Hot Loss Transfer Issues

wondering what's new in the loss transfer world?

Well, since the Ontario Court of Appeal has shown an interest in loss transfer principles, there have been developments related to the limitation period, the doctrine of *LACHES*, the strict interpretation of the Fault Determination Rules, a modified application of the "ordinary rules of law" and the approval of multiple deductibles.

Loss Transfer is definitely hot - what's next?

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Feb/2016

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INTRODUCTION

The loss transfer mechanism has been operating for over 25 years in Ontario. It has been an area of law which has grown steadily through creative arguments made by insurance defence counsel and thoughtful (sometimes daring) decisions by knowledgeable arbitrators.

Over the past two decades, it seemed relatively rare for a loss transfer issue to attract the attention of the Court of Appeal. However, in the last few years, the Court of Appeal seems quite interested in loss transfer. Recent appellate intervention has led to some significant changes to the relatively stable world of loss transfer.

LIMITATION PERIOD

Starting with the private arbitration decision by Arbitrator Scott Densem in *Federation v. Kingsway* (December 16, 2010), the law related to the limitation period applicable to loss transfer under the "New" *Limitations Act, 2002* began to be formed.

Arbitrator Densem concluded that the "new" Act does indeed apply to loss transfer matters, such that there is a two year limitation period to advance loss transfer claims. However, he found that the limitation period begins to run from the day after a Request for Indemnification is delivered, not from the date that the cause of action arises (i.e. the date the first party insurer paid the benefit), as was concluded by the Ontario Court of Appeal (in *State Farm Mutual Automobile Insurance Company v. Dominion of Canada General Insurance Company*[1]) under the predecessor *Limitations Act*.

Arbitrator Densem concluded:

> As a matter of statutory interpretation, the "clock" must start on the limitation period at the first moment all of the conditions in section 5 of the *Limitations Act, 2002* have been satisfied. Therefore, the proper way to give effect to the statutory wording in a loss transfer indemnity case is to stipulate that the second insurer has either acted or omitted to indemnify the first insurer if it has not done so by the first day following receipt of the Loss Transfer Request. This is the first point in time by which all of the conditions in section 5 (a) of the Limitations Act, 2002, are satisfied, thus triggering the commencement of the 2 year limitation period. (pp. 20-21)

On appeal, Justice Belobaba upheld the arbitration decision and affirmed that the two-year loss transfer limitation period begins to run the day after the Request for Indemnification is delivered. In dismissing the further appeal, the Court of Appeal in *Markel Insurance Company of Canada v. ING Insurance Company of Canada*[2] stated:

> [26] Once a legally valid (i.e., apart from any issue as to limitations) claim is asserted by the first party insurer's Request for Indemnification, the second party insurer is under a legal obligation to satisfy it. All the facts are present

1 (2005) O.J. No.4642

2 2012 ONCA 218—which was heard together with the *Federation v. Kingsway* appeal

> to trigger the legal obligation of the part of the second party insurer to indemnify the first party insurer for the loss. The situation has crystallized into complete and valid legal claim that is immediately enforceable against the second party insurer. There is nothing more that must happen to create the legal obligation of the second party insurer to pay the claim.
>
> [27] In my view, it must follow that the first party insurer suffers a loss from the moment the second party insurer can be said to have failed to satisfy its legal obligation to satisfy the loss transfer claim. I agree with the arbitrator in Federation v. Kingsway that the first party insurer suffers a loss caused by the second party insurer's omission in failing to satisfy the claim the day after the Request for Indemnification is made.

This decision has created significant uncertainty for insurers with respect to the calculation of limitation periods for the purpose of loss transfer. It represents a departure from the manner in which the limitation period for loss transfer has been applied previously in accordance with the prior *Limitations Act* (it ran from the date each SABS payment was made by the first party insurer).

Now, a second party insurer will be able to effectively control the limitation period by withholding delivery of a Request for Indemnity. It could wait decades after the SABS and tort claims are resolved before demanding loss transfer indemnity. Once the second party insurer refuses to pay, the claim can be arbitrated, despite the passage of an enormous amount of time and prejudice against the second party insurer.

This seems contrary to the intent of the legislature in drafting the *Limitations Act, 2002*. Although the Act seeks to implement a shorter basic limitation period (2 years) and create certainty in the timing of litigation matters, for loss transfer, precisely the opposite result has been created. Arbitrator Densem recognized the possibility of lengthy delays, but reconciled his decision to permit such situations to develop by suggesting that second party insurers should be secure in the enforcement of the equitable defence of *laches*.

LACHES

Notwithstanding the Court of Appeal's interpretation of the limitation period for loss transfer, second party insurers continued to assert the defence of *laches* in cases where loss transfer claims were advanced late. However, in September 2013, in *Intact Insurance Co. of Canada v. Lombard General Insurance Co. of Canada*[3], Justice Chiappetta found that the equitable doctrine of *laches* does not apply to loss transfer claims. She noted that a "statutory claim under s.275 of the *Insurance Act* is devoid of equitable relief" and "granting the equitable *laches* defence pursuant to this particular statutory claim is not appropriate."

However, the subsequent decision by Justice Lederman in *Zurich Insurance Company v. TD General Insurance Company*[4] found (contrary to Justice Chiappetta) that the equitable doctrine of *laches* is indeed available to assist second party insurers in situations where a first party insurer seeks to advance loss transfer claims many years after accident benefits began to be paid.

The Ontario Court of Appeal heard the appeals from Justice Chiappetta's and Justice Lederman's decisions together.[5] The Court agreed with Justice Chiappetta that the defence of *laches* cannot be invoked in response to a loss transfer claim under s.275 of the *Insurance Act*. The Court Appeal held that "a loss transfer claim is clearly a statutorily provided legal right to indemnity and not an equitable claim or claim for equitable relief.

As such, based on the current state of the law, there now is no protection for second party loss transfer insurers against late surfacing loss transfer claims, even if they are advanced many years after the loss. As determined by Justice Chiappetta and now endorsed by the Court of Appeal there is no place in loss transfer for the operation of the equitable doctrine of *laches*. Leave to appeal to the Supreme Court of Canada is currently being sought.

3 2013 ONSC 5878
4 2014 ONSC 3191
5 2015 ONCA 764

Quantum of Indemnity

In *Wawanesa Mutual Insurance Company v. Axa Insurance (Canada)*[6], Axa refused to indemnify Wawanesa in relation to the costs of insurer related medical assessments on the basis that they were not "in relation to such benefits paid" by Wawanesa, as outlined in s.275(1). The Court of Appeal upheld the decision of Justice Green and confirmed in a 2-1 ruling that "Section 275 (1) of the *Insurance Act* does not entitle first party insurers to indemnification for the cost of insurer generated medical assessments".

Writing for the majority, Weiler J.A. explained that while she agreed that the ordinary meaning of the words "in relation to" in s.275(1) encompasses more than accident benefits paid by the insurer to the insured, she was not satisfied that the wording was broad enough in scope to include insurer generated medical assessments (which is the same result reached by Moldaver, J. as he then was in the *Jevco v. Guarantee*[7] decision and by Mandel, J. in *Jevco v. Prudential*[7]).

Although the decision was essentially an affirmation of the current state of the law, the comments made by the Court in the decision will have broader applicability for loss transfer quantum disputes. Notably, Justice Weiler recognized that Wawanesa and Axa "may owe each other a duty of good faith". Justice Weiler explained that: "Wawanesa could face a challenge from Axa if it did not act reasonably and simply paid Statutory Benefits without exercising its right to an insurer generated medical assessment in appropriate cases. Wawanesa incurs the risk that it will not be indemnified for Statutory Benefits at all if it does not require an insurer generated medical assessment where appropriate."

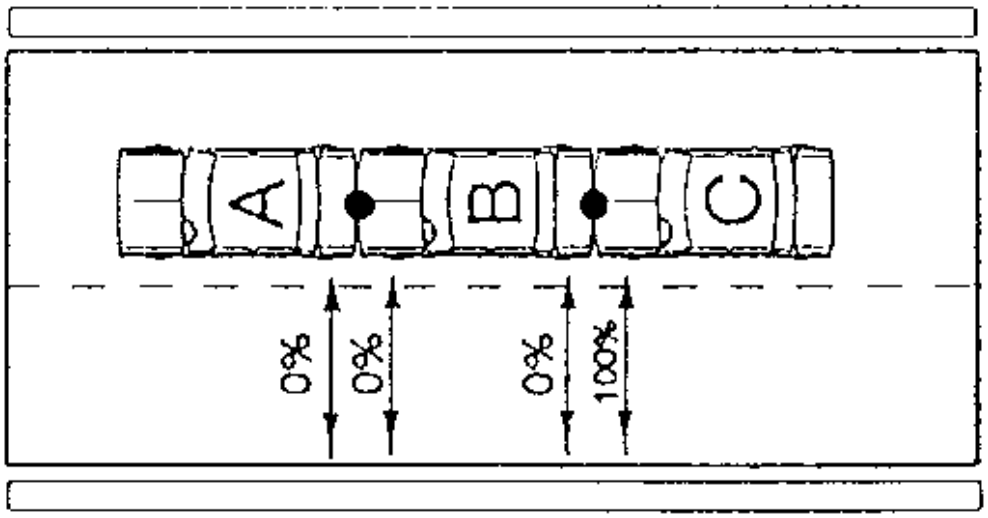
The ability to argue that a first party insurer owed the second party insurer a duty to act in good faith, will greatly support any challenge to the "reasonableness" of accident benefit payments made by the first party insurer. Furthermore, the Court's comments will be supportive of the position that a first party insurer's demand for loss transfer indemnity should be reduced in cases where the first party insurer does not pursue and undertake reasonable and appropriate loss control measures, such as investigations and insurer medical examinations.

6 2012 ONCA 592

7 (1994) unreported; [1995] I.L.R. I-3194

FAULT DETERMINATION RULE 9(4)

Section 9(4) of the Fault Determination Rules (FDRs) deals with "chain reaction" rear-end collisions involving three or more vehicles. The language of the section and the corresponding diagram (below) specifically addresses the allocation of fault as between vehicles A & B, and as between vehicles B & C, but not as between vehicles A & C (which do not collide).



In *GAN General Insurance Co. v. State Farm Mutual Automobile Insurance Co.*[8], Justice Pitt held that, when rule 9 applies to an incident, there is no allocation of fault between vehicles that do not collide with each other. Therefore, the insurer of vehicle A has no ability to recover loss transfer indemnity as against the insurer of heavy commercial vehicle C.

However, in *Royal & Sunalliance Insurance Company of Canada v. Axa Insurance (Canada)*[9], Justice Chapnik held that, based on the intention of the legislation, the insurer of a vehicle that initiates a chain reaction collision is liable to indemnify all other insurers for the SABS payments flowing from the incident.

8 (1999), 19 C.C.L.I. (3d) 266 (Ont. S.C.)
9 2012 ONSC 3095

In *State Farm Mutual Automobile Insurance Company v. Old Republic Insurance Company of Canada*[10], Justice Perell applied the same rationale as Justice Chapnik in *Royal & Sunalliance Insurance* and found that, notwithstanding there was no collision between the heavy commercial vehicle (C) and the private passenger vehicle (A), 100% fault should be attributed to vehicle C and loss transfer indemnity is available to the insurer of vehicle A.

On further appeal of Justice Perell's decision in *State Farm Mutual Automobile Insurance Company v. Old Republic Insurance Company of Canada*[11], the Court of Appeal considered all of the conflicting decisions and essentially concluded that Justice Pitt's original interpretation was correct.

The Court's decision is founded on its interpretation of the term "incident". Justice Simmons, writing for the panel, cited six reasons why the word "incident" as used in s.9(4) "can refer only to the collision identified in the particular sub-clause - and that it cannot reasonably refer to the entire chain reaction".

Unlike Justices Chapnik and Perell, the Court of Appeal focused on the plain wording of the FDRs rather than principles of fairness to confirm that pursuant to s.9(4) of the FDRs, there is no apportionment of liability amongst non-colliding vehicles. Consequently, the insurer of the heavy commercial vehicle C which initiates a rear-end chain-reaction collision will not be responsible to pay loss transfer indemnity to the insurer of vehicle A.

10 2014 ONSC 3887
11 2015 ONCA 699

In the past, parties have generally accepted that loss transfer fault determined in accordance with the "ordinary rules of law" would be the same as liability determined by a court in a tort proceeding, however, the Ontario Court of Appeal in *State Farm Mutual Automobile Insurance Company v. Aviva Canada Inc.*[12] has now concluded that the interpretation and application of the "ordinary rules of law" in the context of loss transfer disputes is distinct from the approach required in a pure tort analysis.

The loss transfer dispute arose after a motorcyclist was inured when he swerved to avoid a vehicle turning left through a stopped lane of traffic. At the arbitration, the parties agreed that fault was based on "the ordinary rules of law" as prescribed by Rule 5(1) of the Fault Determination Rules (FDRs), but they were divided on how the Rule should be interpreted and applied. Rule 5(1) reads:

> 5.(1) If an incident is not described in any of these rules, the degree of fault of the insured shall be determined in accordance with the ordinary rules of law.

The arbitrator reasoned that any fault determination under the FDRs (including that made pursuant to Rule 5) must be informed by Rule 3 of the FDRs, as well as relevant *Highway Traffic Act* provisions, caselaw and in consideration of the potential outcomes under the FDRs.

Rule 3 is an umbrella provision which requires that the degree of fault be determined without reference to various circumstances. Rule 3 states:

> 3. The degree of fault of an insured is determined without reference to,
> (a) the circumstances in which the incident occurs, including weather conditions, road conditions, visibility or the actions of pedestrians; or
> (b) the location on the insured's automobile of the point of contact with any other automobile involved in the incident.

The Arbitrator opined that, if this case had been considered within the context of a tort action, some contributory negligence might be attributed the non-left turning vehicle. However, based on her analysis of the ordinary rules of law for loss transfer, she found the left-turning to be 100% at fault for the accident.

12 2015 ONCA 920

On appeal, Justice Spence set aside the award and declared that the non-left turning vehicle was only 50% at fault, finding that the Arbitrator erred in law when she disregarded the circumstances of the accident and failed to attribute contributory negligence to the motorcyclist.

On further appeal, the Court of Appeal agreed with the arbitrator and restored her finding that the left-turning driver was 100% at fault, noting that the "ordinary rules of law" does not mean "the ordinary rules of tort law". The Court noted that, if that was the legislative intention, it would have included the word "tort". Furthermore, the Court agreed that Rule 3 of the FDRs has general application and informs all fault determinations made under Rule 5(1).

The Court reinforced the notion that the central purpose of the Ontario loss transfer scheme is to provide an expedient and summary method of resolving indemnification claims, stating:

> A determination of liability in tort law is often a lengthy, detailed and nuanced process, which requires findings of fact on the very circumstances excluded from consideration by Rule 3. By precluding a pure tort law approach to fault determination, Rule 3 acts in harmony with the purpose of the legislative scheme because it promotes an expedient, more summary approach for determining fault.

Although the Court accepted that "determining fault without reference to pure tort law creates some uncertainty as to what can be referred to in making that determination.", it did not provide any clear guidance, direction or clarity to assist parties regarding what specific factors or principles should now be considered in applying the "ordinary rules of law" in loss transfer disputes.

Unfortunately, this decision has injected a measure of further uncertainty in the loss transfer world. Parties can no longer assume that the resolution of the liability dispute in the tort matter will determine or even guide the fault determination in the related loss transfer matter. All we really know is that, according to the Court of Appeal, fault determination under Rule 5(1) should not be made according to the ordinary rules of tort law and it should be done by a more expedient and summary method.

Multiple Deductibles Permitted

Justice Faieta of the Ontario Superior Court has just released a decision (*Economical Mutual Insurance Company v. Northbridge Commercial Insurance Company*[13]) finding that the $2,000 loss transfer deductible in s.275(3) applies to each person who receives accident benefit payments. Previously, the only appeal case dealing with this issue was a 1994 decision of Justice Holland (*Jevco Insurance Co. v. Progressive Casualty Co.*[14]) where the Judge found that the deductible was only applicable to indemnity claims for accident benefits paid to the named insured.[15]

Justice Faieta's decision is very well-reasoned and seems to accord with the purpose of the loss transfer deductible (more so than Justice Holland's). Justice Faieta recognized that loss transfer is claimant-centric and indemnity considerations could be different depending on the claimants and their insurers. Justice Faieta also accepted that below a certain threshold ($2,000), it would be inappropriate for insurers to have to incur transaction costs to reallocate losses in the loss transfer scheme. The Judge concluded:

> The approach of applying a single deductible greatly dilutes the pragmatic cost avoidance ... interpreting the deductible provided by s.275(3) of the *Insurance Act* to apply to each claim of indemnification for statutory accident benefits paid to each person involved in an accident is a just and reasonable result.

Technically, there are now two conflicting decisions from the same level of court. However, it is anticipated that insurers will likely accept Justice Faieta's interpretation and apply the deductible for all claimants subject to loss transfer, given the more thorough, thoughtful and compelling analysis provided by Justice Faieta and the impracticality of pursuing loss transfer indemnity for less than $2,000.

13 2016 ONSC 458

14 [1994] O.J. No. 3152 (Gen.Div.)

15 However, Arbitrator Malach decided not to follow that decision in *Farmers v. Cigna* (1997)