IN FACT AND IN LAW

Life and Disability Insurance

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The Court of Appeal clarifies the extent of a financial institution's duty to inform in situations involving loan insurance

By Evelyne Verrier

On July 17, 2006, the Court of Appeal rendered a judgement concerning the duty of financial institutions making loans to inform and advise their clients.[1] *This decision, written by Judge Jacques Chamberland, sheds further light on the obligations of group loan insurance policyholders.*

The facts

In early June 1994, the Respondent, 9000-7048 Québec inc. ("9000-7048"), the share capital of which was held 50/50 by Gratien Drapeau and Michel Miller, approached the Appellant to borrow $250,000 to finance a commercial building development.

The Appellant agreed on condition that it be granted a moveable hypothec over certain equipment and that Messrs. Drapeau and Miller guarantee the loan. At the same time, they applied for life insurance coverage provided under a group insurance policy that The Prudential Insurance Company of America had issued in favour of the Appellant. In its narration of the facts,

the Court of Appeal insisted on the latter point and, contrary to the trial judge's finding, emphasized that life insurance coverage was not one of the Appellant's conditions for granting the loan.

An insurance application was completed and signed by Messrs. Drapeau and Miller and the insurance premiums were automatically debited from the Respondent's bank account from November 23, 1994 to February 1996.

Part 2 of the insurance application reads as follows:

[translation]

"To be eligible for life insurance, you must be at least 18 years old and less than 70. The maximum amount is $3,000,000 (for all insured business loans). For each insurance application, a Part 3 "Health Declaration" must be completed. Where the aggregate of all your business loans is $200,000 or more but less than $500,000, you must provide evidence of insurability in the form of blood tests (a paramedical service will contact you shortly).

In addition, you must complete a detailed health questionnaire (Form No. 13844F) if one of the following conditions applies:

a) you answered "Yes" to any of the questions in Part 3 "Health Declaration";

b) you applied for insurance more than 31 calendar days after the authorization date of your business loan or line of credit;

c) the aggregate of all your insured business loans is $500,000 or more;

[1] *Banque Nationale du Canada* v. *9000-7048 Québec inc.*, July 17, 2006, 200-09-004980-048, Judges Robert, Chamberland and Dutil.

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The Prudential will examine the health declaration and questionnaire and inform you whether it has approved or refused your insurance application."

And Part 6 reads as follows:

[translation]

"I (we) hereby authorize The Prudential Insurance Company of America, to debit my (our) chequing account indicated below monthly for all amounts owing in relation to this insurance coverage. This authorization may be cancelled at any time upon written notice to that effect from me (us)"

(emphasis added)

Towards the end of November 1994, a nurse contacted Messrs. Drapeau and Miller to complete the medical questionnaire required by the insurer and to obtain the blood samples. They refused to undergo the tests requested by the nurse. She then informed the insurer, who closed its file.

It was only in early March 1996, several months before Mr. Drapeau's death on November 1, 1996, that the insurer reimbursed the insurance premiums that had been collected by crediting the Respondent's account with an equal amount.

According to the insurer, each of Messrs. Drapeau and Miller had been notified, by a letter dated December 5, 1994, of its decision not to act on the life insurance application. However, there was nothing on file proving that the two letters had been actually mailed and received, and Mr. Miller stated that he never received the letter intended for him. The Bank did not remember receiving a copy of any such letters, of which there were no copies in its files.

Thus, it was only after Mr. Drapeau's death that 9000-7048 became aware that the insurance file had been closed ever since December 1994.

The Superior Court's judgement

Based on the foregoing facts, the trial judge held that the Bank had committed a fault thereby rendering itself liable towards 9000-7048, in essence due to its negligence in not following-up with the group insurance file, given that the Bank was the company's mandatary for the purposes of obtaining the life insurance coverage. Moreover, the Bank had not provided the applicants with a copy of the duly completed and signed insurance application form, contrary to the requirements of section 282 of the *Regulation respecting the application of the Act respecting insurance*[2] *(*the "*Application Regulation*"*)*. From June 1994 to March 1996, the Bank also led its clients to believe that they were insured by deducting the insurance premiums during that period.

Basing itself on the provisions of article 2139 of the *Civil Code of Québec* concerning mandates, the Court's view was that the Bank, specifically as the policyholder, had not been diligent in administering the contract and that the situation in which 9000-7048 found itself was the result of the Bank's negligence. The Court therefore rendered judgement against the Bank up to the amount of the balance owing on the loan on the date of Mr. Drapeau's death.

[2] R.S.Q., c.A-32, r.1, sec. 282.

[3] *Compagnie Trust Royal* v. *Luc Veilleux,* [2000] R.R.A. 53, *57*.

The Court of Appeal's judgement

At the outset, the Court stated that no contract governing the Bank's obligations as the policyholder of the group insurance contract had been filed into evidence, with the result that it would be risky to express an opinion regarding the services that the Bank may have undertaken to provide the insurer.

Justice Chamberland then cited the principle that he himself had stated in *Compagnie Trust Royal v. Luc Veilleux,* and that the trial judge had made his own:

[translation]

"[27] I am therefore inclined to characterize the basic contractual relationship between the Appellant and the clients, including Paulette Veilleux, who used its services to finance the purchase price of a building, as a service contract. The Appellant thereby undertakes to inform its clients of the various financial services that it offers and properly advise them. Thus, it is required to act in the best interests of its clients, prudently and diligently; however, it does not have an obligation of result.[3]"

(emphasis added)

Contrary to the trial judge, the Court of Appeal was of the view that the Appellant had not failed to fulfil that obligation. Indeed, the Appellant's representative had recommended life insurance to its clients, helped them to complete the application form, explained that evidence of insurability in the form of blood tests was required, forwarded the duly completed and signed application form to the insurer and informed Mr. Drapeau that a nurse would contact him and his partner, Mr. Miller, to carry out the blood tests, which occurred towards the end of November 1994.

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The Court then deals with one of the arguments put forward by 9000-7048, being that the Bank failed to provide a copy of the application form to its clients, as required by sections 281 and 282 of the *Application Regulation*[4].

Because the case before the Court did not involve misrepresentations made by the applicants, the fact that the Appellant had failed to provide a copy of the form would not, in this context, constitute a fault rendering it liable towards the Respondent. Indeed, the absence of coverage on the date of the death was due primarily to the careless disregard of Messrs. Drapeau and Miller who saw fit to not provide the requisite blood samples. Mr. Miller refused because he was afraid of fainting, whereas Mr. Drapeau asked the nurse to start with his partner Miller and get back to him in the event she was successful. However, the explanations provided by the Bank's representative and the application form itself were clear as regards the blood test requirement.

The Court then considered a further argument submitted by 9000-7048, being that the Bank was negligent in managing the file, in contravention of section 258 of the *Application Regulation*[5], which reads as follows:

> **"258. The policy-holder of a group life insurance contract must be able to provide for the management of the master policy and for the collection and remittance of premiums."**

While acknowledging that the Bank could have been more rigorous in managing its files, the Court did not believe that the absence of follow-up of the file constituted a fault. In the Court's view, and given that no contract defining the Bank's obligations was submitted into evidence, the Appellant did not have an obligation towards 9000-7048 in that respect. Once the insurance application was sent to the insurer, the insurer assumed responsibility for examining the application, making its decision in relation thereto and ensuring that the insurance premiums were debited from 9000-7048's bank account pursuant to the authorization provided in the application. In the event of refusal, the insurer was responsible for informing the applicants and reimbursing the insurance premiums collected, which it was slow in doing, but did before Mr. Drapeau's death.

The Court therefore allowed the appeal, quashed the judgement in first instance and dismissed 9000-7048's lawsuit against the Bank.

Conclusion

To summarize, the Court of Appeal defined the Bank's duty to inform and advise its clients when it acts as the policyholder of a group insurance contract. It should be noted that, in this case, the insurance on the life of the two shareholders was not a condition of the loan, and the Appellant never led its clients to believe, either in writing or verbally, that their lives were insured.

Furthermore, as the insurer was not being sued and no contract governing the respective obligations of the policyholder and the insurer had been put into evidence, consideration of section 258 of the *Application Regulation* was irrelevant.

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[4] R.S.Q., c.A-32, r.1, ss. 281-282

[5] R.S.Q., c.A-32, r.1, s. 258

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