

Reasonable, or Unreasonable? That is the Question – Using Discretion in Construction Projects Should be Reasonable

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On February 5, 2021, the Supreme Court of Canada (“**SCC**”) released its decision in *Wastech Services Ltd. v Greater Vancouver Sewerage and Drainage District*^[1] (“**Wastech**”). This decision will impact all contract-bound members of the construction industry. The SCC analyzed contracts which allow for “discretion”, and the limits on how that discretion is exercised. *Wastech* was heard alongside *C.M. Callow Inc. v. Tammy Zollinger, et al.*^[2] in December 2019.

See our earlier post on *C.M. Callow* [here](#), which analyzes the duty of honest performance that parties to a contract have and works through the effects of the duty, including the duty that parties must not lie or otherwise knowingly mislead each other about matters directly linked to the performance of the contract.

What You Need to Know

- There is a duty to exercise contractual discretion in good faith;
- The duty imposes a modest requirement that parties exercise their contractual discretion reasonably, in a manner consistent with the purpose for which it was created;
- Whether a party has satisfied this duty in a particular instance is case-specific and depends on the context and wording of the contract as a whole;
- Parties may include provisions in the contract that help identify the purposes for which the discretion is granted;
- Exercising discretionary powers in a manner that is unconnected to the purposes of the contract may constitute a breach of the duty of good faith; and
- The duty does not require a contracting party to subordinate its interests to those of the other party.

What Happened in *Wastech*

The Greater Vancouver Sewerage and Drainage District (“**Metro**”) and Wastech Services Ltd. (“**Wastech**”) entered into a long-term contract for the transportation and removal of waste to three disposal sites. The parties had a long-standing contractual relationship.

The contract gave Metro “absolute discretion” to allocate waste between the sites and provided that Wastech would be paid differing rates depending on which disposal facility the waste was directed to.

In 2011, Metro reallocated waste from a disposal facility further away to one that was closer, which resulted in Wastech’s not achieving a cost/revenue target identified in the contract.

Wastech claimed that Metro breached the contract by allocating waste in a manner that deprived Wastech of the possibility of achieving the target, contrary to Metro's duty of good faith.

The SCC held that this reallocation did not constitute a breach of its good faith duties, and in particular the duty to exercise discretion in good faith, because it was consistent with the purposes for which the discretion was created (operating efficiently and managing costs well). The contract did not guarantee that Wastech would achieve the target.

The fact that Metro's exercise of discretion caused Wastech to lose an anticipated benefit was not sufficient to conclude that Metro's discretion was not exercised in good faith.

The SCC clarified that unreasonableness means to exercise a power outside and unconnected to the purposes for which the discretion is granted under the contract. The SCC indicated that this will occur, for example, where the exercise of discretion is arbitrary or capricious.

The SCC clarified that while the intentions of the parties are not relevant to whether the duty applies, they are critical to whether a party's exercise of contractual discretion was actually unreasonable.

Practical Implications on the Construction Industry

To avoid potential litigation, parties to a construction contract should:

- Consider whether the contract provides for any sort of discretionary decision-making powers.
- Consider whether the action is permissible under the terms of the agreement.
- Even if permitted by the contract, determine whether the action is not in good faith, as per the test in *Wastech* – which considers whether the action is within the purpose for which the discretion is granted under the contract and considers the intentions of the parties in light of the overall contract.
- Take preventative measures and clearly identify the reasons a discretionary power is included in the contract.

Owners, contractors, consultants, suppliers, and various other contract-bound members of a construction project will be impacted by the decision in *Wastech*. These members should be aware that inserting discretionary clauses in the contract without indicating the purpose for which the discretion should be used for may result in an unintended variety of actions that might be approved as "reasonable" under the clause. On the other hand, using one's discretion under the clause may be deemed unreasonable if the purpose of the clause is for a specific purpose and the actions run outside the limits of the clause.

The following examples pertaining to a construction project may be impacted by the decision in *Wastech*:

1. If a contract allows for an owner to have discretion to make decisions (such as the approval of work), the owner may have to use their discretion in a manner consistent with the purpose of the clause and have a bona fide reason to reject work, even if it appears that they have wide latitude to accept or reject. If the contract, read as a whole, defines the work expected and the purpose for which work can be rejected, the owner's decision may have to be in line with that purpose.
2. If the contract between a contractor and subcontractor states that the contractor may, in its absolute, sole and unfettered discretion, at any time from time to time extend the date of the project's completion in order to ensure high quality, the contractor may have broad discretion to extend the completion date to meet the goal of ensuring high-quality work on the project (as long as their actions are deemed reasonable and comply with the duty of good faith). Note that, however, even if contractor exercises this discretion, the parties would still be subject to any other clauses relating to compensation for extensions of contract time – the contractor would just not be in breach for the extension.
3. If a supplier asks for compensation on materials supplied that were more expensive than the contractor or subcontractor

expected, and the discretion clause stated that they must supply materials that are high quality and meet the project's demands, then the supplier may not be penalized in using their discretion if they can show that the decision was reasonable and meets the goal stated for the discretion clause.

4. If a clause in the contract allows the subcontractor to use their discretion to design and implement project specifications to meet the project's needs, then it may be irrelevant if the contractor expected different specifications, as long as the subcontractor's discretion was executed reasonably and compiles with the contract and its objective (to meet the project's needs).

For any questions or concerns regarding how the duty of good faith may impact your ongoing and new construction projects, and for a review of your construction contracts to determine where the duty may apply please contact [Faren Bogach](#) or [Paul Conrod](#).

[\[1\]](#) 2021 SCC 7.

[\[2\]](#) 2020 SCC 45.

The information and comments herein are for the general information of the reader and are not intended as advice or opinion to be relied upon in relation to any particular circumstances. For particular application of the law to specific situations, the reader should seek professional advice.

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