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SCC FINDS INSURER PARTICIPATION IN LITIGATION NOT A PROMISE TO MAINTAIN COVERAGE

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A. INTRODUCTION

The Supreme Court of Canada ("SCC") has found that an insurance company that was unaware of a policy violation could deny full coverage once it was made aware of the violation in question, in a decision that could have implication for all insureds, including charities and not-for-profits. In the case of *Trial Lawyers Association of British Columbia v Royal & Sun Alliance Insurance Company of Canada*,[1] published on November 18, 2021, the SCC considered whether an insurer had waived its right to deny full coverage when it provided a defence to litigation brought against the estate of one of its insureds. Ultimately, the court concluded the insurer did not waive its right and could deny coverage because it did not know of the policy breach.

B. BACKGROUND

Mr. Steven Devecseri died in a motorcycle accident in 2006. Mr. Bradfield and Mr. Caton, who were injured in the same accident, each sued the estate of Mr. Devecseri (the "estate") who had been insured by Royal & Sun Alliance Insurance Company of Canada ("RSA"). As a result, RSA defended the estate in the two lawsuits. However, three years after the accident and over a year into litigation, RSA discovered that Mr. Devecseri had consumed alcohol immediately before the accident in breach of the insurance

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[1] 2021 SCC 47.

policy. As a result, RSA promptly stopped defending the estate and denied coverage which reduced the amount Mr. Bradfield and Mr. Caton could claim from $1 million to the statutory minimum coverage of $200,000.

Eventually, both of Mr. Caton and Mr. Bradfield received judgments in their favour against the estate, but Mr. Bradfield further sought to recover judgment against RSA, claiming that the insurance company waived its right to deny full coverage when it provided a defence in court to Mr. Bradfield's claim against the estate. While the trial judge allowed Mr. Bradfield's claim to succeed, the Ontario Court of Appeal denied the claim upon appeal, finding that RSA could deny coverage, despite its involvement in the litigation, because it did not know of Mr. Devecseri's policy breach. Mr. Bradfield further appealed to the SCC. After being granted leave, he reached a settlement with RSA and discontinued his appeal. The Trial Lawyers Association of British Columbia (the "Association") asked to be substituted as the appellant, a request which the SCC granted. The Ontario Trial Lawyers Association also participated in the hearing as an intervenor.

C. ANALYSIS BY THE SCC MAJORITY

The SCC Majority noted that since both parties agreed there was no written waiver by RSA of its rights to deny full coverage (as allowed by subsection 131(1) of the *Insurance Act*[2]), the only issue before the court was whether RSA was barred from denying coverage "because it responded to claims against Mr. Devecseri's estate long after it could have discovered evidence of [his] policy breach".

In its analysis, the SCC Majority considered the common law defence of "promissory estoppel", which is a doctrine where a party may establish "that the other party has, by words or conduct, made a promise or assurance which was intended to affect their legal relationship and to be acted on". Three things must be demonstrated in order for there to be promissory estoppel: (1) the parties were in a legal relationship at the time of the promise; (2) the promise was intended to affect that relationship and be acted upon; and (3) the other party in fact relied on the promise, resulting in prejudice, inequity, unfairness or injustice. The purpose of promissory estoppel is to protect against the inequity of allowing a party to abandon its promise after another entity relies on it to their detriment.

[2] RSO 1990, c I.8.

In applying the doctrine of promissory estoppel to the facts of the case before them, the SCC Majority found that the claim failed, because RSA "gave no promise or assurance intended to affect its legal relationship with Mr. Bradfield". RSA had a duty to investigate the claim against Mr. Devecseri, but it had no additional duty to Mr. Bradfield to investigate any policy breaches. While these points were sufficient to dispose of the appeal, the SCC Majority provided further analysis.

One of the arguments made by the Association was that despite RSA's ignorance of Mr. Devecseri's policy breach, it should be found that RSA's conduct gave assurance that it would not deny coverage on the basis of the policy breach. However, the SCC Majority noted that a requirement of promissory estoppel is that "a promise or assurance must be *intended* to affect the parties' legal relationship" and that "the significance of *intention* depends entirely on what the promisor *knows*" (emphasis in original). Therefore, RSA could not intend to alter a relationship by promising not to act on information that it did not have.

In some cases, knowledge may be imputed to an insurer. For example, the SCC Majority agreed that:

> where an insurer is shown to be in possession of the facts demonstrating a breach, an inference may be drawn that the insurer, by its conduct, intended to alter its legal relationship with the insured – notwithstanding the fact that the insurer did not realize the legal significance of the facts or otherwise failed to appreciate the terms of its policy with the insured.

In this case, however, it was undisputed that RSA did not know that Mr. Devecseri had consumed alcohol in contravention of his motorcycle license prior to the accident.

Nor could RSA be found to have constructively known of Mr. Devecseri's breach. In light of the strong economic incentives for insurers to deny coverage, the SCC in *Fidler v Sun Life Assurance Co. of Canada*[3] found that insurers have a duty to the insured to investigate claims fairly and in a balanced and reasonable manner and to "not engage in a relentless search for a policy breach". Therefore, the SCC Majority declined to find that insurers are bound by a duty to know the things that are within their grasp in situations where a claim is made under an existing contract.

The SCC Majority also noted that an insurer's duty to investigate claims fairly is owed only to the insured (the estate of Mr. Devecseri) and not to third parties like Mr. Bradfield. To allow a relationship between

[3] 2006 SCC 30.

the insurer and a third-party claiming against the insured would result in "no justice" because such a relationship would lack mutuality. For example, if Mr. Bradfield had known that Mr. Devecseri consumed alcohol, "he would be under no obligation to RSA to disclose that fact" while RSA would have "a duty to Mr. Bradfield to discover that selfsame fact".

An additional claim was made by the Association that section 258 of the *Insurance Act*[4] allowed Mr. Bradfield to assert a right of coverage as against the RSA "both on his own behalf and by 'stand[ing] in the shoes' of Mr. Devecseri's estate". However, the SCC Majority found that it was unclear, based on the text of the statute "whether Mr. Bradfield can assert an estoppel argument on behalf of Mr. Devecseri's estate" as proposed by the Association. Accordingly, the SCC Majority refrained from definitively concluding whether a third party can bring a claim on behalf of the insured, but instead listed several problems that would arise if the court did accept the Association's arguments about section 258. There was no clear or unambiguous conduct by RSA that amounted to assurance that it would refrain from denying coverage if a policy breach was discovered later. The SCC Majority concluded that where "an insurer responds to a claim against its insured by defending, it is communicating — to the insured *and* to the third-party claimant — only that the claims against its insured are of a type that fall within the terms of coverage".

Finally, the SCC Majority notes that the Association did not establish that there was detrimental reliance on an alleged promise of RSA. The goal of promissory estoppel is "to address unconscionable, unjust, or unfair conduct". Therefore, there must be evidence of "prejudice, inequity, unfairness or injustice before courts will give hold a promisor to its promise".

D. ANALYSIS BY JUSTICE KARAKATSANIS, CONCURRING

In the concurring reasons by Justice Karakatsanis, she agreed that the appeal should be dismissed and with much of the majority's legal analysis. However, she offered a different analysis of promissory estoppel. While the SCC Majority said that the promisor cannot intend to affect the legal relationship unless they have actual knowledge of the facts underlying that relationship, Justice Karakatsanis disagreed that actual knowledge was required to analyze the promisor's intent. The intent of the promisor must be evaluated objectively, based on the standard of what a reasonable person would do, rather than subjectively by

[4] *Supra*, note 2.

looking at what the promisor actually intended at a particular point in time. "Subjective intent is unknowable to anyone other than the promisor," wrote Justice Karakatsanis, and the jurisprudence "has long established that the intent of the promisor in promissory estoppel must be interpreted objectively". Under an objective approach, the court would consider all the facts that the promisor "knew or reasonably can be taken to have known". Therefore, the SCC Majority's position, which required actual knowledge of the facts, "distracts from the true inquiry and unduly constrains the flexibility inherent in equity".

Promissory estoppel, as noted earlier, is meant to prevent inequity and as such its application must be fair to both parties. The fact-finder, in carrying out an objective analysis, "must look at the entire context, including what the promisor knew or can be taken to have known". Justice Karakatsanis cited the case of *Western Canada Accident and Guarantee Insurance Co v Parrott*[5] as an illustration of a case where actual knowledge of the facts supported the inference that the promisor intended to change legal relations. Nevertheless, "it does not follow that actual knowledge is therefore a requirement of promissory estoppel". Knowledge should not be a bright-line rule, but rather, simply part of the context that informs the objective analysis of a promisor's conduct.

Justice Karakatsanis concluded that she agreed with the SCC Majority that RSA's conduct could not be interpreted as an unequivocal assurance that it would continue to provide coverage even if the policy was void and that the Association's appeal should be dismissed. Unlike the SCC majority, however, she recommended an objective analysis for promissory estoppel in which a promise is intended to be legally binding where it would be reasonable for the promissee to rely on it.

E. CONCLUSION

While the SCC Majority and Justice Karakatsanis' concurrence both reach the same result, their in-depth analyses of promissory estoppel are important for any insured to consider. An insurance provider may defend a claim in court, but this does not mean that they cannot pull coverage at a later time if new information comes to light which limits or voids policy coverage. Even in situations where further investigation by the insurer would likely turn up information of a policy breach, the SCC has signaled that it is reluctant to impose a requirement on insurers to investigate these situations, over concerns that this may result in an unfair investigation process. As such, a practical takeaway from this decision for charities

[5] (1921), 61 SCR 595.

and not-for-profits, as well as for all other insureds, is that it is essential to both know, as well as comply with, the terms and conditions of applicable insurance policies. This will allow them to avoid being denied coverage, because denial can occur even after a defence has been initiated where the breach in the insurance policy comes to light at a later time.