IN FACT AND IN LAW

Damage Insurance

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Nullity of an Insurance Contract and Criminal History: Clear and Specific Questions Must Be Asked

By Bernard Larocque

On February 8, 2005, the Court of Appeal issued two judgments[1] that clarify the burden of proof of the parties with respect to the nullity of an insurance contract. These two judgments are all the more interesting given that they deal with the issue of the impact of criminal history on the moral risk that the insured or the prospective insured poses for an insurer.

The Rouette *judgment, written by Mr. Justice Dalphond, sets out the principles and criteria that must guide the courts when determining whether a policy should be annulled. The* Bergeron *decision, rendered by the same judges and also for the reasons expressed by Mr. Justice Dalphond, merely applies the same principles.*

The Facts

The *Rouette* Case

Mr. Rouette entered into a long-term automobile lease in March 1999. Wawanesa, his prospective insurer, asked him through its representative whether he was ever found guilty of "impaired driving" or had any "revocation or suspension of his driver's licence". All the questions pertained to the operation of motor vehicles, including the number of claims that occurred during the six preceding years. No question aimed at determining whether the insured had a criminal record for any other type of offences.

Following an accident that occurred in November 2000, the vehicle was declared a total loss. It should be noted that Mr. Rouette had previously filed three other claims and had been indemnified on two occasions by Wawanesa for claims related to another vehicle.

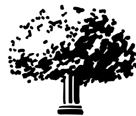
In the course of its investigation, the insurer discovered that Mr. Rouette had a significant criminal record for offences committed between 1980 and 1991, such as:

- breaking and entering;
- theft;
- possession of an instrument suitable for the purpose of committing an offence;
- possession of property obtained by crime;
- abetting fraud;
- impersonation;
- fraud;
- possession of drugs;
- refusal to comply with a probation order;
- etc.

The *Bergeron* Case

Mr. Bergeron was the owner of a motor vehicle since 1992. In 1998, he insured the vehicle with Lloyd's. Less than a month after the effective date of the policy, the vehicle caught fire and was totally destructed. The fire seemed to have originated from a mechanical defect.

The insurer discovered that Mr. Bergeron had been convicted of criminal offences between 1984 and 1998, namely:



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[1] *La Compagnie Mutuelle d'Assurance Wawanesa* vs. *Rouette*, Court of Appeal, Justices Beauregard, Dalphond and Doyon, 500-09-013929-039, February 8, 2005.

Bergeron vs. *Lloyd's Non-Marine Underwriters*, Court of Appeal, Justices Beauregard, Dalphond and Doyon, 500-09-010512-010, February 8, 2005.

- conspiracy and theft of a motor vehicle (1984);
- possession of stolen auto parts (1995);
- possession of stolen motor vehicle parts (1996);
- possession of a stolen container (1998).

The insurer therefore considered that the insurance contract was invalid and refused to pay the indemnity.

The Evidence

In both the *Rouette* and *Bergeron* decisions, the insurers relied on the testimony of three insurance company representatives, namely, a representative of their own respective companies and two representatives of independent companies. In both cases, the insurers maintained that the criminal history constituted an increase of the moral risk and that they would not have accepted such risk had they known about the criminal past of insureds Rouette and Bergeron.

In the *Rouette* case, the trial judge concluded that the contract was valid, that the insured did not make any false declaration or concealment and that Wawanesa failed to demonstrate the "materiality" or even the relevance of the criminal record in respect of the insurance contract.

In the *Bergeron* case, the trial judge ruled that the circumstances were relevant and that the policy had to be annulled since Bergeron's criminal past would have constituted, in the eyes of a reasonable person, a material fact that the insured had the obligation to disclose to his insurer.

The Court of Appeal Judgments

The Court confirmed the validity of the two insurance policies issued by Wawanesa and Lloyd's. However, it ruled in both cases that the criminal history of the insured was of such a nature as to influence a reasonable insurer in its decision to accept the risk and recognized that had the insurers known about such criminal histories, they would not have accepted the risks. Nevertheless, relying on Article 2409 C.C.Q., the Court concluded that in both cases, a reasonable insured would not have deemed it necessary to disclose his criminal history and therefore did not have to disclose it.

The Court noted the history of the relevant provisions, namely, Articles 2408 and 2409 of the *Civil Code of Québec*.

Mr. Justice Dalphond concluded that by passing such provisions, the legislator had intended to reconcile the interests of the insurer and the insured. The legislator therefore imposes on the insurer the obligation to demonstrate that the omitted information was such that it would have influenced the decision of a reasonable insurer. If the insurer succeeds in so demonstrating, the insured then bears the burden of proving that he nevertheless behaved as a normally provident insured would have.

The Insurer's Burden

According to the Court of Appeal, the insurer's burden of proof is comprised of three steps:

- a subjective step, that is to say that if the insurer had been correctly informed, it would not have accepted the risk;
- objective evidence that another reasonable insurer would have behaved in the same way;
- a step consisting in demonstrating to the judge that the practice of these insurers is reasonable.

With respect to the objective evidence, in both decisions (*Bergeron* and *Rouette*), the insurers succeeded, in demonstrating to the Court that the undisclosed information was relevant to them.

As for the second step, Wawanesa and Lloyd's succeeded in proving, through the testimony of representatives of other insurers having experience in underwriting insurance policy, that other insurers would have behaved in the same way they did.

Lastly, with respect to the third step, it is not sufficient for an insurer to prove that two other insurers would have behaved in the same way it did. It also has to convince the Court that such decision is rational and objective, in the sense that the general practice is reasonable, by setting out the reasons why the undisclosed elements would increase the risk for an insurer.

For instance, a conviction for gross indecency would not increase the risk with respect to the owner or driver of a motor vehicle, no more than a conviction for shoplifting would represent a greater risk of an accident occurring. In some cases, it could go as far as presenting statistical evidence.

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However, the Court of Appeal came to the conclusion, in both cases, that the prior convictions of Messrs. Rouette and Bergeron were relevant in the assessment of the risk since they increased the likelihood of fraudulent claims.

The Insured's Burden

The novelty of these decisions lies in the analysis by the Court of Article 2409 C.C.Q., which reads as follows:

> **"Art. 2409. The obligation respecting representations is deemed properly met if the representations are such as a normally provident insured would make, if they were made without material concealment and if the facts are substantially as represented."**

The insured must demonstrate that he acted as a reasonable person would have under similar circumstances. The Court insists on the fact that the prudent concept of the "normally provident insured" is to be analysed in light of the circumstances and the insured's knowledge of insurance and related issues. Therefore, a business having an insurance department comprised of representatives from the insurance industry will not necessarily be judged on the same basis as someone who does not have any special knowledge of insurance.

In both cases, the Court concluded that, in the light of the questions asked by the insurers, a reasonable insured would not have disclosed his criminal history. It noted that in both cases, the insureds did not make any false representations and correctly answered all the questions that were put to them. In the *Rouette* case, since the insured had been asked about certain types of convictions, the Court was of the opinion that a reasonable insured would have concluded that the other type of convictions were of no interest to the insurer. In other words, Mr. Justice Dalphond concluded that, although a residual obligation remains to disclose relevant facts, an insurer who asks questions on a subject while delimiting them, defines its requirements and must live with the consequences.

The reasoning in the *Bergeron* case is the same. If a reasonable person, asked a specific question as to the nature of the actions and the period of time during which they were committed may conclude that only the actions that are relevant to the question interest the insurer and constitute circumstances likely to influence its decision, he will be deemed to have reasonably answered the question. In these circumstances, the importance of Mr. Bergeron's criminal record failed to convince the judge of the contrary.

In conclusion, insurers must reflect on the following excerpts of Mr. Justice Dalphond's decision in the *Rouette* case:

> **[Translation] "[42] In conclusion, if the insurers do not wish to insure persons with a criminal record that is unrelated to the operation of a motor vehicle or possession thereof, they have to directly ask the appropriate questions to applicants."**
>
> **"[43] To be sure, the current situation, where the insurer fails to ask a question to applicants who have a criminal record except as to offences related to the operation of a motor vehicle that they would have committed during a definite prior period of time, then collects premiums for years and, upon the occurrence of a loss, concludes that the policy is void, is unacceptable. The insurer cannot, on the one hand, benefit from the premiums of persons that it deems undesirable as a group and, on the other hand, invoke the nullity of the policy when one of such persons suffers a loss."[2]**

This judgment is rather severe and fails to take into account the fact that premiums are determined for a risk that is both future and time-limited. However, these considerations failed to impress the Court.

Such is the current state of jurisprudence. A file analysis concluding to denial of coverage on the grounds of a failure to disclose a criminal record will henceforth have to take it into account.

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[2] *La Compagnie Mutuelle d'Assurance Wawanesa* vs. *Rouette*, Court of Appeal, Justices Beauregard, Dalphond and Doyon, 500-09-013929-039, February 8, 2005, pp. 13-14.

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