From Bad Faith to Good Faith, Honestly

Since 2002, many insurers have treated the Supreme Court of Canada's decision in *Whiten v. Pilot Insurance Co.*[1] as a baseline of service. To boil down the fundamental premise of *Whiten* to a rule of thumb, it is fairly easy (and an oversight) to look at the headnotes of the decision which begin with, "The respondent insurer's conduct towards the appellant was exceptionally reprehensible." The not-so-gold standard of exceptional reprehensibility is often used as a simplification of the common law's definition of bad faith. That is a mistake. The *Whiten* decision is an analysis of punitive damages, but the finding of bad faith was a foregone conclusion in the Supreme Court of Canada decision. For an insurer, operating in good faith is much more than a small step past being exceptionally reprehensible.

Faith and Fairness

The duty of faith owed by an insurer to an insured is better explained in the subsequent Supreme Court of Canada decision of *Fidler v. Sun Life Assurance Co. of Canada*[2]. The decision cites a description of the duty from the Ontario Court of Appeal in *702535 Ontario Inc. v. Lloyd's London, Non-Marine Underwriters* (2000)[3]:

> The duty of good faith also requires an insurer to deal with its insured's claim fairly. The duty to act fairly applies both to the manner in which the insurer investigates and assesses the claim and to the decision whether or not to pay the claim. In making a decision whether to refuse payment of a claim from its insured, an insurer must assess the merits of the claim in a balanced and reasonable manner. It must not deny coverage or delay payment in order to take advantage of the insured's economic vulnerability or to gain bargaining leverage in negotiating a settlement. A decision by an insurer to refuse payment should be based on a reasonable interpretation of its obligations under the policy. This duty of fairness, however, does not require that an insurer necessarily be correct in making a decision to dispute its obligation to pay a claim. Mere denial of a claim that ultimately succeeds is not, in itself, an act of bad faith.

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[1] *Whiten v. Pilot Insurance Co.*, 2002 SCC 18.
[2] *Fidler v. Sun Life Assurance Co. of Canada*, 2006 SCC 30.
[3] *702535 Ontario Inc. v. Lloyd's London, Non-Marine Underwriters*, 2000 CanLII 5684 (ON CA), 184 D.L.R. (4th) 687, at para. 29.

This standard of fairness, therefore, is the threshold that insurers must meet. The challenge for insurers is that fairness is a general notion that can be subjective and circumstantial, and possibly subjected to the sadly logical t-shirt I once saw at a mall kiosk: "I don't discriminate, I hate everyone equally". If the t-shirt's sentiment was applied in the context of an insurance claim, it could be deemed fair and exceptionally reprehensible at the same time.

The Import of Honesty

A recent decision of the Supreme Court of Canada has further specified the duty of good faith and what it demands of parties to any contract, including a contract of insurance. The Supreme Court of Canada's 2014 judgment in *Bhasin v. Hrynew*[4] is a decision about good faith in the context of a commercial contract. Writing for the Court, Mr. Justice Cromwell recognizes that the current state of the Canadian common law surrounding the doctrine of good faith is "uncertain", and "lacks coherence"[5]. As such, Cromwell J. proposes an incremental approach toward clarifying the law surrounding the doctrine of good faith, which includes the adoption of a new duty applicable to contract law in general: the duty of honesty.

As Mr. Justice Cromwell explains, Canadian courts have found that certain classes of contractual relationships require a duty of good faith to be implied by law. Such relationships include:

- employment agreements particularly in the context of termination of employment;
- insurance (see *Fidler & Whiten*, above, and note that a reciprocal duty exists whereby an insured has a duty to act in good faith by disclosing facts material to the insurance policy); and
- tendering agreements.[6]

Mr. Justice Cromwell describes the "organizing principle" of good faith as the general notion that a contracting party should have "appropriate regard to the legitimate contractual interests of the contracting partner". The standard is specified at paragraph 63 of the *Bhasin* decision: "parties generally must perform their contractual duties honestly and reasonably and

[4] *Bhasin v. Hrynew*, 2014 SCC 71.
[5] *Bhasin*, supra, at para. 41.
[6] *Bhasin*, supra, at paras. 53-56.

not capriciously or arbitrarily." However, good faith does not require that a party serve the interests of the contracting party. It is enough that a party should not seek to undermine those interests in bad faith.[7]

Within this "organizing principle" of good faith, Mr. Justice Cromwell specifies the duty of honesty owed by contracting parties that is applicable to all parties engaged in the spectrum of contract law. In other words, parties to any contract are now legally required to deal honestly with one another.

This newly recognized duty will undoubtedly have important implications for the world of Canadian contract law, particularly because *Bhasin* stands for the principle that a party can be sued for breach of contract where it is found that they have actively misled or deceived another party in their performance of a contract. Furthermore, this new duty is not something that parties are free to contract out of.

Extra-Honest Insurance

For insurers, the *Bhasin* decision may not have created any greater duties than what already existed. In the claims context, insurers and claims adjusters already had a contractual obligation to act in good faith. *Bhasin* has given more structure to the concept of fairness. Now, the good faith obligation includes the reasonableness and balance described in the *Fidler* case, and the explicit duty of honesty explained in *Bhasin*, further specified by the requirement that an insurer is not to be capricious or arbitrary.

Honesty is a concept subject to interpretation. Is it dishonest to "plead the fifth" and not answer a question? At paragraph 86 of *Bhasin*, Mr. Justice Cromwell refers to the duty of disclosure that an insurer has to the insured, citing *Whiten* for the proposition that an insurer must disclose material facts. The insurance context is used as a contrast to general commercial agreements. Paragraph 86 of *Bhasin* is a clarification that the duty of honesty is not a duty of disclosure, but insurance contracts are an exception. Insurers continue to have a higher standard of honesty than parties to a commercial contract. Paragraph 86 ends with Mr. Justice Cromwell distinguishing between a failure to disclose and "active dishonesty". It appears as though a party

[7] *Bhasin*, supra, at para. 65.

to a commercial contract can “plead the fifth” and not respond to a query so long as they do not have a contractual duty to disclose information. Insurers, on the other hand, must comply with disclosure obligations that are legislated and usually specified in policies.

The Implications

The duty of an insurer to operate in good faith has not increased, but has become more specific. For insurers, the implication of the *Bhasin* decision is most likely to manifest itself in examinations for discovery on a coverage case. Now, a claimant’s counsel can plead bad faith and specify dishonesty. On discovery, claimant’s counsel can point to claims handling correspondence and press an insurer about whether their communications represented the truth, the whole truth and nothing but the truth. The vagaries of disclosure of the whole truth will certainly become fodder for allegations of dishonesty. It is quite easy, particularly when snapping off emails from a mobile device, to skirt around bad news or give partial answers. This may not be active dishonesty, but it appears as though an insurer’s duty of honesty incorporates “the whole truth” in claims correspondence.

Although the duty of good faith has not increased, the *Bhasin* case heightens the responsibility and care that insurers need to take in all correspondence with claimants. The *Bhasin* decision and the expanding duty of honesty is a good reminder that all claims handlers should pay attention to omissions in their correspondence that may be construed as deceptive.