took advantage of the situation to declare the Tenant in breach of the lease, which amounted to a breach of the Landlord's duty of good faith in its performance of the Agreement. The Tenant was awarded damages totalling \$369,260.00 including the second instalment due under the Agreement, as well as the rent that it paid under the original lease after the early termination date.

Lessons Learned

Although *Callow* expanded the scope of the duty of honest performance to include silence, it appears that silence in and of itself does not equal a breach of the duty of good faith. Courts will take a measured approach in applying *Callow*, especially where there is mere silence without an intention to knowingly mislead.

This publication is a general discussion of certain legal and related developments and should not be relied upon as legal advice. If you require legal advice, we would be pleased to discuss the issues in this publication with you, in the context of your particular circumstances.



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