

A Commentary on Recent Cases and Relevant Legal Issues

1. *Limitations Act, 2002* – Important Changes Regarding Claims for Contribution and Indemnity

Although the *Limitations Act, 2002* (the “*Act*”) has already been in force for two years, its interpretation and application by the Ontario courts is still in its infancy.

As of January 1, 2004, when the *Act* came into force, defendants no longer have one year post judgment in the main action to commence their claims for contribution and indemnity.

Pursuant to section 18 of the *Act*, defendants in actions served after January 1, 2004 have only two years from the date of service of the Statement of Claim to claim over for contribution, whether by way of crossclaim or third party claim.

As a practical matter, this is a significant change because co-defendants will often agree to hold off on initiating crossclaims against one another (reserving their rights to do so in the future). This can be a useful tool in order to maintain a united front vis-à-vis the plaintiffs. However, if the parties employ the same strategy in claims served after January 1, 2004, they run the risk of running out of time if two years go by without issuing a crossclaim.

Consequently, defendants who wish to reserve their rights to claim over against one another for contribution and indemnity

would be wise to issue their crossclaims at the outset (i.e., when they deliver their Statements of Defence) even if they agree with their co-defendants not to actively pursue them for the time being. The inquiries into potential third parties must also be conducted at an early stage of an action.

2. *Limitations Act, 2002* – Death of the “Standstill Agreement”

Before the enactment of the *Limitations Act, 2002* (the “*Act*”) businesses, insurers and adjusters alike often entered into standstill agreements as a practical approach to avoid potential litigation. By virtue of such agreements, the parties would agree to suspend the statutory limitation period pending a reasonable opportunity to investigate and potentially resolve any given conflict without resorting to litigation.

As of January 1, 2004, when the *Act* came into force, agreements to suspend or extend a limitation period are no longer generally permissible pursuant to section 22. That section does not affect or set aside standstill agreements entered into before January 1, 2004.

The prohibition against entering into standstill agreements is proving to be problematic and is creating unnecessary litigation which might otherwise be resolved through successful negotiation. The Ontario government has recognized that there is a

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problem with section 22 of the *Act* and recently introduced Bill 14/06, which will permit agreements to suspend or extend limitation periods.

The proposed legislation would not allow parties to mutually agree to shorten a prescribed limitation period. However, if Bill 14 is enacted, it will enable businesses, insurers, adjusters and others to resume their previous practice of postponing litigation, in appropriate circumstances, while they explore practical solutions which may avoid formal litigation.

Bill 14 passed second reading by the Legislature on April 11, 2006, which brings Ontario one step closer to the revival of the standstill agreement. We will continue to follow the progress of Bill 14 and will report on this issue in future editions of our Newsletter.

3. CGL Policies – Has the Ontario Court of Appeal opened the Flood Gates for Insurance Claims by Contractors?

On April 5, 2006, the Ontario Court of Appeal released an important decision that may have a profound impact on construction litigation across Ontario and beyond.

In *Bridgewood Building Corporation v. Lombard General Insurance Company*, Lombard insured two general contractors under two Commercial General Liability (CGL) policies, but denied indemnity to them for the cost of repairing new homes that had structural deficiencies attributable

to defective concrete supplied by a subcontractor.

The judge who heard the initial application for coverage had ordered Lombard to indemnify the contractors. Lombard subsequently appealed to the Ontario Court of Appeal.

Lombard took the position that there was no coverage under the CGL policies because it is a well settled “general principle” that CGL policies are not intended to cover repair or replacement costs arising out of an insured’s own defective work or product. In other words, the “general principle” was that CGL policies are intended only to cover an insured’s tortious liability to third parties, not including the repair or replacement of its own work.

The Court of Appeal rejected this argument, stating that the key to coverage did not lie in what might be widely understood as the general nature of a CGL policy and on “general principles” of insurance law. Rather, the focus in determining coverage should be upon the language of the insuring agreements and their interpretation based on the words the parties have used (any ambiguities to be resolved in favour of the insured pursuant to the doctrine of *contra proferentem*).

In particular, the focus should be on what the policy actually said, whether the alleged acts fell within its provisions, whether any exclusion applied to take the claim outside of coverage, and whether there were any exceptions to that exclusion which would

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operate to bring the claim back into the insuring agreement.

In this case, the Court of Appeal found that the claims fell squarely within the insuring agreement and also within the exception to the “your work” exclusion, which stated that the exclusion did not apply if the damaged work, or work out of which the damage arose, was performed on the contractor’s behalf by a subcontractor.

This decision may have a tremendous impact on construction litigation because it widens what was traditionally understood to be the scope of the CGL policy. This is good news for contractors seeking coverage for defects arising from the work of their sub-contractors. In multi-party litigation, engineers and other consultants may also benefit from expanded coverage for contractors because, as a practical matter, this may result in more “deep pockets” at the negotiating table. However, it can be expected that insurers will review their policy wordings, in light of this decision, to more clearly restrict the ambit of their CGL policies.

4. *Kohanski v. St. Paul Guarantee Insurance Company - Duty to Defend - Directors’ and Officers’ Liability Policy - “Insured-versus-Insured Exclusion”*

On March 4, 2006, the Ontario Court of Appeal granted an appeal by St. Paul Guarantee Insurance Company (“St. Paul”) and set aside an order requiring the insurer to defend Kohanski (a former director and

President of a professional association) in an action commenced against him.

In January 2003, two former employees of Master Insulators’ Association of Ontario (“MIA”) sued MIA, alleging breach of contract, wrongful dismissal, bad faith discharge and defamation. MIA counterclaimed against the employees and added Kohanski as a defendant to the counterclaim. MIA claimed damages against Kohanski for breach of fiduciary duties, conspiracy, and breach of ss. 134 of the *Ontario Business Corporations Act*.

After putting St. Paul on notice of the claim, the insurer denied coverage to Kohanski on the basis of Section IV(7) of the policy, which provided that the insurer would not be liable to make payment for loss in connection with any claim brought by the corporation against its own directors and officers. Since MIA had brought the counterclaim against its own director, the insurer refused to respond to the claim.

The judge who first heard the application by Kohanski concluded that the insurer owed a duty to defend. This was overturned on appeal, with the Court of Appeal ruling that the applications judge had erred in finding a duty to defend in the circumstances of this case.

The Court of Appeal found that while the insurer may have had to respond on behalf of Kohanski if the former employees had sued him directly, there was no duty to defend a counterclaim by MIA against its own director by virtue of the exclusion

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clause (known in insurance parlance as an “insured versus insured” exclusion).

The Court of Appeal went on to conclude that because MIA’s claim was clearly and unambiguously excluded from coverage, St. Paul could not have a duty to indemnify Kohanski under the policy. There being no possibility of a duty to indemnify, the insurer could have no duty to defend.

5. *Allan v. CHC (Canada) Casinos Ltd.* – Adjusters’ Reports and Litigation Privilege

As an insurer or a business operator, have you ever wondered whether investigative reports prepared before litigation commences or is threatened will be producible if a lawsuit ensues?

In *Allan v. CHC*, a 2005 decision of the Superior Court of Justice, a casino retained an adjuster to investigate a slip and fall on its premises. While the injured individual had not yet retained a lawyer or commenced a lawsuit, the casino was being proactive in trying to “cut [potential litigation] off at the pass” by investigating and attempting to negotiate a settlement. Subsequently, when litigation ensued, the plaintiff sought production of the adjuster’s reports.

The motions judge dismissed the motion and ruled that the documents were subject to litigation privilege and therefore not producible. In ruling in favour of the casino, the court did not distinguish between investigating a claim for the purpose of negotiating a settlement and investigating a claim for the defence of litigation. In the

judge’s view, “they are simply way points on the same path.”

In ruling that the adjuster’s reports were privileged, the court distinguished this fact scenario from situations where documents were producible because they had been generated by insurers in the ordinary course of fulfilling their contractual obligations to their own insureds (e.g., where an insurer was responding to and assessing an insured’s first party claim).

This decision is good news for businesses and their insurers who wish to be proactive in investigating and attempting to settle third party losses before they turn into lawsuits, without fear that the investigative reports they obtain may be producible if litigation ensues.

6. Litigation Privilege – Letters to Experts – Are they Producible?

Whether opposing parties in a lawsuit can have access to a letter of instruction or retainer to an expert is an interesting topic and still an uncertain one in Ontario. This issue is relevant not only to lawyers, but also to parties to the litigation, their insurers and the professional consultants who have been retained to act as experts.

There are several earlier cases that have refused production of instruction letters (e.g., *Calvaruso v. Nantais* [1992] O.J. No. 345 (Gen. Div.) and *Mahon v. Standard Life Insurance Company* [2000] O.J. No. 2042).

However, in a more recent decision, *Walker v. Baskin Robbins* [2004] O.J. No. 1930, the

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court ordered production of a lawyer's instruction letter where the expert's report made specific reference to the instruction letter being one of the pieces of information relied upon by the expert in arriving at his conclusions.

There remains considerable uncertainty as to when a letter of instruction to an expert may be producible in litigation. Accordingly, as a lawyer, adjuster or insurer, the safest approach to take when retaining an expert is to assume that there is a very real prospect that the letter of instruction may be producible in a lawsuit.

While perhaps stating the obvious, the letter of instruction should be as neutral as possible and should never suggest the conclusion that you would like the expert to reach. This will not only avoid the potential embarrassment of a prejudicial letter, but more importantly any potential impact on the perception of the expert's independence and objectivity.

If you have been retained as an expert, and the letter of instruction to you is lacking in detail, you can always request additional information by telephone or in a meeting from the party who retained you.

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