CLARK WILSON LLP

TOP CASES IN P&C INSURANCE

PRESENTED AT THE PROEDGE SEMINAR

UBC Robson Square, C680 – HSBC Classroom,
800 Robson Street, Vancouver, BC, V6Z 3B7

JUNE 12, 2017 (1:00 pm – 4:15 pm PST)

PRESENTED BY MEMBERS OF THE
INSURANCE PRACTICE GROUP
CLARK WILSON LLP

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FAULTY WORKMANSHIP EXCLUSION

Ledcor Construction Ltd. v. Northbridge Indemnity Insurance Co., 2016 SCC 37

PRESENTED BY **SATINDER SIDHU**

Faulty Workmanship

Summary

- Coverage dispute over whether the faulty workmanship exclusion in a builders risk policy (the "Exclusion") excludes only the cost of redoing the faulty work or whether it also excludes repairing or replacing that part of the project on which the contractor performed the faulty work.
- SCC found that only the cost of redoing the faulty work is excluded but the hefty cost of replacing the damaged property is covered.

Faulty Workmanship

Facts

- Station Lands Ltd. ("Station Lands") retained Ledcor Construction Ltd. ("Ledcor") as construction manager for the construction of the EPCOR Tower in Edmonton.
- Station Lands obtained an "All Risks" policy (the "Policy") from Northbridge Indemnity Insurance Company and other insurers (the "Insurers") for the project.
- Ledcor and all other contractors involved in the project were additional insureds.

Faulty Workmanship

Facts cont'd

- The Exclusion in issue read as follows:

  This policy section does not insure:

  …

  b. The cost of making good faulty workmanship, construction materials or design unless physical damage not otherwise excluded by this policy results, in which event this policy shall insure such resulting damage.

Faulty Workmanship

Facts cont'd

- A trade contractor named Bristol Cleaning ("Bristol") was retained by Station Lands to do a "construction clean" of the building's exterior at a cost of about $45,000.
- In carrying out its work, Bristol caused damage to the windows.
- The glass had to be replaced at a cost of about $2.5 million.
- Station Lands and Ledcor claimed the replacement costs under the Policy.
- The Insurers claimed the Exclusion applied to the replacement cost of the windows and a coverage action ensued.

Faulty Workmanship

The Trial Decision

- At trial, Ledcor and Station Lands argued that the Exclusion only removed coverage for the cost of having to re-do the cleaning with proper methods and tools.
- The damage to the windows was “physical damage not otherwise excluded” and therefore covered.
- The Insurers argued that “work” and “workmanship” did not just apply to the labour of the task but also the materials being worked on.

Faulty Workmanship

The Trial Decision cont'd

- The trial judge concluded that both interpretations were plausible and that prior case law on the subject was inconclusive and inconsistent.
- Having found the Policy to be ambiguous, the judge applied the doctrine of *contra proferentum* to reach the conclusion that the damage to the windows was covered.
- The Insurers appealed.

Faulty Workmanship

The Appellate Decision

- The appellate court reasoned that because the initial grant of coverage extends to “physical loss or damage”, the Exclusion must exclude from coverage some *physical damage*.
- The appellate court then focused on what *physical damage* is excluded as the “cost of making good faulty workmanship” and what *physical damage* was covered as “resulting damage”.

Faulty Workmanship

The Appellate Decision cont'd

- To establish a dividing line, the court devised the physical or systemic connectedness test:
  1. the extent or degree to which the damage was to a portion of the project actually being worked on at the time, or was collateral damage to other areas;
  2. the extent to which the damage was a natural or foreseeable consequence of the work itself; and
  3. whether the damage was within the purview of normal risks of poor workmanship, or whether it was unexpected and fortuitous.

Faulty Workmanship

The Appellate Decision cont'd

- The court concluded that the damage to the windows and the cost of their replacement was excluded from coverage, as the damage was physically or systematically connected to the very work the contractor had performed.
- The damage was caused directly by the scraping and wiping motions involved in cleaning the windows.
- The contractor intentionally applied these motions to the windows, therefore the damage was not accidental or fortuitous.
- Replacing the windows would be "making good the faulty workmanship" and these costs were excluded.

Faulty Workmanship

The SCC Decision

- The Exclusion need not encompass physical damage.
- Although exclusions should be read in light of the initial grant of coverage, perfect mutual exclusivity between the Exclusion and the initial grant of coverage is not required.
- The policy contains other exclusions that do not pertain to "physical loss or damage" (e.g., exclusions stemming from contractual breach and government imposed penalties).
- The "physical or systemic connectedness test" was unnecessary and built on a flawed premise.

Faulty Workmanship

The SCC Decision cont'd

- The general rules of contractual interpretation will answer whether the damaged windows are covered.
- The Exclusion is ambiguous as the word "damage" figures only in the exception to the exclusion leaving it open to interpret that "making good faulty workmanship" means to redo the faulty work only.
- To resolve the ambiguity, the SCC considered the reasonable expectations of the parties as to the meaning of the Exclusion.

Faulty Workmanship

The SCC Decision cont'd

- The purpose of the builders' risk policy is to provide broad coverage for construction projects – which by their nature are susceptible to accidents and errors.
- There is a high possibility of damage by one tradesman to the property of another and to the construction as a whole.
- Allocating risk in the builders' risk policy can allow the projects to proceed without the risk of litigation about liability for damage among the contractors.

Faulty Workmanship

The SCC Decision cont'd

- The expectation of broad coverage is furthered by a narrow interpretation of the Exclusion that only excludes coverage for the cost of redoing the faulty work/recleaning the windows.
- The SCC also considered the need to avoid interpretations that would bring about a commercially unrealistic result.
- Recovery for damage to the windows in the circumstances of this case must have been anticipated when the policy was purchased.

Faulty Workmanship

The SCC Decision cont'd

- Interpreting the Exclusion to only preclude the cost of redoing the faulty work aligns with commercial reality and leads to a sensible result.
- The court found that this interpretation does not transform the policy into a construction warranty and encourage contractors to perform their work improperly or negligently.
- Contractors would still want to guard against faulty work to ensure they are paid.

Plenert V. Melnik Estate, 2016 BCSC 403

PRESENTED BY **DAVID BUXTON-FORMAN**

Litigation Privilege

Facts

- Action arises from a MVA that occurred on Highway 1
- The MVA was serious, involving multiple vehicles and one fatality – 5 related actions
- The road maintenance contractor, Emil Anderson Maintenance Co. Ltd., was a third party to the action
- At the time of the MVA, Emil was insured by Continental Casualty Company (the Province was an additional insured)
- Continental was notified of the MVA by the Province, and the notice enclosed an article about the accident and a note that the independent adjuster for another party had asked for the maintenance schedule for the highway

Litigation Privilege

Facts

- Continental, as well as its independent adjuster, carried out an investigation of the MVA and produced a series of reports
- Emil claimed litigation privilege over the reports
- The Defendants brought an application seeking production of the reports

Key Issue

- Was Emil entitled to claim litigation privilege over the reports?

Litigation Privilege

The Test

… a document which was produced or brought into existence either with the dominant purpose of its author, or of the person or authority under whose direction, whether particular or general, it was produced or brought into existence, of using it or its contents in order to obtain legal advice or to conduct or aid in the conduct of litigation, at the time of its production in reasonable prospect, should be privileged and excluded from inspection.

- *Hamalainen (Committee of) v. Sippola* (1992), 1991 62 B.C.L.R. (2d) 254

Litigation Privilege

The Test

- The analysis requires consideration of the following questions:
  - Was litigation in reasonable prospect at the time the document was produced, and
  - If so, what was the dominant purpose for its production?

The Test

- The threshold for determining whether litigation is "in reasonable prospect" is a low one.

> … litigation can properly be said to be in reasonable prospect when a reasonable person, possessed of all pertinent information including that peculiar to one party or the other, would conclude it is unlikely that the claim for loss will be resolved without it.
>
> *- Hamalainen*

The Test

- A claim of privilege will succeed when a party can establish that a document produced for multiple purposes, one of them being litigation, was produced for the dominant purpose of litigation
- A finding of dominant purpose involves an individualized inquiry as to whether, and if so when, the focus of the investigation/inquiry shifted to litigation
- At some point in the information gathering process the focus of the inquiry will shift such that its dominant purpose will become that of preparing the party for anticipated litigation

The Arguments

- Reasonable Prospect of Litigation
  - Emil argued that there was a reasonable prospect of litigation from the first notice to Continental that the MVA was serious and another independent adjuster had asked questions about the maintenance of the highway
  - Relied on *Panetta v. Retrocom Mid-Market Real Estate Investment Trust*, 2013 ONSC 2386:

    …there is no purpose for the creation of documents by an insurer in a tort context other than: (1) for anticipated litigation; (2) for setting reserves; or (3) for seeking legal advice. For completeness, I would add, as a corollary to (1): for the purpose of settlement, which I see as inextricably entwined with "anticipated litigation

The Arguments

- Reasonable Prospect of Litigation
  - The Defendants argued that litigation was not a reasonable prospect at that time, as Continental did not know who was involved in the MVA and there was no information as to the condition of the roads or Emil's involvement
  - Pointed to a statement from the Province in the notice to Continental that it was reporting the claim "out of an over-abundance of caution"

The Arguments

- Dominant Purpose
  - Emil argued that Continental was purely a third party insurer involved for the sole purpose of litigation and the potential payment of a third party loss
  - Emil argued that anytime Continental starts an investigation, litigation is the only purpose and the only reason documents are created

The Arguments

- Dominant Purpose
  - The Defendants argued that one of the purposes of the investigation and the documents produced during the investigation must have been to investigate the facts of the accident
  - They argued that until those facts were determined, it could not be said that litigation was the dominant purpose for the inquiry

The Decision

- Reasonable Prospect of Litigation?
  - Yes

“… given the type and severity of the accident and the fact that another adjuster was making inquiries about road maintenance, I am satisfied that litigation involving Emil Anderson was in reasonable prospect at the time the claim was reported to Continental”

Litigation Privilege

The Decision

- Dominant Purpose of Litigation?
  - Yes

> "There is no evidence that they were created for multiple purposes. The evidence is that the only reason for the investigation was to defend against potential litigation, which I have found was reasonably in contemplation. That evidence is supported by the limited role of the liability insurer in this matter, which was to defend and indemnify Emil Anderson and the Province."

The Implications

- It may be easier for insurers to claim privilege over adjusters reports in the context of defending tort claims
- Our courts appear more willing to find that the majority of the investigations carried out by liability insurers are privileged
  - Carve out for ICBC and other “universal” insurers
- Case represents a departure from the recent trend of decisions promoting increased transparency and disclosure

MISREPRESENTATION AND OMISSION

Bahniwal v. The Mutual Fire Insurance Company of British Columbia, 2016 BCSC 422

PRESENTED BY **REID BROOKS**

Misrepresentation & Omission

Summary

- The insurer wrongfully denied coverage under a fire insurance policy.
- The insurer took the position that the insurance policy was void because of the insured's failure to disclose the existence of a marijuana grow-operation – both a misrepresentation and material change.
- The Court found that the insurer had not established that the insured knew of the grow operation. However, the Court restricted the insured's recovery to actual cash value, as opposed to the replacement value.

Misrepresentation & Omission

Facts

- The plaintiff, the insured, and her husband owned a: 1) a residence (the "House"); and 2) storage facility with an attached living suite (the "Facility").
- The insured did not live in the House or the Facility.
- The insured rented the House and the Facility to a tenant, Mr. Nickson.
- On August 16, 2010, a fire broke out in the Facility. The fire completely destroyed the Facility and its contents.
- At the time of the fire, the Facility was insured against fire under an insurance policy with The Mutual Fire Insurance Company of British Columbia (the "Policy").

Misrepresentation & Omission

Facts cont'd

- The cause of the fire was never determined.
- Following the fire, the insured sought recovery under the Policy on a replacement cost basis.
- On November 15, 2010 the insurer elected to void the Policy pursuant to breaches of statutory conditions 1 (misrepresentation) and 4 (material change).

Misrepresentation & Omission

Facts cont'd

- Misrepresentation

  1. If any person applying for insurance falsely describes the property to the prejudice of the insurer, or misrepresents or fraudulently omits to communicate any circumstance which is material to be made known to the insurer in order to enable it to judge of the risk to be undertaken, the contract is void as to any property in relation to which the misrepresentation or omission is material.

Misrepresentation & Omission

Facts cont'd

- Material Change

  4. Any change material to the risk and within the control and knowledge of the insured avoids the contract as to the part affected by the change, unless the change is promptly notified in writing to the insurer or its local agent.

- The basis for the insurer's decision to treat the Policy as void was that there was evidence that, at some point before the fire, a marijuana grow operation had been undertaken in the Facility without the insurer's knowledge or approval.

Misrepresentation & Omission

Facts cont'd

- The insurer treated this as a misrepresentation or material change, or both, contrary to statutory conditions 1 and 4.
- The insurer took the position that if they had known of the grow operation, they would not have renewed the Policy in March 2010 (4 months before the fire).
- The critical issue before the Court was whether the insured was aware of the grow operation in the Facility.
- The insurer argued that the insured, and her husband, "must have seen" the grow operation.

Misrepresentation & Omission

Decision

- Mr. Justice Joyce held that the insured did not have knowledge of the grow operation on the Facility, based on the following findings of fact he made at trial:
  - The insured, and her husband, were credible when they testified that they never smelled marijuana on the property and never saw anything out of the ordinary, despite attending the Facility and going inside on two occasions;
  - It was accepted that the hydro bill was passed off to the tenant without looking at it closely as the tenant was responsible for payment and always paid on time; and

Misrepresentation & Omission

Decision cont'd

- – Despite being paid in cash by the tenant, the insured's husband offered a reasonable explanation for why he did not question this arrangement – because it benefited him to have cash to pay seasonal workers.

- Accordingly, the insured was entitled to indemnity under the Policy (more to come on this).
- The insured sought punitive damages against the insurer on the basis that the insurer jumped to a conclusion that suited it and denied coverage on a mere suspicion.

Misrepresentation & Omission

<u>**Decision cont'd**</u>

- Mr. Justice Joyce dismissed the insured's claim for punitive damages on the following basis:

  > "While the defendant ultimately has been unsuccessful in its denial of liability on the grounds of misrepresentation, I do not believe that it acted with undue haste or in bad faith in taking the position that it took and in dealing with this claim. While ultimately unsuccessful at trial, the defendant had a reasonable basis for taking the actions it did and did not act on a <u>mere</u> suspicion." (para. 87)

Misrepresentation & Omission

Decision cont'd

- In support of his decision to dismiss the claim for punitive damages, Mr. Justice Joyce relied on the following facts:
  - One day after the fire, the insurer executed an Investigation Authorization form;
  - The insurer retained an insurance adjuster;
  - The adjuster retained Fire Pro Investigations to investigate the cause and origin;
  - The adjuster promptly obtained statements from the insured, her husband, the tenant, firefighters, as well as hydro records; and

Misrepresentation & Omission

Decision cont'd

- Fire Pro Investigations provided a report to the adjuster indicating that they believed there had been a marijuana grow operation in the Facility.

- In short, Mr. Justice Joyce found that the insurer had complied with its duty to investigate the claim fairly and diligently.

Misrepresentation & Omission

Impact

- Statutory conditions 1 and 4 codify the common law rule that whether or not a misrepresentation or non-disclosure is "material" is always a question of fact.
- Whether or not a fact is material is to be assessed objectively from the point of view of a reasonable insurer (not a reasonable person).
- The Courts will not lay down general rules with respect to what types of facts are material. However, it is accepted that the insured must disclose the "special facts" which would influence the insurer's ability to understand and estimate the risk.

Misrepresentation & Omission

Impact cont'd

- The onus of proving a breach of statutory conditions 1 or 4 is on the insurer. In order to satisfy this onus, the insurer must establish that:
  - there has been a misrepresentation or an instance of non-disclosure (omission);
  - the misrepresentation or non-disclosure (omission) was material; and
  - the insurer was induced to enter into the contract in reliance upon the misrepresentation or non-disclosure (omission).

Misrepresentation & Omission

Impact cont'd

- In addition, the test for whether a fact is material or not is whether the fact would have influenced a "reasonable insurer" to decline the risk or to charge a higher premium. The test places the burden of proof on the insurer to show that its own practice in considering that a misrepresentation is material to the risk is in line with the practice of a number of other insurers. Thus, an insurer should lead evidence to demonstrate that the fact in question is taken into account in the course of its own underwriting procedures as well as the underwriting procedures of other insurers (this adds a subjective consideration to the analysis).

Misrepresentation & Omission

Impact cont'd

- In this action, the Vice President of Underwriting for the insurer testified that had the insurer been aware of the presence of a marijuana grow operation, they would have declined to extend coverage or, if its existence came to their knowledge after the Policy had been extended, the insurer would have voided the Policy.

Misrepresentation & Omission

Impact cont'd

- The impact of this decision is that, if a homeowner's property is being used for an activity that could jeopardize their insurance coverage, as long as the homeowner can prove they were unaware of that activity, it protects the homeowner from loss. Owners of rental properties must merely show that they exercised "reasonable" care in monitoring the activities on their property. As a result, insurers may wish to undertake a more rigorous assessment of the practices of owners of rental properties to determine whether they have met the reasonableness test.

Replacement Cost vs. ACV

- Mr. Justice Joyce confirmed that insurers who issue replacement cost endorsements are not required to fund replacement of damaged property in advance.
- The Policy contained a Replacement Cost Extension that provided replacement cost indemnity subject to, in part, the following condition: “replacement shall be effected by the Insured with due diligence and dispatch”.

Replacement Cost vs. ACV

- The insurer took the position that the insured was restricted to recovery only of the ACV of the buildings and contents because the insured had not yet caused replacement (approximately 5 years after the fire), and, in doing so, breached the above condition.
- The insured argued that it did not have the money to cause replacement. However, the evidence established that the insured had the financial means to rebuild and replace that which was lost in the fire (she had the ability to borrow the necessary money against other real estate) but made the decision to await the result of the lawsuit before doing so.

Replacement Cost vs. ACV

- Mr. Justice Joyce found there was no obligation on the insurer to fund the replacement.
- Accordingly, Mr. Justice Joyce found that the insured had failed to meet the condition of rebuilding with due diligence and dispatch and was not entitled to indemnity on a replacement value basis for her loss.

Gill v. Ivanhoe Cambridge, 2016 BCSC 252

PRESENTED BY **RAMAN JOHAL**

Coverage for Negligent Parenting

Facts

- 2 year old boy falls through a missing glass partition in a shopping mall and suffers serious injury
- Litigation guardian (dad) names multiple defendants in civil claim
- Defendants name plaintiff's father as 3rd party for negligent supervision
- Economical Insurance denies coverage to the father on basis of family exclusion clause

Coverage for Negligent Parenting

Issue

- Exclusion – "There is no coverage in this Section for claims arising from …Bodily injury to the Insured or to any person residing in the Insured's household other than a Residence Employee
- Can a 3rd party claim for negligent parenting be interpreted to be a claim "arising from" bodily injury to the Insured's son?

Coverage for Negligent Parenting

Law

- Interpretation of an Insurance Agreement
  - When the language is clear and unambiguous, court should give effect to the clear language
  - When there is ambiguity, resolve based on reasonable expectations of the parties
  - Determined objectively while viewing the agreement as a whole

Coverage for Negligent Parenting

Analysis

- Ambiguous whether "arising from" applies to indirect claims
- Elsewhere in the policy, "arising from" was qualified with language making it clear that indirect claims were included
- Purpose of family exclusion clause to prevent collusion
- Action clearly not collusive between family members
- Resolve ambiguity in favour of the Insured for these reasons

PUNITIVE DAMAGES

Arsenovski v. Bodin,
2016 BCSC 359
2016 BCSC 649
2016 BCCA 178

PRESENTED BY **RAMAN JOHAL**

Punitive Damages

Facts

- Pedestrian couple from former Yugoslavia – Mr. hit by car and Mrs. fell and suffered bruises
- Mrs. made claim to ICBC with friend as translator
- Written statement drafted by adjuster signed by Mrs.
- Adjuster referred couple to Bodily Injury Claims Investigation Team and Special Investigations Unit at ICBC
- SIU Officer drafted a report to crown counsel (“RTCC”) recommending Plaintiff be charged with fraud (*Criminal Code*) and making a false statement (*Insurance (Motor Vehicle) Act* (BC)) (“IMVA”)

Punitive Damages

Facts cont'd

- Mrs. charged with making a false statement under IMVA
- On the first day of trial – Crown stayed the charge
- Mrs. sued ICBC for malicious prosecution
- Many inaccuracies included in the RTCC
- ICBC relied on hospital records that Mrs. had not signed and for which there was no evidence she had the benefit of a translator
- ICBC did not make inquiries about hospital records

Punitive Damages

Decision

- ICBC did not have a subjective belief that Mrs. guilty of making a false statement and basis for recommending criminal charges not properly founded
- Re: malice – Defendant "framed and misstated the evidence in the RTCC narrative to confirm his belief that …Mrs…going to try defraud and advance false civil claims… no effort to neutrally and objectively state the facts…motives and conduct…such a perversion of the office of an ICBC SIU officer that the element of malice in the tort of malicious prosecution has been proven."

Punitive Damages

Decision cont'd

- *Whiten v Pilot Insurance Co,* 2002 SCC 18 – punitive damages are meant to punish the defendant rather than compensate a plaintiff.
- Proportionality (6):
  - Proportionate to the blameworthiness of the defendant's conduct;
  - Proportionate to the degree of vulnerability of the plaintiff;.
  - Proportionate to the harm or potential harm directed specifically at the plaintiff;

Punitive Damages

Decision cont'd

- Proportionality (6) cont'd:
  - Proportionate to the need for deterrence;
  - Proportionate, even after taking into account the other penalties, both civil and criminal, which have been or are likely to be inflicted on the defendant for the same misconduct; and
  - Proportionate to the advantage wrongfully gained by a defendant from the misconduct.

Punitive Damages

Decision cont'd

- Conduct was "so high-handed, reprehensible and malicious that it offends this Court's sense of decency and is deserving of the punishment of punitive damages"
- Award needed to be sufficiently large that it would not be treated "as a cost of doing business" but "it is very difficult to find and compare cases"
- Significance of false accusations of dishonesty on an individual's reputation – even where not a public figure or not a professional
- Court ordered $350,000 in punitive damages against ICBC

SPECIAL COSTS

Williams v. Canales, 2016 BCSC 1811

PRESENTED BY **RAMAN JOHAL**

Special Costs

Facts

- Personal injury claim by Williams against her personal trainer Canales and others (the "Insureds")
- Intact denied coverage and declined to defend Insureds based on an exclusion clause in the policy
- Insureds brought third party proceedings against Intact seeking declaration it is obligated to defend Insureds and seeking reimbursement for defence costs incurred to date
- Insureds also brought third party proceedings against the broker because of the denial of coverage from Intact

Special Costs

- Insureds successful after summary trial in third party proceedings against Intact
- Insureds sought special costs against Intact and Broker sought a Sanderson Order against Intact
- Special costs (or solicitor-and-client costs) significantly higher than tariff costs and more closely approximate actual legal fees charged by a lawyer
- Special costs awarded when opposing party engaged in outrageous, scandalous or reprehensible conduct deserving of rebuke from the Court

Special Costs

Decision

- Held that Intact required to pay special costs to Insureds despite no finding of reprehensible conduct on the part of the Intact:

> [22] Entitlement to solicitor-and-client costs in the third party proceeding flows directly from the unique nature of the insurance contract which entails a duty to defend at no expense to the insured. The obligation to save harmless the insured from the costs of defending the action is sufficiently broad to encompass the third party proceedings. It is the contractual basis for the claim to solicitor-and-client costs that justifies the award and therefore constitutes an exception to the usual rule that solicitor-and-client costs will not be awarded except in unusual circumstances.

Austerville Properties Ltd. v. Nandha Enterprises Ltd. et al,
2016 BCSC 1963

PRESENTED BY **SAMANTHA IP** and **SEAN TESSAROLO**

Tort Immunity, Insurance Covenants & Corporate Attribution

The Main Parties

- Landlord → Austeville Properties Ltd.
- Insured corporate tenant → Nandha Enterprises Ltd. [Represented by Clark Wilson LLP]
- Principals of corporate tenant → Manjeet (wife) and Harjit Nandha (husband)
- Arsonist → Kamaljeet Josan, a "family friend" of Manjeet

Extraordinary Facts

- In 2004, corporate tenant leased property at 680 West Broadway in Vancouver, B.C. from the landlord to operate a Taco Del Mar
- Corporate tenant operated two Taco Del Mar franchises (one on Broadway and one in Delta)
- The wife had primary responsibility for the day-to-day operations of NEL's two restaurants

Tort Immunity, Insurance Covenants & Corporate Attribution

The Fire & Explosion

- 2:30 am on February 13, 2008, a fire and explosion occurred at Broadway Taco Del Mar
- Extensive damage to landlord's building and other units adjacent and across the street, resulting in about $3.5 million being paid to landlord by its property insurer (property damage and business interruption loss)

The Aftermath

- View of the Taco Del Mar after the explosion

The Aftermath cont'd

- View of debris on West Broadway after the explosion

Extraordinary Facts cont'd

- Police investigation commences
- Fire is considered suspicious almost immediately
- Wife, husband and others are questioned about the fire that day
- Wife is last seen by her family on February 14, 2008. She was found deceased the following day. Her death was determined to be a suicide.

Arsonist gets Caught

- Police arrest and charge the arsonist (Josan) with intentionally causing damage by fire
- Josan was convicted of arson and was sentenced. He admitted to the arson

The Arsonist & the Wife

- 6 months before the fire, the wife had approached Josan to set fire to the Broadway Taco Del Mar. She told him she was desperately unhappy, could not run two restaurants on her own, and did not have enough time to spend with her children. He felt sorry for her and agreed to help.
- She provided him with the alarm code, keys and information regarding the location of restaurant's security features
- Arson gone wrong – Josan suffered serious burns to his lower body as a result of the explosion being triggered prematurely while he was still in the Premises

The Subrogated Claim

- Austeville's insurer commences subrogated claim on May 28, 2008, against:
  1. corporate tenant
  2. the Estate of the wife
  3. the husband
  4. the arsonist – Josan
  5. Cheetan Deep Turna

The Insurance Covenant

- The lease between corporate tenant and the landlord contained the following insurance covenant:

7. LANDLORD'S COVENANTS

7.05. To insure the building to its full insurable replacement value against loss or damage by fire. The expense of such insurance shall be borne as provided in paragraphs 12.01 and 12.02 hereof. To the extent that any loss or damage to the building is covered by insurance maintained by the Landlord hereunder, the Landlord releases the Tenant from any and all liability for such loss or damage whether or not the same is caused by or contributed to by or through the negligence of the Tenant or its servants and agents.

What is an Insurance Covenant?

- An insurance covenant is a provision commonly included in commercial leases where one party undertakes to insure the property against loss or damage and the other undertakes to pay for the insurance
- These covenants result in "**tort immunity**" for the party paying for the insurance
- The insured party cannot sue the party paying for the insurance for **losses which are covered** by the insurance the parties agreed to obtain

The Landlord's Claims

- Landlord made the following claims at trial:
  - Josan and the Estate of the wife were liable for the tort of conspiracy;
  - Corporate tenant was liable for breach of lease and vicariously liable for wife's conduct; and
  - If corporate tenant breached the lease, then husband and wife were liable as indemnifiers under the lease.

The Landlord's Claims cont'd

- The big picture →landlord was bringing a subrogated claim seeking compensation from other insurer(s) for losses arising from an intentionally set fire
- Neither insurer wanted to be saddled with the cost of paying for the fire

Tort Immunity, Insurance Covenants & Corporate Attribution

The Legal Questions

1. When the principal of a small company, which leases premises from a landlord, conspires to set fire to the premises, should the corporate tenant be attributed with that principal's act of conspiring to commit arson?; and
2. Is the corporate tenant immune from liability in tort by operation of the insurance covenant?

Subrogating Insurer's Position

1. How can the tenant benefit from the protection of the insurance covenant when it intentionally set the fire?;
2. That would lead to commercial absurdity wouldn't it?; and
3. The wife was the company – it was a small closely held company and so the company ought to be attributed with the wife's actions.

Defence Position

1. In considering insurance covenants, the focus is not on how or why the act occurred (ie. who caused the fire or how), but rather did the risk of the insured peril pass to the party whose insurance has been paid for (ie. the landlord).
2. Here the corporate tenant was **NOT** the same as the wife because she conspired with Josan to set the fire for personal and not corporate reasons. As such the wife's actions should not be attributed to the corporate tenant.

No Legal Precedent

- No case in Canada to date considering the effect of an insurance covenant in the context of arson
- Prior cases on insurance covenants on negligence and breaches of contract – should the effect of insurance covenants extend to clearly intentional acts – arson?

The Law From Taco Del Mar

1. Not every act of a director can be attributed to the company in a small closely held company. The test of corporate attribution must be satisfied.

2. Tort immunity arising from an insurance covenant *can* extend to intentional acts, at least in the circumstances of this case.

Corporate Attribution – The Law

- The natural person and a corporation, even one where the person is the sole-shareholder, director and officer, are two separate individuals in the eyes of the law
- In order to attribute the conduct of a natural person to a corporation, the natural person must be a "**directing mind**" of the corporation and his or her actions must be taken:
  a. within the **field of operation** assigned to him or her;
  b. not totally in **fraud** of the corporation; and
  c. by design or result partly for the **benefit** of the company.

Corporate Attribution – Landlord's Position

- Landlord argued that the wife was the corporate tenant because it was a small company with only two directors and two shareholders and the wife was the primary operator of the business
- Because the wife was tenant, the tenant had breached the lease by conspiring to set fire to the Taco Del Mar with Josan

Corporate Attribution – The Judge Held

- Both the wife and husband were directing minds of the corporate tenant
- Wife's actions were **outside the scope of her authority** as a director and officer of tenant:
  - She was acting for her own personal purposes (wanted to spend more time with her children)
  - She was not acting in relation to the restaurants or tenant's business

Corporate Attribution – The Judge Held cont'd

- Landlord failed to prove any **actual or intended benefit** to the corporate tenant by torching the restaurant
- Landlord's theory - the restaurant was suffering financially. She wanted to burn the restaurant down in order to get out of the lease – the "benefit" to the corporate tenant
- In support, the landlord put into evidence corporate financial statements purporting to show that the company was suffering financially

Financial Background of Tenant

- 2007 financial statements show an “accumulated deficit” of $126,597
- Corporate tenant met its financial obligations to employees and creditors from 2005 – 2008
- This was a start-up restaurant business
- In 2007, wife and husband tried to sell both Taco Del Mar restaurants
- Neither restaurant sold

Corporate Attribution – The Judge Held cont'd

- Landlord failed to prove that corporate tenant was suffering financially
- STRATEGIC FLAW - financial statements of corporation alone were insufficient, without expert evidence, to say that corporate tenant "benefited" by having one of its restaurants destroyed
- Josan's evidence at trial was that the wife never mentioned the corporate tenant – lack of proof that the arson plan had anything to do with the corporate tenant

Corporate Attribution – Judge's Technical Findings

- While not fraud in the classic sense, the wife's actions were aimed at the destruction of one of the corporate tenant's two restaurants
- As a result, the wife ceased to operate as a directing mind of the corporate tenant
- There was no evidence that husband knew of the conspiracy to destroy the restaurant

Corporate Attribution – What If?

The Inside Scoop

- Husband had no idea that his wife was terribly unhappy and wanted to burn down the restaurant to get out of the lease in order to spend time with her children
- Husband believed the two restaurants were doing relatively well considering it was a start up business
- What if landlord did prove the corporate tenant was not doing well financially?
- What if the wife were still alive to testify?

Corporate Attribution – The Buck Stopped There

- Because the acts of the wife could not be attributed to the corporate tenant, the corporate tenant did not breach the lease
- The claims against the husband would also fail
- The Honourable Mr. Justice Bowden did not have to decide the insurance covenant issue, but he did …

The Insurance Covenant

- Prior to this decision, insurance covenants have been held to protect parties from tort liability in cases of negligence, vicarious liability, breach of contract and even gross negligence
- No Canadian decision addresses whether insurance covenants protect parties from tort liability where the cause of the loss results from an intentional act - arson

The Insurance Covenant cont'd

Two Opposing Perspectives

- The landlord argued that to interpret the insurance covenant as barring a tort claim arising from an intentional act would lead to a commercial absurdity!!!
- Defence argued that:
  - insurance covenant was all about shifting risk of a specific insured peril, fire, between the parties under the contract; and
  - tenant had paid for the landlord's property insurance under the lease. Therefore, tort immunity should exist so long as the damage is covered by that insurance, which was the case here.

The Insurance Covenant cont'd

The Judge Held

> *"The provisions of [the insurance covenant]* ***had the effect of shifting to the plaintiff the risk of damage to its property from an insured peril, namely, fire****. This is the case regardless of whether the tenant's conduct in relation to the fire is characterized as a breach of the lease, negligence, or even gross negligence.* ***The insurance obligation under the covenant is concerned with the occurrence of the peril and not the cause of peril****. (D.L.G. & Associates Ltd. v. Minto Properties Inc., 2015 ONCA 705 and Orion Interiors Inc. v. State Farm Fire and Casualty Co., 2016 ONCA 164).* ***I would extend that reasoning beyond gross negligence to include an intentional tort****."* [emphasis added] (para 54)

The Result

- The Estate of the wife and Josan were liable to the landlord in the amount of $3,000,000 for conspiring to set fire to the Taco Del Mar
- The tenant had not breached the lease and was not vicariously liable for the wife's actions, the claim against it was dismissed
- The claim against the husband and Cheetan Deep Turna were dismissed

Impact of Decision on Insurance Industry

- This is a controversial decision and was made in light of unique underlying facts → may not be readily applied to future decisions
- May further restrict subrogated claims in the context of insurance covenants
- This decision is being appealed to the British Columbia Court of Appeal

Impact of Decision on Insurance Industry cont'd

- Landlords and their property insurers beware!
- Subrogating insurers may not be permitted to subrogate in the context of an insurance covenant providing tort immunity to the beneficiary tenant, even if the tenant commits an intention tort.
- Property insurers should consider requiring approval of insured landlord's commercial leases

Impact of Decision on Insurance Industry cont'd

- Brokers will play a role when placing CGL policies for landlord insureds
- This decision is in favour of allocating risk to the subrogating insurer rather than the defending CGL insurer
- To avoid the effect of Taco Del Mar, should commercial insurers consider revising policy wording to manage the risk of not being able to subrogate against at fault parties?

LIMITATION PERIOD

Trombley v. Pannu, 2016 BCCA 324

PRESENTED BY **DAVID BUXTON-FORMAN**

Limitation Period

Facts

- Mr. Trombley was injured in a slip and fall accident on rented premises
- A two year limitation period applied to his claim against his landlords, Mr. and Mrs. Pannu
- Shortly before the expiry of the limitation period, the adjuster appointed by the Pannus' liability insurer sent a "without prejudice" letter to counsel for Mr. Trombley that invited settlement discussions
- Settlement discussions did not take place and Mr. Trombley subsequently commenced an action after the expiry of the limitation period

Limitation Period

Key Issue

- Did the “without prejudice” letter amount to an acknowledgment of some liability, such that the respondent confirmed the cause of action and extended the limitation period?

Limitation Period

Former *Limitation Act*

5(1) If, after time has begun to run with respect to a limitation period set by this Act, but before the expiration of the limitation period, a person against whom an action lies confirms the cause of action, the time during which the limitation period runs before the date of the confirmation does not count in the reckoning of the limitation period for the action by a person having the benefit of the confirmation against a person bound by the confirmation.

(2) For the purposes of this section,

(a) a person confirms a cause of action only if the person

(i) acknowledges a cause of action, right or title of another

…

(5) For the purposes of this section, an acknowledgment must be in writing and signed by the maker.

(6) For the purposes of this section, a person has the benefit of a confirmation only if the confirmation

(a) is made to the person or to a person through whom the person claims ...

Limitation Period

Current *Limitation Act*

(1) If, before the expiry of either of the limitation periods that, under this Act, apply to a claim, a person acknowledges liability in respect of the claim,

(a) the claim must not be considered to have been discovered on any day earlier than the day on which the acknowledgement is made, and

(b) the act or omission on which the claim is based is deemed to have taken place on the day on which the acknowledgement is made.

(6) Subsection (1) does not apply to an acknowledgement, other than an acknowledgement referred to in subsection (7), (8) or (9), unless the acknowledgement is

(a) in writing,

(b) signed, by hand or by electronic signature within the meaning of the *Electronic Transactions Act*,

(c) made by the person making the acknowledgement or the person's agent, and

(d) made to the person with the claim, the person's agent or an official receiver or trustee acting under the *Bankruptcy and Insolvency Act* (Canada).

The Test

- In order to establish confirmation, one of two events must be proven: (1) that the party acknowledged the cause of action, or (2) that there was a payment made in respect of the cause of action.

> … a party can only be held to have acknowledged the claim if that party has in effect admitted his or her liability to pay that which the claimant seeks to recover … a person can acknowledge as a bare fact that someone has asserted (by making a claim) a cause of action against him, without acknowledging any liability. Simple acknowledgement of the "existence" of a cause of action is insufficient … Acknowledgment must involve acknowledgment of **some liability**.

- *Ryan v. Moore*, 2005 SCC 38

Limitation Period

The Letter

- The critical paragraphs of the letter read:

> As the matter of investigation and assessment has continued, there has been no indication of what is expected in terms of settlement. As we are nearing the two year mark following the date this incident occurred, in an attempt to keep matter moving forward, please forward your settlement demands.
>
> We thank you in advance for forward [*sic*] the requested records, and we look forward to further discussions regarding settlement.

Limitation Period

Mr. Trombley's Position

- Reasonable to believe that an invitation to engage in settlement discussions constitutes an acknowledgement of some liability, absent an express reservation or disclaimer
- Inviting settlement discussions implies an intention to pay something on a claim
- The "without prejudice" notation was meaningless as the communication did not contain any terms of settlement

Limitation Period

The Pannus' Position

- No reasonable person would interpret the letter to indicate, expressly or impliedly, an intention or willingness to admit liability
- The invitation to engage in settlement discussions was merely part of the ongoing investigation and assessment of the claim
- There is no positive obligation or duty on the adjuster to include a reservation or disclaimer in the letter to avoid the letter being interpreted as an acknowledgement

Limitation Period

The Decision

- Trial judge found that the letter did not contain a confirmation of the cause of action because it did not demonstrate an intention to admit “some liability”
- Upheld on appeal

Limitation Period

The Reasons

- Settlement proposals are commonly requested without an intention of admitting liability
- The purpose of the letter was to find out the other party’s position in order to:
  - avoid the costs of litigation,
  - reduce a party’s potential risk if liability is ultimately found against them, and
  - in some cases simply to determine if a claim is worth settling, without admitting liability, for its nuisance value alone

Limitation Period

The Reasons

- An invitation to engage in settlement discussions may be an acknowledgment of a cause of action, but not an implied acknowledgment of "some liability" in every case
- The "without prejudice" notation:
  - reinforced that the letter was made during ongoing investigation and assessment where liability was a live issue, and
  - could constitute a reservation or disclaimer on any admission of liability

Limitation Period

<u>The Implications</u>

- Communications from examiner and adjusters to potential plaintiffs can affect the limitation period
- In order to avoid extending the limitation period:
  - Make it clear that liability is in issue
  - Consider marking all communication "without prejudice"
  - Reiterate expiration date for limitation period in communications
  - Include a reservation or disclaimer
  - Avoid making partial payments

DUTY TO DEFEND – PRE-TENDER LEGAL COSTS

Lloyd's Underwriters v. Blue Mountain Log Sales Ltd., 2016 BCCA 352

PRESENTED BY **SAMANTHA IP**

Pre-Tender Defence Costs

Issue

- Should an insurer be responsible for paying an insured's defence costs incurred BEFORE the insurer receives notice of the "claim" from the insured?

Pre-Tender Defence Costs

Prior State of Law

- Common sense – how can an insurer be on risk for a loss before it receives notice of it?
- State of the law before this decision – the issue was whether an insured ought to be relieved from forfeiture and whether the insurer was prejudiced from the late notice
- There were few decisions on point

Pre-Tender Defence Costs

Kelowna (City) v. Royal Insurance Co. of Canada,
[1992] B.C.J. No. 147 (S.C.)

- The insured did not notify the insurer of the claim until a few days before trial, some five years after the claim commenced. Ultimately, the insured was successful in defending the claim and the claim was dismissed at trial. Notwithstanding this late notice, the insured claimed defence costs back from the insurer.

Pre-Tender Defence Costs

- ***Kelowna (City) v. Royal Insurance Co. of Canada*, [1992] B.C.J. No. 147 (S.C.) cont'd**
- The insured in the *Kelowna* decision admitted to the late notice and thus, **breach** of the policy, and so the only issue for the Court to decide was whether the insured ought to be relieved from forfeiture pursuant to the *Insurance Act.* R.S.B.C. 1979, c.200, which was in operation at that time
- This Court did not find the insurer in the *Kelowna* decision to have suffered any prejudice and ordered the insurer to pay defence costs, the amount of which was yet to be determined

Pre-Tender Defence Costs

- ***Falk Bros. Industries Ltd. v. Elance Steel Fabricating Co. [1989] 2 S.C.R.***
- Notice is generally not treated as a condition precedent to coverage and so breach of a notice provision will be treated as **imperfect compliance** and subject to relief from denial of coverage or relief from forfeiture

Pre-Tender Defence Costs

***ING Insurance Co. of Canada v. Federated Insurance Co. of Canada*, [2005] O.J. No. 1718 (C.A.)**

- The Ontario Court of Appeal made a blanket statement that an insurer's duty to defend does not arise until it receives notice of a claim
- But in *ING*, decision dealt with the claim of equitable contribution by a primary insurer against an excess insurer for defence costs incurred by the primary insurer in defending an action against a common insured – not co-primary as in Blue Mountain
- Excess insurer not plainly at risk – not concurrent obligation

Pre-Tender Defence Costs

- ***ING Insurance Co. of Canada v. Federated Insurance Co. of Canada*, [2005] O.J. No. 1718 (C.A.) cont'd**
- Ontario Court of Appeal found that the two insurers became adverse in interest and the excess insurer did not benefit from the defence undertaken by primary insurer.
- Primary insurer notified excess insurer *close to trial* that it would tender its limits and leave the defence to excess insurer.
- Found that it was not fair and equitable in these circumstances to require excess insurer to share in defence costs.
- Not a case regarding breach or "relief from forfeiture"

Pre-Tender Defence Costs

The Facts

- Insured companies operate in Canada and US
- Insured companies and one principal were sued in US and Canada
- Lloyd's insurer in Canada and Evanston (Markel) in US
- Evanston notified of claim and provided defence
- Lloyd's was notified later and also assumed defence
- Lloyd's did not take issue with steps to date by Evanston and retained same defence counsel

Pre-Tender Defence Costs

Background

- Should Lloyd's be responsible for "pre-tender defence costs" incurred by Insured in defending litigation in Washington State before giving Lloyd's notice of claim?
- Lloyd's sought declaration against insured that it had no obligation to pay pre-tender defence costs
- Evanston concerned that such a declaration would affect Lloyd's duty to defend and hence the ability of Evanston to seek equitable contribution from Lloyd's to share in pre-tender defence costs
- Evanston retained CW to intervene

Pre-Tender Defence Costs

Background cont'd

- Under standard liability policy, Insurer's responsibility to defend and indemnify Insured subject to prompt notice
- Lloyd's position – notice to an insurer is a prerequisite to its assumption of the duty to defend – did not breach insured
- Insured & Evanston position – duty to defend arises at the same time as the cause of action and Lloyd's not prejudiced by delay in providing notice on Washington claim
- Supreme Court hearing judge found no prejudice to Lloyd's because of late notice and granted Insured relief from forfeiture

Pre-Tender Defence Costs

After The Hearing

- Lloyd’s appealed – Evanston and insured responded
- Evanston was under a duty to defend, but then succeeded in Washington state in obtaining a court declaration that there was no coverage
- Evanston withdrew from the appeal
- The case proceeded to appeal with Lloyds and the insured, and the Court of Appeal reversed the hearing judge’s decision.

Pre-Tender Defence Costs

Court of Appeal

- Court of Appeal determined that chambers judge erred by employing relief from forfeiture analysis instead of giving effect to the unambiguous terms of the insurance contract
- Although Insured breached the notice clause, Insurer **waived its right to rely on this breach** and implemented its obligations to provide indemnification and a defence.
- Thus, no forfeiture of coverage that would engage a relief from forfeiture analysis.
- There was a clear Voluntary Payments clause

Pre-Tender Defence Costs

Court of Appeal cont'd

- LAW TODAY – An insurer is *generally* not on risk for pre-tender defence costs.
- Where an insurer does not hold insured in breach (for late notice), relief against forfeiture not available with respect to costs incurred prior to providing notice of claim to Insurer
- This subject policy had a clear Voluntary Payment Clause that "the insured shall not, except at his own cost, voluntarily make any payment… or incur any expenses".

Pre-Tender Defence Costs

Court of Appeal cont'd

- Court of Appeal accepted Lloyd's interpretation of policy, distinguishing between "repudiation" cases and "implementation" cases to make this point:

> *…The insurer in these cases* ***waives the insured's breach of the notice*** *clause and honours the "essential bargain" by providing coverage and a defence going forward. There is thus no forfeiture of insurance, and the insured's obligations under the policy likewise remain in place. Since the duty to defend does not arise until notice or tender has occurred, the voluntary payment clause imposes responsibility for pre-tender defence costs on the insured. Whether the insurer has suffered prejudice from late notice is irrelevant.*

Pre-Tender Defence Costs

If Sam Appeared In The Court of Appeal For Evanston....

- Lloyd's could not have breached the insured in any event – there was no prejudice from the late notice. By Lloyd's taking the position of "no breach" it was not giving up anything, but acknowledging its contractual requirements
- Lloyd's benefitted from defence paid for by Evanston
- Simply by framing its position as no breach, should Lloyd's be entitled to take the framework of analysis out of law established by our Supreme Court of Canada?
- The Voluntary Payment Clause of the policy must be clear in order for this case to apply

Pre-Tender Defence Costs

Impact

- Where insured makes voluntary payment prior to giving notice of claim to insurer, and the insurer, upon receiving notice of the claim, does not deny coverage, the pre-tender voluntary payment is not recoverable against insurer and is not subject to relief against forfeiture analysis…but depends on policy wording.

CLARK WILSON LLP

These materials are necessarily of a general nature and do not take into consideration any specific matter, client or fact pattern.

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THANK YOU