# Canada

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## Causes of Action

### *Is there a statutory basis for an insured to bring a bad faith claim?*

Section 439 of the Ontario Insurance Act, 1990 R.S.O. c. I.8 (amended to 2003) states that: "No person shall engage in any unfair or deceptive act or practice." "Person" is deemed by section 438 to include an individual, a corporation, a Lloyd's name, a mutual benefit society or fraternal society.

Similar language is found in the respective insurance acts of some other Canadian common law Provinces and Territories. *See*, *for example*, s. 509 of Alberta's Insurance Act, R.S.A. 2000, c. I-3, which has similar wording.

The federal Competition Act, R.S. 1985, c. C-34 also provides a statutory cause of action against business entities, including insurance companies, for transgressions such as unfair competition, unfair advertising and price fixing or collusion.

The legislative provisions permitting bad faith actions are seldom, if ever, used. Instead, plaintiffs rely on common law cases to mount an action based on the insurer's common law duty to act with good faith and fair dealings with its insured.

### *Can a third party bring a statutory action for bad faith?*

A third party will not usually have an interest in a statutory bad faith claim against an insurer since the statutory cause of action is arguably personal to the policyholder.

### *Is there a common law cause of action for bad faith?*

Yes, in Canadian common law, the contract of insurance carries with it an implied obligation on both parties to act in utmost good faith. An insurer is, therefore, required "to act promptly and fairly at every step of the claims process." *See Wadhwani v. State Farm Mut. Auto. Ins. Co.*, 2010 ONSC 2479, 2010 CarswellOnt 3340 (Ont. S.C.J. 2010) (citing *702535 Ontario Inc. v. Lloyd's London, Non-Marine Underwriters* (2000), 184 DLR (4th) 687 (Ont. C.A.)) at paras. 28-30.

Canadian insurance law has recognized and followed old English authority that the relationship between insurer and policyholder is one of *uberrimae fides* or utmost good faith. *See Carter v. Bohem* (1766), 97 E.R. 1162, [1558–1774] All E.R. 183 (Eng. K.B.). For a comparative analysis of the utmost good faith principle in Canada, the U.S. and England, *see Saskatchewan Crop Insurance Corp. v. Deck*, 2008 CarswellSask 84 (C.A.). *See also* Roderick S.W. Winsor, *Good Faith In Canadian Insurance Law* (Toronto: Canada Law Book, 2007+ looseleaf service) and Gordon H. Hilliker, *Insurance Bad Faith*, 3d Ed. (Markham: LexisNexis Canada, 2015).

### *What cause of action exists for an excess carrier to bring a claim against a primary carrier?*

There is no statutory or contractual connection between the excess carrier and the primary carrier, so the excess carrier's claim cannot be pleaded directly as bad faith: *Willis v. Hope* (1990), 48 CCLI 126 (Ont. Dist. Ct.). *See also Overload Tractor Servs. Ltd. v. ICBC* (1989), 39 CCLI 18 (B.C.C.A.).

However, two Canadian decisions at the appellate level have recognized that the duties between primary and excess insurers may extend beyond contract. *See Hollinger Int'l Inc. v. Am. Home Assur. Co.*, 2006 CarswellOnt 188 (Ont. S.C.J.) (citing *Broadhurst & Ball v. Am. Home Assur. Co.* (1990), 1 O.R. (3d)

225 (C.A.)) and *Aetna Ins. Co. v. Canadian Sur. Co.* (1994), 24 CCLI (2d) 257 (Alta. C.A.) ("duties may flow from a primary insurer to an excess insurer under certain circumstances"). For example, when a damage claim threatens to exceed the primary coverage, the reasonable foreseeability of impingement on the excess policy creates a three-way duty of care between the primary insurer, the excess insurer and the insured. *Hollinger Int'l Inc. v. Am. Home Assur. Co.*, 2006 CarswellOnt 188 (Ont. S.C.J.).

The doctrine of equitable subrogation or contribution is recognized. A primary insurer can impose a defense cost funding obligation on an excess/umbrella insurer which is "plainly at risk." *Broadhurst & Ball v. Am. Home Assur. Co.* (1990), 1 OR (3d) 225 (C.A.). Although no case has been decided on this issue, arguably an excess carrier should not be precluded, in the right factual circumstances, from claiming punitive damages over and above its equitable remedies for contribution or in recovery by subrogation. Such damages, however, would not be categorized as "bad faith" damages for the excess carrier but instead would arise in the context of construing the primary carrier's relationship with the policyholder.

The Ontario Court of Appeal suggests an excess insurer will have to pay a portion of the primary insurer's defense costs where that excess insurer knows of a claim, and sits back to benefit from the work of the primary insurer. *ING Ins. Co. of Can. v. Federated Ins. Co. of Can.* [2005] ILR I-4404, [2005] O.J. No. 1718, 138 A.C.W.S. (3d) 1159, 197 O.A.C. 324, 22 C.C.L.I. (4th) 1, 75 O.R. (3d) 457.

### *What causes of action for extra-contractual liability have been recognized outside the claim handling context?*

The statutory provisions contained in the Insurance Act and the Competition Act are examples of "bad faith" causes of action (false or misleading advertising, tied selling, price fixing) which are not in the claims context.

Potential extra-contractual liability for insurers include: inducing a breach of contract (*Iakoupov v. Pilot Insurance Co.*, 2005 CarswellOnt 7070 (Ont. S.C.J. 2005)), unlawful interference with economic relations, (*Saskatchewan Government Insurance v. Medynski*, 2012 SKQB 157 (Sask. Q.B.) and *Leavitt v. Hooper*, 2012 NBQB 74 (N.B. Q.B.)) and unjust enrichment (*Zaprzala v. Manufacturers Life Insurance Co.* 2014 ONSC 3358 (Ont. S.C.J.)). The Supreme Court of Canada in a landmark decision imposed a duty of honest performance as between all contracting parties. The duty imposes a "minimum standard of honesty" providing the other contracting party the opportunity "to protect their interests" should the contract not work out. It is unclear whether this duty places additional obligations on parties to an insurance contract or whether the Supreme Court's decision simply extends principles already applicable to insurance policies to all other forms of contractual dealings in Canada. What is clear is damages awarded for breach of duty of honest performance are not necessarily punitive. *Bhasin v. Hrynew*, 2014 SCC 71 (S.C.C.).

There is a divide in Canada as to whether a breach of the duty of good faith between an insured and its insurer arises out of the insurance policy or is an independent tort. For a discussion regarding this divide please *see Forestex Management Corp. v. Underwriters at Lloyd's*, 2004 FC 1303 (F.C.C.). *See also Ins. Corp. of British Columbia v. Hosseini*, 2006 BCCA 4 (B.C.C.A.) (a breach of the duty of good faith is a breach of a "contractual duty"); *Walsh v. Nicholls*, 2004 NBCA 59 (N.B.C.A.) (an insurer's breach of its duty of good faith and fair dealing can sound in both tort and contract).

It has been held in at least one Canadian province that a claim of "bad faith" by itself does not constitute a complete cause of action. The alleged bad faith must be tied to some alleged breach of duty to complete the cause of action. *Blanchard v. Ins. Corp. of British Columbia*, 2009 CarswellBC 2948 (B.C.S.C. 2009). In another province, however, an appellate level court held that it was not plain and obvious that the representative plaintiffs' claims for breach of the duty of good faith could not succeed. The lower court's decision, striking the cause of action, was overturned on this basis. *Kang v. Sun Life Assurance Co. of Can.*, 2013 ONCA 118 (Ont. S.C.J.). For a discussion of the debate over contract-based

and tort-based analysis in the Canadian context, *see* the texts on the subject by R. Winsor and G. Hilliker, cited above.

## Damages

### *Are punitive damages available?*

Yes, punitive damages are available against the insurer for bad faith conduct when the conduct constitutes a separate actionable tort. *See*, *e.g.*, *Whiten v. Pilot Ins. Co.*, [2002] 1 SCR 595 (S.C.C.). However, not every breach of good faith gives rise to an award of punitive damages. *Asselstine v. Mfrs. Life*, 2005 BCCA 292, 22 CCLI (4th) 169 (C.A.) *additional reasons in* 2005 BCCA 465, 26 CCLI (4th) 68 (C.A.). In one case, the Ontario Superior Court of Justice held that punitive damages were not necessarily warranted in circumstances where an insurer breached its duty of good faith to the insured because of unfairness and deception. *Cont'l Ins. Co. v. Almassa Int'l Inc.*, [2003] O.J. No. 1125, [2003] O.T.C 226, 121 A.C.W.S. (3d) 950, 46 CCLI (3d) 206. In another instance, the Saskatchewan Court of Appeal stated that the trial judge erred in awarding punitive damages, but awarded the same amount as properly being charactized as damages for breach of the duty of good faith. *Wilson v. Saskatchewan Gov't Ins.*, 2012 SKCA 106, [2013] 5 W.W.R. 286, 16 C.C.L.I. (5th) 171, 223 A.C.W.S. (3d) 702, 405 Sask R. 8, 563 W.A.C. 8.

Canadian courts generally are conservative and punitive damages, as a rule, will be awarded rarely. Within those rare occasions, they will be more frequently awarded in non-commercial contexts, due to the relative sophistication imbalance of the parties involved. *Whiten v. Pilot Ins. Co.*, [2002] 1 SCR 595 (S.C.C.). *See also Ferme Gerald Laplante & Fils Ltee. v. Grenville Patron Mut. Fire Ins. Co.* (2002), 61 O.R. (3d) 481 (Ont CA), *leave to appeal to the Supreme Court of Canada refused*, SCC File No. 29485, SCC Bulletin 2003; *Khazzaka v. CGU Ins. Co. of Canada*, [2002] OJ No 3110, [2003] I.L.R. I-4138, 115 A.C.W.S. (3d) 984, 162 O.A.C. 293, 28 C.P.C. (5th) 15, 43 C.C.L.I. (3d) 90, 66 O.R. (3d) 390; *Fernandes v. Penncorp Life Ins. Co.*, 2013 ONSC 1637 (Ont. S.C.J. 2013). In the insurance context, when the insurer does not adhere to its duty it may be liable for extra-contractual damages including punitive damages for bad faith. Punitive damages is a rational response to the insurer's bad faith conduct, since without such an award the insurer "would not have been required to pay more than its policy required it to pay and there would be nothing to deter it from acting similarly in the future." *Kings Mut. Ins. Co. v. Ackermann*, 2010 CarswellNS 285 (C.A.).

Quantum of punitive damages awarded is a controversial issue in Canada. Critics of punitive damages have expressed concerns that high jury awards would bring the administration of justice in Canada in disrepute. However, the Saskatchewan Queen's Bench has affirmed that jury awards of punitive damages have a long and important history in Anglo-Canadian jurisprudence. The Queen's Bench noted that the $1 million punitive damages award in *Whiten v. Pilot Insurance Co.*, [2002] 1 SCR 595 (S.C.C.), based on the facts before it, must not have caught the attention of the insurance industry. Consequently, the court awarded a combined total of $4 million in punitive damages against two insurers. *Branco v. Am. Home Assurance Co.*, 2013 SKQB 98 (Sask. Q.B.).

### *Are attorneys' fees recoverable?*

Traditionally, the remedy for bad faith conduct prior to litigation is punitive damages, as opposed to an award of increased costs. *Asselstine v. Mfrs. Life*, 2005 BCCA 292, 22 CCLI (4th) 169 (C.A.), *additional reasons in* 2005 BCCA 465, 26 CCLI (4th) 68 (CA). However, at least one court has awarded an increased costs award (substantial as opposed to partial indemnity) in addition to damages for breach of the good faith obligation. *See Wilson v. Saskatchewan Gov't Ins.*, 2012 SKCA 106, [2013] 5 W.W.R. 286, 16 C.C.L.I. (5th) 171, 223 A.C.W.S. (3d) 702, 405 Sask R. 8, 563 W.A.C. 8 (in Canadian common law jurisdictions, "costs" are usually construed as including what in most U.S. jurisdictions would be confined to attorneys' fees).

In most Canadian common law jurisdictions, "costs generally follow the event," meaning the successful party is usually entitled to recover a portion or a substantial portion of its overall costs from the unsuccessful party. *See*, *e.g.*, Ontario Courts of Justice Act, R.S.O. 1990 c. C.43, section 131; Ontario

Rules of Civil Procedure, Rule 49 and 57. This is not unique to bad faith litigation and is applicable generally as the inherited "English rule" or "loser pays rule" as compared with the "American rule" which by default, absent special statute or other provision, requires each party to pay its own overall costs regardless of the outcome, success of a party, etc.

Cost orders in Canadian common law courts are usually in the discretion of the court. Factors impacting a costs award include the existence of written offers to settle, the difficulty of the case, or novelty of the law, and the conduct of parties or their counsel. In one case, fraudulent behavior on the part of an insured justified an increased award of costs. *See*, *e.g.*, *Halpern Invs. Ltd. v. Sovereign Gen. Ins. Co.*, 2005 ABQB 105 (Alta. Q.B.).

Insurers have on occasion argued, albeit unsuccessfully, that an allegation in a pleading of bad faith in the absence of support merits an award of special costs in the insurer's favor. *See More Marine Ltd. v. Axa Pac. Ins. Co.*, 2010 CarswellBC 133 (S.C.). There is however case law that supports an increased cost award against the policyholder when the insurer successfully defends a bad faith and malice claim that the policyholder insisted be litigated in the absence of supporting evidence. According to the court there was no question the malice and bad faith claim increased the time and cost of litigating the action. *Nassim v. Perth Ins. Co.*, 2009 CarswellNS 815 (S.C.).

### *Are consequential damages recoverable?*

Yes. A breach of the duty to act fairly and in good faith may result in an award of consequential damages distinct from the proceeds payable under the policy and punitive damages. *Ferme Gérald Laplante & Fils Ltée v. Grenville Patron Mut.* (2002), 217 D.L.R. (4th) 34, (Ont. C.A.), *additional reasons in* 2002 CarswellOnt 3612 (C.A.), *leave to appeal refused* (2003), 191 OAC 397 (note) (S.C.C.). Other cases providing that consequential damages may be available to an insured if its insurer acts in bad faith include: *Bow Valley Res. Servs. v. Kansa Gen. Ins. Co.* (1991), 56 BCLR (2d) 337 (C.A.) and *702535 Ontario Ltd. v. Non-Marine Underwriters, Lloyd's London, Eng.* (2000), 184 DLR (4th) 687 (Ont. C.A.).

### *Can a plaintiff recover damages for emotional distress?*

Yes. Conduct which represents a breach of the insurer's good faith duty, but is not reprehensible enough to warrant punitive damages may result in an award for what is sometimes referred to as "aggravated damages" for emotional distress. *Fidler v. Sun Life Ins. Co. of Can.*, [2002] 11 WWR 352 (B.C.S.C.) (Proposition cited for upheld: Conduct which represents a breach of an insurer's good faith duty can attract an award for aggravated damages, even if it does not rise to the level of bad faith required for punitive damages).

Aggravated damages are available as additional compensation if the insured establishes that the breach of contract caused mental distress. However, an independent actionable wrong is not required for an award of mental distress. *Fidler v. Sun Life Assurance Co. of Can.*, 2004 CarswellBC 1086 (C.A.) at para. 42 (Proposition cited for upheld: there is no requirement for an independent actionable wrong in awarding damages for mental distress arising out of a breach of contract). The Supreme Court of Canada has held it is reasonably foreseeable that intangible injuries and mental distress may flow from the insurer's wrongful refusal to pay benefits even where the insured suffers no immediate financial hardship. *See Fidler v. Sun Life Assurance Co. of Can.*, [2006] 2 SCR 3 (S.C.C.). In Ontario, the superior court has also found that, while mental distress as a consequence of breach must reasonably be contemplated by the parties to attract damages, it does not have to be the dominant aspect or even the "very essence" of the bargain. *McQueen v. Echelon Gen. Ins. Co.*, 2009 CarswellOnt 5716 (S.C.J.), *upheld in* 2011 ONCA 649 (C.A.).

A court making an award of mental distress damages in a denial of benefits claim must be satisfied that: (a) an object of the contract was to secure a psychological benefit that brings mental distress upon breach within the reasonable contemplation of the parties, and (b) the degree of mental suffering caused by the breach was sufficient to warrant compensation. *McQueen v. Echelon Gen. Ins. Co.*, 2009 CarswellOnt 5716 (S.C.J.).

In one case, an insured was awarded $50,000 in aggravated damages by establishing that her "peace of mind" had been breached because the insurer did not look after her needs properly. The Ontario Superior Court held there was no need to prove a separate actionable wrong. *Monks v. ING Ins. Co. of Can.* (2005), 24 CCLI (4th) 1 (Ont. S.C.J.) (Proposition cited for upheld: An award for $50,000 for aggravated damages was reasonable; insured did not need to prove a separate actionable wrong).

In a B.C. case, because the policyholder's action for ongoing disability benefits was dismissed, the trial judge also dismissed her claim for extra contractual damages, including damages for mental distress *See Andreychuk v. RBC Life Ins. Co.* 2008 CarswellBC 2558 (C.A.).

## Elements of Proof

### *What is the legal standard required to prove bad faith in a first party case?*

The legal standard of proof is the civil "on a balance of probabilities" rather than the criminal "beyond reasonable doubt."

What constitutes bad faith, however, will depend on the circumstances in each case. Canadian common law courts will look at the conduct of the insurer throughout the claims process to determine whether it has acted fairly and promptly in responding to the claim. *702535 Ontario Inc. v. Non-Marine Underwriters, Lloyd's London, Eng.* (2000), 184 DLR (4th) 687 (Ont. C.A.) at p. 694, *leave to appeal refused* [2000] SCCA No. 258 (S.C.C.). Most judges and commentators agree that any attempt to ascribe an exact meaning to "bad faith" is an unwise, and probably quixotic undertaking. *Walsh v. Nicholls*, 2004 NBCA 59 (C.A.).

The term "bad faith," in the context of s. 267.8(22) of the Ontario Insurance Act has been interpreted to mean a conscious doing of a wrong or dishonest act and a state of mind affirmatively operating with ill will or an improper or illegal design. Bad faith is different from negligence, in that it involves intent. Bad faith is to be distinguished from and is not simply bad judgment. *See Peloso v. 778561 Ontario Inc.*, 2005 CarswellOnt 2480 (S.C.J.).

For a review of what is required to prove bad faith *see Insurance Corp. of British Columbia v. Hosseini*, 2006 BCCA 4 (C.A.) and *Kings Mutual Insurance Co. v. Ackermann*, 2010 CarswellNS 285 (C.A.).

### *What is the legal standard required to prove bad faith in a third party failure to settle a claim?*

This issue, on an evidentiary standard, has not been raised or litigated in Canada, but is most likely to be the same as above: a "on a balance of probabilities" taking into account evidence on the factors noted above. However, in Ontario the court has held that a primary insurer must have a "justifiable basis" to refuse to respond to a proposed settlement fairly and promptly. *Hollinger Int'l Inc. v. Am. Home Assur. Co.*, 2006 CarswellOnt 188 (Ont. S.C.J.). Other case law suggests that an insurer must consider the policyholder's interests equally with its own interests when presented with a limits offer of settlement.

In British Columbia, the insured owner and driver of a motor vehicle was sued for personal injuries by a passenger. The claim was worth more than the policy limits and consequently the passenger offered to settle for the full policy limits with the insurer. The insurer did not consent to this proposed settlement. The case went to trial and the plaintiff obtained a judgment in excess of policy limits. The insurer was then forced to pay the amount of the judgment excess of policy limits. The B.C. Court, in holding in favour of the insured, noted the insurer's failure to consider the insureds interests equally with its own in refusing to settle, thereby exposing the insured to a risk of excess judgment. This case suggests that at least in B.C. insurers must apply a balancing of interests analysis when determining whether to settle a claim. *See Shea v. Manitoba Pub. Ins. Corp.*, (1991), 55 BCLR (2d) 15 (B.C.S.C.).

### *Is there a separate legal standard that must be met to recover punitive damages?*

Yes. The threshold standard to establish punitive damages in the insurance context is that the conduct of the insurer must be significantly improper or egregious. *Strikaitis v. RBC Travel Ins. Co.*, 2005 BCSC 103 (B.C.S.C.). *See also Cont'l Ins. Co. v.*

*Almassa Int'l Inc.*, [2003] O.J. No. 1125, [2003] O.T.C 226, 121 A.C.W.S. (3d) 950, 46 CCLI (3d) 206.

To recover punitive damages, the policyholder must show that the insurer's conduct has been malicious, arbitrary, high-handed or highly reprehensible. Evidence of such conduct will support the policyholder's claim that the insurer has committed a separate, actionable tort and damages will be awarded commensurate with the harm caused, degree of misconduct and relative vulnerability of the policyholder. *Whiten v. Pilot Ins. Co.*, [2002] 1 SCR 595 (S.C.C.); *see also Strikaitis v. RBC Travel Ins. Co.*, 2005 BCSC 103 (B.C.S.C.) (a punitive damages award, in the context of an insurance claim case, requires high-handed, malicious, arbitrary or reprehensible misconduct which markedly departs from accepted standards of decent behavior).

The legal test for overturning a properly instructed jury's decision in awarding punitive damages decision is whether a reasonable jury could have concluded that an award of punitive damages was rationally required to punish the insurer's misconduct. *Kings Mut. Ins. Co. v. Ackermann*, 2010 CarswellNS 285 (C.A.).

### *Does a bad faith claim require evidence of a pattern or practice of unfair or deceptive conduct?*

The *Whiten* and *Branco* cases, discussed above, demonstrate that a breach of the insurer's duty to act in good faith in one case, if carried through to trial, can result in liability for bad faith conduct and an award of punitive damages. *See Whiten v. Pilot Ins. Co.*, [2002] 1 SCR 595 (S.C.C.); *Branco v. Am. Home Assurance Co.*, 2013 SKQB 98 (Sask. Q.B.). Canadian courts prefer to adopt a contextual approach. According to the Ontario Superior Court of Justice, "An error in the processing of a claim may not be illustrative of bad faith itself if it is an isolated event in the course of conduct." *Blake v. Dominion Gen. Ins. Co.*, 2013 ONSC 6069 (S.C.J.). A pattern of insurer's bad faith conduct in the course of other cases or as a matter of corporate policy will be taken into account when assessing the quantum of punitive damages. *Whiten v. Pilot Ins. Co.*, [2002] 1 SCR 595 (S.C.C.).

Ultimately, what constitutes bad faith will depend on the circumstances in each case. *702535 Ontario Inc. v. Non-Marine Underwriters, Lloyd's London, Eng.* (2000), 184 DLR (4th) 687 (Ont. C.A.) at p. 694, *leave to appeal refused* [2000] SCCA No 258 (S.C.C.). For a review of the nature and scope of the duties owed by an insurer to its insured, please *see Insurance Corp. of British Columbia v. Hosseini*, 2006 BCCA 4 (C.A.) (citing *Shea v. Manitoba Pub. Ins. Corp.*, (1991), 55 BCLR (2d) 15 (B.C.S.C.)).

### *On what issues is expert evidence required to establish bad faith?*

There is no requirement to call expert witnesses in bad faith insurance claims. Indeed, counsel must take care to call experts who have relevant experience in the Canadian market. *See*, *e.g.*, *Flewwelling v. Blue Cross Life Ins. Co. of Can.*, [1999] AJ No 381 (Alta. Q.B.) (where the court restricted an American expert to giving evidence on general risk management issues out of concern that his other experience would not be relevant to the Canadian context).

Apart from legislation governing evidence generally, each Canadian province and territory regulates the conduct of its own courts including qualification of expert witnesses. In Ontario, expert testimony is governed by Rule 53 of the Rules of Civil Procedure. This rule requires that expert reports be prepared and served prior to trial and that the expert submit his/her qualifications to the court for challenge by opposing counsel. Readers are encouraged to consult local counsel for up-to-date developments in evidence standards in a particular province or territory.

### *On what issues is expert evidence precluded?*

Experts are generally precluded from addressing the proper interpretation of coverage obligations or a similar purely "legal" question which the court alone must decide. *See for example* cryptic remarks alluding to this issue in *Co-operative Avicole v. Co-operators General Insurance Co.* (1997), 44 CCLI (2d) 1 (O.C.J.).

However, in Ontario (Canada's most populous province), practitioners should be aware of the requirement that any issue the expert purports to address must be included in the expert's pre-trial

report. Rule 53.03(3). Readers should consult local counsel for up-to-date developments and local rules in a particular province or territory.

### *Is a bad faith claim viable if a coverage decision has been determined to be correct?*

There is a divide in Canadian case law on this issue. Under the first line of authority, there must be a valid and favorably decided action on the policy before an ongoing bad faith claim will crystallize. *Forestex Mgmt. Corp. v. Underwriters at Lloyd's*, 2004 FC 1303 (F.C.C.). The British Columbia court of first instance considered the *Forestex Management Corp.* decision which in turn relied on the following approach endorsed in *Bartlett v. John Hancock Mutual Life Insurance Co.* (1988), 538 A. 2d 997:

> Clearly plaintiff could never show an absence of a reasonable basis for denial of benefits if the insurer can prove that no benefits were owed under the policy. If the insurer prevails on the breach-of-contract action, it could not, as a matter of law, have acted in bad faith in its relationship with its policyholder. . . .

*See Brennard v. Sun Life Assurance of Canada*, 2011 BCSC 759, at para. 25 (B.C.S.C.), *Andreychuk v. RBC Life Ins. Co.* 2008 CarswellBC 2558 (C.A.); *Wonderful Ventures Ltd. v. Maylam*, 2001 BCSC 775 (B.C.S.C.); *Lawrence v. Ins. Corp. of British Columbia*, 2001 BCSC 1530, at para. 27 (B.C.S.C.); *Sanders v. Clarica Life Ins. Co.*, 2003 BCSC 403, at para. 8 (B.C.S.C.).

Under the second line of authority, however, it is not necessary for the insured to establish coverage for its bad faith claim to succeed. For example according to an Alberta court, the plaintiffs in the *Whiten v. Pilot Insurance Co.*, [2002] 1 SCR 595 (S.C.C.) and *Fidler v. Sun Life Assur. Co. of Can.*, 2004 BCCA 273 (B.C.C.A.) decisions would have been successful regardless of whether there was a policy claim extant at the time of trial. *Baudisch v. Co-operators Gen. Ins. Co.* [2005] AWLD 576 (Alta. Prov. Ct.). In Ontario, it has been held the insurer's duties of good faith and fair dealing with its insured start the day it receives a claim. *Maschke Estate v. Gleeson* (1986), 54 OR (2d) 753 (Ont. H.C.). This suggests a court can impose an award if the bad faith tort is proven even in the absence of coverage.

However, in *Barker v. Zurich Insurance Co.*, [2001] OJ No 358 (Ont. C.A.), *leave to appeal dismissed* [2004] Bulletin 29996 (S.C.C.), the Ontario Court of Appeal found the jury verdict was in error on the coverage issue and concluded that "without a sustainable verdict on the issue of liability under the insurance contract, the award for punitive damages cannot stand." This appellate authority strongly suggests that a bad faith claim is not viable in the face of an insurer's successful coverage defense.

Judicial commentary in the context of successful motions to bifurcate proceedings also appears weighted in favor of dismissing a bad faith claim in the absence of a viable contract verdict. Rationale includes the fact the bad faith tort is arguably derivative of improper performance under the contract between the parties: in the absence of a duty to perform, there can be no bad faith tort. *See obiter* comments in *Wonderful Ventures Ltd. v. Maylam* (2001), 31 CCLI (3d) 298 (B.C.S.C.); *Lawrence v. ICBC*, [2001] BCJ No 2516 (B.C.S.C.); *Sovereign General Insurance Co. v. Tanar Industries Ltd.*, [2002] AJ No 107 (Alta. Q.B.); and *Brennand v. Sun Life Assurance Co. of Canada*, 2011 BCSC 759 at para 25.

The mere fact that an insurer denies coverage and is subsequently found to have done so incorrectly will not automatically result in a finding of bad faith or an award of punitive damages. Nor does impatience amount to bad faith. *Paomar Holdings Ltd. v. Lloyd's Underwriters* (2003), 2 CCLI (4th) 298 (Ont. S.C.J.); *Lastiwka v. Alberta Blue Cross*, [2000] AJ 1443 (Alta. Q.B.), *reversed on unrelated grounds* [2003] AJ No 52 (Alta. C.A.); *Kings Mut. Ins. Co. v. Ackermann*, 2010 CarswellNS 285 (C.A.).

### *Is a third party bad faith claim viable if the plaintiff does not prevail in the underlying claim?*

There appear to be no decided cases on this point in the Canadian common law jurisdictions. Other than in the Civil Code jurisdiction of Quebec, a third party claimant has no direct right of action on a liability policy absent an enforceable and unsatisfied judgment against the policyholder or an assignment of the rights in the policy.

## Practice and Procedure

### *Statute of limitations*

Readers are cautioned to consult local counsel for a definitive review of the applicable limitation period in any particular province or territory. In Ontario, the limitation period for a bad faith claim is two [2] years under the Ontario Limitations Act, 2002, S.O., Schedule Beauchamp, Sections 4 and 15(2): *St. Denis v. TD Ins. Home & Auto Liberty Ins. Co. of Can.*, 2005 CarswellOnt 5080 (S.C.J.); *See also Dundas v. Zurich Canada*, 2012 ONCA 181.

In Ontario, under the Limitations Act, generally, actions must be commenced no later than two [2] years after the discovery of the claim: Section 4. Time begins to run on actions for contribution and indemnity on the date the original statement of claim is issued. Section 18. Other provinces and territories have varying limitation periods.

Arguably, when a bad faith action is commenced against an insurer for a series of actions, as opposed to a single incident, the court is faced with determining from a review of all facts when the insured "discovered" the existence of a bad faith claim. Time arguably runs from that date forward in those provinces and territories recognizing a discoverability analysis. Again, readers are cautioned to consult with local counsel for an up to date review in a given Canadian province or territory.

### *Under what circumstances will bad faith claims be dismissed or stayed pending the resolution of the underlying claims?*

A stay of the bad faith claim was ordered pending an appeal of the underlying claim where the court was satisfied that the insurer was not pursuing an appeal in order to gain a tactical advantage. The stay was justified because the prejudice to the insurer defendant in having to disclose privileged communications in the context of the bad faith claim outweighed the prejudice to the insured attributable to a seven- to eight-month delay in order to resolve the appeal. *Nayyar v. Mfrs. Life Ins. Co.*, 2012 BCSC 470 (Appellant courts refused a re-hearing and/or reconsideration of a stay of action ordered by Walker J., (In Chambers)).

Another decision stayed a bad faith claim pending against the insurer to await the resolution of an appeal in a separate proceeding regarding the interpretation of the insurance policy at issue in the bad faith case. The Manitoba Court's "stay of proceedings" analysis was based largely on the Manitoba Rules of Civil Procedure. *See Carriere Estate v. Coseco Ins. Co.*, 2010 CarswellMan 102 (Man. Q.B. 2010). In granting the stay, the Manitoba Court relied on the following passage from the decision of *Varnam v. Canada (Minister of Health and Welfare), Director of Bureau of Dangerous Drugs and College of Physicians and Surgeons (BC)* (1987), 12 FTR 34 (TD):

> A stay of proceedings is never granted as a matter of course. The matter is one calling for the exercise of a judicial discretion in determining whether a stay should be ordered in the particular circumstances of the case. The power to stay should be exercised sparingly and a stay will only be ordered in the clearest cases. In an order to justify a stay of proceedings two conditions must be met, one positive and the other negative: (a) the defendant must satisfy the court that the continuance of the action would work an injustice because it would be oppressive or vexatious to him or would be an abuse of the process of the court in some other way; and (b) the stay must not cause an injustice to the plaintiff. On both the burden of proof is on the defendant. Expense and inconvenience to a party or the prospect of the proceedings being abortive in the event of a successful appeal are not sufficient special circumstances in themselves for the granting of a stay . . . .

### *Under what circumstances will bad faith claims be severed for trial from the underlying claim?*

The Supreme Court of Canada in the *Whiten v. Pilot Insurance Co.*, [2002] 1 SCR 595 (S.C.C.) case stated: "Where a trial judge is concerned that the claim for punitive damages may affect the fairness of the liability trial, bifurcated proceedings may be appropriate."

There is a division in the Canadian jurisprudence on this issue in the context of privileged documentation that might answer the bad faith/punitive claims

while being potentially embarrassing to the insurer in the contract claim.

In Ontario, bad faith claims will normally be heard together with the underlying contract actions because the courts historically do not favor bifurcation. Where the allegations of bad faith require the insurer to raise defenses calling for waiver of litigation or solicitor/client privilege, Ontario and Newfoundland courts take a restrictive view. *See Sempecos v. State Farm Fire & Cas. Co.*, [2001] OJ No 4887 (S.C.J.), *aff'd* [2002] OJ No 4498 (Div. Ct.), *aff'd* 38 CPC (5th) 64 (Ont CA); *Lundrigan v. Non-Marine Underwriters, Lloyd's of London*, [2002] NJ No 30 (Nfld. S.C. T.D.). Note, however, in the *Sempecos* decision, the Ontario Court of Appeal did acknowledge more cases have been released since the original trial decision. The panel dismissed the appeal without prejudice to the insurer to bring a motion again on better evidence of prejudice while stating that the law had in fact changed. Nevertheless, there is still no automatic bifurcation of bad faith claims from underlying coverage claims in Ontario. Such issues are still normally tried together. *SNC-Lavalin Eng'rs & Constructors Inc. v. Citadel Gen. Assur. Co.* (2003), 63 OR (3d) 226 (Master).

Western Canadian courts allow bifurcation if sufficient evidence of the prejudice is produced. In what appears to be the leading decision on point, the court in *Wonderful Ventures v. Maylam* (2001), 31 CCLI (3d) 298 (B.C.S.C.) ordered that the bad faith claim against the insurer be heard separately from the coverage action. The court ordered the bifurcation because it found that in order to defend itself from the bad faith allegations, the defendant would have to disclose privileged communications. *See also Brennard v. Sun Life Assurance of Canada*, 2011 BCSC 759, *Lawrence v. ICBC*, [2001] BCJ No 2516 (BCSC); *Sovereign Gen. Ins. Co. v. Tanar Indus. Ltd.*, [2002] AJ No 107 (Alta. Q.B.); *Kursar v. BCAA Ins. Corp.*, 2004 BCSC 1006 (S.C.); *Stuart v. Mfrs. Life Ins. Co.*, 2004 BCSC 501, [2004] B.C.W.L.D. 821, [2004] B.C.J. No. 729, 10 C.C.L.I. (4th) 142, 130 A.C.W.S. (3d) 711 (the policy action and bad faith claims were severable because if the insured was unsuccessful in its contractual claim then the breach of good faith claims would "go away" and there would be a substantial savings in costs); *Stevens v. Sun Life Assur. Co. of Can.*, 2004 BCSC 468 (B.C.S.C.) (a bad faith claim against an insurer was stayed pending the resolution of a breach of contract issue where the insurer was entitled to the protection of its confidential corporate policies); *Norex Petroleum Ltd. v. Chubb Ins. Co. of Can.*, 2008 CarswellAlta 520 (Alta. Q.B., 2008) (finding the case was exceptional and the bad action should be severed from the contractual claims).

Bifurcation is not an absolute rule in bad faith claims where post-litigation conduct and solicitor-client privilege are raised. *Nayyar v Mfrs. Life Ins. Co.*, 2010 BCSC 1588.

Rules of Practice sometimes address issue bifurcation, but are not necessarily reflective of the common law position. *See for example*, Ontario Rule 5.05 which generally provides relief against joinder of claims that will result in prejudice. The courts in Ontario have historically been reluctant to grant the necessary bifurcation to achieve the purpose of this rule when plaintiffs plead claims in tandem.

Issue bifurcation was appropriate in New Brunswick where an insurance coverage case regarding the rejection of insurance benefits involves tort and contract-based claims for bad faith. *Walsh v. Nicholls*, 2004 NBCA 59 (N.B.C.A.).

### *Under what circumstances will the compensatory and punitive damages claims be bifurcated?*

As noted above, where the court perceives on the evidence that the punitive or bad faith claims will prejudice the fair adjudication of the contract claim, bifurcation should follow. However, where the contract claim has already been decided favorably to the policyholder, the likelihood of bifurcation between compensatory and punitive damages is remote as there are not the same prejudice issues perceived to be in play.

### *How does a bankruptcy petition (by either the insured or the insurer) affect the prosecution and defense of bad faith and extra-contractual claims?*

An insured's bankruptcy or insolvency results in an automatic stay of claims against the insured. For

claims made by a bankrupt insured, the cause of action will vest to the estate as an asset to be pursued at the discretion of the court and trustee. In *Future Health Inc. (Trustee of) v. State Farm Mutual Insurance Co. of Canada*, 2013 ONSC 6691, *leave to appeal refused* 2014 ONSC 356, the court refused to dismiss the bad faith action, as it was not plain and obvious that the bad faith claim could not be brought by the trustee in bankruptcy. The insurer unsuccessfully argued that the bad faith claim was an action *in personam*, and as such, could not vest in the trustee.

An insurer's bankruptcy or insolvency will result in an automatic stay of all claims against it. The party pursuing a stayed action may seek leave to lift the stay if it can demonstrate the claim will not reduce the target party's assets (*i.e.*, if there is E&O insurance or some other non-estate reserve to cover the claim against the insurer). Otherwise, such claims must be proven along with other unsecured creditors and, in the absence of a judgment, may have little or no value. Claims of this nature will not be answered by an industry fund set up to deal with insurer insolvency or bankruptcy.

In Ontario it appears a court will admit, for consideration purposes, a concession on the part of a bankrupt primary carrier of its previous bad faith conduct. *Plaza Fiberglas Mfg. Ltd. v. Cardinal Ins. Co.*, 1990 CarswellOnt 634 (O.S.C., H.C.J. 1990) (Proposition cited for upheld: a Court will admit a concession of bad faith on behalf of a bankrupt primary insurance carrier). The priority of such a claim as compared with other claims on policies issued by the company is doubtful until judgment is secured.

### *How does insolvency or the intervention of a state guaranty fund affect the prosecution and defense of bad faith and extra-contractual claims?*

This issue has not been addressed by Canadian courts, *but see* above.

## Defenses and Counterclaims

### *Is evidence regarding the reasonableness of the conduct of the insured or third party claimant admissible?*

In *Wachal v. Crown Life Insurance Co.* (1999), 14 CCLI (3d) 284 (Man. Q.B.), the court refused to allow an award of punitive damages at least in part because the plaintiff exaggerated her medical condition. This was corroborated with video surveillance evidence. (*See also* "Reverse Bad Faith" below).

### *Is "advice of counsel" a recognized defense?*

This has yet to be fully litigated. However, in *Wonderful Ventures Ltd. v. Maylam*, [2001] BCJ No. 1144 (B.C.S.C.), the court, in ordering bifurcation, confirmed that privileged information in the insurer's file was "relevant to the defense" of bad faith allegations, but privileged in the context of the contractual claim. *See also Lawrence v ICBC*, [2001] BCJ No 2516 (B.C.S.C.); *Sovereign Gen. Ins. Co. v ..Tanar Indus. Ltd.*, [2002] AJ No 107 (Alta. Q.B.); and *Brennand v. Sun Life Assurance Co. of Canada*, 2011 BCSC 759.

Some courts have held that where a party attempts to justify its position "on the grounds of detrimental reliance upon the legal advice received," it waives the privilege associated with that legal advice. *Guelph (City) v. Super Blue Box Recycling Corp.* (2004), 2 CPC (6th) 276 (Ont. S.C.J.) (citing *Davies v. Am. Home Assurance Co.* (2002), 60 OR (3d) 512 (Ont. Div. Ct.) and *Sovereign Gen. Ins. Co. v Tanar Indus. Ltd.*, [2002] AJ No 107 (Alta. Q.B.)). However, a recent Ontario decision affirms that litigation privilege always trumps claims of bad faith. One court has held there is no "bad faith exception" to the litigation privilege rule. *See Kavanagh v. Peel Mutual Insurance Co.*, 2009 CarswellOnt 6377 (Ont. S.C.J. 2009) (citing *Davies v. Am. Home Assurance Co.* (2002), 60 OR (3d) 512 (Ont. Div. Ct.)). In contrast, in *Keane v. Dominion of Canada General Insurance Co.*, 2008 CarswellOnt 8233 (Ont. S.C.J. 2008), the insurer had to produce its claims file in a sealed envelope for the court so a determination could be made as to which portions had to be produced to the insured. It was held that material covered by litigation privilege had to be disclosed if relevant to claim of bad faith conduct. Cases

involving the production of otherwise privileged documents raise the issue of bifurcation.

A B.C. Court has held that a request by an insurer for legal advice, without more, cannot found a claim based on either bad faith or negligence. *Pearlman v. Am. Commerce Ins. Co.*, 2009 CarswellBC 387 (C.A.).

### *What other defenses are available?*

The Ontario Court of Appeal has suggested in *Khazzaka v. CGU Insurance Co. of Canada*, [2002] OJ No 3110, [2003] I.L.R. I-4138, 115 A.C.W.S. (3d) 984, 162 O.A.C. 293, 28 C.P.C. (5th) 15, 43 C.C.L.I. (3d) 90, 66 O.R. (3d) 390, that because the insurer's duty of good faith extends right up to the date of trial, evidence of a review process at regular intervals would be admissible and relevant in the bad faith claim. The suggestion is that if the insurer demonstrates a claims review process that is fair in all respects, even if it proves to be mistaken, an insurer will have discharged its good faith duty.

Cases that hold there must be a valid and favorably decided action on the policy before an ongoing bad faith claim will crystallize suggest that a bad faith action may be defended on the basis that the insured does not have a valid and favorably decided action on the policy. *Forestex Mgmt. Corp. v. Underwriters at Lloyd's*, 2004 FC 1303 (F.C.C.).

### *Is there a cause of action for reverse bad faith?*

Alberta courts recognize claims for "reverse" bad faith and will award punitive damages against policyholders. *See Andrusiw v. Aetna Life Ins. Co. of Can.* (2001), 33 CCLI (3d) 238 (Alta. Q.B.) and *Haiduc v. Alberta Motor Ass'n Ins. Co.*, [2003] AJ No 392 (Alta. Q.B.). In addition to obtaining punitive damages the insurer may also receive an increased costs award at the end of the trial. *See Al-Asadi v. Alberta Motor Ass'n Ins. Co.*, [2003] 7 WWR 92 (Alta. Q.B.).

According to the B.C. Court of Appeal, an insured's breach of the duty of good faith is an actionable wrong that is independent of a breach of contract claim and can form the basis of a claim for punitive damages. *Asselstine v. Mfrs. Life*, 2005 BCCA 292, 22 CCLI (4th) 169 (C.A.), *additional reasons in* 2005 BCCA 465, 26 CCLI (4th) 68 (CA) (citing *Fidler v. Sun Life Assur. Co. of Canada*, 2004 BCCA 273 (B.C.C.A.)).

Similarly, it is "trite law" in Ontario that conduct amounting to a breach of good faith by an insured will disentitle the insured relief against forfeiture. *Can. Newspapers Co. v. Kansa Gen. Ins. Co.*, [1996] ILR I-3369 (Ont. C.A.).

In the absence of other higher level authority, reverse bad faith remains an open question in many Canadian jurisdictions.

## Other Significant Cases Involving Bad Faith and Extracontractual Claims

The financial vulnerability of the insured and the insurer's exploitation of this will be a significant factor in assessing availability and quantum of extra-contractual damages. *See Whiten v. Pilot Insurance Co.*, [2002] 1 SCR 595 (S.C.C.); *Clarfield v. Crown Life Ins.*, [2000] OJ No 4074 (Ont. S.C.J.).

The setting of artificially low reserves for a loss may represent an act of bad faith on the part of the insurer. Discovery was permitted on this issue. *Osborne v. Non-Marine Underwriters, Lloyd's of London* (2003), 5 CCLI (4th) 124 (Ont. S.C.J.). However, the information relating to the setting of reserves per se does not have a semblance of relevance in an insurance bad faith action. *Lin (Litig. Guardian of) v. Belair Ins. Co.*, 2009 CarswellOnt 8215 (Ont. Mas. 2009).

There is conflicting authority in Canada as to whether or not an insured can assert a separate bad faith action against the adjuster or other employees of the insurer arising out of the manner in which the insured's claim was handled. In *Spiers v. Zurich Insurance Co.* (1999), 45 OR (3d) 726 (S.C.J.) (Upheld: Appellant court refused leave to appeal), a concurrent bad faith claim against the insurance adjuster was allowed to continue alongside the claim against the insurers. In *Burke v. Buss*, [2002] OJ No 2938 (Ont. S.C.J.), the court refused to follow *Spiers*. In Alberta, the court ordered a bad faith claim against an adjuster to trial owing to the conflicting case law on point. *Abassi v. Portage La Prairie Mut. Ins. Co.*, 2003 ABQB 760, [2003] I.L.R. I-4235, [2003] A.W.L.D. 501, [2003] A.J. No. 1118, [2004] 3 W.W.R. 665, 125 A.C.W.S. (3d) 245, 23 Alta. L.R. (4th) 293,

347 A.R. 275, 5 C.C.L.I. (4th) 34. One appellate decision suggests the possibility of extending the tort of bad faith to adjusters in cases where there is a malicious intent, on the part of the adjuster, to harm the insured. *Walsh v. Nicholls*, 2004 NBCA 59 (N.B.C.A.).

The insurer's duty of good faith and fair dealing puts the onus on the insurer to make available for inspection by an insured, at any time until a claim is resolved, those documents in the insurer's possession or control which will allow an insured to satisfy himself that his claim has been handled by the insurer in good faith and that he has been dealt with fairly. *Alexander v. Great-West Life Assurance Co.*, 2004 NBQB 285 (N.B. Q.B., 2004).

The proposition that an insurer may never settle claims against their policies unless the settlement involves all insureds has been rejected in Ontario. However, an insurer must only accept reasonable settlement offers or else the insurer risks breaching its duty of good faith. *Hollinger Int'l Inc. v Am. Home Assur. Co.*, 2006 CarswellOnt 188 (Ont. S.C.J.).

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