IN FACT AND IN LAW

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Damage Insurance

THE COURT OF APPEAL AUTHORIZES AN INSURER TO INSTITUTE A SUBROGATORY RECOURSE AS A PREVENTIVE MEASURE

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ON MAY 14, 2009, MADAM JUSTICE MARIE-FRANCE BICH OF THE COURT OF APPEAL, PUT AN END TO A CONTROVERSY IN THE CASE LAW ON THE INTERPRETATION BY ARTICLE 216 C.C.P. CONCERNING THE PROCEDURAL MEANS AVAILABLE TO THE INSURER TO PROTECT ITS SUBROGATION RIGHTS.[1]

THE COURT CONSIDERED THE FOLLOWING QUESTION: "CAN AN INSURER, WHO IS BEING SUED BY ITS INSURED FOR REFUSING TO PAY THE INDEMNITY, FORCE THE INTERVENTION OF A THIRD PARTY WHO IS POTENTIALLY LIABLE FOR THE LOSS?"

IN OTHER WORDS, WHERE AN INSURER DENIES COVERAGE IN THE CONTEXT OF THE CONTRACTUAL RECOURSE INSTITUTED BY ITS INSURED, IS IT DEPRIVED OF AN EXTRACONTRACTUAL (SUBROGATORY) RECOURSE AGAINST THE THIRD PARTY WHOM IT BELIEVES TO BE RESPONSIBLE FOR THE LOSS, WHERE THE INSURED CHOSE NOT TO SUE THAT THIRD PARTY?

AFTER THOROUGHLY REVIEWING THE CONTROVERSIAL CASE LAW ON THE ISSUE, THE COURT ANSWERED THE QUESTION IN THE AFFIRMATIVE, AND ALLOWED THE INSURER TO IMPLEAD THE POTENTIALLY LIABLE THIRD PARTY IN THE LITIGATION BETWEEN THE INSURER AND ITS INSURED.

[1] *Kingsway General Insurance Co.* v. *Duvernay Plomberie et Chauffage inc.*, 2009 QCCA 926, Gendreau, Morissette et Bich JJ.

THE FACTS

The facts were relatively simple.

Kingsway, the appellant (together with Lloyd's and Lombard) (hereinafter collectively referred to as "Kingsway") insured the property of Sanum Knit Fabrics Ltd. (hereinafter "Sanum").

Plumbing work was carried out by Duvernay Plomberie et Chauffage Inc. (hereinafter "Duvernay") at the premises of Sanum and, the following day, Sanum suffered significant damage as a result of water leakage, which it assessed at $248,000.

After spending $6,800 to limit the damage, Kingsway denied Sanum's claim, alleging that Sanum had made false statements regarding the circumstances surrounding the water damage, and that it had exaggerated the extent of the damage incurred.

Dissatisfied, Sanum instituted proceedings against Kingsway, who reiterated its grounds for the denial of the claim in its defence. However, Sanum neglected to sue Duvernay, even though it alleged in its action against Kingsway that the damage to its property had been caused by the faulty execution of the repair work performed by Duvernay.

Fearing that this omission would be detrimental to its interests, Kingsway filed an amended motion to institute proceedings in warranty and forced intervention against Duvernay, the third party potentially liable for the damage incurred by Sanum, in which it petitioned the Court for the following conclusions:

> [Our translation]
>
> GRANT this amended Motion to Institute Proceedings in Warranty and Forced Intervention;
>
> ORDER Defendant in Warranty and in Forced Intervention to intervene as Defendant in the main proceedings [...];
>
> ORDER Defendant in Warranty and in Forced Intervention to indemnify the main Plaintiff, Sanum Knit Fabric Ltd. in the event any judgment is rendered in its favour arising from the facts alleged in the Motion to Institute Proceedings;
>
> ORDER Defendant in Warranty and in Forced Intervention to indemnify Plaintiffs in Warranty and Forced Intervention for any judgment that may be rendered against them in the main proceedings, in principal, interest, additional indemnity and costs;
>
> [...]

Duvernay responded to Kingsway's recourse by filing a Motion for Dismissal of the Motion to Institute Proceedings in warranty and forced intervention for the reasons summarized by Madam Justice Bich as follows:

> [Our translation]
>
> [19] Respondent answers that the amended motion in warranty and forced intervention must be dismissed for two reasons that may be summarized as follows:
>
> - Having denied payment to their insured of the indemnity under the insurance policy, the appellants, who have no contractual or extra-contractual relationship with the respondent, may not invoke subrogation under 2474 C.C.Q., have no right of action against the respondent and, as a result, lack the legal interest to sue the respondent; therefore, it cannot implead the respondent.
>
> - Nor can a forced intervention be used as a means of adding a defendant to the main action, as the appellants seek to do, since such action is completely unrelated to the respondent's liability and concerns only Sanum and the appellants in their respective capacities as the insured and insurers. The respondent is foreign to this dispute and its participation is not required in the least to ensure the complete resolution thereof. The legal bases for the main action, as drafted, and for the action in liability which could be instituted against the respondent, whether by Sanum or by the subrogated insurer, are completely different.

JUDGMENT ON FIRST INSTANCE

On May 6, 2006, relying on the cases of *Agripak* v. *Compagnie d'assurance Guardian du Canada*[2] and *Gagné* v. *La Garantie compagnie d'assurance*,[3] Mr. Justice Pierre Tessier of the Superior Court, dismissed the recourse in warranty and forced intervention against Duvernay. He concluded that there was no subrogation because Kingsway had paid nothing to Sanum. Furthermore, given that the recourse by Sanum was solely based on the insurance contract, there was no reason to implead Duvernay since it could not be condemned on an extra-contractual basis to pay an indemnity instead of Kingsway, which had not yet paid anything.

ARTICLE 216 OF THE CODE OF CIVIL PROCEDURE (C.C.Q.)

Article 216 C.C.Q., which is at the heart of this debate, reads as follows:

> Any party to a case may implead a third party whose presence is necessary to permit a complete solution of the question involved in the action, or against whom he claims to exercise a recourse in warranty.

This provision permits any party to add a third party to a proceeding by way of forced intervention, or a defendant to call a third party into warranty.

The judgment deals with these concepts and other issues.

COURT OF APPEAL JUDGMENT

The Court of Appeal set aside the judgment of the Superior Court and attempted to find a practical solution to the situation.

Indeed, before dealing with the intricacies of the distinction between forced intervention and forced impleading and the scope of article 216 C.C.P., Madam Justice Bich shed some new light on these types of problematic situations in the following passage from her judgment:

> [Translation]
>
> [22] This case is quite unusual and calls for a solution that may in some respects, seem to stretch the usual rules, but which, in the end, will resolve a practical problem that is difficult to overcome, and do so in a manner that is compatible with the notion of the economical and effective management of legal resources.

[2] [2008] R.R.A. 394 (S.C.)

[3] B.E. 99BE-456 (C.Q.)

This was a clear reference to the guiding principle provided for in Article 4.2 C.C.P. and the Court of Appeal's concern to avoid a multiplicity of proceedings and ensure the effectiveness of the administration of justice.

Citing a series of judgments,[4] Madam Justice Bich then reviewed the various principles applicable to the forced intervention and impleading. She noted that the Court of Appeal, in *Eclipse Bescom Itée* v. *Soudures d'Auteuil inc.*[5], had ruled that actions in warranty presupposed that there was a pre-existing legal nexus or relationship. This required that the appellant in warranty prove, in order to institute the action, that it benefited from an obligation of warranty, which was frequently contractual, but could also be legal in nature.

Rejecting a legalistic interpretation of the criterion of necessity provided for in article 216 C.C.P. for the intervention of a party in a proceeding, Madam Justice Bich stated as follows:

[Translation]

[45] (...) it is appropriate to expand upon the meaning that we are to give to what is necessary for a complete solution of a dispute pursuant to article 216 C.C.Q., both to avoid the multiplication of proceedings relating to the same situation or factual cause (in this case, water damage at the premises of Sanum) and to avoid contradictory judgments. This is certainly consistent with the principles set forth in the *Code of Civil Procedure*, notably article 2, particularly given the reform in 2003, which clearly seeks to promote better management of judicial affairs and the more effective use of resources by limiting proceedings and recourses.

Madam Justice Bich then rejected the decisions which deny the insurer the right to call a third party into warranty on the basis that, where the insurer denies the insured's claim, it cannot yet be subrogated into the insured's rights (article 2474 C.C.Q.) because the subrogatory action has not yet come into existence.[6]

Commenting on the case of *Commerce & Industry* v. *Montréal*, [1993] R.J.Q. 475 (C.A.), in which the Court of Appeal recognized the possibility of an anticipatory subrogatory recourse under certain circumstances, she writes:

[Translation]

"[51] It is therefore the very occurrence of the loss that creates this prospective state of subrogation. Of course, unlike what happened in this case, in *Commerce and Industry Insurance Co.*, the insurer acknowledged its obligation to indemnify, which thereupon enabled it to "use all the rights of the insured against third parties". The refusal to indemnify in the present case cannot however preclude the potential subrogation arising from the loss (or the claim filed by the insured on the basis of such loss) and therefore prevent the appellants from relying on this potential subrogation to implead the respondent in the proceeding involving the insured. Let me explain.

[52] Whether the insurer pays the insurance indemnity voluntarily or following an order of the court, which always presupposes a denial of the claim, it is subrogated in the rights of the insured against the third party liable for the loss. Article 2474 C.C.Q. makes no distinction in this respect between the two cases (that is to say, voluntary and forced payment) and the insurer benefits from the subrogation in both cases. In a certain way, one may consider the insured's action against the insurer for payment of the indemnity as an episode in the processing of the claim which does not alter the dynamics of the subrogation nor can it preclude the "prospective subrogation", discussed in the case of *Commerce and Industry Insurance Co., supra*, which is a prospective or *in futuro* subrogation that is sufficient, from a procedural point of view, to confer on the insurer a sufficient interest to act against the third party who caused the loss, at the very least by attempting to protect its potential subrogatory recourse from prescription, which would otherwise be acquired. (our emphasis).

Madam Justice Bich distinguished the situation in the case before her from that in the case of *Éclipse Bescom* case, as follows:

[Translation]

"[61] On the one hand, in a very concrete manner, by allowing the respondent to be impleaded in this case, according to the terms discussed above, we are already putting in place the procedural framework necessary for an order to be made against the person who truly caused the loss in the event that a judgment concludes that the respondent is liable, and, in the end, orders the appellants to pay Sanum the indemnity under the insurance policy. The idea behind subrogation in the context of insurance, as expressed

[4] *CGU* v. *Wawanesa*, [2005] R.R.A. 312 (C.A.); *Fonds d'assurance responsabilité professionnelle du Barreau du Québec* v. *Gariépy*, [2005] R.J.Q. 409 (C.A.); *Cegerco Constructeur inc.* v. *Tetra Pak Canada inc.*, [2002] R.J.Q. 648 (C.A.); *Lavigne* v. *Turgeon*, J.E. 98-763 (C.A.); *Allard* v. *Mozart Itée*, [1981] C.A. 612

[5] [2002] R.J.Q. 855 (C.A.)

[6] *Touzin* v. *Assurance générale des Caisses Desjardins*, [2003] R.L. 64 (S.C.); *Yazaryan* v. *Palandjian*, B.E. 2005BE-523 (S.C.); *Agripak Itée* c. *Compagnie d'assurance Guardian du Canada*, [2008] R.R.A. 394 (S.C.); *American Home Assurance* c. *Construcsim inc.*, J.E. 2004-1750 (S.C.)

in article 2474 C.C.Q., is that we wish to ensure that in the end the person who caused the damage, i.e. the person legally liable for the damage, is ultimately held accountable for it. Therefore, by authorizing the impleading of the respondent, we enable *all* the actors in the dispute arising from the loss to be present, and in doing so mobilize the legal system only once to resolve all the issues of fact and law raised by this loss.

[62] At the same time, by allowing the impleading at this stage, this interrupts the prescription period from running against the respondent (or will have had this effect from the date of service of the proceeding in first instance). As we know, the rights of the insured Sanum against the respondent are prescribed by three years (and in the present case, by three years from January 16, 2006, the date of the loss), which would normally have expired on January 16, 2009. Now, if we disallow the impleading, such prescription will have been irremediably acquired, since the insured will not have sued the respondent in time. And if the prescription of the insured's rights were thus acquired, the subrogation of the appellants in these rights, in the event that a judgment ordered them to pay the insurance indemnity, would be impossible. On the other hand, by allowing the respondent to be joined in the debate as a full party thereto, we interrupt the prescription (or acknowledge that it was interrupted by the impleading application), and we accordingly protect the right of subrogation conferred on the appellants by article 2474.

[63] This double consequence in no way harms the insured or the respondent, who suffers no prejudice, whether by being required to answer in a Court of law for the fault with which it is charged, or by being denied the benefit of the extinctive prescription in its favour. By so doing, we rather ensure (in keeping moreover with the objective of article 2474 C.C.Q.) that the person who truly caused the loss does not escape liability.

And further:

[67] Now, if the insurer is responsible for protecting its right of action against third parties, as we assert in the excerpt above, which is not an unreasonable proposition, it seems appropriate to allow it to do so by impleading the said third party in the action instituted against it by the insured, where the insured has not done so itself. As for the third party thus impleaded, I repeat, it suffers no prejudice, since it can neither complain about being brought into a legal debate which could lead to a finding of civil liability against it, nor about not benefiting from extinctive prescription." (our emphasis)

COMMENTS

The Court of Appeal has therefore proposed a practical solution to a problem that, although rather theoretical, has given headaches to attorneys representing insurance companies. In situations where the insurer denied coverage, and the insured sued the insurer but not a third party who was potentially ultimately liable, insurers' attorneys were being forced to use various strategies to avoid the prescription of the insurer's recourse against the third party. Insurers will now be able to bring the third party who is potentially liable into the dispute by way of a forced impleading. Their argument will be that this is necessary for a full resolution of all the issues connected with the same fact situation, that is: the insured's right to indemnification by the insurer, and the finding of liability against the person actually responsible for the loss.

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