



# The Supreme Court in Flames: Fire Insurance Decisions after Kosmopoulos

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# The Supreme Court in Flames: Fire Insurance Decisions after Kosmopoulos

## **Abstract**

This article examines three recent Supreme Court of Canada decisions on fire insurance after the historic Kosmopoulos decision. In all three cases, the author finds a distressing lack of concern with relevant statutory provisions, policy arguments, and precedent. Responsibility for this deplorable state of affairs must be shared between the Court and counsel. Insurance law is a very complex body of law, deserving as much care as that of, say, the law of the Charter.

# THE SUPREME COURT IN FLAMES: FIRE INSURANCE DECISIONS AFTER *KOSMOPOULOS*®

BY REUBEN A. HASSON\*

This article examines three recent Supreme Court of Canada decisions on fire insurance after the historic *Kosmopoulos* decision. In all three cases, the author finds a distressing lack of concern with relevant statutory provisions, policy arguments, and precedent. Responsibility for this deplorable state of affairs must be shared between the Court and counsel. Insurance law is a very complex body of law, deserving as much care as that of, say, the law of the *Charter*.

Cet article examine trois arrêts récents de la Cour suprême du Canada sur l'assurance-incendie après l'arrêt historique de *Kosmopoulos*. Dans les trois arrêts, l'auteur constate un manque de souci décourageant à l'égard des dispositions des lois, arguments politiques et précédents. La responsabilité pour cette situation déplorable doit se partager entre la Cour et les avocats. Le droit de l'assurance est un domaine très complexe qui mérite autant d'attention que, disons, le droit de la *Charte*.

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## I. INTRODUCTION

In *Kosmopoulos v. Constitution Insurance Co.*,<sup>1</sup> the Supreme Court of Canada allowed a plaintiff, who owned all of the shares in a company, but who had insured the company's property in his own name rather than in the company's name, to recover on the policy from the insurer when the property was destroyed by fire.<sup>2</sup> This seemingly obvious result was produced by the most impressive insurance law decision the Supreme Court has given in its entire history. The Court examined the precedents carefully and critically. The relevant academic writings were put to intelligent use and the policy issues in the case were meticulously examined. To some commentators, it seemed difficult to believe that this was the same Court whose previous insurance decisions, until then, had displayed a lack of learning and had resolutely failed to address any of the policy issues at stake.

The purpose of this article is to show that, in three decisions since *Kosmopoulos*, the Court has returned to its old ways and to explain why this might be so. In fact, these decisions may be worse than any of the insurance decisions from 1875-1980. Before discussing these three cases in detail, the significance of the *Kosmopoulos* decision must be examined: first, to show its significance; and second, because it is

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<sup>1</sup> [1987] 1 S.C.R. 2, aff'g (1983), 42 O.R. (2d) 428 (C.A.), aff'g [1981] I.L.R. 539 (Ont. S.C.) [hereinafter *Kosmopoulos*]. Wilson J. gave a judgment on behalf of five members of the court; McIntyre J. would simply have reversed the decision in *Macaura v. Northern Assurance Co.*, [1925] A.C. 619 (H.L.).

<sup>2</sup> For comments on the lower court decisions, see J.S. Ziegel, "Shareholder's Insurable Interest—Another Attempt to Scuttle the *Macaura v. Northern Assurance Co.* Doctrine: *Kosmopoulos v. Northern Assurance Co.*" (1984) 62 Can. Bar Rev. 95; M.G. Baer, Annotation (1983), 1 C.C.L.I. 83; and L. Stuesser, "Insurable Interest: The Supreme Court of Canada Adopts the Factual Expectancy Test, 1987-88" (1987-88) 13 C.B.L.J. 226, who points out that the case did not have a happy ending. Stuesser writes, at 228 [citations omitted]:

The Supreme Court's final judgment was delivered almost 10 years after the fire that gave rise to the action. What has happened to Mr. Kosmopoulos in the interim? The story is not a happy one. He managed to reopen the store without the benefit of insurance money. He borrowed. He eventually was forced to sell his home. In 1980, was forced to close the store. Mr. Kosmopoulos, a former self-employed small businessman, turned to a factory job.

relevant to the first of three cases I propose to examine, that of *Scott v. Wawanesa Mutual Insurance Co.*<sup>3</sup>

## II. THE IMPORTANCE OF *KOSMOPOULOS*

In any system of law that recognizes the existence of private property, it will be necessary to distinguish insurance from wagering or betting.<sup>4</sup> Legitimate insurance involves the protection of property, the destruction of which causes loss to the insured.<sup>5</sup> Usually, the insured will own or have some other property interest in the property which is damaged or destroyed, but this need not be so. The insured may seek to insure public property, such as a road, damage to which would cause him or her loss.<sup>6</sup> Similarly, a lender of money for the construction of a property will want to be able to insure the property against loss.<sup>7</sup> When wagering, one is not seeking to protect against economic loss; the object here is to make a windfall gain. Thus, suppose I am convinced that a building, in whose damage or destruction I have no interest beyond that of any other citizen, will collapse within a year. If I enter into a contract with an insurer to pay me \$50,000 if the building collapses within a year, and it does, I cannot collect from the insurer, however formal my contract may appear to be. The court will deny me the \$50,000 because I

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<sup>3</sup> [1989] 1 S.C.R. 1445 [hereinafter *Scott*]. For an effective criticism of this decision, see N. Rafferty, "Developments in Contract and Tort Law: The 1988-89 Term" (1990) 1 Supreme Court L.R. (2d) 269 at 311-18; for an earlier critique, see M.G. Baer, "Recent Developments in Canadian Law: Insurance Law" (1985) 17 Ottawa L. Rev. 631 at 643-48.

<sup>4</sup> But see the comments of L.C.B. Gower, *Review of Investor Protection*, vol. 1 (London: H.M.S.O., 1982) at 27, para. 4.04 [citations omitted], showing that the line is not absolutely clear:

Another problem that has caused difficulty in recent months is that of distinguishing between legitimate investments and unenforceable gaming contracts. The public have been offered arrangements ranging from betting on whether the quoted price of a listed stock on an index (such as the FT Index) will rise or fall to entrusting a capital sum to a company to invest and to use the income to bet on race horses. On the face of it, all of these seem more akin to gaming and wagering contracts and therefore unenforceable. On the other hand, in the former type the objectives of the participants may be indistinguishable from those when purchasing options or futures. To treat them as gaming contracts would be the worst possible way of protecting investors. The Act must

<sup>5</sup> The classic article is by B. Harnett & J.V. Thornton, "Insurable Interest in Property: A Socio-Economic Reevaluation of a Legal Concept" (1948) 48 Colum. L. Rev. 1162.

<sup>6</sup> *Farmers' Mutual Insurance Co. v. New Holland Turnpike Road Co.*, 122 Pa. 37 (1888), which held that there was no insurable interest.

<sup>7</sup> *Guarantee Co. of North America v. Acqua-Land Exploration Ltd.*, [1966] S.C.R. 133 [hereinafter *Guarantee*].

am betting. Although the courts, at one time, enforced wagering agreements with some enthusiasm,<sup>8</sup> they do not do so at the present time.<sup>9</sup>

All this seems elementary. If the courts had followed the decision of Lawrence J. in *Lucena v. Craufurd*,<sup>10</sup> the line would have been clear. In that case, the Judge held that an insured could recover if she suffered "factual expectation of loss." Unfortunately, Lawrence J. had the misfortune to sit with Eldon L.C. who sought to improve Lawrence J.'s definition of insurable interest by requiring that, in addition to a loss, the plaintiff must have a "legal or equitable interest" in the property. Eldon L.C. sought to show that if Lawrence J.'s definition of "insurable interest" were to prevail an ordinary seaman would be able to insure the ship in which he sailed. The fact that seamen did not earn enough to do this does not seem to have occurred to Eldon L.C., who seems to have made delay, rather than common sense, the touchstone of his insurance decisions.<sup>11</sup> Having insured the ship in which he had sailed, the sailor would then (in Eldon L.C.'s logic) seek to insure the next ship in which he sailed, and so on, *ad infinitum*. The point here is that no seaman would have had the resources to insure any ship. Moreover, the insurer of the ship would only want to deal with the master (or owner) of the ship. Unfortunately, it was Eldon L.C.'s test rather than Lawrence J.'s that was to prevail, with the result that many legitimate insurances were treated as unenforceable bets.<sup>12</sup>

#### A. Turning Insurance Contracts into Wagers

Under Eldon L.C.'s test, buyers of goods had no insurable interest unless they could show either that they would have received

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<sup>8</sup> See, for example, *March v. Pigot* (1771), 5 Burr. 2802, 98 E.R. 471 (K.B.) (wager on survivorship of fathers of the wagerers); and *Hussey v. Crickitt* (1811), 3 Camp. 168, 170 E.R. 1343 (C.P.) (wager on who was older).

<sup>9</sup> See *supra* note 4.

<sup>10</sup> (1806), 2 Bos. & Pul. (N.R.) 269, 127 E.R. 630 (C.P.) [hereinafter *Lucena*], *aff'd* (1808), 1 Taunt. 325, 127 E.R. 858 (H.L.).

<sup>11</sup> See the essay by W. Hazlitt, "Lord Eldon and Mr. Wilberforce" in W. Hazlitt, *The Spirit of the Age* (Menston, Eng.: Scholar Press, 1971) at 234. Hazlitt writes of Eldon L.C., at 238: "He delights to balance a straw, to see a feather turn the scale or make it even again, and divides and subdivides a scruple to the smallest fraction. ... Delay seems, in his mind, to be of the very essence of justice."

<sup>12</sup> See Gower, *supra* note 4 at 27.

specific performance<sup>13</sup> or that property in the goods had passed to them.<sup>14</sup> It is true that terms such as cash insurance freight (CIF) and freight on board (FOB) removed many uncertainties here, but there were still many unresolved problems. In cases where the plaintiff had to demonstrate either the availability of specific performance or the passage of property as a basis for obtaining an insurable interest, it would frequently require a trial and an appeal to determine these questions. A lender who lent money for a construction project would have no insurable interest, unless he or she had taken out a security interest in the property.<sup>15</sup> Unsecured creditors had no insurable interest in the property.<sup>16</sup>

In *Kosmopoulos*, the Supreme Court, by adopting Lawrence J.'s test of "factual expectation" of loss in *Lucena*, made it possible for these (and other) insureds to recover.<sup>17</sup> Before the decision in *Kosmopoulos*, the subject of insurable interest had been a bonanza for insurers and examiners in insurance law. For the ordinary citizen, who was legally unadvised or advised incompetently, the law presented a trap. It was a disgrace that judges and lawyers had to read hundreds of pages of judicial decisions before they could advise on whether the contract was enforceable.<sup>18</sup> If the *Kosmopoulos* case did not consign libraries to the scrap heap, it relegated many arcane decisions to the junk heap. No other Canadian decision in insurance law has had that beneficial effect. Those commentators who thought that *Kosmopoulos* represented a new approach by the Supreme Court to the resolution of insurance problems were soon gravely disappointed.

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<sup>13</sup> In Canadian law, specific performance is very seldom decreed outside of contracts for the disposition of interests in land.

<sup>14</sup> Although a reading of the Ontario *Sale of Goods Act*, R.S.O. 1990, c. S.1, s. 19, regarding the passing of property, leads one to believe that property passes once the contract is made, either shipment or delivery is generally necessary to transfer property. See, for example, *Carlos Federspiel & Co. S.A. v. Charles Twigg & Co.*, [1957] 1 Lloyd's Rep. 240 (Q.B.).

<sup>15</sup> See *Guarantee*, *supra* note 7.

<sup>16</sup> See generally E.W. Patterson & H.J. McIntyre, "Unsecured Creditor's Insurance" (1931) 31 Colum. L. Rev. 212.

<sup>17</sup> See *Clark v. Scottish Imperial Insurance Co.* (1879), 4 S.C.R. 192.

<sup>18</sup> In just over twenty years, three decisions on insurable interest were heard by the Supreme Court of Canada: *Guarantee*, *supra* note 7; *Wandlyn Motels Ltd. v. Commerce General Insurance Co.*, [1970] S.C.R. 992; and *Kosmopoulos*, *supra* note 1. In addition, there were scores of provincial decisions both at the appellate level and at first instance: see D. Dumais, *Insurable Interest in Property Insurance Law* (LL.M. Thesis, Osgoode Hall Law School, York University, 1986).

1. Visiting the sins of the children on their parents: *Scott v. Wawanesa Insurance Co.*<sup>19</sup>

Since at least the middle of the nineteenth century, all members of the insured family living in their home were listed as insureds in home insurance policies. This did not mean that they all owned the property. For one thing children could not own property, nor could women at that date.<sup>20</sup> The purpose of listing the wife and children as insureds was to protect their personal property. If they did not list their personal property, they ran afoul of what is now section 148(2) of the Ontario *Insurance Act*.<sup>21</sup> The notion that if the spouse's child burned down the house then the owners would be disqualified was not argued until 1979. In the following year, it was successfully argued that a wife, even if she was not listed as an insured, who set fire to the matrimonial home, disqualified both herself and her innocent spouse from recovery.

In *Rankin v. North Waterloo Farmers Mutual Insurance Co.*,<sup>22</sup> the Ontario Court of Appeal had to decide whether a fire started by a retarded sixteen-year-old son of the parents, all of whom were described as the insureds in the policy, defeated the right of the parents to recover. In a fine opinion, Weatherston J.A. canvassed English, Canadian, and American decisions and showed that the case law in these jurisdictions refused to deprive an insured of coverage because of the misconduct of a co-insured. The British Columbia Supreme Court, two years after *Rankin* was decided, held that, although a wife who set fire to her husband's property was not listed as an insured, she destroyed his right to the property as well.<sup>23</sup> By the time the *Scott* case was decided by the Supreme Court in 1989,<sup>24</sup> the Ontario<sup>25</sup> and Newfoundland courts<sup>26</sup>

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<sup>19</sup> *Supra* note 3.

<sup>20</sup> See C.B. Backhouse, "Married Women's Property in Nineteenth-Century Canada," (1988) 6 *Law & Hist. Rev.* 211.

<sup>21</sup> R.S.O. 1990, c. I.8.

<sup>22</sup> (1980), 100 D.L.R. (3d) 564 (Ont. C.A.) [hereinafter *Rankin*].

<sup>23</sup> See *Wiens v. Fireman's Fund Insurance Co. of Canada*, [1981] I.L.R. 443 (B.C.S.C.) [hereinafter *Wiens*].

<sup>24</sup> *Supra* note 3.

<sup>25</sup> See *Rankin*, *supra* note 22; and *Higgins v. Orion Insurance Co.* (1985), 50 O.R. (2d) 352 (C.A.), regarding partnership.

<sup>26</sup> See *Murdock v. Commercial Union Assurance Co.* (1981), 30 Nfld. & P.E.I. R. 311 (Nfld. S.C.); and *Walsh v. Canadian General Insurance Co.* (1988), 70 Nfld. & P.E.I. R. 89 (Nfld. S.C.). In these two cases, the Newfoundland Courts used the *Fire Insurance Act*, R.S.N. 1970, c. 30, s. 11(b)



protected the innocent party, whereas the courts of British Columbia penalized the innocent party.<sup>27</sup>

We have seen that the rationale for listing dependent children and non-owning spouses as insureds in the policy was to protect their personal property. A different rationale for this rule was offered by Larry Gilbertson in the Law Society of Upper Canada Special Lectures on Insurance in 1987.<sup>28</sup> According to Gilbertson, “[o]ne of the practical reasons for this exclusion is that there is so much potential for collusion between assureds. It may be very difficult to obtain evidence to prove the complicity of the other assured or assureds.”<sup>29</sup> The same Eldon-like<sup>30</sup> thinking was echoed in the Wawanesa Insurance Co.’s factum before the Supreme Court of Canada. The factum stated in part:

The exclusion of the coverage for the deliberate acts of members of the Scott household is in no way unreasonable. ... He (a member of the household) has inside knowledge of the times at which the house will be empty. He can be seen loitering about the property without attracting attention. In addition, he is subject to family and personal pressures from other members of the household which may provide a motive for arson absent in outsiders.<sup>31</sup>

Unfortunately, this rationale for disqualifying all insureds, after a fire had been started by a fifteen year old living at home, was not addressed by the appellant’s factum in the *Scott* case. Nor did the Supreme Court deal with this alleged reason for the clause. In fact, the rationale is absurd.<sup>32</sup> A dishonest insured would most likely look for a professional arsonist to do the job. The professional arsonist will provide skill and divert suspicion from the owner of the property.<sup>33</sup> If insureds employ their teenagers to set fire to the matrimonial home there is a serious risk that the job will be botched, and that the youth will

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(now R.S.N. 1990, c. F-10, s. 11(b)) to nullify an “unreasonable” term in a fire insurance policy. For the corresponding Ontario provision, see the *Insurance Act*, *supra* note 21, s. 151(b).

<sup>27</sup> See *Wiens*, *supra* note 23; and *Zouzounas v. Royal Insurance Co. of Canada* (1984), 5 C.C.L.I. 207 (B.C.S.C.).

<sup>28</sup> See “Multiple Assureds: Does the Wrongdoing of One Contaminate the Rights of the Innocent?” in Law Society of Upper Canada, *Special Lectures on Insurance Law* (Toronto: L.S.U.C., 1987) 211.

<sup>29</sup> *Ibid.*

<sup>30</sup> See *supra* notes 10-12 and accompanying text.

<sup>31</sup> Respondent’s Factum, *Scott*, *supra* note 3, File No. 20161, on file with the Supreme Court of Canada at 5.

<sup>32</sup> In the voluminous literature on insurable interest in property over two centuries, I know of no writer or judge who has advanced the possibility of disqualifying all insureds in this context.

<sup>33</sup> Even if the adult insured commits arson, he or she will often see to it that the property is overinsured: see *Harnett & Thornton*, *supra* note 5 at 1183.

suffer serious injury, or death, particularly if the teenager is mentally retarded, or disturbed.<sup>34</sup> Even if successful, there is the risk that the youth will be indiscreet and boast of his or her prowess.

The respondent's factum cited *Bryant*,<sup>35</sup> a case in which the husband had burned down the matrimonial home. A United States District Court, applying Kentucky law, held that the wife was not entitled to recover. In the course of his opinion, Bertelsman D.J. held, denying recovery to the wife, that "[t]o accept the emotionally appealing argument of the plaintiff would be to rewrite the policy and impose upon the insurance company a risk that it did not insure."<sup>36</sup> By citing this case, the respondent made it appear that Kentucky law, and those states that follow the same rule, represents the American position. In fact, as one might expect, the American cases are split, with a majority giving protection to the innocent spouse, (or to innocent spouses, where the fire had been started by their child(ren)).<sup>37</sup> The appellant's factum does not cite a single American authority, and many of the authorities cited have nothing to do with the protection of joint interests.<sup>38</sup> In citing the old law about the role of the court's function being to interpret, rather than rewrite the policy, the respondent's factum must have struck a sympathetic chord with all members of the Supreme Court. It is anathema for the courts to admit that they rewrite insurance contracts, even though they frequently do.<sup>39</sup>

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<sup>34</sup> This was the situation in the *Rankin* case: see *supra* note 22 and accompanying text.

<sup>35</sup> *Bryant v. Allstate Insurance Co.*, 592 F. Supp. 39 (E.D. Ky. 1984) [hereinafter *Bryant*].

<sup>36</sup> *Ibid.* at 41.

<sup>37</sup> In recent years, a majority of jurisdictions have allowed the innocent party to recover: see R.E. Keeton & A.I. Widiss, *Insurance Law* (St. Paul, Minn.: West, 1988) at 516 [citations omitted], who write:

[I]t is generally recognized that when a structure is destroyed as the result of arson committed by someone who has no connection with the insured owner, fire insurance will provide indemnification for the owner. Furthermore, the concept underlying such decisions—that the loss is a fortuity from the vantage point of the insured—has been extended to an innocent insured when a fire was intentionally set by a co-owner of a property who was also an insured.

<sup>38</sup> Two of the five cases cited deal with the law of insurable interest before *Kosmopoulos*, *supra* note 1. The factum does not cite the relevant Canadian authorities on the subject.

<sup>39</sup> See, for recent examples, *Inn. Cor International Ltd. v. American Home Assurance Co.* (1973), 2 O.R. (2d) 64 (C.A.); and *Wigle v. Allstate Insurance Co. of Canada* (1984), 49 O.R. (2d) 101 (C.A.).

a) *Scott v. Wawanesa Insurance Co.: The opinions*

At first instance, Wood J. refused to give judgment for the insurer.<sup>40</sup> He followed *Rankin*<sup>41</sup> which had canvassed fully the American authorities. The British Columbia Court of Appeal, in a judgment by McDonald J.A.,<sup>42</sup> sought to extend the rationale of *Kosmopoulos* to the point of absurdity; in its view, young Scott “would benefit by the continued existence of the dwelling.”<sup>43</sup> But this alone cannot be enough to give a teenager living at home an insurable interest. On the same basis, friends of the Scott family, who occasionally visited the Scotts, would be able to insure the Scott’s home. This is not the kind of interest that *Kosmopoulos* intended to give. The second ground given by the Court was that the clause was unambiguous:

It is unnecessary to decide whether the indemnification obligation is joint or several. The exclusionary clause is unambiguous. Assuming the position more [sic] favourable to the respondents, that it is several, the exclusionary clause bars recovery where the loss is caused by a wilful act of the insured.<sup>44</sup>

The Court of Appeal’s finding that the exclusionary clause is unambiguous is startling in view of the fact that both Canadian courts<sup>45</sup> and American courts<sup>46</sup> are evenly divided on its interpretation. Indeed, when it decided the appeal, the Supreme Court of Canada itself split 4-3 on the interpretation of an allegedly unambiguous clause.

A majority of the Supreme Court affirmed the decision of the British Columbia Court of Appeal.<sup>47</sup> L’Heureux-Dubé J. stressed the same two factors that had been relied upon by the Court of Appeal. Once again, *Kosmopoulos* was inflated beyond its proper scope. In the majority’s words:

even if we were to accept the more narrow definition suggested by the appellants, it would be impossible to say that the insurable interest of the infant Charles Scott was

<sup>40</sup> (1984), 13 D.L.R. (4th) 752 (B.C.S.C.).

<sup>41</sup> *Supra* note 22.

<sup>42</sup> (1988), 30 D.L.R. (4th) 414 (B.C.C.A.).

<sup>43</sup> *Ibid.* at 418.

<sup>44</sup> *Ibid.* at 420.

<sup>45</sup> See *supra* notes 25-27.

<sup>46</sup> See *supra* note 37 and accompanying text.

<sup>47</sup> *Scott*, *supra* note 3. L’Heureux-Dubé J. gave the judgment of the majority with McIntyre J., Lamer J. (as he then was), and Wilson J. concurring. La Forest J. gave a dissenting opinion with Dickson C.J. (as he then was) and Sopinka J. concurring.

limited to his personal possessions. He had a direct relationship to the family home and its contents, since they were his source of accommodation and support.<sup>48</sup>

An insurable interest is not, as the majority seems to think, something that can be thrust on an individual, to that person's disadvantage. The whole concept of insurable interest is meant to benefit an insured, who, consciously, seeks to protect some property, the damage or destruction of which, will prejudice the insured. The teenage Scott neither intended to protect the property he was living in, nor did he have the contractual capacity to do so. Having rescued the law of insurable interest from a morass of absurdity in *Kosmopoulos*, two years later the same Court has created a different swamp for the concept.

La Forest J. gave a convincing dissenting judgment for the minority. He rightly stressed that the purpose of adding teenagers as insureds was to protect their personal property. This judgment has since come in for sharp criticism from de Grandpré<sup>49</sup> as reflecting the poor quality of recent Supreme Court of Canada decisions. For de Grandpré, the minority violated "la doctrine classique"<sup>50</sup> which was well-stated, in his view, in *MacGillivray & Parkington on Insurance Law*:

A Court will not require the parties to have reached separate agreement on the terms of the insurance apart from the essential terms described above. When an applicant seeks insurance over from a particular insurer, he impliedly offers to take an insurance on the insurers usual or standard terms of cover.<sup>51</sup>

The notion that a policy only has one meaning is not classical, or any other kind of, law; words of a policy can be read in different ways and this has always been the case. De Grandpré, when he was on the bench, found that the interpretation of insurance policies by appellate courts were sometimes wrong, and then for good measure, introduced sociological factors to justify his decision. In *Commonwealth Construction Co. v. Imperial Oil Ltd.*,<sup>52</sup> the principal contractor and the subcontractor were insured as co-insureds. The Alberta Supreme Court (Appeal Division), nevertheless, held that the principal contractor could sue the subcontractor for damage caused by it, to the principal contractor. Writing for the Supreme Court, de Grandpré J. reversed the

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<sup>48</sup> *Ibid.* at 1467.

<sup>49</sup> See L.-P. de Grandpré, "La Cour Suprême du Canada: Ses Jugements Récents en Assurance" (1993) 61 *Assurances* 31.

<sup>50</sup> *Ibid.* at 34.

<sup>51</sup> *Ibid.* at 35, citing M. Parkington, *MacGillivray and Parkington on Insurance Law*, 8th ed. (London: Sweet & Maxwell, 1988) at 90-91.

<sup>52</sup> [1978] 1 S.C.R. 317, rev'g (1974), 46 D.L.R. (3d) 399 (Alta. S.C. (A.D.)).

court below. In reaching his conclusion, he stressed the inconvenience and delay that would be caused on a building site, if the various parties could sue one another.<sup>53</sup> This is a radically bolder decision than the dissent of the minority in *Scott*. It appears, therefore, that de Grandpré does not, himself, take the “doctrine classique” too seriously.

Another disappointing feature of *Scott* is that Wilson J., who wrote the court’s opinion in *Kosmopoulos*, subscribed to the majority view in *Scott*. Unlike her truly radical decision in *Kosmopoulos*, the decision in *Scott* is purely formalistic. In her well-known Betcherman lecture,<sup>54</sup> Wilson J. spoke of areas of the law where:

the principles and the underlying premises are so firmly entrenched and so fundamentally sound that no good would be achieved by attempting to re-invent the wheel. ... I have in mind areas such as the law of contract.<sup>55</sup>

In *Kosmopoulos* Wilson J., interestingly enough, was prepared to play the role of (re)inventor. In *Scott*, her role was quite the opposite. Wilson J. asked none of the questions one would have expected her to ask, such as “why is the teenager listed as an insured?” Had she asked this question, she would have found that the purpose of listing the teenager was to protect his personal property.

The above quotation is a startling statement from Wilson J. considering that her decision for the Court in *Kosmopoulos* was truly a radical one. What the Court achieved in that case has not been achieved in the United States or Great Britain. It was a change that had to be made by legislation in Australia.<sup>56</sup> Yet, in *Scott*, Wilson J. put her name to a purely formalistic opinion. It is also bizarre that a self-professed champion of women’s rights should, unwittingly, have destroyed the wife’s principal asset—her half-share in the home. Almost invariably, the wife will be at a disadvantage in competing in the labour market after her loss.<sup>57</sup> A wife is also prejudiced by the destruction of her husband’s property interest in a case like *Scott*. If she is the beneficiary under his will, she will recover less. If the marriage breaks down, the

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<sup>53</sup> *Ibid.* at 319-30.

<sup>54</sup> B. Wilson, “Will Women Judges Really Make a Difference?” (1990) 28 *Osgoode Hall L.J.* 507.

<sup>55</sup> *Ibid.* at 515. For a good critique of Wilson J.’s views from a feminist corporate and tax lawyer, see M. Maloney, “Economic Actors in The Work of Madame Justice Wilson” (1992) 15 *Dalhousie L.J.* 197.

<sup>56</sup> See *Insurance Contracts Act*, 1984, Austl. Acts P. 1983, vol. 1, no. 80, s. 17.

<sup>57</sup> See, for example, J.A. Fudge, “Reconceiving Employment Standards Legislation: Labour Law’s Little Sister and the Feminization of Labour” (1991) 7 *J.L. & Social Pol’y* 73.

husband will have less money with which to pay maintenance. These (and other) dire consequences arise from viewing the law of contract as being in a state of near perfection.<sup>58</sup>

b) *Developments After Scott v. Wawanesa Insurance Co.*

In *Peters (Trustee of) v. Fireman's Fund Insurance Co. of Canada*,<sup>59</sup> the husband set fire to the house he jointly owned with his wife. At first instance, the trial Judge held that the wife had no insurance claim, following the *Scott* case. The Court of Appeal for the Northwest Territories held that a whole range of inquiries had to be made including "were Mr. and Mrs. Peters both occupying the house on the date of the fire? If not, when were they separated or divorced?"<sup>60</sup> The Court does not explain the significance of these findings. Perhaps, if the trial Judge found in a new trial that the spouses were cohabiting, *Scott* would apply, whereas, if they were divorced or separated, the courts might seek to protect the wife's property. But this is only a guess. One can understand the desire on the part of the lower courts to create exceptions to unjust rules, but an uncertain rule combined with exceptions of uncertain scope seems to offer the worst of both worlds.

III. NON-DISCLOSURE IN FIRE INSURANCE: *FORD V. DOMINION OF CANADA GENERAL INSURANCE CO.*<sup>61</sup>

A. *Introduction: Common Law Fraud v. Equitable Fraud*

In this section it will be necessary to distinguish between common law fraud and its equitable counterpart. A fraudulent statement at common law was defined in a series of cases stretching from *Pasley v. Freeman*<sup>62</sup> to *Derry v. Peek*<sup>63</sup> and *Nocton v. Ashburton*.<sup>64</sup> A reasonable working definition of fraudulent misrepresentation (or

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<sup>58</sup> See the text accompanying *supra* note 55.

<sup>59</sup> [1992] N.W.T.R. 193 (C.A.).

<sup>60</sup> *Ibid.* at 196.

<sup>61</sup> [1991] 1 S.C.R. 136 [hereinafter *Ford*].

<sup>62</sup> (1789), 3 Term. Rep. 51, 100 E.R. 450 (K.B.).

<sup>63</sup> (1889), 14 App. Cas. 337 (H.L.).

<sup>64</sup> [1914] A.C. 932 (H.L.).

deceit) was given by Cairns L.C. in *Peek v. Gurney*.<sup>65</sup> For there to be deceit, Cairns L.C. stated that:

[T]here must ... be some active misstatement of fact, or, at allevents such a partial and fragmentary statement of fact as that the withholding of which is not stated makes that which is stated absolutely false.<sup>66</sup>

To this definition, there should be added two minor extensions. A person who gives an opinion may incur liability for deceit, provided that the statement of opinion is made with an intent to deceive another party to her detriment.<sup>67</sup> Finally, liability for deceit can be incurred solely by conduct. If the seller of a home covers over serious cracks in the floors or walls so as to mislead the purchaser into thinking that the house was in good structural shape, this behaviour would be treated as common law fraud.<sup>68</sup>

### B. *Equitable Fraud*

In the nineteenth century, the concept of "equitable fraud" also existed. As my colleague David Vaver says, this concept became a "passe partout"<sup>69</sup> for striking down unfair bargains where there had been no fraud. Over time, some close relationship between the parties was required so that the weaker party was protected unless he or she got independent advice; these relationships include parent and child,<sup>70</sup> guardian and ward,<sup>71</sup> religious adviser and disciple,<sup>72</sup> doctor and patient,<sup>73</sup> solicitor and client,<sup>74</sup> and trustee and *cestui que trust*.<sup>75</sup>

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<sup>65</sup> (1873), L.R. 6 H.L. 377.

<sup>66</sup> *Ibid.* at 403.

<sup>67</sup> "The state of a man's mind is as much a fact as the state of his digestion": *Edgington v. Fitzmaurice* (1885), 29 Ch.D. 459 at 483 (C.A.), Bown L.J.

<sup>68</sup> See, for example, *Obde v. Schlemeyer*, 353 P.2d 672 (Wash. S.C. 1960) [hereinafter *Obde*].

<sup>69</sup> See his case comment on *Smyth v. Szep* (1992), 63 B.C.L.R. (2d) 52 (C.A.): "Unsettling Settlements: Of Unconscionability and Other Things" (1992) 50 *Advoc.* 749 at 752.

<sup>70</sup> *Powell v. Powell* (1899), [1900] 1 Ch. 243.

<sup>71</sup> *Taylor v. Johnston* (1882), 19 Ch.D. 603.

<sup>72</sup> *Allcard v. Skinner* (1887), 36 Ch.D. 145 (C.A.).

<sup>73</sup> *Williams v. Johnson*, [1937] 4 All E.R. 34 (P.C.).

<sup>74</sup> *Wright v. Carter*, [1903] 1 Ch. 27 (C.A.).

<sup>75</sup> *Thomson v. Eastwood* (1877), 2 App. Cas. 215 (H.L.).

In other situations the court can hold, on the given facts, that a bank, for example, exercised unfair power over an individual, so that the contract becomes unenforceable.<sup>76</sup> This kind of pressure might be called "fraud in equity" but, today, it is more likely to be said that the bank owed a "fiduciary duty" to the customer<sup>77</sup> or guarantor,<sup>78</sup> or that there was "inequality of bargaining power" such as to justify the court in setting the contract aside.

This elementary statement of the law is necessary as an introduction to trying to understand the term "fraudulent non-disclosure" in fire insurance, which is the language used in the *Insurance Act*.<sup>79</sup> In other kinds of disclosure listed in the *Insurance Act*, for example, life,<sup>80</sup> motor,<sup>81</sup> and accident and sickness,<sup>82</sup> the word "fraudulently" is not used.

If we say that "fraudulently" means making a dishonest statement with intent to deceive,<sup>83</sup> it might be argued that there can never be a "fraudulent" non-disclosure. This, however, is not so. Assume that an agent comes to inspect property that is seriously damaged, but which the insured covers up so as to mislead the agent. That would, in my view, be a fraudulent non-disclosure.<sup>84</sup> Again, if an insured attempted to procure insurance for a building that was already in flames, a court would be justified in holding that the insured was liable for fraudulent non-disclosure. Since insurance deals with uncertainties, there is an implied representation that the building is not presently being destroyed by fire.<sup>85</sup>

A good reason for giving "fraud," in the fire insurance section, its common law meaning lies in the fact that it is common for insurers not to use proposal forms when insuring a building against fire. The insurer will often want to examine for itself the structure of the building, the

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<sup>76</sup> See, for example, *Lloyd's Bank v. Bundy*, [1975] Q.B. 326 (C.A.) [hereinafter *Lloyd's Bank*].

<sup>77</sup> *Woods v. Martins Bank*, [1959] 1 Q.B. 55.

<sup>78</sup> *Lloyd's Bank*, *supra* note 76.

<sup>79</sup> See *Insurance Act*, *supra* note 21, s. 148(2).

<sup>80</sup> *Ibid.* s. 183.

<sup>81</sup> *Ibid.* s. 233(4).

<sup>82</sup> *Ibid.* s. 308.

<sup>83</sup> Such cases must, of necessity, be rare.

<sup>84</sup> See *Obde*, *supra* note 68.

<sup>85</sup> This argument is similar to the one made by the respondents in *Taylor v. London Assurance Co.*, [1934] O.R. 273 (C.A.) [hereinafter *Taylor*], but without success.



number of sprinklers, and other features of the building. The effect of this examination will be to reduce the scope of disclosure on the part of the insured to vanishing point. Since 1934, "fraudulent non-disclosure" has been given its common law meaning—the most recent Supreme Court decision to the contrary notwithstanding.<sup>86</sup> It is reasonable to believe that if Canadian insurers were seriously troubled by having to prove common law fraud, they would have pressured the government to change the *Insurance Act* accordingly, as they have done in the past whenever they needed to do so.<sup>87</sup>

The first appellate court to consider the meaning of "fraudulent non-disclosure" was the Ontario Court of Appeal in *Kadishewitz v. Laurentian Insurance Co.*<sup>88</sup> In this case, the insurer refused to pay after a fire. It alleged that the insured had failed to disclose: (1) a previous loss by fire; (2) that the husband of the insured had been convicted of robbery; (3) that the insured had served a term in jail; (4) that the plaintiff had been engaged in business as a bootlegger; and two other allegedly material facts. Five Judges held that even if all the facts were true, the insurer could not avoid the policy because the insurer had not been able to prove fraud. Before the ink was dry on the decision in *Kadishewitz*, a differently constituted Court of Appeal in *Taylor*<sup>89</sup> held, 3 to 2, that there was no need for the insurer to prove common law fraud. In *Taylor*, Middleton J.A. relied on *Greenwood v. Martins Bank*,<sup>90</sup> to the effect that deliberate silence might amount to fraud.<sup>91</sup> Davis J.A. held that the plaintiff had made an imperfect representation which he equated with equitable fraud. Finally, Mulock C.J.A. stated that the insurer need not prove common law fraud.

The Supreme Court of Canada, unanimously reversed the *Kadishewitz* decision in an opinion given by Duff C.J.<sup>92</sup> The former Chief Justice admitted that lawyers had always used "fraud" in a variety of senses.<sup>93</sup> Lawyers had sometimes used fraud to describe a situation in which the insured had failed to disclose a material fact. But in this case

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<sup>86</sup> See *Ford*, *supra* note 61.

<sup>87</sup> See, for example, the changes made to the law of subrogation after the decision in *Globe & Rutgers Fire Insurance v. Truedell* (1927), 60 O.L.R. 227 (C.A.).

<sup>88</sup> [1931] O.R. 529 (C.A.).

<sup>89</sup> *Supra* note 85.

<sup>90</sup> [1933] A.C. 51 at 57 (H.L.).

<sup>91</sup> *Supra* note 85 at 283-84.

<sup>92</sup> *Kadishewitz v. Laurentian Insurance Co.*, [1935] S.C.R. 422 [hereinafter *Kadishewitz*].

<sup>93</sup> *Ibid.* at 425.

there was no reason for giving fraud any meaning other than its common law meaning. On the facts of the case, there had been no fraud.

The *Taylor* case stood unchallenged for more than half a century. Probably it is still the law, but its authority has been shaken by the bizarre decision in *Ford*.<sup>94</sup> In this case, Ford, the insured, applied for fire insurance on his building. Though Ford did not realize it, there was attached to the policy an application form filled out by someone else (perhaps Keith, the insurer's agent), that stated that the plaintiff had suffered no losses or cancellations. Keith stated that, just before meeting with Ford, he had received a telephone call from someone informing Keith that Ford had one loss and one cancellation. At first instance,<sup>95</sup> De Graves J. was very critical of Dominion's failure "to do an internal check by consulting the Insurance Bureau. Probably these checks would have revealed the plaintiff's insurance odysseys."<sup>96</sup> De Graves J., however, continued: "[i]n any event I find there was no disclosure of the insurance fraud at Lunder. Even by the most loose standards of an insurer, if disclosure had been made, the application would have been denied."<sup>97</sup> Later, he stated: "[t]he law of insurance requires complete disclosure. The doctrine of *uberrimae fidei* applies."<sup>98</sup> All this is, of course, impeccable English law. However, it is not Canadian law.

The majority of the Court of Appeal,<sup>99</sup> Huband J.A. with O'Sullivan J.A. concurring, held that in a new trial, the trial Judge could reject Ford's claim either because: (1) Ford had committed arson or

<sup>94</sup> *Supra* note 61.

<sup>95</sup> *Ford v. Dominion of Canada General Insurance Co.* (1988), 54 Man. R. (2d) 283 (Q.B.) [hereinafter *Ford Q.B.*].

<sup>96</sup> *Ibid.* at 289. Rendall and Stuesser are both critical of the insurer's failure to make inquiries of the insured. See J.A. Rendall, Annotation (1989), 34 C.C.L.I. 224 at 225 (Man. Q.B.); and L. Stuesser, "Review of Insurance Law in the 1990s" (1994) Man. L.J. 250 at 261, where he writes:

Ford is not a sympathetic plaintiff; his actions reek of fraud. At the same time Dominion is not an overly sympathetic defendant; its actions reek of negligence. Insurers are in the business of risk assessment and surely it is not too much to ask for insurers to do some investigation of a risk when put on notice as to potential problems. On the facts most favourable to the insurer, Dominion was aware that Ford had a prior loss and a prior cancellation. Surely a reasonable insurer would have probed these prior matters.

I agree with both writers, but am old fashioned enough to believe that applying a relevant statute is better than a scramble across the often treacherous terrain of the common law.

<sup>97</sup> *Ford Q.B.*, *supra* note 95 at 289.

<sup>98</sup> *Ibid.*

<sup>99</sup> *Ford v. Dominion of Canada General Insurance Co.* (1989), 62 Man. R. (2d) 244 (C.A.) [hereinafter *Ford C.A.*].

caused others to commit arson; and/or (2) because Ford had submitted proofs of loss that were so inflated as to be fraudulent.

De Graves J. had not considered these grounds because, in his view, Ford lost on the grounds of non-disclosure. Philp J.A. delivered a separate concurring opinion that is breathtaking in its ignorance of the law. He said:

This fundamental principle of insurance law has been applied by the Courts for over 200 years. The cases are referred to by Professor E.R. Hardy Ivamy in his text, *General Principles of Insurance Law* ... at chapters 12 and 13. ... This is the principle that De Graves J., applied in arriving at his conclusion that Ford failed to make full disclosure of all material facts, and that, therefore, his policies of insurance were void.<sup>100</sup>

The citation of a New Zealand text edited by an English author, to solve a Canadian legal problem, is not without its charm. Unfortunately, Ontario has a special statutory provision,<sup>101</sup> to say nothing of a relevant Supreme Court decision,<sup>102</sup> to deal with the problem of disclosure in fire insurance. Of these, Philp J.A. seems unaware. The insured appealed to the Supreme Court of Canada.

The following judgment on the appeal was given on behalf of the Supreme Court by Cory J.:

I am in agreement with the minority reasons given by Philp J.A. ... . As a result, I would allow the appeal, set aside the order of the Court of Appeal and restore the judgment at trial. The appellant is entitled to its costs of this appeal and throughout these proceedings.<sup>103</sup>

Both the judgment of Philp J.A. and the Supreme Court judgment are *per incuriam* because neither mentions the relevant statute or Supreme Court decision, but some lower courts might follow the decision,<sup>104</sup> since it is the last word on the subject. This state of affairs is highly unsatisfactory. It is difficult to believe that some unfortunate litigant will have to finance an action to re-establish the law as it has been understood to be for nearly sixty years.

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<sup>100</sup> *Ibid.* at 249 [citations omitted].

<sup>101</sup> See *Insurance Act*, *supra* note 21, s. 148(1).

<sup>102</sup> See *Kadishewitz*, *supra* note 92.

<sup>103</sup> *Ford*, *supra* note 61 at 136.

<sup>104</sup> Both lower courts and the Supreme Court are likely to say that the *Ford* decision "turns on its own special facts."

#### IV. THE DOCTRINE OF INCREASE OF RISK: *LEJEUNE V. CUMIS INSURANCE SOCIETY INC.*<sup>105</sup>

While the law relating to the duty to disclose in fire insurance is unfavourable to the insurer in Canadian law,<sup>106</sup> the law relating to increase of risk is extremely favourable to it. An insurer can avoid paying if it shows the risk insured has increased without its consent since the policy issued, but in England this applies only if there has been a drastic change in property use—for example, a change from residential to business use.<sup>107</sup> In Canadian law the test for increase of risk has been recently stated in these terms:

Whether a change is material to the risk is a question of fact in each case. The question is: if the change had been disclosed would it have influenced a reasonable insurer to either decline or to have stipulated for a higher premium.<sup>108</sup>

If the reader has a sense of *déjà vu*, he or she is correct. This is the same test for non-disclosure that the Supreme Court rejected in *Taylor*.<sup>109</sup> By making the question of increase of risk a question of fact, the insurer can bring in considerations of “moral hazard.”<sup>110</sup>

<sup>105</sup> [1989] 2 S.C.R. 1048 [hereinafter *Lejeune*].

<sup>106</sup> See *supra* notes 85-94 and accompanying text.

<sup>107</sup> See, for example, Pollock C.B., who denied the insurer the right to complain of “a mere increase in danger” in *Baxendale v. Harvey* (1859), 4 H. & N. 444, 157 E.R. 913 at 915 (Ex. Div.) [hereinafter *Baxendale*]. Pollock C.B. observed:

It is like the case of a person who has an oven on his premises, and instead of using it for baking bread he uses it for some other purpose. If a person who insures his life goes up in a balloon, that does not vitiate his policy. ... [T]he society having had notice of the nature of the risk were not entitled to any notice by reason of the increase in danger. A person who insures may light as many candles as he please[s] in his house, though each additional candle increases the danger of setting the house on fire.

I am indebted to this and other references in K. Nicholson’s excellent article “Mid-Term Alterations in the Risk: What Can be done?” [1991] I.L.J. 27.

<sup>108</sup> *Lewandowski v. Waterloo Mutual Insurance Co.* (1985), 12 C.C.L.I. 288 at 292 (Ont. H.C.J.), *aff’d* [1987] I.L.R. 8627 (Ont. C.A.) [hereinafter *Lewandowski*].

<sup>109</sup> *Supra* note 85.

<sup>110</sup> The notion of moral hazard is based on a simplistic theory of moral behaviour which posits that the promise or expectation of a benefit conditioned on the happening of an event generates incentives for the potential beneficiary to cause that event to occur, or to claim that it has occurred. Thus, over valuation of insured property is taken as evidence that the insured intends to destroy the property.

Moreover, having rejected the ordinary duty of disclosure at the formation level in fire insurance contracts,<sup>111</sup> the doctrine is imported at a later stage in the fire insurance contract. There is even less justification for imposing a duty of disclosure on the insured during the currency of the policy than there is at the formation stage. At the formation stage the applicant may be alerted by the agent or by a statement in the proposal form that there might be something that he or she should reveal.<sup>112</sup> Once the policy has been issued, however, there is nothing to alert the insured that she will have to disclose, for example, that she has started to smoke, had a child with her partner, or had taken in an elderly relative.<sup>113</sup> Indeed, were insurance companies to insist on getting this information, they would find themselves swamped by it.

The kind of inquiry that is currently needed is illustrated by the recent case of *Lewandowski*.<sup>114</sup> In this case the wife, who had a joint interest in the home, left the house with her child because of her husband's alleged alcoholism. After the property had burned down, the husband made a claim. The insurer denied the claim because of the husband's alcoholism and because of his failure to disclose the fact that his wife had left the farm. Callaghan J. found that, although the husband had been drunk on a number of occasions, he was not an alcoholic. The Judge found that the husband was able to take care of the farm.<sup>115</sup> This fact was able to dispose also of the insurer's argument that he had not disclosed the fact that his wife had left him.<sup>116</sup> While the case has a happy ending, it is a disgrace that a case like this should require four days of hearing into evidence that is highly subjective and has little to do with the doctrine of increase of risk as properly understood. Since what was insured was a farm, questions relating to the severity of the husband's drinking problem and the fact that the wife left the farm should have been entirely irrelevant to the court. If each judge can balance the factors referred to in *Lewandowski*, this could

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<sup>111</sup> See *Taylor*, *supra* note 85, for an interpretation of "fraudulent omission" in a predecessor of *Insurance Act*, *supra* note 21, s. 148(2), stat. cond. 1.

<sup>112</sup> Even though proposal forms are not generally used in fire insurance inspections, oral questions may be used.

<sup>113</sup> See the statement of Pollock C.B., *supra* note 107.

<sup>114</sup> *Supra* note 108.

<sup>115</sup> *Ibid.* at 291-92.

<sup>116</sup> *Ibid.* at 291. For an increase of risk to occur, the change in the risk must be within the "control" of the insured: see *Insurance Act*, *supra* note 21, s. 148(2), stat. cond. 4. It is impossible to see how the wife's desertion could be under the "control" of the husband.

easily mean that another judge hearing the same evidence might have decided the case differently from Callaghan J.

This proposition is forcefully illustrated by the decision of Scott D.C.J. in *Doherty v. Home Insurance Co.*,<sup>117</sup> decided one year after *Lewandowski*. In *Doherty*, Mr. Doherty insured his home at 56 Briar Knoll, Kitchener, with the Maplex Insurance Company. Later, Doherty and his fiancée, Lebon, bought a house in their joint names at Rothsay Drive, Kitchener. Doherty telephoned his agent, Durocher, to arrange insurance coverage for the newly purchased house. He informed Durocher that Lebon might live at Rothsay, but after they were married, she would be living at Briar Knoll and they might rent Rothsay. The agent placed insurance with the Home Insurance Company. After the couple married, the Rothsay house was rented to a family named Day with their two children. While the Day family was in occupation of the house, a freak fire occurred without negligence on their part.

Home Insurance argued that they would not insure rented residential premises unless the owner insured his principal residence with them—which was not the case here. The philosophy behind this is that the tenant, having no pride of ownership, has no financial interest and takes less care of the premises than the owner would. The insured argued that there had been no increase in risk relying on the decision in *Ryan v. Citadel General Assurance Co.*<sup>118</sup> In that case, the plaintiff, a tenant, had insured the contents of the house. At the time, he was living there with his wife and child. His wife left him, taking the child, and he was joined by two male friends as paying guests. After the fire had occurred, the insurer refused to pay on the ground that there had been a material change of risk in that the house was no longer used as a “single family dwelling.” In *Ryan*, Smith J. rejected the insurer’s argument emphatically:

I am not persuaded that a reasonable insurer would or should consider occupancy more hazardous when a man and a woman are in a common law relationship for instance or for that matter when two males and two females with or without sexual content in their relationship occupy a single-family dwelling together. It would be straining the concept of reasonableness to define the risk in those terms given today’s societal attitudes. The materiality of a change along the lines just described is not self-evident.<sup>119</sup>

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<sup>117</sup> (1985), 14 C.C.L.I. 104 (Ont. Dist. Ct.) [hereinafter *Doherty Dist. Ct.*], rev’d (1987), 19 C.C.L.I. 314 (Ont. Div. Ct.) [hereinafter *Doherty Div. Ct.*].

<sup>118</sup> (1983), 42 O.R. (2d) 586 (H.C.J.) [hereinafter *Ryan*].

<sup>119</sup> *Ibid.* at 591.

In *Doherty Dist. Ct.*, Scott D.C.J. refused to accept the *Ryan* case since, in that case, Ryan was still living in the premises and the insured contents were still there. In *Doherty*, only one of the owners of the Rothsay house lived there briefly; the house was occupied by tenants.

Scott D.C.J. rejected the insurer's argument without appearing to require evidence from other insurers relating to increase of risk. She wrote:

It would be contrary to reason to say that there was no material change in the risk when the property was rented and the tenants moved in. There is nothing unreasonable in Home's policy not to insure rented residential property.<sup>120</sup>

Even if Home Insurance had this policy, it was not demonstrated that other "prudent insurers" followed it. The Divisional Court, in an opinion by O'Brien J., reversed the decision on precisely this ground:

There was no evidence, statistical or otherwise, to support this conclusion. There was no evidence that this was a view generally (or reasonably) held in the insurance industry. ... Home's refusal was not an absolute one, they *would* insure rental property *if* the principal residence were also insured with them. This would appear to be a marketing rather than an underwriting decision.<sup>121</sup>

Again, the outcome is satisfactory but it should not have taken three years and an appeal to reach an obvious result. The doctrine of increase of risk as understood in these and other cases bears no relation to the doctrine as understood in England,<sup>122</sup> Australia,<sup>123</sup> or New Zealand.<sup>124</sup> Why Canada should have a doctrine in this area that is particularly favourable to insurers is beyond comprehension.

All of this is by way of prelude to the remarkable, unanimous Supreme Court decision in *Lejeune*.<sup>125</sup> Although the appeal is from Quebec, the law is identical to that in other common law provinces,<sup>126</sup>

<sup>120</sup> *Doherty Dist. Ct.*, *supra* note 117 at 113.

<sup>121</sup> *Doherty Div. Ct.*, *supra* note 117 at 317 [emphasis in original]. The court relied extensively on M.G. Baer, Annotation (1985), 14 C.C.L.I. 104 at 106.

<sup>122</sup> See *Baxendale*, *supra* note 107; see also *Pim v. Reid* (1843), 6 Man. & G. 1, 134 E.R. 784 (C.P.); and *Beauchamp v. National Mutual Insurance Co.* (1937), 57 Lloyd's Rep. 272 (K.B.).

<sup>123</sup> See, for example, *Wilshire v. Guardian Assurance Co.* (1912), 15 C.L.R. 516 (Aust. H.C.); and *Southern Cross Assurance Co. v. Australian Provincial Assurance Ltd.* (1939), 39 S.R. 174 (N.S.W.S.C.).

<sup>124</sup> See *Dawson v. Monarch Insurance* (1976), [1977] 1 N.Z.L.R. 372 (S.C. Christchurch).

<sup>125</sup> *Supra* note 105.

<sup>126</sup> See *Insurance Act*, *supra* note 21, ss. 148(2) (property), 234(1) (motor vehicle), and 290-329 (accident and sickness).

with a few immaterial exceptions.<sup>127</sup> The insured, the owner of a four apartment buildings, leased the large premises on the ground floor to the Maison des Jeunes Inc., a group of young people aged between fourteen and eighteen years. In January 1981, a fire started in the ground floor hallway destroying the building. The insurer refused to indemnify the insured because the building was no longer occupied as a "private dwelling." At first blush, this decision seems incredible. Had the insured leased an apartment to children doing their homework or studying for exams for a few hours a day, it would seem inconceivable that anyone would describe this as a change in the use of the premises, so as to render the property no longer a "private dwelling." Further, if the doctrine of increase of risk is to be given any sensible meaning, it is impossible to say that there has been an "increase in risk" so as to defeat the insured's claim.

Indeed, Côté A.C.J. held that the expert witnesses were not agreed as to whether there had been an increase of risk. Unable to use this ground, the Judge denied recovery on the basis that the lease to the Maison des Jeunes changed the character of the "private dwelling." Côté A.C.J. did not say what the property had become after it had lost its character as a "private dwelling."<sup>128</sup> A majority of the Quebec Court of Appeal reversed the Superior Court's judgment by a majority of 2 to 1.<sup>129</sup> LeBel J.A. (with whom Beauregard J.A. concurred) thought that the lease of the premises had not changed the character of the insured building. The insurer had not defined what it meant by "private dwelling" and the activities of the Maison des Jeunes were no different from the gatherings that might occur in any family having young people at home.

The factums to the Supreme Court for both appellant and respondent concerned themselves solely with the question of increase of risk. De Grandpré points out that Gonthier J. spends ten of his eleven page opinion discussing the doctrine of increase of risk only to find it inapplicable. In a single page, the Supreme Court decides that the use by the Maison des Jeunes is inconsistent with the description of the premises as a "private dwelling." De Grandpré notes that no authorities are cited in the single-page judgment, and states that Gonthier J.'s

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<sup>127</sup> The Quebec statute is based on the French law of 1930; it allows the owner of property to recover a proportionate amount of the loss, unless the insured is guilty of bad faith; see *An Act to amend the Act respecting insurance and to again amend the Civil Code*, S.Q. 1979, c. 33, amending R.S.Q. 1977, c. A-32, arts. 2566, 2488, and 2500.

<sup>128</sup> *Lejeune v. Cumis Insurance Society Inc.*, [1985] C.S. 608 at 612.

<sup>129</sup> [1988] R.J.Q. 1 (C.A.).



opinion "m'a fort désappointé."<sup>130</sup> While de Grandpré is shocked by the style of this ramshackle opinion,<sup>131</sup> I am disturbed by the implications of the decision. The Supreme Court, in my view, is giving the go-ahead to any court that cannot find any increase of risk, to find a prohibited use of the premises, even if one cannot find that prohibited use on any sensible reading of the policy. One can only hope that *Lejeune* is relegated to obscurity.

## V. CONCLUSION

Fire insurance cases are not the most important problem in the Canadian legal universe. However, one should not underestimate their importance to the individuals who are denied protection by shoddy opinions that pay no regard to statutes, binding authority, or sensible public policies. Despite the thousands of pages that have been written by eminent jurists and judges on the importance of not depriving an insured of coverage, in the absence of a compelling social policy, the Supreme Court appears not to have read this vast literature. De Grandpré offers three explanations for "cette situation désespérante":<sup>132</sup> (1) that judges do not have the background to write with authority in insurance law; (2) that judges are bewitched (médusés)<sup>133</sup> by the writings of university academics; and (3) that many judgments are written by law clerks fresh out of law school.

To take the second explanation first, it is difficult to see how the judges could become befuddled by the one Canadian text available in English,<sup>134</sup> since that treatise does not advance novel ideas for the judges. It substantially records what the Canadian law is. If the judges looked more often at American authorities,<sup>135</sup> they would write better opinions since American judges and commentators have a deeper understanding of insurance law than their Canadian or English counterparts.

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<sup>130</sup> *Supra* note 49 at 23.

<sup>131</sup> *Ibid.*

<sup>132</sup> *Ibid.* at 40.

<sup>133</sup> *Ibid.*

<sup>134</sup> See C. Brown & J. Menezes, *Insurance Law in Canada*, 2d ed. (Toronto: Carswell, 1991).

<sup>135</sup> This was the strength of Laskin C.J.'s decisions in the area of insurance law.

It is true that law clerks and counsel are weak in their grasp of insurance to the point of ignoring relevant statutes,<sup>136</sup> but the reason for this ignorance comes from the disgraceful neglect of insurance in law schools. The subject does not appear in the list of specialties set out in the 1994-95 Canadian teachers' handbook. Some law schools do not teach the subject at all; others teach property insurance, neglecting life and disability insurance. Other students regard it as part of contracts and they fail to study a subject that has its own special vocabulary and is as complex as, say, constitutional law, which every Canadian student is required to take.

There is one final complicating factor and that is the *Canadian Charter of Rights and Freedoms*.<sup>137</sup> Since the Supreme Court regards this as its most essential work, questions of insurance law tend to be regarded by the justices, the academics, and the law clerks as relatively insignificant. Yet it is difficult to see why a trivial case such as *Andrews v. Law Society of B.C.*<sup>138</sup> is more important than, for example, *Scott*.<sup>139</sup> If the Court is going to continue to hear insurance cases, it must be prepared to devote the same care to them that it devotes to *Charter* cases. Unless it does this, the public will be better served by the court's not hearing these cases at all. These cases are too important to be regarded as a "breather" from the court's real work.<sup>140</sup>

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<sup>136</sup> See *Ford*, *supra* note 61. A student in an examination paper gave me fourteen examples of where the courts had ignored insurance statutes. All of them were correct.

<sup>137</sup> Part I of the *Constitution Act, 1982*, being Schedule B to the *Canada Act 1982* (U.K.), 1982, c. 11 [hereinafter *Charter*].

<sup>138</sup> [1989] 1 S.C.R. 143.

<sup>139</sup> *Supra* note 3.

<sup>140</sup> After this article was written, I read L. Cunningham's fine article, "The Right of an Innocent Co.—Insured Spouse to recover under a 'Joint' Insurance Policy" (1994) 8 *Otago L. Rev.* 169. The author shows that, until recently, the New Zealand courts refused to protect the property rights of an innocent, co-insured spouse. However, in *Maulder v. National Insurance Co. of New Zealand Ltd.* (1992), [1993] 2 N.Z.L.R. 351 (H.C. Wellington), an innocent widow was entitled to recover half the value of the family home which her husband had burnt down when he killed himself.