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Business

Rights, remedies between primary, excess insurers: Duties owed

By **Stephen Ross and Erin Crochetière**

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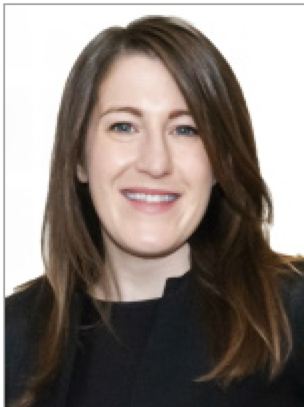

Erin Crochetière

(May 14, 2020, 12:08 PM EDT) -- This article examines the nature and scope of the duties owed between primary and excess insurers from a Canadian perspective, including a consideration of common issues that arise when multiple layers of insurance are potentially applicable to a claim.

The article is divided into three parts. Part three considers the general duty owed between primary and excess insurers, to act reasonably in the circumstances of any given case and provides practical advice to help insurers meet this duty. This part also outlines the duties owed between primary and excess insurers in the auto insurance context. Finally, part three provides a summary and conclusion regarding the underlying legal principles applicable to disputes between primary and excess insurers.

General duty to act reasonably

As such, it appears that there are a number of different approaches, and causes of action, that can be said to govern the relationship between primary and excess carriers and the nature of the rights and remedies that may be invoked as between them, including:

- Equitable subrogation;
- Equitable contribution; and
- A tort-based duty of care.

Although the cause of action may be characterized in different ways, all of the approaches share a common theme: the guiding principle at law as it relates to the relationship between primary and excess insurers is one of equity, fairness and reasonableness. The law recognizes that the actions and file handling of a primary insurer can have a direct and adverse impact on an excess insurer.

Similarly, once an excess insurer is put at risk by a claim, they too will likely have a duty to become involved in the adjusting of the claim, to act reasonably and to contribute towards defence costs.

As such, an excess insurer can likely, through one or more of the mechanisms set out above, hold a primary insurer to account (financially) in terms of the following non-exhaustive list of potential missteps:

- Failure to promptly investigate the liability and damages aspect of a claim as presented against the insured;
- Failure to take proper steps to control and adjust the loss in terms of due diligence, loss control measures and expert retention;

- Failure to advance defences reasonably available to the insured, including limitation periods or other legal defences to the claims advanced;
- Failure to contribute to a proportionate share of the defence and the plaintiff's costs of a claim in excess of the primary limits, with the contribution of each in proportion to the indemnity payments made, or to be made, by each insurer;
- Improperly eroding the limits by making *ex gratia* payments for claims not representing viable third-party liability claims as against the insured; and
- Failure to take reasonable steps to ensure the claim or claims are settled within the primary limits.

Similarly, a primary insurer should have a remedy against an excess insurer where the excess insurer (assuming it is put at risk by the claim) refused to share relevant information, acted unreasonably in the adjusting of the loss or in the conduct of settlement negotiations, or failed to contribute a proportionate share of defence costs.

Although it is likely that an excess insurer is entitled to receive a copy of the primary insurer's file (and vice versa) and to seek and review the support available for all payments made, the actual level of permissible scrutiny has not been well outlined at law.

It is the authors' view that an excess insurer should not be entitled to engage in an infinite retroactive analysis of all aspects of the primary carrier's file handling and payments. Different insurers may adjust the same claim differently and the law should concern itself with only major file handling issues or errors in judgment.

It is submitted that excess insurers should not be permitted to second-guess every decision made by a primary insurer. Only when the primary insurer's conduct falls below the standard of care expected of a reasonable liability insurer in similar circumstances should an excess carrier be entitled to a remedy at law.

Where circumstances warrant, the same standard should apply to the conduct of an excess insurer — to act as a reasonable liability insurer when put at risk by a loss.

Duties owed between primary, excess insurers in auto insurance context

The respective provincial *Insurance Acts* provide yet another source of law that may have implications in the context of disputes between primary and excess insurers, particularly in automobile insurance claims. For example, s. 257(4) of the Ontario *Insurance Act* provides: "Where indemnity is provided to the insured under two or more contracts and one or more of them are excess insurance, *the insurers shall, as between themselves, contribute to* the payment of expenses, costs and reimbursement for which provision is made in section 245 [costs of investigations, defence costs, costs assessed against the insured etc.] *in accordance* with their *respective liabilities* for *damages awarded against the insured*." [Emphasis added.]

As such, in the automobile context, the *Insurance Act* itself stipulates that primary and excess insurers should contribute proportionately to the costs of defending a claim.

Notably, there is some debate in the law regarding the circumstances to which this provision applies. In one decision, the Court of Appeal held that this provision only applies when a matter has proceeded to judgment, and not necessarily when a matter settles (see *ING Insurance Co. of Canada et al. v. Federation Insurance Co. of Canada* [2005] O.J. No. 1718, paragraph 33).

However, it is the authors' view that the outcome in that case was driven by its fairly unique and extreme facts and that, otherwise, the provision would and should likely have more widespread application.

There are other *Insurance Act* provisions applicable to an insurer's file handling in the automobile insurance context. If a primary insurer fails to follow the procedures as required by the Act, and the failure causes financial harm or prejudice to the excess insurer, it is likely that there are legal remedies available to the excess insurer.

In short, the duty owed by a primary insurer to an excess insurer is all the more robust in the automobile context given the heavily regulated and rather onerous nature of the obligations on third-party liability insurers in that milieu.

Conclusion

Although the law in Canada governing disputes between primary and excess insurers is in its infancy, remedies are available when an insurer's financial interests have been prejudiced by the actions of another insurer.

Whether the remedy arises out of the principle of equitable contribution, equitable subrogation, a duty of care in tort or by operation of statute, the law recognizes that, where an excess insurer is harmed by the unreasonable actions of a primary insurer, equity and fairness dictates that a remedy be granted.

In such circumstances, the primary insurer should be held accountable to the excess insurer for financial losses caused by the primary insurer's unreasonable conduct.

However, it is not enough that the excess (or other) insurer would have adjusted the claim differently. It is the authors' view that, so long as the primary insurer's actions were reasonable and met the standard of care expected of a reasonable liability insurer in a similar situation, an excess insurer should not be entitled to a remedy.

In this respect, primary insurers should ensure that they promptly investigate a claim, take all proper steps to control a loss and advance all defences reasonably available on behalf of an insured.

Similarly, where an excess insurer is put at risk by a claim, they should be required to become involved in the adjusting of the claim and be held to a standard of reasonableness. In particular, an excess insurer should be sure to share all relevant information, to act reasonably in not delaying settlement and contribute towards defence costs.

As stated at the outset, the law with respect to the rights and remedies as between primary and excess insurers is not well developed in Canada.

In this article, we explored the key authorities on point in the Canadian and U.S. context and looked to draw some overarching themes or principles.

In the end, we conclude that there is clearly a relationship of proximity between primary and excess insurers such that one party knows, or ought to know, that a failure to act reasonably on its part could cause financial loss to the other.

It is the writers' view that where an insurer is put at risk by a loss, the reasonable foreseeable losses that flow from the failure to act as a reasonable liability insurer in similar circumstances should also be recoverable.

It is hoped that this article provides some assistance as it relates to the state of the law in this area, and as it may relate to the development of a general duty as between primary and excess insurer to act reasonably, or to make good on the financial losses that flow from the breach of such a duty.

This is part three of a three-part series. Part one: Rights, remedies between primary and excess insurers: Introduction, guiding principles; part two: Rights, remedies between primary, excess insurers: Equitable subrogation, duty of care.

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