SUPREME COURT OF NOVA SCOTIA
Citation: *Grafton Connor Property Inc. v. Murphy*, 2015 NSSC 195

Date: 2015-06-30
Docket: Hfx No. 293148
Registry: Halifax

Between:

GRAFTON CONNOR PROPERTY INCORPORATED, a body corporate, c.o.b. GRAFTON-CONNOR GROUP, and BEAUFORTH INVESTMENTS INCORPORATED, a body corporate, c.o.b. NORTH END BEVERAGE ROOM

Plaintiffs

v.

SEAN MURPHY, in his quality as Attorney in Fact in Canada for Lloyd's of London Underwriters and MARSH CANADA LIMITED, a body corporate

Respondent

Judge:	The Honourable Justice Arthur J. Leblanc
Heard:	June 9-13, 16-20, 23-27 and 30, July 2-4, and October 30, 2014 in Halifax, Nova Scotia
Final Written Submissions:	October 30, 2014
Counsel:	John P. Merrick, Q.C., Darlene Jamieson, Q.C. and Tammy Manning for the Plaintiffs Michael S. Ryan, Q.C. and Richard W. Norman, for the Defendant Sean Murphy Christopher C. Robinson, Q.C., Kevin Gibson and Ian Dunbar, for the Defendant Marsh Canada Limited

By the Court:

[1] The North End Beverage Room ("North End Pub" or "the Pub") in Halifax was consumed by fire on March 7, 2007. The building was owned by Beaufort Investments Incorporated, part of a group of companies with shared ownership and management collectively known as the Grafton Connor Group of Companies ("Grafton Connor").

[2] At the time of the fire, the North End Pub was insured by Lloyd's of London Underwriters ("Underwriters") under an insurance policy effective from July 1, 2006 to July 1, 2007 (the "Policy"). The Policy, which insured all Grafton Connor locations, had been placed with Underwriters through Marsh Canada Limited ("Marsh"), a registered insurance broker.

[3] In the course of investigating the fire, Underwriters discovered that, contrary to the information it received at the time it bound coverage, the Pub was neither sprinklered, nor was it entirely of masonry construction. As a result, Underwriters denied the claim on the basis of material misrepresentation.

[4] Following denial of the claim, Grafton Connor commenced this action against Underwriters and Marsh.

Positions of the Parties

Grafton Connor

[5] Grafton Connor says the misinformation concerning the construction of the North End Pub and the existence of a sprinkler system does not entitle Underwriters to void coverage under the Policy. It pleads and relies on Endorsement 10 to the Policy, which reads, in part, "Any unintentional error or omission made by the Insured shall not void or impair the insurance hereunder …"

[6] Alternatively, if the court concludes that Endorsement 10 does not apply, Grafton Connor says Underwriters was negligent in its assessment of the risk in relation to the North End Pub. According to Grafton Connor, if Underwriters had met the standard of care of a reasonably prudent underwriter, the errors regarding the construction and the sprinkler system would have been discovered. But for the negligence of Underwriters, Grafton Connor says it would have been able to obtain valid coverage with Underwriters or another insurer.

[7] In the further alternative, if Underwriters was entitled to void the Policy and is not liable in negligence for the value of the loss, Grafton Connor claims against Marsh in contract and tort. Grafton Connor alleges, among other things, that the error regarding the sprinkler system originated with Marsh. Furthermore, it says Marsh had knowledge in 2003, and possession in 2006, of an inspection report that indicated that the North End Pub was not sprinklered.

[8] In addition to the above claims, Grafton Connor claims against both defendants for compensation for the delay in being able to redevelop the property. It claims to have suffered three categories of consequential loss. First, the cost of construction has risen over the period of the delay and Grafton Connor will have to incur that additional cost when it is able to proceed. Second, it has lost the profit it could have generated from the development during the period it has been delayed. Third, it has lost the ability to obtain video lottery terminals ("VLTs") for a reconstructed North End Pub, resulting in the loss of the business.

[9] Finally, Grafton Connor claims that the conduct of both Underwriters and Marsh was so egregious and objectionable that aggravated and punitive damages are warranted.

Underwriters

[10] Underwriters says Grafton Connor's breach of the duty to disclose all material information entitled it to void the Policy. According to Underwriters, if anyone other than Grafton Connor is responsible for the denial of its insurance claim, it is Grafton Connor's agent, Marsh, for negligently failing to obtain the necessary material information from the insured and disclose that information to Underwriters.

[11] Underwriters denies that it failed to meet the standard of care of a reasonably prudent underwriter in its assessment of the risk. It says it had no duty to investigate the accuracy of the information provided by Grafton Connor through Marsh and to somehow unearth that the information was false.

[12] According to Underwriters, Endorsement 10 to the Policy is not intended to excuse pre-contractual material misrepresentations. It does not relieve Grafton Connor from its duty to accurately represent the properties to be insured.

[13] In the alternative, if Grafton Connor is entitled to coverage under the Policy, Underwriters says that its recovery is limited in two ways. First, Grafton Connor

grossly underinsured the North End Pub, triggering the application of the co-insurance provision of the Policy. Second, Underwriters says the Policy is a scheduled policy, not a blanket policy, and any indemnity must be limited to the stated value of the Pub: i.e. $650,000 for the building, $180,000 for the contents, and $150,000 for business interruption, for a total of $980,000.

[14] Underwriters denies that it breached its duty of good faith to Grafton Connor or otherwise acted in a manner that would entitle Grafton Connor to consequential, aggravated, or punitive damages.

[15] Finally, Underwriters counterclaims against Grafton Connor for $95,000, the amount it paid for debris removal at the site after the fire. Since the Policy for the property was void *ab initio*, Underwriters says it was not responsible for the cost of debris removal and Grafton Connor has been unjustly enriched by its payment of this invoice.

Marsh

[16] Marsh, like Grafton Connor, takes the position that Endorsement 10 precludes Underwriters from voiding coverage for the North End Pub. Even if Endorsement 10 does not apply, Marsh says there is no liability on its part. It says it regularly asked Grafton Connor to confirm that the information listed in the application forms and location detail summaries it circulated was correct. Marsh denies that a broker has any duty to independently verify the representations of an insured, particularly where the knowledge of the correct state of affairs is within the actual knowledge of the insured.

[17] In the alternative, if Marsh was negligent, it says Grafton Connor was *more* negligent, and is liable for its own loss on the basis of contributory negligence.

[18] Like Underwriters, Marsh says Grafton Connor is not entitled to consequential damages. It further denies any conduct on its part warranting an award of aggravated or punitive damages.

[19] Finally, Marsh crossclaims against Underwriters for any amounts it is found to owe to Grafton Connor.

Ruling on Objection at Trial

[20] Before outlining the key issues in this matter, I wish to rule on an objection made at trial concerning the identification of handwriting by a lay witness. On June 27, 2014, Underwriters called Ian Harrison to the stand. Mr. Harrison was the claims adjuster for Underwriters who investigated the North End Pub claim, and the author of the October 7, 2007, letter to Grafton Connor denying coverage.

[21] During cross-examination, counsel for Grafton Connor referred Mr. Harrison to the placing slip that was generated when Marsh came to the box seeking coverage with Underwriters. Mr. Harrison was asked about the underwriter's "scratch" that appeared on the document. An underwriter's "scratch" refers to the underwriter's initials and individual stamp that appears on documents he or she has reviewed. Counsel then directed Mr. Harrison to a second document, and asked whether it was safe to conclude that the scratches on these documents belonged to the same individual.

[22] Counsel for Marsh objected on the basis that Mr. Harrison was not a handwriting expert, and was not qualified to give an opinion on whether the scratch belonged to the same underwriter. The writing, counsel said, should speak for itself. Although I initially overruled the objection and allowed Mr. Harrison to answer the question, I subsequently asked the parties to make further submissions to the court on the admissibility of the evidence.

[23] Counsel for Grafton Connor was seeking an opinion from a lay witness as to whether the two scratches were made by the same person. Paciocco and Stuesser's *The Law of Evidence in Canada*, 6th ed (Toronto: Irwin Law, 2011) summarizes the law governing lay opinion evidence at p 183:

> Lay witnesses may present their relevant observations in the form of opinions where
>
> * they are in a better position than the trier of fact to form the conclusion;
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> * the conclusion is one that persons of ordinary experience are able to make;
>
> * the witness, although not expert, has the experiential capacity to make the conclusion; and
>
> * the opinions being expressed are merely a compendious mode of stating facts that are too subtle or complicated to be narrated as effectively without resort to conclusions.

[24] Opinion evidence of lay witnesses has been permitted for the purpose of identifying handwriting on a disputed document. In Bryant, Lederman, and Fuerst, *The Law of Evidence in Canada*, 4th ed, (Markham: LexisNexis Canada, 20014), the authors write at p 780:

> A lay witness may be able to recognize a person's handwriting by reason of a regular exchange of correspondence with that person or by having seen numerous other examples of the individual's handwriting. The lay witness must be familiar with the handwriting before he or she is able to provide an opinion of the author of the handwriting. If the witness has had sufficient opportunity to acquire knowledge of the handwriting in question, the frequency and number of observations, goes to weight. …

[25] I am satisfied that in his role as claims adjuster with Underwriters, Mr. Harrison would have developed a familiarity with the individual scratches of the lead underwriters, and would have accumulated the experience necessary to opine on whether the scratches in question belonged to the same underwriter. I therefore maintain my earlier decision to dismiss the objection.

Issues

[26] This action raises the following issues:

The Claim under the Policy

1. Does Endorsement 10 to the Policy preclude Underwriters from voiding coverage?
2. If not, is Underwriters entitled to void the Policy on the basis of material misrepresentation?
3. If the Policy was properly voided, is Underwriters liable in negligence for the value of the claim under the Policy?
4. If Underwriters is not liable under the Policy or otherwise, is Marsh liable to indemnify Grafton Connor for the value of the claim?

The Value of the Claim Under the Policy

1. Does co-insurance apply?
2. If co-insurance applies, did Marsh negligently fail to advise Grafton Connor of the risk of co-insurance?

3. Is the Policy a blanket or a scheduled policy?
4. If the Policy is a scheduled policy, did Marsh negligently fail to obtain blanket coverage?

Consequential and Exemplary Damages

1. Is Grafton Connor entitled to consequential damages?
2. Is Grafton Connor entitled to aggravated and/or punitive damages?

Crossclaim by Marsh against Underwriters

1. If damages are ordered against Marsh, is Underwriters liable to indemnify Marsh?

Counterclaim

1. Is Underwriters entitled to its counterclaim of $95,000?

Expert Witnesses

[27] The parties in this matter filed expert opinion evidence from eight experts. There were no objections to the qualifications of these experts, and all reports were admitted by consent.

History of the North End Pub

[28] The North End Pub was a longstanding fixture in the north end community until March 7, 2007. Before it was razed by fire, the structure consisted of two integrated buildings. The original building, which housed the North End Diner, was a century old, while the second building, which housed the pub business, was constructed in 1950. Neither part of the structure was sprinklered.

[29] Located across from the Stadacona establishment of Canadian Forces Base Halifax, the North End Pub was a successful and popular community hangout. Its regular clientele consisted of north end residents and armed forces personnel who enjoyed drinking beer and playing VLT machines. For many years, the Pub sold between 110 and 130 kegs of beer per week.

[30] The business of the North End Pub had three components: the food (the North End Diner), the VLTs, and the pub. The VLTs were the most profitable aspect of the business. The Pub operated at least eight VLTs pursuant to license agreements with Atlantic Lottery Corporation, and the revenue from these machines exceeded the provincial average.

The Grafton Connor Group

[31] Gary Hurst is the President and owner of the Grafton Connor Group of Companies. He has been in the restaurant and pub business for over forty years.

[32] Mr. Hurst obtained a Bachelor of Commerce degree from Dalhousie University in 1963, and completed a law degree in 1966. He articled with the law firm of Stewart McKeen and Covert in 1966, and worked for them as an associate until 1969. He then left the firm and worked for Hardman Bryson Consultants for one year.

[33] In 1970, Mr. Hurst was a principal in the development of the Truro Shopping Centre and, two years later, he developed the Bridgewater Mall. He developed the Engine Room in Truro, and Captain Kidd's Restaurant and Lounge in Bridgewater Mall, which later became Tomorrow's Lounge. In 1974, Mr. Hurst bought the North End Pub.

[34] In 1978/1979, Mr. Hurst partnered with Ed Raymond to purchase the Carleton Hotel. They later bought the Cornwallis Properties Building on Argyle Street and developed the Five Fishermen Restaurant. The partners then purchased what is now called the Grafton Connor Building on Grafton Street and set about developing the various restaurants and pubs that comprise the approximately 44,000 square foot location. In the late 1990s, they purchased the Sunnyside and Esquire Restaurants in Bedford.

[35] The Grafton Connor Group of Companies was owned by Mr. Hurst, Mr. Raymond and John O'Hearn until 2001, when all ownership interests were sold to Mr. Hurst. The payout of the purchase price took place over several years, with Mr. Raymond continuing to be involved in the business until 2003.

[36] In addition to the North End Pub, Grafton Connor has operated and insured a number of businesses in Nova Scotia. Since 1995, Grafton Connor has insured the downtown building known as the Five Fishermen building, which contains the Five Fishermen Restaurant, Five Fishermen Grill, and part of the Liquor Dome

business. It insures the Cornwallis Property Limited building and the Grafton Connor Building, a joint venture of Five Fishermen Limited and Cornwallis Properties Limited, that houses Cheers, Grafton Street Dinner Theatre, Taboo, and a Pizza Pizza outlet. Outside of downtown Halifax, Grafton Connor operates and insures Sunnyside One, Sunnyside Two, the Riverside Pub, the True North Restaurant, and the Esquire in Bedford, Kempster's restaurant on Kempt Road in Halifax, the Redwood Grill on Lacewood Drive, Brewster's restaurant at the end of Hammonds Plains Road, and Tomorrow's Lounge in Bridgewater.

Marsh Secures Grafton Connor's Business

[37] Mr. Hurst was responsible for placing insurance for the Grafton Connor properties until 1996. He dealt with local insurance brokerages – Simpson Hurst followed by Bell & Grant – on property coverages, and with Fraser & Hoyt on liability coverages. Before he moved to Florida to build his restaurant business, Mr. Hurst delegated responsibility for placement of property coverages to Mr. Raymond. Mr. Raymond was responsible for placing the insurance until 2003, when the task was given to Steve McMullin. In 2003, Mr. McMullin held the position of controller at Grafton. He was named Vice President of Finance in 2004.

[38] Mr. Raymond was a law school classmate of Mr. Hurst. He practised corporate-commercial and administrative law for 12 years with McInnes Wilson and Hallett, becoming a partner in the firm and earning a Queen's Counsel appointment. Mr. Raymond left the practice of law in 1980 or 1981 to become a restaurateur/bar owner.

[39] Mr. Raymond began his partnership with Gary Hurst in 1979, five years after Mr. Hurst purchased the North End Pub on his own. At no time did Mr. Raymond have an ownership interest in the Pub.

[40] During the years Mr. Raymond was responsible for insurance placement, several brokers, including Marsh, were soliciting Grafton Connor's business. Blake Miller began working for Marsh as an account executive in 1996. At that time, Marsh was launching its national Molson Customer Care Program in Nova Scotia. The Molson Customer Care Program was an insurance package sponsored by Molson and designed specifically for the hospitality industry.

[41] Mr. Miller first approached Mr. Raymond in 1997 with the goal of convincing him to obtain a quote for insurance through the Molson Program. The quote was not accepted by Grafton Connor at that time.

[42] Two years later, Marsh was successful in obtaining Grafton Connor's property insurance business. From 1999 until 2003, it placed the property insurance with various insurance companies, including Cigna International, ACE/INA, Lombard, and Zurich North America Canada.

Placing Coverage in the London Market

[43] In May 2003, Marsh learned that the previous insurer on the Grafton Connor account would not be renewing the property coverage for the 2003-2004 policy. At this time, the Grafton Conner account was being managed by Eric Bourque, who had taken over from Blake Miller in 2002.

[44] After six years as an account executive, Mr. Miller had transitioned into the role of risk placement specialist. The risk placement specialist deals primarily with account executives in the office, who advise him of their account needs. The risk placement specialist then goes to the market to get renewal terms or obtain new alternative quotes. A risk placement specialist has no direct contact with the insured.

[45] Once Mr. Bourque informed Mr. Miller that the Grafton Connor account needed a new insurer, Mr. Miller e-mailed Marsh's affiliate, Marsh UK in London, England, to determine whether it could quote insurance for the Grafton Connor account.

[46] Mr. Miller attached three documents to his e-mail to Marsh UK: a Location Details Summary, a risk summary, and a claims history. The Location Details Summary took the form of an eight-column spreadsheet pertaining to nine Grafton Connor properties. For each location, the summary included information on construction type, monitored alarms, hydrants, sprinklers, building values, contents values, and business interruption. For the North End Pub, the Location Details Summary indicated that the property was of masonry construction, and 100 percent sprinklered.

[47] As an accredited Lloyd's broker, Marsh UK was entitled to place business with Lloyd's of London Underwriters. Shortly after receiving Mr. Miller's correspondence, Marsh UK approached Underwriters with a copy of Mr. Miller's

e-mail and the documents attached thereto in order to obtain a quote for coverage. Martin Pope was the lead underwriter who dealt with the Grafton Connor application. He reviewed the documents and proposed two coverage options under the Marsh UK "FourM" lineslip facility. The first option was based on a rate of .45 percent, with a premium of $60,280.54, and a deductible of $10,000. The second option was based on a rate of .35 percent ,with a premium of $46,884.86, and a deductible of $25,000. Grafton Connor chose the second option, and coverage was bound effective July 1, 2003.

[48] Eric Bourque's time at Marsh was short, ending in early 2004. Not long after his departure, Andrew Timmons took over as account executive for the Grafton Connor account. He was responsible for renewing coverage with Underwriters for 2004-2005. That year, Grafton Connor added two locations to the policy – the Riverside Pub and the Esquire. The Riverside Pub, like the North End Pub, was listed in the Location Details Summary as being of masonry construction and 100 percent sprinklered. The Esquire was listed as being of frame construction, 100 percent sprinklered, and having no monitored alarms. Underwriters insured the Grafton Connor properties at a rate of .35 percent with a premium of $61,758.

[49] Andrew Timmons left Marsh prior to the 2005-2006 renewal. Michael Maloney became the account executive responsible for the Grafton Connor account. Underwriters agreed to renew the policy at a reduced rate of .33 percent with a premium of $58,922.

[50] When Marsh UK applied to Underwriters to renew coverage for 2006-2007, the year of the fire, Christian Corby was the lead underwriter on the renewal. The premium for the Policy was $58,133, based on a rate of 0.33 percent.

Misrepresentations and the Insured's Duty to Disclose

[51] This action arose as a result of alleged material misrepresentations by an insured during pre-contractual negotiations. Insurance contracts are subject to the doctrine of "*uberrimae fides*" which holds the parties to a standard of utmost good faith in their dealings with each other. At the negotiation stage of the relationship, the insured must act in good faith by disclosing all material facts to the insurer.

[52] In deciding whether to cover a risk and, if so, on what terms, an insurer places complete reliance on information provided by the insured. In other words, "the insurer knows nothing of the risk to be undertaken and the insured knows

everything": *Ford v Dominion of Canada General Insurance Co*, [1989] MJ No 674, 1989 CarswellMan 98 (CA) at para 32. Because of this disparity in access to essential information, the duty of utmost good faith requires the insured to make full and complete disclosure of all matters relevant to the risk the insurer is being asked to assume: *Coronation Insurance Co v Taku Air Transport Ltd*, [1991] 3 SCR 622, [1991] SCJ No 96 at para 24. If the insured should fail to fulfill its duty of disclosure, whether fraudulently or inadvertently, the insurer is entitled to void the contract: *Carter v Boehm* (1766), 3 Burr 1905 at 1909.

[53] The duty to disclose all material facts applies even in the absence of questions from the insurer: *WH Stuart Mutuals Ltd v London Guarantee Insurance Co* (2004), 16 CCLI (4^{th}) 192 (Ont CA) at para 11, leave to appeal refused, [2005] SCCA No 86. The duty extends not only to information known to the insured, but also to information the insured ought reasonably to know: Craig Brown, *Insurance Law in Canada* (Looseleaf: Updated to 2014) at 5-5. Finally, an insured need not disclose facts that are in the public domain and should be known to the insurer: *Coronation Insurance Co, supra*.

[54] The insurer's right to void coverage induced as a result of a material misrepresentation has been codified in the form of a statutory condition. This means that the condition forms part of every contract and must be printed on every insurance policy. Statutory Condition 1, found in the schedule to Part VII of the *Insurance Act*, RSNS 1989, c 231, provides:

> Misrepresentation - If any person applying for insurance falsely describes the property to the prejudice of the insurer, or misrepresents or fraudulently omits to communicate any circumstance which is material to be made known to the insurer in order to enable it to judge of the risk to be undertaken, the contract shall be void as to any property in relation to which the misrepresentation or omission is material.

[55] A misrepresentation under Statutory Condition 1, as under the common law, need not be intentional. A misrepresentation made unintentionally entitles the insurer to void the policy: *Pereira v Hamilton Township Farmers' Mutual Fire Ins Co*, 2006 CarswellOnt 2279, [2006] OJ No 1508 (CA).

[56] The common law duty to disclose applies only during pre-contractual negotiations. Once the contract is in force, an insured is not required to disclose fresh information to the insurer, regardless of how material that information may be to the risk: Dennis Boivin, *Insurance Law* (Toronto: Irwin Law, 2004) at p 114.

The *Insurance Act* modifies the common law with respect to fire and automobile insurance, imposing a post-negotiation duty to disclose. Statutory Condition 4 states:

> Material Change – Any change material to the risk and within the control and knowledge of the insured avoids the contract as to the part affected thereby, unless the change is promptly notified in writing to the insurer or its local agent, and the insurer when so notified may return the unearned portion, if any, of the premium paid and cancel the contract, or may notify the insured in writing that, if the insured desires the contract to continue in force, the insured must, within fifteen days of the receipt of the notice, pay to the insurer an additional premium, and in default of such payment the contract is no longer in force and the insurer shall return the unearned portion, if any, of the premium paid.

[57] As required by the legislation, Statutory Conditions 1 and 4 were included in the Policy and form part of the contract between the parties.

Does Endorsement 10 to the Policy Preclude Underwriters from Voiding Coverage?

[58] Endorsement 10 to the Policy provides as follows:

> ERRORS AND OMISSIONS
>
> Any unintentional error or omission made by the Insured shall not void or impair the insurance hereunder provided the Insured reports such error or omission as soon as reasonably possible after discovery by the Insured's Home Office Insurance Department and further provided that in the event of any error or omission including a declaration of the Insured's total insurable values being less than (80%) eighty percent of the actual insurable values at the time of declaration, any loss payable in respect of the property involved or other insurable interests in the loss shall be reduced in the proportion that the said insurable value bears to the declared insurable value provided that this provision shall only apply when the actual building(s) or individual property(ies) or other insurable interests involved in the loss are the subject of an incorrect declaration of values.
>
> ALL OTHER TERMS AND CONDITIONS REMAIN UNCHANGED.

[59] Grafton Connor and Marsh argue that Endorsement 10 prevents Underwriters from avoiding coverage where the insured makes an unintentional misrepresentation. In other words, by including Endorsement 10, Underwriters has given up its right under Statutory Condition 1 to void coverage on the basis of unintentional, material misrepresentations.

[60] Underwriters disagrees, and points out that the word "misrepresentation" does not appear in the clause. It submits that Endorsement 10 is an errors and omissions clause that is intended to provide a means for the insured to rectify minor, immaterial errors or omissions with respect to the insured property.

[61] The "overriding concern" when interpreting insurance policies and other commercial contracts "is to determine 'the intent of the parties and the scope of their understanding'": *Sattva Capital Corp v Creston Moly Corp*, 2014 SCC 53, [2014] SCJ No 53 at para 47, citing *Jesuit Fathers of Upper Canada v Guardian Insurance Co of Canada,* 2006 SCC 21, [2006] 1 SCR 744, at para 27 *per* LeBel J. To accomplish this, the court "must read the contract as a whole, giving the words used their ordinary and grammatical meaning, consistent with the surrounding circumstances known to the parties at the time of formation of the contract": *Sattva,* at para 47.

[62] In *Sattva*, Rothstein J for the Court, explained the justification for considering the surrounding circumstances:

> 47 … Consideration of the surrounding circumstances recognizes that ascertaining contractual intention can be difficult when looking at words on their own, because words alone do not have an immutable or absolute meaning:
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> > No contracts are made in a vacuum: there is always a setting in which they have to be placed... . In a commercial contract it is certainly right that the court should know the commercial purpose of the contract and this in turn presupposes knowledge of the genesis of the transaction, the background, the context, the market in which the parties are operating.
> >
> > (*Reardon Smith Line*, at p. 574, *per* Lord Wilberforce)
>
> 48 The meaning of words is often derived from a number of contextual factors, including the purpose of the agreement and the nature of the relationship created by the agreement… As stated by Lord Hoffman in *Investors Compensation Scheme Ltd. v. West Bromwich Building Society*, [1998] 1 All E.R. 98 (H.L.):
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> > The meaning which a document (or any other utterance) would convey to a reasonable man is not the same thing as the meaning of its words. The meaning of words is a matter of dictionaries and grammars; the meaning of the document is what the parties using those words against the relevant background would reasonably have been understood to mean. [p. 115]

[63] Rothstein J elaborated on the role of surrounding circumstances in contractual interpretation:

> 57 While the surrounding circumstances will be considered in interpreting the terms of a contract, they must never be allowed to overwhelm the words of that agreement … The goal of examining such evidence is to deepen a decision-maker's understanding of the mutual and objective intentions of the parties as expressed in the words of the contract. The interpretation of a written contractual provision must always be grounded in the text and read in light of the entire contract ... While the surrounding circumstances are relied upon in the interpretive process, courts cannot use them to deviate from the text such that the court effectively creates a new agreement …
>
> 58 The nature of the evidence that can be relied upon under the rubric of "surrounding circumstances" will necessarily vary from case to case. It does, however, have its limits. It should consist only of objective evidence of the background facts at the time of the execution of the contract … that is, knowledge that was or reasonably ought to have been within the knowledge of both parties at or before the date of contracting. Subject to these requirements and the parol evidence rule discussed below, this includes, in the words of Lord Hoffmann, "absolutely anything which would have affected the way in which the language of the document would have been understood by a reasonable man" (*Investors Compensation Scheme*, at p. 114). Whether something was or reasonably ought to have been within the common knowledge of the parties at the time of execution of the contract is a question of fact.

[64] In searching for the intent of the parties, the court should avoid an interpretation that would bring about "a result which would not be contemplated in the commercial atmosphere in which the insurance was contracted": *Consolidated-Bathurst Export Ltd v Mutual Boiler and Machinery Co*, [1980] 1 SCR 888 at p 901. In other words, "the interpretive process should begin with an effort to construe an insurance policy in a commercially reasonable fashion which harmonizes all of its different parts": Geoff Hall, *Canadian Contractual Interpretation Law*, 2d ed (Markham: LexisNexis Canada, 2012) at p 207.

[65] If an ambiguity exists after application of the normal rules of construction, the court may rely on a number of special rules applicable to the interpretation of insurance policies. These rules have developed in recognition of the adhesionary nature of an insurance contract. Unlike ordinary commercial contracts, the terms and conditions of an insurance contract are not negotiated between the parties. Consequently, ambiguities will be construed against the insurer: *Brisette Estate v Westbury Life Ins Co*, [1992] 3 SCR 87, [1992] SCJ No 86, at para 4 *per* Sopinka, J. As a corollary of this principle, coverage provisions will be construed broadly and exclusion clauses narrowly: *Reid Crowther & Partners Ltd v Simcoe & Erie General Insurance Co*, [1993] 1 SCR 252, [1993] SCJ No 10, at para 33. Lastly,

the court "should try to give effect to the reasonable expectations of the parties, without reading in windfalls in favour of any of them": *Jesuit Fathers*, at para 33.

[66] Turning to Endorsement 10, it appears to be a hybrid of an errors and omissions clause and a co-insurance clause. The first part of the clause states a general rule applicable to errors and omissions by the insured:

> Any unintentional error or omission made by the Insured shall not void or impair the insurance hereunder provided the Insured reports such error or omission as soon as reasonably possible after discovery by the Insured's Home Office Insurance Department …

[67] The remainder of the endorsement is a co-insurance clause that applies where the error or omission relates to the insured's declared values of insured property:

> … and further provided that in the event of any error or omission including a declaration of the Insured's total insurable values being less than (80%) eighty percent of the actual insurable values at the time of declaration, any loss payable in respect of the property involved or other insurable interests in the loss shall be reduced in the proportion that the said actual insurable value bears to the declared insurable value provided that this provision shall only apply when the actual building(s) or individual property(ies) or other insurable interests involved in the loss are the subject of an incorrect declaration of values.

[68] Under this part of the clause, if the total insurable values declared by the insured are less than eighty percent of the *actual* insurable values at the time of the declaration, the insured will not be entitled to full indemnity for its loss.

[69] Grafton Connor and Marsh say that any misrepresentations regarding the construction of the North End Pub and the presence of sprinklers therein are excused pursuant to the first part of Endorsement 10, the general errors and omissions clause. For the reasons that follow, I disagree.

[70] Although the proper interpretation of an errors and omissions clause has not been considered by a Canadian court, Underwriters has provided several English decisions, two of which I find instructive. The facts in *Highlands Insce v Continental Insce*, [1987] 1 Lloyd's Rep 109 (Com Ct), like those in the case at bar, involved the destruction of an insured property by fire. The court considered, among other things, whether an errors or omissions clause precluded the reinsurer from avoiding the reinsurance contract after it was discovered that the property,

contrary to the information provided by the broker, was not sprinklered. The clause provided:

> Error and omission clause
>
> The insured hereunder is not to be prejudiced by an unintentional and/or inadvertent omission error incorrect valuation or incorrect description of the interest, risk or property, provided that notice is given to the Company as soon as practicable upon the discovery of any such error or omission.

[71] Steyn J (as he then was) concluded that the language of the clause was "not apt to allow its incorporation in the contract reinsurance": p 117. He deemed it necessary, however, to consider the scope of the clause in the event that, contrary to his view, it was incorporated *mutatis mutandis* in the reinsurance contract:

> For the purpose of this case it is not necessary to consider what this provision *does* govern. It is sufficient to record that in my judgment the reliance by the reinsured on it in this case is entirely misconceived. Significantly, the clause contains no provision for an additional premium. That may be commercially acceptable in relation to formal errors, e.g. the address of the insured premises. It is, however, quite inconceivable that it was intended to apply to a risk which was materially misrepresented. No doubt, as was submitted on behalf of Highlands, there are a number of other answers to the reliance placed on this provision. It is sufficient, however, to record that I am quite satisfied that it does not apply to a precontractual material misrepresentation, which entitled the reinsurers to avoid on the grounds of misrepresentation. Inevitably, this argument must fail. (p. 117)

[72] The English Court of Appeal's decision in *Pan Atlantic v Pine Top Insurance*, [1993] 1 Lloyd's Rep 496, involved a failure by Pan Atlantic to disclose the complete claims record and insurance history to the underwriter during the broking of a reinsurance contract. Pan Atlantic sought to rely on Article XV to the contract, the errors and omissions clause, which provided:

> ERRORS AND OMISSIONS CLAUSE
>
> It is hereby declared and agreed that any inadvertent delays, omissions or errors made in connection with this Reinsurance shall not be held to relieve either of the parties hereto from any liability which would have attached to them hereunder if such delay, omission or error had not been made, provided rectification be made upon discovery, and it is further agreed that in all things coming within the scope of this Reinsurance the Reinsurer shall share to the extent of their interest the fortunes of the Reinsured.

[73] According to Pan Atlantic, the nondisclosure of the additional losses was the result of "inadvertent omissions" and the clause clearly intended that there be no right of avoidance for non-disclosure if the omission was inadvertent. Steyn LJ rejected Pan Atlantic's position for two reasons. First, there was nothing in the language of Article XV or in its essential nature to persuade him that it was intended to exclude the right of avoidance in cases of inadvertent omissions. Second, it was "commercially inconceivable" that an insurer would give up the right of avoidance without providing for an increase in premium:

> But there is another reason why I regard the language of art. XV as inapt to cover a case where a party is otherwise entitled to avoid the contract for non-disclosure. The words "in connection with this reinsurance" are of wide import. But those words must receive their colour from the context. Let me postulate a case of such a serious non-disclosure that, if the underwriter had known the true position, he would not have written the risk at all. In the result the underwriter incurs enormous losses. If Pan Atlantic's construction is right, they would be protected against avoidance even in such a case provided that the non-disclosure was inadvertent. On Pan Atlantic's construction this far-reaching and indeed unfair result cannot be avoided. But let me assume a less serious non-disclosure, i.e. a case where the underwriter would have taken a smaller line and asked for an increased premium if he had known the true facts. It seems commercially inconceivable that art. XV was intended to give protection against non-disclosure in such a case without a counter-stipulation for the fixing of an additional premium. It is therefore difficult to read art. XV as excluding a right to avoid for non-disclosure without any corresponding right to an additional premium. The absence of an express stipulation for the fixing of an additional premium is in my view a significant factor tending to show that the language of art. XV is not apt to take away the basic common law right of avoidance for non-disclosure. (p. 503)

[74] The House of Lords ([1994] 3 All ER 581) confirmed the decision of the Court of Appeal with respect to this issue, noting at p 619:

> Pan Atlantic maintains that the non-disclosures relied upon by Pine Top were inadvertent and therefore excused by the opening words of art XV. Notwithstanding the energetic argument of Mr Beloff QC I am quite satisfied that art XV is inapt for this purpose. The matter is thoroughly discussed by Steyn LJ who has said all that is necessary on the matter.

[75] I recognize that the wording of the clauses considered in *Highlands* and *Pine Top* is not identical to that used in Endorsement 10. I also note that the *Pine Top* decision involved an omission, not a misrepresentation. I am satisfied, however, that the reasoning is equally applicable in this case. When one considers the

contract as a whole and the surrounding circumstances, the interpretation proposed by Grafton Connor and Marsh is commercially unreasonable.

[76] The terms and conditions of an insurance contract are the product of the underwriter's assessment of the risk, calculated using the information provided by the insured. To interpret the word "error" in the Endorsement as including misrepresentations would mean that, after coverage is bound, an insurer who learns of an unintentional misrepresentation that materially increases the risk would have no means of increasing the premium, nor any right to void the insurance policy. Yet the same insurer, pursuant to Statutory Condition 4, would have the right to increase the premium or void the contract if it learned from the insured of a material *change* to the risk occurring after coverage was bound. I do not accept that this result was contemplated by either party to the insurance contract.

[77] While it may be possible, as Marsh suggests, for an insurer to vary its statutory right to avoid a contract for unintentional misrepresentation, I find that the contract would have to include clear and unequivocal language to that effect. The use of the word "misrepresentation" would be an appropriate starting point.

[78] In my view, then, Endorsement 10 must have been intended to cover minor errors or omissions by an insured that do not materially affect the risk undertaken by the insurer; in the words of Steyn J in *Highlands Insce*, "formal errors" are what the provision contemplates.

[79] Having concluded that the Endorsement does not apply to excuse unintentional material misrepresentations, I need not consider the argument by Underwriters that the misrepresentations by Grafton Connor were made recklessly.

Were the Misrepresentations Material?

[80] Underwriters will be entitled to void coverage for the North End Pub if it can prove that the statements made by Grafton Connor through Marsh regarding the construction of the building and the sprinkler system were material misrepresentations.

[81] Not every misrepresentation or omission will affect the validity of an insurance contract. The misrepresentation or omission must be material to the insured risk. A fact is material if it would influence a prudent insurer in deciding whether to issue the policy or in determining the amount of the premium: *Mutual Life Insurance Co v Ontario Metal Products Co Ltd*, [1925] 1 DLR 583 (PC) at p

588. Objective materiality, however, does not end the inquiry. As the Ontario Court of Appeal noted in *Sagl v Cosburn, Griffiths & Brandham Insurance Brokers Ltd*, 2009 ONCA 388, [2009] OJ No 1879, "there is a subjective element to the test as well. The non-disclosure or misrepresentation must have induced the insurer to enter into the contract" (para 51). (See also *Pine Top, supra*; *Taylor v London Assurance Corp*, [1935] SCR 422 (SCC); *Wells v Canadian Northern Shield Insurance Co*, 2007 BCSC 1844, [2007] BCJ No 2714).

[82] What is required to show inducement? As Boivin explains in *Insurance Law*:

> There can be no inducement unless the insurer raising a defence would have declined the risk or requested a greater premium for coverage but for the failure to disclose. (p 134)

[83] It is common ground that the representation that the Pub was sprinklered was a misrepresentation. The representation that it was of masonry construction, however, is more controversial. Underwriters says Grafton Connor repeatedly misrepresented that the building was of masonry construction when, in reality, it was built partly of wood. Grafton Connor, on the other hand, says the description of the building's construction was accurate.

[84] Underwriters relies on the evidence of Christian Corby, the lead underwriter who renewed coverage for 2006-2007. Mr. Corby testified that when a building is described with the single word "masonry", he expects that the entire structure is made of brick. Even a building with five percent cladding would not qualify as masonry. If any portion of the building is not of masonry construction, the description is a misrepresentation.

[85] Grafton Connor's argument regarding the accuracy of the masonry description is as follows. In 1999, when Marsh first acquired Grafton Connor's business, the application form for insurance contained five options for "Building Construction":

- Wood frame
- Non-Combustible (masonry/concrete walls/steel deck roof)
- Fire Resistive (reinforced concrete floor, roof, walls, and structure)
- Veneer (wood-frame with brick facing)

- Masonry (masonry/concrete walls/wood deck roof)

[86] Mr. Raymond testified that when he reviewed the application, he believed the choice of masonry construction was accurate. He had been at the North End Pub several times and observed exterior brick, cinderblock, stone in the basement, and the roof. He thought the building also had a wood component, but he thought perhaps every building had a wood component. In any case, the masonry designation was, in his opinion, the best available choice on the form.

[87] According to Mr. McMullin's evidence at trial, he did not know what the word "masonry" meant before the fire in 2007. Since the construction type for the North End Pub had been chosen prior to his involvement in placing the insurance, he assumed it was accurate.

[88] At trial, Gary Hurst described the integrated building as being steel structure on the side that housed the pub business, and frame construction on the other, with brick façade and cladding, and tar and gravel roof.

[89] Blake Miller, the account manager for Marsh from 1999 to 2002, gave a definition of masonry that was consistent with the description provided by Mr. Hurst. He testified that masonry, generally speaking, is wood-frame with masonry. Mr. Miller said that some underwriters deem masonry to include wood-frame construction with masonry on the outside of the building, and, had Grafton Connor asked him for the definition of masonry when he was account manager, that is what he would have told them. Accordingly, Grafton Connor says the representation of the North End Pub as being of masonry construction was in keeping with the Marsh understanding of the term.

[90] Furthermore, the North End Pub was inspected on November 15, 2002, by Glenn Cox of Technical Risk Services, Inc. ("TRS"), at the direction of Zurich, the insurer for Grafton Connor at the time. The TRS inspection report, which will be discussed in more detail later, described the construction of the Pub as follows, at p 3:

> "The building's exterior walls are constructed of brick on steel frame. The floor construction is concrete and the roof is tar and gravel on steel frame."

[91] Grafton Connor says the description provided by these professionals is consistent with masonry construction.

[92] Martin Pope, the lead underwriter who dealt with Grafton Connor's application for coverage in 2003, was shown a copy of the TRS report and directed to the above description of the premises. He was asked if the description of the building's construction complied with the term "masonry", as used in the Location Details Summary. Mr. Pope agreed that the description in the report would satisfy the requirements of the masonry description used in the summary.

[93] In my view, there are problems with Grafton Connor's submission that the masonry description was not a misrepresentation. First, whether Marsh shared Grafton Connor's belief that "masonry" was an appropriate description for the North End Pub's construction is irrelevant to the accuracy of the representation. Second, the TRS report appears to describe only the portion of the building that was built in 1950, and housed the pub business. There is no dispute that the older part of the structure was of wood-frame construction. The report, however, makes no reference to a wood component. Although the TRS report was frequently referred to at trial, Mr. Cox was not called as a witness, leaving this discrepancy unexplained.

[94] The Location Details Summary provided a one-word description of the North End Pub's construction: "masonry". The *Collins Canadian Dictionary* (Toronto: Harper Collins, 2010) defines "masonry" as "stonework or brickwork" and "the craft of a mason." The *Concise Oxford Dictionary*, 8th ed (Oxford: Clarendon Press, 1990) defines "masonry" as "stonework." The *Merriam-Webster Dictionary* (online) defines "masonry" as "the stone, brick, or concrete used to build things" and "work done using stone, brick, or concrete." There is nothing in the foregoing definitions of "masonry" to suggest that the word includes or encompasses any material other than stone, brick, or concrete. The only evidence before the court to support a more generous interpretation of the term comes from Blake Miller, account manager at Marsh, who testified that some underwriters understand "masonry" to include wood-frame construction with masonry on the outside of the building. While it was open to Grafton Connor or Marsh to provide expert evidence to confirm a specialized understanding of the word in underwriting circles, no such evidence was filed.

[95] Furthermore, while Grafton Connor's official position is that "masonry" accurately describes a building that has both stone and wood components, Mr. Hurst and Mr. Raymond conceded at trial that the most accurate description of the building's construction would be "mixed construction." I agree.

[96] Like the representation that the building was 100 percent sprinklered, I am satisfied that the description of the North End Pub as being of masonry construction was a misrepresentation. The proper description of the building would have been "mixed construction." While "mixed construction" was not an option on the initial applications for insurance, it could easily have been raised with Mr. Miller and added to the forms by hand, below the pre-printed options. From 2003 onward, when application forms were no longer used, Grafton Connor could have asked Marsh to change the description in the Location Details Summary to "mixed construction" at any time.

[97] Having found that Grafton Connor made two misrepresentations about the North End Pub to Underwriters, I must determine whether those misrepresentations were material to the risk.

[98] Grafton Connor addressed the materiality of each misrepresentation independently. It argued that although construction type would be material to the hypothetical prudent underwriter in deciding whether to insure and on what terms, the evidence concerning the addition of the Esquire restaurant to the insurance program proves that the construction type of the individual properties was not material to Underwriters.

[99] When Grafton Connor applied for coverage with Underwriters in 2003, all nine of the properties identified on the Location Details Summary were described as being of masonry construction, and having monitored alarms and sprinklers. The premium rate approved by Underwriters for 2003/2004 was .35 percent.

[100] The following year, Grafton Connor added the Riverside Pub and the Esquire. Blake Miller dealt with Anne Pont at Marsh UK on the 2004 renewal. He wrote as follows in his email to her dated June 3, 2004:

> With respect to the above-noted renewal, I attach updated schedule of values for the coming term. You will notice that some values have increased slightly, and also, we are adding a location or 2 (see below). Another broker writes the liability on this risk, and, as usual, will be trying to take the property this year. Given this, and the increased values, and the fact that the property market is dipping a bit here, I would request that you do your very best to get a renewal rate of .3%, which will still generate more premium, and will hopefully keep us competitive.

[101] Although the Esquire was listed as being of frame construction with no monitored alarms, the premium rate remained the same at .35 percent. It appears

that the other factors raised by Mr. Miller were more influential in calculating the premium than the Esquire's construction type. In 2005/2006, Underwriters actually reduced the rate from .35 to .33 percent. According to the evidence, then, Underwriters covered a wood-framed building with no monitored alarms *without* an increase in premium.

[102] Underwriters admits that the premium rate did not increase with the addition of the Esquire restaurant, but denies that this means the construction type of the North End Pub was immaterial to its determination of the premium. Mr. Corby testified that knowing a building's construction type is of great importance when determining the premium for the contents of the structure. A building made of wood is more likely to be completely destroyed in a fire, along with the contents. As a result, the rating and pricing of the risk exposure would be strongly influenced by the construction type. Mr. Pope gave similar evidence, testifying that a wooden structure is less desirable, and would attract a higher premium, than a masonry structure.

[103] Underwriters also relies on an exchange of emails between Marsh and Marsh UK in February and March 2006 concerning the proposed addition of the Thirsty Duck, a new rented location of wood-frame construction, to the policy. Underwriters indicated that if it were to be added, the premium rate for that location would be higher than the main program of insurance:

> Lynn,
>
> Please find u/w's quote attached below [attached document].
>
> To clarify; the rate of 50 cents should be applied to the proposed contents value of CAD $200,000. Please confirm that no building coverage is required. The reason why the rate is higher than the main program is because of the wood-frame construction and the fact that they are only looking for contents cover.
>
> We look forward to hearing you [sic] thoughts.

The Thirsty Duck was added to the policy by endorsement on March 30, 2006.

[104] Trevor Clegg, the underwriting expert retained by Underwriters, provided his opinion as to whether the construction type of the North End Pub would have been material to Underwriters. Mr. Clegg has been involved in the insurance industry for 42 years. Prior to setting up his consultancy in January 2006, he worked for 36 years in the insurance and reinsurance industry. Twenty-eight of

those years were spent working in the London Market, where he held senior positions in both the Company Market and Lloyd's.

[105] Mr. Clegg has worked at the most senior level in both underwriting and claims. He currently holds the position of Non-Executive Director of a Lloyd's Managing Agency. In that role, he is a member of the Underwriting Committee and is responsible for overseeing Underwriting Peer Review on behalf of the Board. He is also appointed as the Independent Underwriting Peer Reviewer to five Lloyd's syndicates and one Bermudian reinsurer. He provides Independent Claims Peer Review for two of those syndicates.

[106] Mr. Clegg continues to undertake underwriting and claims reviews of managing general agents, insurers and reinsurers on behalf of London Market and international clients. Finally, he provides services as an expert witness and arbitrator. Mr. Clegg was qualified to give expert evidence in the field of insurance generally, and, in particular, the subjects of underwriting, claims, and the role of a broker in the London market.

[107] Asked to comment on whether he would have considered the fact that the North End Pub was only partly built of masonry in deciding whether to accept the risk or set the premium, Mr. Clegg noted, "it is obvious that masonry construction represents a far lesser risk than wood, or part wood, construction", and described construction type as "one of the most important material facts to an underwriter of property risks": Expert Report, p 14. According to Mr. Clegg, if he had been the lead underwriter on the file and was advised of the true construction of the building, he had "no doubt" that he would have been influenced to either reject the risk, or amend the terms relative to the risk: Expert Report, p 15.

[108] Underwriters says the above evidence proves the type of construction was objectively and subjectively material; it agreed to insure and renew in reliance on the representation that the building was "masonry".

[109] With respect to the misrepresentation that the North End Pub was sprinklered, Grafton Connor relies on the evidence of its underwriting expert, Frank Szirt. Mr. Szirt is an insurance consultant who has worked in the property-casualty insurance industry since he graduated from the University of Toronto in 1965. Mr. Szirt obtained his Associate of the Insurance Institute of Canada (A.I.I.C.) designation in 1969, and he is a Chartered Insurance Professional (C.I.P.).

[110] During his 46-year career, Mr. Szirt has been involved in all lines of general insurance as an underwriter, underwriting manager, consultant, and executive. He has served as the Chief Executive Officer at a specialty insurer and, in 2008, as the Interim Executive Director of the General Insurance OmbudService (GIO). Mr. Szirt was qualified to give expert evidence on the standard of care of a Canadian underwriter and broker in placing property and liability insurance, and the process employed by the underwriter in avoiding insurance.

[111] Mr. Szirt agreed that, generally speaking, the presence or absence of a sprinkler system is a material fact. That being said, he was not satisfied that it influenced the underwriting decision in this particular case. He based his conclusion on a number of factors.

[112] First, Mr. Szirt stated that Underwriters failed to inquire about risk features which prudent and reasonable underwriters in the Canadian market routinely consider in underwriting a restaurant or tavern, including, among others, the age of the building, housekeeping, the heating and electrical systems, and the kitchen equipment. In his opinion, the failure by Underwriters to inquire about these important risk characteristics suggests that other important risk-related information, including the presence or absence of a sprinkler system, "may have been similarly disregarded": Rebuttal Report, p 10.

[113] Second, Mr. Szirt said Lloyd's had no underwriting or rating manual to guide underwriters in terms of line limits and the application rates which depend, *inter alia*, upon construction, occupancy and protection. The rate quoted by Underwriters for the Grafton Connor properties was a composite rate, presumably made up of the weighted average of the building, contents and business interruption rates applicable to each insured location. However, since Underwriters did not establish the individual rates, "there was no apparent relationship between the composite rate and the exposure to loss which the rate is intended to mirror": p 15, Expert Report. In other words, the rate was market-driven, having no actuarial foundation.

[114] Third, Mr. Szirt said the lack of follow-up questions about the alleged sprinkler system proves that it was not material to Underwriters:

> It is self-evident that, everything being equal, a 100% sprinklered risk is a better fire risk than an unsprinklered one. At the same time, to be meaningful from an underwriting point of view, more detailed information about the system is needed. The underwriter must further determine not only whether the sprinkler system is

> alarmed, but also whether the alarm is local or connected to a central station and whether the connection is ULC approved. The type of system influences both the size of the credit applied to the basic rate and the insurer's line limit. …
>
> (Expert Report, p 15)

[115] Finally, Mr. Szirt pointed out that in 2003, Grafton Connor was in urgent need of an insurer, and Underwriters communicated its decision through Marsh UK in a single day. Mr. Szirt considered this an "unusually quick response", which "gives rise to the possibility that the reason Lloyds accepted GCG was independent of risk characteristics": Rebuttal Report, p 11. He concluded by stating that, "[t]here is no concrete evidence that the sprinkler system affected the amount of insurance it accepted and/or the premium charged": Rebuttal Report, p 11.

[116] Underwriters, on the other hand, says it relied on the misrepresentation concerning the presence of a sprinkler system in determining the rate to be applied to the Grafton Connor properties. Mr. Pope testified that if Underwriters had known that the North End Pub was not sprinklered, it would probably have continued to underwrite the risk, but for a "far higher rate."

[117] Mr. Pope's evidence was supported by the following comments by Mr. Clegg:

> Sprinklers: Once an ignition source for fire has occurred in premises it is extremely important to eliminate that source and/or to limit its spread as quickly as possible. In commercial premises such as a bar/restaurant, full sprinklering of the premises is the most effective method of preventing the spread of fire. Therefore, the sprinkler status of the risk is also one of the most important risk characteristics that I would have taken into account. Marsh London told the Lead Underwriter that the North End Beverage Room risk was 100% sprinklered. In fact, it was not sprinklered at all.
>
> Had I been correctly advised that the risk was not sprinklered, and considering one of the perils insured against was the risk of fire, I am absolutely confident that it would have influenced my mind in deciding whether to accept the risk and if so on what terms. (Expert Report, p 15)

[118] In his rebuttal report, Mr. Clegg pointed out that Mr. Szirt's statement that a "100% sprinklered risk is a better fire risk than an unsprinklered one" undermined his conclusion that the presence or absence of a sprinkler system was not a material underwriting factor. In addition, Mr. Szirt's observation that the type of sprinkler system "influences both the size of credit applied to the basic rate and the insurer's

line limit" was an admission that the presence of a sprinkler system warrants that a credit will be applied and a lower premium will be charged.

[119] In Mr. Clegg's view, the alleged failure by Underwriters to ask for further information about the type of sprinkler system was not proof of underwriting indifference to the sprinkler issue. An alarmed sprinkler system, or a system connected to a central station monitoring point, would further improve the protection by potentially leading to a faster fire brigade response. Such a system may be significant when considering a large industrial risk, or a large risk located outside of a metropolitan location. The North End Pub, however, was in a metropolitan location where a fast fire brigade response was likely in the event of a fire. For this reason, a prudent underwriter would allow very little, if any, credit from the premium charged because of an overly sophisticated sprinkler system.

[120] Finally, Mr. Clegg took issue with Mr. Szirt's opinion that the rate quoted by Underwriters was market-driven. He wrote at p 20:

> In my experience there would be no individual actuarial analysis of the rate/premium to be charged for a small commercial risk such as The North End Beverage Room. In any event, all actuarial rates are to some extent market driven as they are based on historic experience. An experienced underwriter in the market on a day to day basis in Lloyd's knows what range of rates applies to different types of risk he is charged with underwriting. …

[121] If the description of construction type was the only misrepresentation made by Grafton Connor, I would find that it was not subjectively material to Underwriters. There is evidence before the court that Underwriters agreed to insure the Esquire, a restaurant described as being of frame construction and having no monitored alarm, without an increase in overall rate.

[122] However, two misrepresentations were made with respect to the Pub, and both related to the structure's ability to withstand a fire. In these circumstances, it would be wrong to consider each misrepresentation in isolation. The question is not whether Underwriters would have insured a mixed construction building with sprinklers on the same terms as it insured a masonry building with sprinklers. Nor are we interested in whether Underwriters would have insured a masonry building with no sprinklers on the same terms as it insured a masonry building with sprinklers. The pertinent question is whether Underwriters would have insured a mixed construction building with no sprinklers on the same terms as it insured a masonry building with sprinklers.

[123] Mr. Corby testified that an underwriter would look at construction type *in conjunction* with fire protections. If the construction was of an inferior type, the underwriter would charge a higher premium and ask more questions about the types of protection at the premises. Mr. Corby's evidence is buttressed by that of Mr. Clegg. While Mr. Clegg addressed the materiality of each misrepresentation individually, he also considered their cumulative materiality:

> The construction and sprinkler status of a proposed risk are both absolutely essential pieces of information that would each influence the mind of a prudent underwriter in deciding whether to accept the risk and if so on what terms. It is also my opinion that in combination the cumulative materiality of these two basic pieces of information would exponentially increase the risk and thus greatly influence an underwriter in assessing such a risk. The risk of fire, considering the combination of a partly wood construction building and the lack of any sprinkler system to suppress any fire, increases the insurance risk associated with the premises by a very significant factor. [Expert Report, p 15]

[124] Having considered all of the evidence, I am satisfied that the misrepresentations by Grafton Connor, when taken together, were objectively and subjectively material. The bulk of Mr. Szirt's opinion evidence on this point was too speculative to rebut the evidence of Mr. Pope and Mr. Corby, the underwriters who dealt with the Grafton Connor account, that they would have charged a higher premium if not for the misrepresentations. Their testimony was supported by Mr. Clegg's evidence that the cumulative effect of wood-frame construction and the absence of sprinklers is a significant increase in risk.

[125] I accept that if Underwriters had been informed that the North End Pub was of mixed construction and lacked a sprinkler system, it would have charged a higher premium for coverage. As a result, Underwriters is entitled to void coverage under the Policy with respect to the Pub.

Is Underwriters Liable to Grafton Connor for the Value of the Claim?

[126] Even if Underwriters was entitled to void the Policy, Grafton Connor says Underwriters negligently failed to assess the risk with respect to the Pub. It asked no questions about the properties, relying instead on Marsh to provide it with the details. Despite knowing some inspections had been done for the prior insurer, Underwriters did not request any surveys or building inspections and simply applied an overall premium rate to the total building values without any investigation of the risk.

[127] Grafton Connor says that if Underwriters had met the standard of care of a prudent underwriter in its assessment of the risk, the unintentional misrepresentations would have been discovered, and Grafton Connor would either have had valid coverage under the Policy at the time of the fire, or it could have obtained coverage elsewhere in the event that Underwriters had elected not to accept the risk. According to Grafton Connor, Underwriters should not be permitted to profit from its own negligence.

[128] Underwriters denies that it failed to properly assess the risk with respect to the North End Pub or the other Grafton Connor properties. It says it had sufficient information upon which to make a prudent underwriting decision. There were no red flags to alert Underwriters that further inquiries were necessary, and there is otherwise no duty on an insurer to investigate the accuracy of information provided by an insured.

[129] Mr. Corby testified that when a risk is placed at Lloyd's, the broker approaches the underwriter in the box and discusses the information they have regarding the risk. If there has been a recent inspection, they will review it together. When Marsh UK approached Underwriters on Grafton Connor's behalf in 2003, it provided Underwriters with a copy of Blake Miller's e-mail of May 26, 2003 and attached documents. In the e-mail, Mr. Miller wrote as follows:

> A gentleman in our office who handles our hospitality program has just informed me that the facility insuring the property on the above account (ECI Zurich) will not be in a position to renew the property as they do not have the capacity going forward (also they cannot subscribe). They will be renewing the liability portion only.
>
> I do realize we are short on time, however, I'm hoping my proposed rates will be attractive enough to generate a quote this week. The expiring average rate is 0.27 at a deductible of $2,500. I would propose a rate in that .35-.37 range with 10k deductible (FourM), based on TIV of $13,390,000 that generates around 50k in premium. Also, we are trying to get inspection reports from Zurich and will advise. Please read the marketing letter first as it identifies those locations comprising the main location (which is 100% subject as all buildings are adjacent/joined).
>
> Please let me know if you will be able to turn something around. The client has no other options at this point. … If you will be unable to quote please let me know as soon as possible.

[130] The e-mail had the following attachments:

- A risk summary providing information about Grafton Connor, including the fact that it was the largest hospitality group in Halifax and had been in business for 20 years. The risk summary explained that the risk consisted of three stand-alone locations and the "main location" or "complex" which housed the remaining six locations;
- A three year claims history indicating the risk was loss free in the preceding three years; and
- A Location Details Summary containing information on construction type, monitored alarms, hydrants, sprinklers, building values, contents values, and business interruption for the nine locations.

[131] Both of the lead underwriters who dealt with the Grafton Connor account testified that the information provided by Marsh UK was sufficient to enable them to make a prudent underwriting decision. Mr. Pope testified that in order to properly assess a risk, he would require details covering occupancy, construction, fire protections and loss record. He said that a Lloyd's underwriter places complete reliance on the placing broker to provide accurate material facts.

[132] Mr. Corby's evidence echoed that of Mr. Pope. He indicated that as a property underwriter at Lloyd's, he would be interested in the occupancy of the insured, the construction of the buildings, fire protections, and loss record.

[133] When asked whether Underwriters would require an inspection of a property in order to offer terms on a risk, Mr. Pope said that it would depend on the complexity of the risk, and whether Underwriters felt that an inspection was necessary. He said he might ask for an inspection of a risk once every three years. When pressed as to whether this was a standard practice, Mr. Pope reiterated that it would depend entirely on the risk in question. If he did not feel an inspection was necessary, he would not request one.

[134] Like Mr. Pope, Mr. Corby testified that there was no standard practice at Lloyd's with respect to requesting inspections. It would depend on the account. If the details of an account, like the protections or construction type, indicated that it was a good risk, he would not be motivated to have an inspection done. If the overall risk was not as good, if there had been a loss in the prior year for example, he might prefer to have an inspection done. Mr. Corby did note, however, that the syndicates writing the business would want an inspection done at some point. He

suggested that this might be once every four years, but it would depend on the nature of the account.

[135] There was much debate at trial as to the appropriate standard of care to be applied when assessing the conduct of Underwriters. Expert reports were filed that described standard underwriting practices in the Canadian and London markets. According to Frank Szirt, the Canadian expert retained by Grafton Connor, a prudent and reasonable underwriter would inquire about and consider a number of risk features when underwriting a hospitality risk. He described those features as follows in his report:

> - Age of building. Until the adjuster's first report Lloyds did not know that the original structure had been built before 1950 and further construction work had been carried out in the 1950s.
> - Public protection. Grade by Fire Underwriters Survey (FUS).
> - Condition of the property. Recent renovations, upkeep, etc. are especially important in the case of an old building.
> - Housekeeping. Special attention to cleanliness, accumulation and/or stage or combustible material, handling of trash, etc.
> - Nature of Operations. Type of "beverage room", i.e. food served?, "sports bar" v. (what underwriters call) "booze hall" (some underwriters also want to know the food/liquor sales split which, incidentally, the 2006 Location Details List included), additional activities (entertainment, dance floor, video games, etc.
> - Heating. Fuel used, age of heating equipment, regular inspection and maintenance, etc.
> - Electrical. Installation and regular inspections to ensure that the wiring can withstand the demands put on it, particularly by the use of electronic equipment, i.e. video games, large number of television sets and, if there is entertainment, electric musical instruments.
> - Kitchen. If food is prepared and served on the premises, the cooking area requires special attention. The condition of places vulnerable to grease build-up – kitchen equipment, hoods, ducts, exhaust system, etc. – is an issue for underwriters. Fire suppression systems, particularly over deep-fat fryers, and their maintenance are also matters to be considered.
> - Private Protection. Number of portable fire extinguishers (checked regularly?), type of alarms, nature of fire suppression system, etc. (p 11)

[136] Mr. Szirt did not consider this an exhaustive list, nor did he suggest that all underwriters would consider all of these risk characteristics in all circumstances. He did not mince words, however, in his opinion that "no prudent and reasonable underwriter would make an underwriting decision based on such scant information as Lloyds accepted [*sic*] the North End Pub": Expert Report, p 11. Mr. Szirt further stated that any prudent and reasonable underwriter writing hospitality business in the Canadian market would have insisted on an inspection of the North End Pub.

[137] Trevor Clegg, the London underwriting expert retained by Underwriters, strongly disagreed with Mr. Szirt. In his report, he concluded that the details supplied by Marsh UK were sufficient for an underwriter in the London market to understand the essential risk characteristics, and to be in a position to set price and terms. He noted that additional information could be provided by a placing broker that would further enhance an underwriter's understanding of the risk, but he considered such information to be "nice to have", rather than essential, to the ability to quote terms. On the issue of inspection reports, Mr. Clegg confirmed the testimony of Mr. Pope and Mr. Corby that it is not standard underwriting practice in the London market to request inspections on all risks, nor to request inspections on what appear to be good risks.

[138] It will only be necessary to consider which standard of care applies if this court accepts Grafton Connor's position that, notwithstanding the insured's duty to disclose all material information, an insurer owes a duty to thoroughly investigate the risk, so that any inadvertent errors or misrepresentations by the insured will be discovered. According to Grafton Connor, this duty enables the insured to obtain valid insurance from the insurer, or to seek coverage elsewhere if the insurer's investigation leads it to decline the risk. In my view, recognition of the duty proposed by Grafton Connor has been previously considered and rejected by the courts.

[139] In *Silva v Sizoo*, [1997] OJ No 4910 (On Ct Gen Div), the plaintiff became disabled in 1993 and submitted a claim to Canada Life, her disability insurer. Since the claim was submitted within the first two years after policy inception, Canada Life made further inquiries and declared the plaintiff's policy void on the basis of material misrepresentations. The plaintiff filed an action to enforce the policy.

[140] After concluding that the plaintiff had indeed made material misrepresentations to Canada Life, Lane J noted that "[m]uch trial time was expended on the issue of whether the underwriter conducted a reasonable and competent underwriting, and whether, if he did not, that would disentitle Canada Life from relying on such of the applicant's misrepresentations as would have been unmasked in a competent investigation" (para 86). In other words, the plaintiff argued that if Canada Life had met the standard of a reasonable and prudent underwriter in its investigation of the risk at the time she applied for coverage, any misrepresentations would have been discovered and corrected.

[141] Lane J emphasized that "[i]t must not be forgotten that the underwriter is entitled to rely on the applicant to perform her full duty of disclosure" (para 87). If an insurer makes additional inquiries, "it is for the protection of the insurer, not pursuant to any duty owed to the applicant …": (para 87). An insurer, he noted, "is not required to be a detective" and "need not automatically distrust statements made on an Application so as to be required to look behind them": (para 93). After thoroughly canvassing the jurisprudence on the issue, he concluded:

> 97 In summary, these cases show that the rule that insureds are bound to disclose all material facts on pain of having the policy avoided is alive and well. It is, as it always has been, subject to some exceptions. An insured need not disclose what the insurer actually knows, nor that which is so notorious in the industry or place concerned that any competent underwriter in the field would know it. There is a duty on an insurer not to close his eyes to the obvious, to that which is tantamount to notice; and not to refrain from asking because he prefers not to know the answer to a question which stares him in the face. There may be others, I do not pretend to be exhaustive. <u>But there is no general duty owed by an underwriter to an applicant for coverage to conduct a reasonable investigation or otherwise to act as a reasonably competent underwriter. "Plaintiff may not shift the burden of truthfulness which was upon the insured into a burden of distrust and additional inquiry on the part of the defendant"</u> … [*Emphasis added*]

[142] The reasons of Lane J in *Silva* were deemed to be a correct statement of the law by the Ontario Court of Appeal in *Pereira v Hamilton Township Farmers' Mutual Fire Insurance Co*, 2006 CarswellOnt 2279, [2006] OJ No 1508. In that case, the Court noted that an applicant for insurance "cannot be heard to say I may have been wrong, but you [the insurer] should have checked" (para 63). (See also *Armstrong v North West Life Insurance Co of Canada*, [1990] BCJ No 1690 (CA); *Lafarge Canada Inc v Little Mountain Excavating Ltd*, 2001 BCSC 218, [2001] BCJ No 732; *Sholidis v Economical Mutual Insurance Co*, [2005] ILR I-4438, [2005] OJ No 2155 (ONCA))

[143] In my view, if Canadian underwriters are more meticulous in their assessment of a hospitality risk than those in the London market, that fastidiousness is for the protection of the insurer, not the applicant for insurance. Under the doctrine of utmost good faith, an applicant for insurance must completely disclose to the insurer all information relevant to the risk. If the underwriter feels that the information provided by the applicant is sufficient to make a prudent underwriting decision, and there are no red flags to suggest that the information is false, the underwriter is under no obligation to take further investigatory steps, or ask additional questions to test the accuracy of that information.

[144] That being said, if the underwriter knows that certain information is material to the risk and fails to make inquiries that would produce that information, it does so at its peril. The underwriter may find itself unable to rely on the insured's failure to disclose the relevant information as a basis for denying a claim under the policy. As the Ontario Court of Appeal explained in *Sagl, supra*:

> 62 I agree with the trial judge that it runs contrary to the good faith obligation that the insurer owes to the insured for the insurer to agree to insure a risk, whether at the binder stage or at the time the policy is issued, when it knows or should know that there is information relevant to the risk that it does not have and that it did not even inquire into or that is incomplete, and then to raise the lack of information as a defence to a claim under the policy.

See also *Federated Life Insurance Company v. Fleet*, 2009 NSCA 76 at paras 25-29.

[145] That is not the situation here. Underwriters did not deny coverage on the basis of a failure by Grafton Connor to disclose information that Underwriters knew was material to its assessment of the risk but chose not to ask about. It denied coverage on the basis that the information provided by Grafton Connor, upon which it relied in determining a premium, turned out to be false.

[146] Having found that there is no duty on an underwriter to thoroughly investigate the risk in order to unearth misrepresentations by the insured, there is no basis for liability on the part of Underwriters for the value of the claim under the Policy.

Liability of Marsh for Indemnity

[147] Grafton Connor says if there is no liability on the part of Underwriters, Marsh should be ordered to indemnify it for the value of its claim under the Policy. According to Grafton Connor, Marsh failed to act as a reasonable and prudent insurance broker during the years it placed insurance coverage on Grafton Connor's behalf. But for Marsh's negligence, the misrepresentations would not have been made to Underwriters, and the loss of the North End Pub would have been covered by the Policy.

[148] The particulars of Marsh's alleged negligence are as follows:

- the misrepresentation regarding the sprinkler system originated with Marsh;
- Marsh failed to advise Grafton Connor to obtain an inspection of its properties;
- Marsh failed to warn Grafton Connor of the importance of the accuracy of the annual Location Details Summary;
- Marsh had notice of the TRS inspection report for the North End Pub in 2003, and possession of the report in 2006, and failed to provide it to Underwriters.

[149] Marsh denies that it was negligent in its representation of Grafton Connor's interests. It says all of the information it provided to Underwriters, including the misrepresentations regarding the construction and the sprinkler system, originated with Grafton Connor. Marsh says it gave Grafton Connor many opportunities over the years to confirm and update the information, and there is no duty on a broker to independently verify the representations of an insured. In the alternative, if Marsh is found to have been negligent, it says Grafton Connor was contributorily negligent to a significant extent and is liable for its own loss.

[150] In assessing the parties' conduct throughout their professional relationship, it is necessary to review the evidence in some detail.

The Marsh Version of Events

[151] Marsh successfully obtained the Grafton Connor property insurance business in 1999. Blake Miller was the account manager at Marsh with initial carriage of the account. His contacts at Grafton Connor at that time were Ed Raymond and Charlotte Henderson, the assistant controller.

[152] Mr. Miller could not recall the specifics of his interactions with Grafton Connor during his time as account manager, nor did he have any notes from that period. As a result, he could testify only to his general practice.

[153] When meeting with a prospective client like Grafton Connor for the first time, his practice was to give the client a blank Molson Business Edge Master Application Form for each property to be insured. He would ask the client to fill out the forms and return them to him. In 1999, the questions on the form would have been prepared by Cigna, the insurer underwriting coverage through its managing general agent, Enterprise Canada Insurance Services Incorporated ("ECI").

[154] According to Mr. Miller, he would never take it upon himself to review a client's insurance files in order to gather the information required to complete the application forms. If a client was to ask him to review its files, he would refuse, because it was the insured's responsibility to provide the underwriting data. Nor would Mr. Miller ever independently inspect a property. In his experience, an insurance company would normally order an inspection if it considered one necessary. He testified that he had never visited any of the Grafton Connor properties, before or after 1999.

[155] Once Mr. Miller received the completed forms from Grafton Connor, he said he would have given them to Kelly Bent, the client representative assisting him at that time. Ms. Bent would have entered the information into the Marsh "GPS" database. The information would then have been forwarded to the insurer to obtain a quote for coverage.

[156] Grafton Connor accepted the insurer's quote and coverage was bound effective June 1, 1999. On July 9, 1999, Mr. Miller sent Mr. Raymond a letter enclosing an abbreviated version of the policy known as a binder. The letter stated in part:

> Enclosed is your policy showing limits, premiums and deductibles as instructed. We ask that you carefully review all documents and contact us if you have any questions or wish to make any changes.

[157] Also on July 9, 1999, Mr. Miller sent Mr. Raymond a form letter that is sent to all Marsh clients to remind them of important things to consider with respect to their coverage. The letter closed by asking the recipient to "[r]eview your policy documents carefully to ensure they conform with your direction."

[158] On July 22, 1999, Mr. Miller sent a memorandum to Charlotte Henderson at Grafton Connor attaching the formal policy documents and asking her to "please read them carefully and call if you have any questions or concerns." He also attached eight copies of the Molson application form, one for each of the physical locations on the policy, which needed to be signed and returned for Marsh's file. These application forms were printed from the Marsh computer system and were intended to reflect the information Grafton Connor had provided in the original blank forms. Mr. Miller asked Ms. Henderson to "take a few minutes and browse them over, making any necessary changes (most of the information is accurate but please look at receipts and, if there are any major discrepancies, please correct them)."

[159] This computer generated version of the 1999 Molson Business Edge Master Application Form for the North End Pub contained numerous errors. Several of the typed responses pertained to Tomorrow's Lounge, another business operated by Grafton Connor, instead of the Pub. Some of the information on the form was incorrect for both locations. The errors included:

- The form stated the "Operating Name" of the business was "Tomorrow's Lounge." The North End Pub was never known as "Tomorrow's Lounge."
- The form stated the "Owner's Name" was "Raymond", instead of Beaufort Investments Ltd.
- The form indicated the "Total square footage" was 3,300. The North End Pub was 21,490 square feet. The square footage of Tomorrow's Lounge was 3,300.
- The form answered "No" to having Recreational Activities (pool tables, darts, games, dance floor, mechanical rides, video games, etc.). That information was incorrect for the North End Pub but correct for Tomorrow's Lounge.
- The form indicated there were no smoke detectors. That information was incorrect for the North End Pub but correct for Tomorrow's Lounge.
- The form asked "Is the property sprinklered? If yes, indicate percentage." The response on the form was "Yes. 100%." That response was incorrect for the North End Pub, but correct for Tomorrow's Lounge.

- The form indicated the "Year Built" was 1950. That information was correct for the newer part of the North End Pub, but not the older part of the property.
- The form indicated the "No. of Years in Business" was 10 years. This was incorrect information for the North End Pub.

[160] In addition, the Molson Business Edge Master Application Form stated that applicants requiring business interruption profits insurance must complete the Business Interruption-Profits Worksheet. The North End Pub required business interruption coverage, but no worksheet was completed. Mr. Miller was "not sure" why the form had not been completed.

[161] The evidence shows that some of the errors on the typed 1999 Molson Business Edge Master Application Form were corrected in handwriting, including:

- Under the heading of "Operating Name", the name "Tomorrow's Lounge" was struck out and "North End Pub" was added in handwriting.
- "Raymond" was struck out and "Beaufort Inv. Ltd." was written in handwriting.
- Under "Type of Operation", a handwritten correction was made to indicate the premises were "Licensed establishment live entertainment/dancing."
- A handwritten change was made to indicate the premises did have recreational activities such as pool tables.
- Amounts for liquor, food and other receipts were scratched out, with a handwritten note to "see schedule."
- The numbers of employees and bartenders/servers were scratched out, with proper numbers added in handwriting.

The information regarding the sprinkler system and the square footage remained uncorrected.

[162] Mr. Miller conceded that Grafton Connor would not have made some of the mistakes in the form, including the name and owner of the property, and the square footage. With regard to the error listing Ed Raymond as the owner of the North End Pub, Mr. Miller testified that he always knew Mr. Raymond was not the

owner. He admitted that even after he noticed that "Tomorrow's Lounge" was scratched out and "North End Pub" was inserted in handwriting on the form, he did not check to see if any other responses on the form were for the wrong location.

[163] On May 3, 2000, with the deadline for renewal approaching, Mr. Miller sent Mr. Raymond a letter attaching a Molson Business Edge Renewal Application for each location. The letter asked that Mr. Raymond verify the information contained in the computer generated forms, make the appropriate changes, and sign and return the forms. The renewal application forms were shorter than the original master application forms and there was a change of insurer from Cigna to ACE/INA.

[164] Despite the handwritten corrections made by Grafton Connor to the 1999 master application form, the renewal application again incorrectly identified the North End Pub's operating name as "Tomorrow's Lounge." In addition, there was no Business Interruption – Profits Worksheet completed for the renewal form, despite Mr. Miller's testimony that these sheets are important.

[165] At some point after sending out the renewal applications, but prior to renewal, Mr. Miller met with Ed Raymond in order to update the account information. He testified that it was his practice to meet with clients at two key times - before renewal, to update the information that would be forwarded to the insurer, and after renewal, to discuss and potentially deliver the policy.

[166] As a result of the pre-renewal meeting with Mr. Raymond, Mr. Miller scratched out "Tomorrow's Lounge" and replaced it with "North End Bev. Room." He also updated liquor, food and other receipt values, corrected the number of employees, and checked the boxes to add VLT and crime protection coverage. There were no changes made to the sprinkler or construction information. According to Mr. Miller, the updated information would have been entered into the Marsh GPS system and sent to ACE/INA for renewal terms.

[167] On June 1, 2000, Mr. Miller wrote to Grafton Connor advising that the policy had been renewed for the June 1, 2000, to June 1, 2001, term and that the policy documents would be sent the following week. Two weeks later, Mr. Miller wrote to Mr. Raymond enclosing the formal policy documents and thanking Grafton Connor for renewing the policy through the Molson Business Edge Program. On July 27, 2000, Kelly Bent forwarded signed renewal applications for all locations to ACE/INA for its records.

[168] The following year, on May 31, 2001, Mr. Miller sent a fax to Mr. Raymond stating that, "as discussed", coverage had been bound for the term June 1, 2001, to June 1, 2002. Mr. Miller testified that he would have spoken or met with Mr. Raymond prior to renewal to discuss the renewal quote. That year, Lombard became the new insurer for the Business Edge Program, which was now sponsored by Benson & Hedges.

[169] As part of Lombard's agreement to take over the program, clients were required to complete a master application form rather than the more abbreviated renewal application form. As in previous years, Marsh sent Grafton Connor a copy of the application with the responses filled in using the information on file. The 2001 Benson & Hedges Business Edge Master Application Form was essentially identical to the 1999 Molson Business Edge Master Application Form.

[170] The operating name on the 2001 computer generated form was finally corrected and stated "North End Beverage Room." However, the application form continued to track past errors, including:

- The owner's name was still incorrectly stated as Ed Raymond, even though that error had been corrected in handwriting on the 1999 form.
- The "Type of Operation" stated that the North End Pub was a licensed establishment with no live entertainment. This was incorrect and had been corrected in handwriting on the 1999 application.
- The "Total Square Footage" continued to be listed as 3300, the square footage of Tomorrow's Lounge.
- The North End Pub was described as having no recreational activities (pool tables, darts, games, etc.). This error had been corrected in handwriting on the 1999 form.

[171] On cross-examination, Mr. Miller could not explain why these errors kept reappearing after they had been previously corrected.

[172] During the 2001-2002 term, Eric Bourque, another broker at Marsh, began assisting Blake Miller with the Grafton Connor account. Mr. Bourque eventually took over as account manager. On August 24, 2001, Mr. Bourque wrote to Charlotte Henderson as follows:

> … I have enclosed the policy applications for each location. As every year, the insurance company requires these to be signed for their records. Please sign and

> date each location in the indicated area and return to my attention at your earliest convenience.

[173] A signed copy of the Benson & Hedges Business Edge Master Application Form for the North End Pub was entered as an exhibit. Someone had scratched out the answer "No" to the question "Are there any smoke detectors?" and checked "yes", writing in that there were 4 smoke detectors at the property. Blake Miller testified that this was not his handwriting. Other errors, like the owner's name and the square footage, remained uncorrected. The application form continued to describe the North End Pub as being of masonry construction and 100 percent sprinklered. The Business Interruption – Profits Worksheet was only partially completed.

[174] Mr. Bourque forwarded the signed applications to the insurer on October 1, 2001. It is unclear from the evidence whether Grafton Connor was asked to review the information on the form *before* coverage was bound, as in previous years, or merely after. Mr. Miller had no specific recollection, but testified that his practice was to sit down with the client or call them to review and update the information on file before renewal each year. He was confident that the information in the application forms would have been reviewed by Grafton Connor prior to renewal.

[175] After coverage had been bound, Grafton Connor wanted to add the Riverside Pub to the policy. On October 2, 2001, Mr. Bourque wrote to Charlotte Henderson requesting certain information regarding the property. He asked her to pay "particular attention to the Building updates & building construction information." He also requested estimated liquor and food sales, estimated amount of other receipts, amount of insurance required on the building and contents, whether crime coverage was required, and the business interruption limit.

[176] The evidence indicates that Mr. Bourque had a conversation with someone at Grafton Connor and obtained some of the necessary information, including that the Riverside Pub was not sprinklered. The remainder of the information was provided by Charlotte Henderson in a fax of October 3, 2001. The following day, Mr. Bourque advised Ms. Henderson that coverage had been bound for the Riverside Pub effective October 5, 2001.

[177] On February 21, 2002, Mr. Bourque sent a fax to Mr. Raymond attaching a claim history for the prior 3 year period. He also requested a meeting the following week with Mr. Raymond "to discuss where we are with your policy at the moment and bring you into the re-marketing of the account." Mr. Bourque

testified that re-marketing meant shopping the account to other insurers to see if any of them could offer a better quote for coverage.

[178] On February 22, 2002, Blake Miller sent a letter to Ed Raymond, advising that the hospitality program, now known as the Enterprise Advantage Program, was going to have a change of insurance providers. Zurich North America Canada would be replacing Lombard as the provider of property, crime, and boiler and machinery coverages. As in previous years, coverage would be underwritten for the insurer through ECI.

[179] On May 29, 2002, Mr. Bourque sent the same form letter to Mr. Raymond that Mr. Miller had sent when coverage was bound in 1999, summarizing the elements of the policy and asking that he review the policy documents carefully. The next day, Mr. Bourque faxed Mr. Raymond the binder of insurance for the June 1, 2002 - June 1, 2003 term.

[180] On June 5, 2002, Mr. Raymond sent Mr. Bourque a letter which stated, in part:

> I would like to confirm the following coverage effective June 1, 2002:
>
> 1. $15,000 Crime Cover for the safe in the My Apartment operation.
> 2. $25,000 for the ATM safe located within the main safe room.
> 3. Coverage for four ATM machines located in the following operations:
>
> - North End Beverage Room
> - My Apartment
> - Cheers
> - The Attic
>
> 4. Attached is a summary of the various amounts for real property, contents and business interruption limits.
>
> We should meet as soon as possible to review the schedule and any outstanding issues. [*Emphasis added*]

[181] This marked the first appearance of a "Location Details Summary" in the correspondence between Marsh and Grafton Connor. Neither Mr. Bourque nor Mr. Miller was certain as to whether this spreadsheet was initially prepared by Marsh or Grafton Connor. This early version of the Location Details Summary had six columns – Location #, Name, Construction, Building Value, Contents

Value, and Business Interruption. The document described the North End Pub as being of masonry construction.

[182] In early March 2003, Mr. Bourque turned his mind to renewal of the Grafton Connor policy. After speaking or meeting with Ed Raymond, Mr. Bourque made several pages of handwritten notes. Included among the notations were references to "Updated Applications – Send email to John", "Glen Cox → YES!!", "get co-ins → 90-80%", and "TRS – Interested in speaking with Glen." Mr. Bourque testified that the reference to "John" would have been John O'Hearn at Grafton Connor.

[183] Mr. Bourque did in fact e-mail Mr. O'Hearn on March 14, 2003, listing some updates Marsh required for the upcoming renewal, including receipts, crime limits, any new security measures, renovations or updates, claims, and updated values for buildings, contents and business interruption. He noted that he had spoken with Ed Raymond earlier in the week and asked that Mr. O'Hearn pass the information on to him.

[184] Prior to the 2003 renewal, Mr. Raymond transitioned responsibility for placing insurance coverage to Mr. McMullin. Mr. Bourque met with Mr. Raymond and Mr. McMullin to discuss the information that required updating. This meeting was followed up on May 7, 2003 with an e-mail from Mr. Bourque to Mr. McMullin. The e-mail stated:

> Steve,
>
> As per my meeting with yourself & Ed, I have placed some information below which we will require updated to proceed with the renewal quotation. Please update and return to my attention at your earliest convenience.
>
> Please review and update the values and limits of each location within the below attachment.
>
> (See attached file: GRAFTON – Location Details Summary.doc)
>
> Please review and update the receipts shown for each location.
>
> (See attached file: GRAFTON – Revenue Breakdown II.doc)
>
> We require an updated claims listing on the Liability for the past year.
>
> This should include the following:
>
> 1) Brief details of the claim
> 2) The date of occurrence
> 3) The amount paid out (if the claim is closed)

4) The amount reserved for each claim.

Steve, regarding the Co-Insurance clause. The upcoming property portion will include a 90% Co-insurance clause for sprinklered locations, and an 80% Co-insurance clause for non-sprinklered locations.

If you have any questions or concerns please do not hesitate to contact me.

[185] The version of the Location Details Summary attached to Mr. Bourque's e-mail now included a "Sprinklered" column. The North End Pub was described as being of masonry construction and 100 percent sprinklered.

[186] Mr. McMullin responded to Mr. Miller's e-mail later the same day. He wrote, in part:

I am attaching an updated Summary list which includes the name of 2 new establishments created within the building. Little Fish in the back of the Five Fisherman lobby and Admirals Quarters in the back of the Attic. I updated a few building values and contents values and also the fact that Riverside is now sprinklered. I did not update the Business Interruption as I'm not sure how it's calculated nor did I change the total.

[187] As discussed earlier in this decision, Mr. Bourque became aware in late May 2003 that Zurich would not be in a position to renew the property coverage for the Grafton Connor account. He informed Blake Miller, now acting as risk placement specialist, of the situation, and Mr. Miller contacted Marsh UK by e-mail to determine whether it could place coverage in the London market. The e-mail attached the updated Location Details Summary, a risk summary, and a claims history.

[188] Marsh UK approached Underwriters the next day and informed Mr. Miller that it could source insurance for the Grafton Connor account under the "FourM" insurance facility. On behalf of Mr. Bourque, Mr. Miller e-mailed Steve McMullin at Grafton Connor on May 30, 2003, with two quotes from Underwriters for property coverage. His e-mail stated that the quotes were "subject to all terms and conditions contained in the Lloyd's FourM wording." Mr. McMullin replied and asked what FourM meant. Mr. Miller responded as follows:

Hi and sorry for any confusion, its just a name, insurers have different names for their wordings for example : "Business Edge", "Pro-Pack" etc. It's a good question though as now I'm thinking the FourM stands for something, I'll let you know when I find out ..

> What you need to know is that the wording is based on a All-Risk Broad Form wording, which is similar to what you have now.

Mr. Miller testified that he did not ever find out what FourM meant and pass that information on to Mr. McMullin.

[189] Nevertheless, Mr. McMullin accepted one of the quotes and coverage was successfully bound effective July 1, 2003. Curiously, the insurance policy for July 1, 2003 to July 1, 2004 was not actually signed and issued by Underwriters until July 20, 2004, 19 days *after* the term had expired. None of the witnesses for Marsh were able to explain this irregularity.

[190] Mr. Bourque left Marsh in early 2004. The circumstances surrounding his departure are unclear. Mr. Bourque testified that he worked for Marsh Private Client Services, the personal lines division of Marsh, and that division was relocated to Montreal. He said he was offered a position as a client representative but was not interested. However, Lynn Stone, a client representative at Marsh, testified that Mr. Bourque was asked to leave. Ms. Stone was unable to say for certain why he had been let go. She testified only that she'd heard rumours, but those rumours were unrelated to the Grafton Connor account.

[191] In her testimony, Ms. Stone explained the role of a client representative at Marsh. The position is essentially a support role. Client representatives work with the account managers, performing the day-to-day servicing of accounts. The scope of a client representative's duties will depend on the account and the specific account manager. Responsibilities can range from the preparation of Certificates of Insurance and invoicing to negotiating renewals and dealing with clients when they have issues or concerns. Ms. Stone testified that the client representative works side by side with the account manager. They keep each other "in the loop." Ms. Stone would normally be copied on e-mails to and from account managers if she was involved on a file.

[192] When Ms. Stone joined Marsh in 1997, her responsibilities were of a mostly clerical nature. As the years went on, she became more involved in the hands-on dealings with the accounts and the clients. Ms. Stone became involved with the Grafton Connor file in April of 2004 when she was asked by the regional manager to respond to an inquiry from a mortgage company. Not long after, Andrew Timmons became the account manager. Mr. Timmons was not called as a witness. As a result, there is very little evidence as to the 2004-2005 renewal. On June 29, 2004, Blake Miller sent Mr. Timmons an e-mail indicating that he had bound

coverage for Grafton Connor effective July 1, 2004. Mr. Timmons left Marsh before the 2005 renewal.

[193] From March 2005 forward, the Grafton Connor account was managed by Michael Maloney, a business development leader at Marsh, with Ms. Stone as the designated client representative for the account. Mr. Maloney first contacted Steve McMullin on March 17, 2005, leaving him a voicemail message. The message addressed three issues. First, Mr. Maloney advised Mr. McMullin that Andrew Timmons was no longer with Marsh. Second, he indicated that he would like to meet with Mr. McMullin to get up to speed on the account. Finally, he said they needed to prepare for the upcoming renewal. Mr. McMullin called Mr. Maloney on March 30, 2005, to arrange a meeting.

[194] The meeting took place on April 8, 2005 on Grafton Street and was attended by Mr. Maloney, Ms. Stone, Mr. McMullin, and Gary Muise, the Vice President of Operations at Grafton Connor. Mr. Maloney brought a number of documents with him to the meeting. The first was an agenda listing several items he intended to review at the meeting. The first item, "intro service team and client" is self-explanatory. The second item, "account history", would involve a discussion with Mr. McMullin and Mr. Muise as to their knowledge of the relationship between Marsh and Grafton Connor. Mr. Maloney said he would have reviewed the existing file, the correspondence, certificates, policy wording, schedules, and the property values going back to 2003.

[195] Mr. Maloney would then have reviewed the "current position." He would have told Grafton Connor about the existing insurance market, where the rates were, and whether prices were increasing or decreasing. Next, he would have discussed Grafton Connor's "renewal objectives." Grafton Connor's objective at this meeting was to save money on its insurance coverage. It wanted lower premiums.

[196] The next item was "renewal requirements", which were set out in a document prepared by Lynn Stone called the "Grafton Connor Group Renewal Review." For property coverage, the "renewal information requirements" were:

- Confirm physical address of locations to be Insured (include any new additions)
- Update Property Values at each location (building, contents, etc)
- Confirm "Named Insured" as it should be shown on policy

- Confirm/Update occupancies at each location

[197] Mr. Maloney says he would have discussed each of these items with Mr. McMullin and Mr. Muise. The information on file from the previous year was set out in a document called the "Commercial Property Coverage Summary", and in a copy of the 2004 Location Details Summary. The Commercial Property Coverage Summary sheet listed the insured's name, the insurer, policy number, limit of liability, business interruption limit, co-insurance requirements (ninety percent), deductible, basis for loss settlement (replacement cost), and sub-limits.

[198] Mr. Maloney testified that he would have reviewed each of the items listed in the Commercial Property Coverage Summary and each column of the Location Details Summary with Grafton Connor. He would have reinforced the importance of accurate information. Mr. Maloney said he would have provided Mr. McMullin with an electronic version of the Location Details Summary to be updated and sent back to him prior to renewal.

[199] Next, Mr. Maloney discussed claims made by patrons of a number of Grafton Connor establishments. Grafton Connor wanted feedback in terms of whether to report the incidents to the insurer or pay the claims directly. Finally, Grafton Connor had been interested in carrying crime coverage but was previously told that it would cost about $20,000. Mr. McMullin asked Mr. Maloney to see if he could get coverage for about $10,000.

[200] Mr. Maloney's handwritten notes of the meeting read as follows:

> Met with Steve to discuss agenda (attached)
>
> His points were as follows
>
> (1) Not aware of changes to team and provided his concern over Account Manager changes over past two years
>
> (2) Renewal objective is to save money
>
> (3) Will have updates to me no later than May 1st
>
> (4) Wants us to quote by June 1st
>
> <u>Action</u>
>
> (1) Send Steve electronic copy of schedule
>
> (2) Cost out business interruption (not sure if they want to carry it)

(3) Smitty's sign → f/u in 10 days → may be below ded.

(4) Split lip $2K follow up with Gary for comments > do we notify u/ws?

(5) Eye damage claim → f/u with Gary for comments > do we notify u/ws?

(6) Quote crime → Get to $10k

(7) Review last year's submissions cameras/swipe cards

[201] Mr. Maloney sent Mr. McMullin an e-mail on April 8, 2005, attaching the Location Details Summary and advising that the approximate cost for business interruption coverage would be $7,500.

[202] Mr. Maloney had some difficulty obtaining the updated version of the Location Details Summary from Mr. McMullin. Although he had agreed to provide the information by May 1, Mr. McMullin did not forward the updated document to Mr. Maloney until May 16, 2005. Once he had the updated information, Mr. Maloney provided it to Lynn Stone, who used it to prepare a Market Submission document and an updated Location Details Summary. To prepare these documents, Ms. Stone simply updated the versions on file from the previous year.

[203] On May 17, 2005, Ms. Stone e-mailed Blake Miller, attaching a renewal submission for Grafton Connor. She asked that he review the attached Market Submission 2005 and Location Details Summary 2005 and advise if she had left out any relevant information. She also noted, "[w]e'd like to have a 15% decrease this year (as per Mike). Expiring premium is $61,758.42 through Lloyds." Mr. Miller then forwarded the information to Marsh UK to take to Underwriters.

[204] Once Underwriters provided a quote, Ms. Stone prepared a Renewal Proposal for the July 1, 2005 – July 1, 2006 term to discuss with Grafton Connor. The Renewal Proposal included updated versions of the Commercial Property Coverage Summary and Location Details Summary that were used in the earlier Renewal Review. Grafton Connor accepted the premium rate of .33 offered by Underwriters and coverage was bound. Policy documents were forwarded by Marsh UK to Blake Miller on August 9, 2005.

[205] That brings us to 2006. On January 26, 2006, Mr. McMullin advised Mr. Maloney that Grafton Connor had completed negotiations to buy the Thirsty Duck pub and wanted a quote for coverage. The Thirsty Duck, which Mr. McMullin described as being of wood frame construction, was added to the policy on March 30, 2006.

[206] With renewal approaching, Ms. Stone updated the Renewal Review documents with the information provided by Grafton Connor during the 2005 renewal. Mr. Maloney met with Mr. McMullin and Mr. Muise on April 26, 2006, to discuss the contents of the Renewal Review. Later that day, Mr. Maloney prepared a memo to Lynn Stone updating her on what needed to be done for the renewal. He indicated that they would be marketing the account to all available markets, not just London, so he needed her to update the marketing submission immediately. He also wrote, *inter alia*, that updated revenue and property values were to be provided by Mr. McMullin within the day. Finally, he told Ms. Stone that Grafton Connor was going to ask WCL Bauld, another insurance brokerage, to provide alternative quotes.

[207] Mr. McMullin provided the updated information by e-mail on the afternoon of April 26, 2006. He wrote as follows:

> Mike,
>
> I just faxed you the application form for our 2006 insurance. I essentially photocopied 2005's, made a couple of changes and re-signed. Also updated the Grafton Connor Holdings, in that fax.
>
> I am attaching an updated sales, valuation document. I'm not the greatest with Word, so I couldn't get it to print properly. I'm sure you'll be able to.
>
> If there is anything else you need, please let me know.

[208] Attached to the email was a document entitled "Grafton Connor Insurance Location Details 2006." Mr. McMullin had made a number of changes to the 2005 Location Details Summary. He provided updated business interruption, liquor sales and food sales values for each location. He changed the construction type listed for the Thirsty Duck from "Frame" to "Masonry." He also changed the Thirsty Duck's sprinklered status from "Yes – 100%" to simply "Yes." Finally, Mr. McMullin changed the "Building Value" of the North End Pub from $600,000 to $650,000.

[209] Ms. Stone e-mailed Blake Miller on April 26, 2006, attaching the renewal submission for the Grafton Connor account, which included the 2006-2007 Market Submission and the updated Location Details Summary provided by Mr. McMullin. She asked that renewal be handled "ASAP as discussed earlier with Mike."

[210] On May 10, 2006, James Brown of Marsh UK contacted Blake Miller about the Grafton Connor account. He wrote, in part:

> Blake,
>
> From looking at our records with respect to the above account, the date for renewal falls on 1st July 2006. Could you please forward full renewal information and an updated claims record, at your earliest convenience so that we can approach Underwriters with plenty of time. Please refer to the below points when supplying us with renewal information.
>
> **1. Information required by Underwriters**
>
> Please review the attached spreadsheet for the expiring risk and advise whether any changes are needed to be updated this [*sic*] for the renewal policy:
>
> Grafton Connor 2005.xls
>
> If changes are required, please advise of the following (where applicable):
>
> - Building Values – Split by location
> - Content Values – Split by location
> - Business Interruption Values – Split by location
> - Full address inc. Zip code/Post code
> - Construction of the building
> - Occupancy
> - Year built and upgraded if applicable
> - No. of buildings
> - No. of stories
>
> **2. Material Facts**
>
> Please consider the following when providing renewal information:
>
> - We have a duty to actively ensure we obtain all material facts from our clients and that they are then passed onto our markets.
> - A material fact is a fact or circumstance that would influence the judgement of a prudent underwriter in fixing the premium or determining whether he will accept the risk and, if so, on what terms.
> - It would not necessarily have led the underwriter to decline to risk or increase the premium, though they would have had the opportunity to have taken the information into account.
>
> **3. Terms of Engagement**

> Please find attached our Terms of Engagement. Would appreciate your confirmation that your client is in agreement with the content:
>
> Specialised Product Transparency Out scope.doc
>
> ….

[211] The same day, Mr. Miller forwarded the Marsh UK e-mail to Mr. Maloney and asked whether he was expecting any changes in values. The next morning, May 11, at 9:34 am, Mr. Maloney responded to Mr. Miller, with a copy to Lynn Stone, indicating that Ms. Stone had the updated values and would supply them to Mr. Miller. Ms. Stone replied at 9:50 am, telling Mr. Miller that "[u]pdated values should have been included with the submission I sent to you a couple weeks ago."

[212] At 10:04 am, fourteen minutes after Ms. Stone's response, Mr. Miller replied to Mr. Brown's e-mail. Although Mr. Brown had asked for certain information that was not included in the Location Details Summary, including the ages of the buildings, the number of stories, and so on, Mr. Miller simply attached the 2006 Market Submission and Location Details Summary, noting that updated values and claims were attached. He said he would "ask the C/E to confirm as per item#3 and will advise in due course." He concluded with, "[w]e have competition from 2 local brokers who have hospitality/pub programs." Mr. Miller testified that he did not contact Grafton Connor to determine whether Mr. McMullin understood the definition of material facts, or to obtain the information Mr. Brown requested that was not in the Location Details Summary. As risk placement specialist, he would not have had direct contact with the client. Ms. Stone testified that she did not contact Grafton Connor either.

[213] After receiving the quote from Underwriters, Mr. Maloney met with Grafton Connor and presented the Renewal Proposal for 2006-2007. On June 30, 2006, Ann Pont of Marsh UK wrote to Blake Miller confirming that coverage had been bound. Ms. Stone sent Mr. McMullin the binder of insurance on July 6, 2006.

[214] Ms. Stone sent the full Policy to Mr. McMullin on September 19, 2006. She asked that he "please review these documents carefully to ensure everything is satisfactory."

[215] On March 7, 2007, a fire destroyed the North End Beverage Pub. Mr. Maloney moved quickly to appoint Len Costello, an adjuster with Crawford & Company, to adjust the claim. As a result of Mr. Costello's investigation, Mr. Maloney learned that the North End Pub was of mixed construction, had no

sprinklers, and had been grossly underinsured. The Location Details Summary listed the replacement cost of the Pub building as $650,000. According to Specialized Property Evaluation Control Services Ltd. (SPECS), the experts retained by Mr. Costello, the replacement cost for the building was $2,174,514.02.

[216] When Mr. Maloney learned of these inaccuracies, he became concerned that there may be other errors in the Location Details Summary. On March 15, 2007, he sent the following e-mail to Mr. McMullin and Mr. Muise at Grafton Connor:

> Steve/Gary,
>
> Although we have a renewal review meeting scheduled and further to our recent meeting, please review your current property schedule of locations to ensure that the information contained therein is 100% accurate. If changes are required (eg construction, protection, values etc,) please advise asap. Values are to be on a replacement cost basis.

A copy of the 2006 Location Details Summary was attached to the e-mail.

[217] The issue of coverage for the North End Pub remained outstanding as the deadline for renewal approached. Either Ms. Stone or Mr. Maloney prepared the annual Grafton Connor Group Renewal Review. The "Renewal Information Requirements" for property coverage had undergone some revisions since the fire. The 2006-2007 requirements were stated as follows:

> Property
>
> - Confirm locations to be Insured (include any new additions)
> - Update Property Values at each location (building, contents, etc)
> - Confirm "Named Insured" as it should be shown on policy
> - Confirm/Update occupancies at each location

[218] The 2007-2008 requirements were expressed somewhat differently:

> Property
>
> - Confirm Named Insured
> - Confirm location values, including any new additions (values to be based on Replacement Cost)
> - Confirm construction/occupancy/protection information for each location
> - Completion of Business Interruption Worksheet required

[219] Ultimately, Grafton Connor decided not to renew through Marsh.

Grafton Connor's Version of Events

[220] When Gary Hurst delegated responsibility to Ed Raymond for placing property insurance in 1996, he never asked him what, if anything, he knew about insurance. Mr. Raymond testified that in 1996, he had no experience in insurance matters other than what incidental exposure he may have had while practising law. He did not recall any specific conversations with Mr. Hurst about what his responsibilities would be in dealing with Grafton Connor's insurance requirements.

[221] Mr. Raymond testified that during the years he was responsible for the insurance, several brokers were in competition for Grafton Connor's business. When brokers asked him to entertain proposals, he gave them the information they requested, answered questions, provided access to the company's files and accounting staff, and made the Grafton Connor premises available for site visits.

[222] Before Marsh obtained the business, Grafton Connor's property insurance was placed through Bell & Grant. Mr. Raymond believed Bell & Grant had conducted inspections of the properties, possibly in 1998.

[223] When questioned as to whether Mr. Miller asked him or his staff for information about the Grafton Connor properties in 1999, Mr. Raymond testified that Mr. Miller had dealt directly with Charlotte Henderson in the accounting office and he could not speak to what information she may have provided to him. He added that Mr. Miller never asked him for any information. Ms. Henderson was not called as a witness at trial.

[224] Mr. Raymond said he did not make the handwritten changes to the 1999 Molson Business Edge Master Application Form. He assumed the changes had been made by Ms. Henderson before she forwarded the application to him for signature.

[225] When Mr. Raymond reviewed the 1999 application forms for signature, he assumed that Mr. Miller had collected the information in it by visiting the properties, reviewing Grafton Connor's insurance files, and consulting with staff in the accounting department. He said Mr. Miller told him at some point that he had visited the properties, but he did not mention which ones. Mr. Raymond did not ask.

[226] Mr. Raymond explained his reliance on Mr. Miller as follows. The Grafton Connor account was a lucrative one. There was no shortage of brokers making proposals each year, competing for the chance to add Grafton Connor to their client base. Mr. Miller had been pursuing Grafton Connor's business for three years, and Mr. Raymond presumed that he had done his "due diligence" and gathered the information he needed to prepare the proposal. Mr. Miller had access to Grafton Connor's insurance files, which Mr. Raymond believed contained previous inspections. Mr. Raymond said he relied on Mr. Miller's expertise, but never told Mr. Miller that he was relying on him for the accuracy of the information.

[227] As previously discussed, when Mr. Raymond reviewed the 1999 Molson Business Edge Master Application Form, he noticed that the form described the North End Pub as being of masonry construction. He felt this was the most accurate description of the available options. He did not ask Gary Hurst whether the description was accurate. As to the representation that the property was 100 percent sprinklered, he assumed that information was accurate and had been verified. During the handful of times he had visited the Pub, he had never noticed whether it was sprinklered. He said he was not an observant person.

[228] When Mr. Raymond was shown his e-mail to Mr. Bourque of June 5, 2002, attaching the Location Details Summary, he said he did not create this document. It had been prepared by someone at Marsh, presumably using information from prior applications.

[229] Mr. Raymond testified that during the years he placed insurance for Grafton Connor, no one at Marsh ever discussed or recommended that he obtain an inspection of the properties.

[230] In 2003, Mr. Raymond transitioned responsibility for placing insurance to Steve McMullin. He said the transition was informal. He simply asked Mr. McMullin to start participating in the meetings.

[231] Mr. McMullin testified that when he took over placing property insurance for Grafton Connor, he had no previous insurance experience. He said there was a learning curve for him in the first year, and Mr. Raymond did not provide any instructions or offer any explanations of the coverage. Mr. McMullin's preparation for his new role consisted of reviewing the 2002-2003 insurance policy.

[232] Mr. McMullin attended a meeting with Mr. Raymond and Eric Bourque on March 17, 2003. Mr. Raymond introduced him to Mr. Bourque and advised that he would be taking over the insurance duties going forward. Mr. McMullin and Mr. Bourque then discussed the renewal process. Mr. McMullin recalled taking some notes at the meeting. Among the notes was a reference to "Masonry ??", which had an "E" beside it, "Inspect propertys (TRS)", also with an "E" beside it, and "Review contents value" with an "S" beside it. Mr. McMullin explained that the letters beside the notes were part of a system he uses for note taking during meetings. If there is a responsibility on his end to do something going forward, he writes the letter "S" beside the task. If there is a responsibility on the part of someone else, he writes their name or initial. The "E" was for Eric. He said he wrote "Masonry ??" because he was confused as to what it meant, and Eric Bourque was supposed to do something about it. It is not clear what Mr. Bourque was supposed to do.

[233] Mr. McMullin testified that the first time he had seen the Location Details Summary was in 2003. He believed the information in it had come from Marsh. He was certain that he did not prepare the document because it was made using Microsoft Word, which, he said, he was not very good at using in 2003. He would have used Excel. There was never a discussion of the categories listed on the schedule, other than business interruption, which Mr. Bourque told him how to calculate.

[234] In May 2003, Mr. Bourque e-mailed Mr. McMullin and asked him, *inter alia*, to "review and update the values and limits at each location." Mr. McMullin said he interpreted this to mean that he should update anything numerical – building value, contents value, and business interruption. At no point was he ever instructed to update the construction or sprinkler information. He believed that information was accurate because it pre-dated his assumption of responsibility for insurance. Every year after 2003 when Mr. McMullin was asked to review the Location Details Summary he maintained the same understanding of his role.

[235] Notwithstanding his evidence that he thought he was only responsible for updating numerical values, Mr. McMullin updated the Location Details Summary in May 2003 to reflect that "the Riverside Pub is now sprinklered." He testified that work was being done in the building with respect to a fire alarm system and he asked someone if that work included sprinklering. This individual told him that it did. He could not recall who the person was, other than that it would have been a "supervisor", and "someone within the Grafton Connor Group."

[236] Furthermore, prior to renewal in 2006, Mr. McMullin changed the construction type of the Thirsty Duck from "frame" to "masonry." His explanation for this change was that 2006 was the first year that the Thirsty Duck had appeared in the Location Details Summary. As a result, it had no "historical relevance", and he had no reason to trust that the "frame" description was correct.

[237] On March 15, 2007, after the fire, Mr. Maloney e-mailed Mr. McMullin and asked him to review the Location Details Summary to ensure that it was accurate. He noted:

> If changes are required (eg construction, protection, values etc,) please advise asap. Values are to be on a replacement cost basis.

[238] Mr. McMullin testified that this e-mail was the first time he had ever been asked by anyone at Marsh to verify and update the construction and protection information. It was also the first time he had ever been told that values were to be on a replacement cost basis. Following this e-mail, Gary Muise hired Tudor Valuations to perform replacement cost valuations for each of the Grafton Connor properties. He retained Jessom Food Equipment and Big Eric's to ascertain contents values.

[239] When Mr. McMullin reviewed the Tudor valuations, he learned for the first time that, contrary to the information in the Location Details Summary, the Riverside Pub and the Esquire Restaurant had no sprinklers.

[240] Mr. McMullin worked with Mr. Muise and Clarence Beckett, a lawyer retained by Gary Hurst, to prepare the Proof of Loss. The values claimed by Grafton Connor in the Proof of Loss form were as follows:

- Building value - $2,174,514.02
- Contents value - $411,357.61
- Business interruption - $154,997.53

[241] Grafton Connor submitted the form to Marsh on June 5, 2007.

The TRS Report

[242] In early 2011, Marsh disclosed an inspection report for the North End Pub prepared in 2002 by TRS. Who received this report, and when, are critical points,

given that the report states that the property had no automatic sprinklers. Page 3 of the report states:

> The building has undergone renovations and upgrades. Contact stated they are currently getting a price on installing a sprinkler system.

[243] It further states at p. 4, under "Automatic Sprinklers":

> There is currently no automatic sprinkler system. The insured is in the process of getting a quote to have the building sprinkler protected.

[244] The TRS report was commissioned by ECI, on behalf of Zurich. Incorporated in Toronto in February 2000, ECI was a managing general agent for multiple insurance companies. Essentially, ECI was an agency of insurance underwriting professionals that developed contracts and affiliations with a number of different insurance companies. Some of those companies were also shareholders of ECI. At inception, its shareholders included Marsh, Lombard, Chubb, Zurich and Aviva. Although Marsh was a shareholder, ECI was a separate corporate entity that operated independently, with its own directors, officers, and staff.

[245] ECI had a mandate from the insurance companies with which it partnered to prudently underwrite the business it was transacting on their behalf. Since hospitality is considered a very difficult class of business, the standard practice was to inspect every risk. The partners would therefore have expected ECI to arrange inspections on their behalf when considering a hospitality risk like Grafton Connor.

[246] Zurich became the insurer for Grafton Connor in 2002 when it took over as insurance provider for the Business Advantage Program. At some point thereafter, ECI retained TRS to inspect two of Grafton Connor's properties for Zurich – the Grafton Connor Building at 1739-1740 Grafton Street, and the North End Pub. The inspections were performed by Glenn Cox of TRS on November 13 and November 15, 2002, respectively.

[247] Two documents accompanied the inspection report for the Grafton Connor Building. The first was a letter from R. Allison of TRS, dated December 6, 2002, addressed to Ed Raymond, and copied to William Kamenetzky of ECI and Catherine Pickell, a program liaison with the Toronto office of Marsh. The second was a document entitled "Recommendations" which set out three

recommendations for the property. At the bottom of the recommendation letter was the following instruction:

> Please reply to: Mr. Bill Kamenetzky
> Enterprise Insurance Services Limited
> 70 University Avenue, Suite 800
> Toronto, Ontario, Canada
> M5J 2M4

[248] The North End Pub report was attached to a letter from R. Allison, dated January 16, 2003, addressed to Harvey Warren, the Manager of the Pub. This letter was also copied to Mr. Kamenetzky and Ms. Pickell.

[249] Although the covering letters for the two reports were addressed to Ed Raymond and Harvey Warren, Douglas Poole, the former President and CEO of ECI, testified that neither man would have received them. He said that inspection reports commissioned by ECI would never be sent to the client. Nor would the reports have been sent to Ms. Pickell of Marsh, or Eric Bourque, the broker handling the account at the time.

[250] Mr. Poole explained that there are two kinds of reports – those that include recommendations by the inspector, and those that do not. If a report did not include recommendations, the underwriter at ECI would be the only recipient. When recommendations were included, the report would be sent to the underwriter at ECI, but a copy of the accompanying recommendation letter would be sent to the local broker. Since the purpose of an inspection is to improve the risk and identify any potential hazards, compliance with the recommendations is in the interests of both the insured and the insurer. ECI therefore chose to enlist the broker's support to convince the insured to comply with the recommendations. ECI would typically request a written response from the broker advising whether the insured intended to comply with the recommendations, and, if so, the timelines proposed for compliance.

[251] Mr. Poole testified that sending inspection reports to the client or the broker, even where recommendations are included, would be contrary to general insurance industry practice. Insurers view inspection reports as their property for two reasons. First, they pay for the reports. Second, there is a risk that clients or brokers may use the report that an insurer has paid for in order to obtain a cheaper product from a competing insurer.

[252] The TRS report for the Grafton Connor Building included three recommendations. According to Mr. Poole's testimony, the report would have been sent to Mr. Kamenetzky at ECI, and a copy of the recommendation letter would have been forwarded to Mr. Bourque to discuss with Grafton Connor. The TRS report for the North End Pub, on the other hand, included no recommendations. Accordingly, the report would have been sent to ECI, but no information in relation to the inspection would have been sent to Mr. Bourque.

[253] The TRS report for the North End Pub was discovered in January 2011 when Blake Miller asked Jeannie Au-Tang, a Senior Vice-President at Marsh in Toronto, to locate the ECI underwriting file for the Grafton Connor account.

[254] Ms. Au-Tang joined Marsh in 1999 as a program manager for two of the company's national programs. She left Marsh in December 2000 to join ECI as Vice-President of Marketing. She stayed with ECI until 2006 when the company was wound up into Marsh. Ms. Au-Tang explained that the offices of ECI and Marsh were both located in the same building on University Avenue in Toronto. After ECI was wound up, its closed files and other property were kept in the Marsh offices for several months until they could be placed in storage at an Iron Mountain facility.

[255] In order to obtain the Grafton Connor underwriting file for Mr. Miller, Ms. Au-Tang had to submit a request to access the file to Iron Mountain, quoting the file name and policy number. When she examined the file, she located the two TRS inspection reports and provided them to Mr. Miller. Mr. Miller provided the North End Pub report to counsel for Marsh and counsel disclosed it to the other parties.

[256] Ms. Au-Tang testified that she did not access Mr. Kamenetzky's files from ECI. Nor did she search Catherine Pickell's files at Marsh's Toronto office for information related to Grafton Connor.

[257] References to the existence of TRS inspection reports appear several times in the evidence. In early March 2003, Mr. Bourque made some notes after speaking with someone at Grafton Connor. The evidence suggests this person was Mr. Raymond and that the men spoke a few days before March 14. Mr. Bourque wrote, "Glen Cox → YES!!", and "TRS - Interested in speaking with Glen."

[258] When asked about these notes, Mr. Bourque had no idea what they were about. He testified that he would not have been involved with any inspections. He

conceded on cross-examination, however, that it was logical, based on his handwritten references to Mr. Cox and TRS, that he would have been aware of the inspections.

[259] On March 17, Mr. Bourque met with Mr. Raymond and Mr. McMullin. He was told that Mr. McMullin would be taking over the insurance duties for Grafton Connor. Mr. McMullin's notes from this meeting state, *inter alia*, "Inspect propertys (TRS)", with an "E" beside it, meaning it was an action item for Eric Bourque.

[260] Mr. McMullin testified that when he wrote this note, he did not know what "TRS" meant. He did not recall any discussion about inspections with Mr. Bourque at that meeting, or with any other Marsh representative at any time thereafter.

[261] Several months after the meeting, on May 20, 2003, Mr. Bourque e-mailed Mr. McMullin as follows:

> Steve, as per our conversation, please advise if the below recommendations have been completed.
>
> Thank you

[262] Beneath this text is what appears to be a cut and paste of an e-mail that was sent to Mr. Bourque. The e-mail stated:

> Risk was inspected on Nov. 13, 2002 and letter of recommendations was sent Dec. 06, 2002.
>
> Looks like the insured has sent in a response stating that they have requested that the appropriate people look after the recommendations. Please confirm all recommendations have been fully complied with.

[263] The e-mail then set out the three recommendations made in the Grafton Connor Building TRS inspection report. Mr. McMullin responded to the e-mail on May 22, 2003:

> Eric,
>
> #'s 2 and 3 were completed a long time ago. Item #1 was reviewed by a qualified electrician but apparently not all of the updates were done. He is currently in the building and will not be leaving until the work is complete. As soon as I receive the word I will send you a follow up e-mail.
>
> …

[264] Mr. Bourque responded on the same day, thanking Mr. McMullin, and advising that he would let the insurers know. He also noted that he would "pass along any news of the renewal as soon as I have it."

[265] Four days after this exchange, on May 26, Blake Miller e-mailed Marsh UK, advising that Zurich would not be in a position to renew Grafton Connor's property coverage, and asking that Marsh UK try and place coverage in the London market. The e-mail notes, "Also, we are trying to get inspection reports from Zurich and will advise."

[266] On May 28, 2003, Mike Clarke of ECI faxed Mr. Bourque a copy of the TRS inspection report for the Grafton Connor Building. That report was never forwarded to Marsh UK or shown to Underwriters.

Findings of Fact

[267] In relation to the above evidence, I make the following finds of fact:

- Although both successful professionals, neither Mr. Raymond nor Mr. McMullin were sophisticated with respect to the placement of commercial property insurance.

- Both men were aware, however, that it is important to provide accurate information to an insurer underwriting coverage.

- Gary Hurst was always aware that the North End Pub was of mixed construction and had no sprinklers.

- Gary Hurst provided no instructions to Mr. Raymond before asking him to assume responsibility for placing property insurance. He did not review the features of any of the properties with Mr. Raymond.

- Mr. Miller had been pursuing the Grafton Connor property business since 1996.

- At no time did Mr. Miller make inquiries to determine Mr. Raymond's level of sophistication with respect to the placement of commercial property insurance.

- In 1999, Mr. Miller filled out the forms with the assistance of Charlotte Henderson.

- At no time did Mr. Miller inquire as to whether inspections had been done on the properties, or recommend that inspections be conducted on the properties.

- Mr. Miller provided the Grafton Connor property information to Kelly Bent, the client representative assisting him on the account. Ms. Bent entered the information into the Marsh GPS system.

- After coverage was bound, a completed application form was printed from the GPS system for each property and sent to Grafton Connor for review and signature.

- When Mr. Raymond reviewed the forms, he believed the information therein had been gathered by Blake Miller. He relied on Mr. Miller to complete the forms accurately.

- Mr. Raymond did not tell Mr. Miller that he was relying on him, nor did he ask Mr. Miller or Ms. Henderson how the information on the forms had been acquired.

- The misrepresentation on the 1999 Molson Business Edge Master Application Form that the North End Pub was sprinklered originated with Marsh. The error was the product of the conflation by Marsh of information pertaining to the North End Pub and Tomorrow's Lounge.

- Neither Mr. Raymond nor Mr. McMullin knew whether the North End Pub was sprinklered. Neither asked Gary Hurst, nor any employee of the Pub, whether the property was sprinklered.

- The misrepresentation that the North End Pub was of masonry construction originated with Marsh in the same manner as the sprinkler misrepresentation. However, when Mr. Raymond reviewed the 1999 Molson Business Edge Master Application Form, he agreed with the description, and adopted it as his own.

- Each year, Grafton Connor had the opportunity to review and update the information being submitted to the insurer in order to renew coverage.

- In 1999, 2000, and 2001, the computer generated copies of the master application and renewal forms sent to Grafton Connor for signature contained numerous errors. Many of these errors were corrected by Grafton Connor in 1999, but recurred in 2000 and 2001.

- The representations that the North End Pub was of masonry construction and 100% sprinklered appeared on the forms each year, and remained uncorrected during the period that Mr. Raymond dealt with the insurance.

- The Location Details Summary was prepared by Marsh.

- In 2003, when Mr. Raymond delegated responsibility for insurance to Mr. McMullin, he gave him no instructions and did not review the various kinds of coverage with him.

- At no time did Mr. Bourque, or any Marsh representative thereafter, make inquiries to determine Mr. McMullin's level of sophistication with respect to the placement of commercial property insurance.

- The first time Mr. McMullin saw the Location Details Summary was in 2003. Marsh did not discuss the individual categories listed on the schedule with him, other than business interruption, which Mr. McMullin was shown how to calculate.

- When Mr. McMullin was asked to update the Location Details Summary, he assumed the information in the construction and sprinkler columns was accurate because it was historical information, and he had no reason to doubt its veracity.

- Following the TRS inspection of the Grafton Connor Building in November of 2002, a recommendations letter was sent to Grafton Connor.

- Although Mr. McMullin's notes of March 17, 2003 state "Inspect propertys – TRS", with the initial "E" beside it, Mr. Bourque did not explain the benefits of property inspection to Mr. McMullin or recommend that he obtain property inspections for each of the Grafton Connor properties.

- Mr. Bourque was aware in 2003 that TRS inspected the Grafton Connor Building and the North End Pub.

- Mr. Bourque received a copy of the TRS inspection report for the Grafton Connor Building from ECI on May 28, 2003. He did not follow up and ask ECI whether it had other Grafton Connor inspection reports in its possession.

- Mr. Bourque never received a copy of the TRS inspection report for the North End Pub.

- Mr. Bourque did not provide the TRS inspection report for the Grafton Connor Building to Marsh UK.

- Despite Mr. Miller's e-mail stating that they were trying to get inspection reports from Zurich, Marsh UK did not follow up with Mr. Miller.

- For several months in 2006, after ECI was wound up, its closed files and other property were kept in the Marsh offices until they could be placed in storage at an Iron Mountain facility.

- The Proof of Loss was filed on June 5, 2007. As of that date, the replacement cost of the North End Pub building was $2,174,514.02 and the replacement cost for the contents was $411,357.61. The business interruption amount was $154,997.53.

Duty of an Insurance Broker

[268] A plaintiff insured may bring an action against an insurance broker in contract, tort, or both. There are certain advantages, however, to proceeding in tort. In both contract and tort, remoteness will limit damages to reasonably foreseeable losses. The difference is the time that foreseeability is assessed. In contract, the loss must have been foreseeable when the parties made the contract, which may be long before the breach. In tort, the loss must have been foreseeable at the time the wrong occurred.

[269] A further advantage is that liability in tort does not require an interpretation of the broker's specific obligations under the contract. As Boivin explains in *Insurance Law*, *supra*, at p 165:

> The most notable advantages of proceeding in tort concern limitation periods and methods of assessing damages. Currently, these are different in contract and in tort. Another advantage is that tort liability does not require an interpretation of the broker's mandate. …

> [L]iability in tort has become the preferred theory of liability over the years, precisely in order to avoid "the complex line of reasoning necessary to lead to liability in contract." In tort, the contract is part of the factual matrix, but it does not need to be subjected to the same degree of scrutiny as under a contractual approach. Rather, the contract is simply one element used to assess whether or not the defendant (the broker, in this case) owed a duty of care to the plaintiff.

[270] In its pleadings, Grafton Connor alleges liability against Marsh in both contract and tort. It says it was a term of the contract that Marsh would act with skill and expertise and with a standard of care of a reasonably prudent broker of property insurance. In other words, it was a term of the contract that Marsh, in carrying out its mandate, would not be negligent. Framed in this manner, and in light of the advantages to a plaintiff of proceeding in tort, the claim in contract is superfluous. If I find liability in negligence, I need not consider the contractual claim.

[271] Both Grafton Connor and Marsh have provided expert opinion on the standard of care of an insurance broker in the circumstances of this case. Grafton Connor relies on the expert report of Frank Szirt. Mr. Szirt is not, and has never been, an insurance broker, but has worked in the insurance industry since 1965.

[272] Mr. Szirt described the duties owed by an insurance broker to a client at p 21 of his report:

> Canadian insurance brokers know that they owe a set of duties to their clients throughout the various stages of the insurance transaction. This set of duties may be summarized under the following categories:
>
> - obtaining and understanding the client's instructions;
> - determining the client's needs and requirements;
> - providing appropriate counsel and advice;
> - effectively marketing the client's risks;
> - confirming coverage or the absence of coverage; and
> - servicing the client's ongoing insurance needs.
>
> The same set of obligations immediately begin with the renewal process.

[273] In his report, Mr. Szirt was very critical of Marsh's handling of the Grafton Connor account. He wrote at p 22:

> [T]he very fact that the underwriting information transmitted to Lloyds in 2003 was incorrect as early as 1999 and persisted during the next seven renewals between 2000 and 2006, speaks to Marsh Halifax's failure to discharge one or more of these obligations. Unfortunately, efforts to track down the source of the problem are impeded by the lack of written notes of Mr. Miller's initial meeting with Grafton Connor Group in 1999 and any of the later "review meetings".

[274] According to Mr. Szirt, the importance of proper file documentation as a form of risk management is well known in the insurance industry, and an absence of such documentation may lead to the inference that the broker's duty has not been discharged.

[275] Mr. Szirt opined that the misrepresentations regarding the sprinkler system and the construction type arose during Mr. Miller's first meeting with Grafton Connor, and, once the initial errors were made, the renewal routine allowed them to persist over the next seven years. The renewal meetings focused on changes that had occurred in the previous year, and risk features which normally remain constant, like construction type and fire protection, were probably not on the agenda.

[276] In Mr. Szirt's opinion, Marsh failed to discharge its duty to provide adequate counsel and advice to Grafton Connor Group in the following ways:

> ..[A]ccording to the evidence, Marsh Halifax
>
> - did not help Grafton Connor Group with how the insurance industry defines "masonry" construction;
> - never explained to Grafton Connor Group the importance Lloyds attached to the accuracy of the information in a signed application and bring home to its client the potentially severe consequences of any inaccuracy;
> - never discussed policy features of potential interest to Grafton Connor Group, such for example as how the 80% coinsurance clause in Endorsement 10 may affect recovery after a covered loss;
> - never reviewed the completed documents together with Grafton Connor Group – specifically the applications up to 2003 and the Location Detail Summaries between 2003 and 2006 – to ensure that the information provided to Lloyds was accurate. (p 24)

[277] When preparing his report, Mr. Szirt was under the misapprehension that Marsh was in possession of the TRS inspection report for the North End Pub in 2003 and failed to provide it to Underwriters. This misapprehension formed the basis for his opinion that Marsh breached its duty to market its client's risk

effectively. Since the factual foundation for this opinion is flawed, I have given it no weight.

[278] Marsh relies on the opinion of its expert, Robert Harder. Mr. Harder is an insurance consultant who has worked in the property-casualty insurance industry since 1971. He has 28 years of experience as an insurance broker placing insurance for mid-size businesses. He was qualified as an expert on the insurance industry, the practice and procedures followed by insurance brokers, and standards applicable to insurance brokers.

[279] Mr. Harder was asked to opine on whether it was reasonable for Marsh to rely on the location information verified yearly by Grafton Connor regarding the North End Pub, and, in particular, the information regarding the sprinkler coverage and type of construction. Mr. Harder's response, reproduced below in full, was brief:

> In completing all of the material underwriting information about a risk to be insured a broker can and frequently must rely on the client giving them that information. It is in order for the broker to depend upon the reliability of that information in accordance with the obligation of utmost good faith applying to the parties to the insurance contract. [*sic*] It is often the case that the only source of information available to the broker about an insurance risk lies with the client.
>
> Marsh was reasonable in relying upon the integrity of their client Grafton Connor, in providing the yearly information about the values for insurance cover on the North End Pub and the attendant information regarding the existence of sprinklers at the location and the type of construction of the building.
>
> The more knowledgeable and sophisticated the buyer/insured, the greater the reliance on the part of the broker. (Expert Report, p 5)

[280] Mr. Harder, unlike Mr. Szirt, was not cross-examined on his report.

[281] In addition to the reports of Mr. Szirt and Mr. Harder, I have considered the relevant case law. The two leading cases on the duty owed by an insurance agent or broker to an insured both involve a failure by the broker to obtain adequate coverage. In *Fine's Flowers Ltd v General Accident Assurance Co of Canada*, [1977] OJ No 2435, 1977 CarswellOnt 54 (CA), Mr. Fine operated a number of greenhouses in connection with his extensive horticultural business. Although he was a successful businessman, Mr. Fine was not particularly well-versed in the subject of insurance. For this reason, he simply told the insurance agent that he wanted "full coverage" for the business.

[282] The agent obtained coverage under a Boiler and Machinery Policy that insured the boilers, but failed to insure the water pumps that supplied water to those boilers. The heating system in some of the greenhouses failed when one of the water pumps seized, cutting off the electricity to both pumps. Without adequate water supply, the boilers shut down and the heat went off in the greenhouses, destroying the crops inside.

[283] The issue before the Ontario Court of Appeal was whether the loss fell within the scope of the agent's duty of care. Wilson JA (as she then was), for the majority, stated as follows:

> 41 The main ground of appeal from the judgment of the learned trial Judge is that he put far too broad and sweeping a duty on insurance agents. They are not insurers. It is not part of their duty to know everything about their clients' businesses so as to be in a position to anticipate every conceivable form of loss to which they might be subject. The agent's duty, counsel submits, is "to exercise a reasonable degree of skill and care to obtain policies in the terms bargained for and to service those policies as circumstances might require".
>
> 42 I take no issue with counsel's statement of the scope of the insurance agent's duty except to add that the agent also has a duty to advise his principal if he is unable to obtain the policies bargained for, so that his principal may take such further steps to protect himself as he deems desirable. The operative words, however, in counsel's definition of the scope of the agent's duty, are "policies in the terms bargained for".
>
> 43 In many instances, an insurance agent will be asked to obtain a specific type of coverage and his duty in those circumstances will be to use a reasonable degree of skill and care in doing so or, if he is unable to do so, "to inform the principal promptly in order to prevent him from suffering loss through relying upon the successful completion of the transaction by the agent": Ivamy, *General Principles of Insurance Law* (2nd ed. 1970), p. 464.
>
> 44 But there are other cases, and in my view this is one of them, in which the client gives no such specific instructions but rather relies upon his agent to see that he is protected, and if the agent agrees to do business with him on those terms, then he cannot afterwards, when an uninsured loss arises, shrug off the responsibility he has assumed. If this requires him to inform himself about his client's business in order to assess the foreseeable risks and insure his client against them, then this he must do. It goes without saying that an agent who does not have the requisite skills to understand the nature of his client's business and assess the risks that should not be insured against should not be offering this kind of service. As Haines J. said in *Lahey v. Hartford Fire Ins. Co.*, [1968] 1 O.R. 727 at 729, [1968] I.L.R. 1-194, 67 D.L.R. (2d) 506, varied [1969] 2 O.R. 833, [1969] I.L.R. 1-261 (C.A.):

> The solution lies in the intelligent insurance agent who inspects the risks when he insures them, knows what his insurer is providing, discovers the areas that may give rise to dispute and either arranges for the coverage or makes certain the purchaser is aware of the exclusion.
>
> 45 I do not think this is too high a standard to impose upon an agent who knows that his client is relying upon him to see that he is protected against all foreseeable, insurable risks.

[284] The reasoning in *Fine's Flowers* was adopted by the Supreme Court of Canada in *Fletcher v Manitoba Public Insurance Co*, [1990] 3 SCR 191, [1990] SCJ No 121, where Wilson J wrote for the Court:

> **54** In my view, *Fine's Flowers* stands for the proposition that private insurance agents owe a duty to their customers to provide not only information about available coverage, but also advice about which forms of coverage they require in order to meet their needs. I note that Professor Snow has summarized the effect of *Fine's Flowers* in "Liability of Insurance Agents for Failure to Obtain Effective Coverage: *Fine's Flowers Ltd. v. General Accident Assurance Co*." (1979*), 9 Man. L.J. 165*, in the following terms, at p. 169:
>
> > The implication of this case and many others like it in recent years seems clear. Consumers who place their faith in insurance agents holding themselves out as competent and find their faith misplaced, will frequently be able to find recourse against the agent. ... [T]he extent of the duty owed by an insurance agent, both in placing insurance and in indicating to the insured which risks are covered and which are not, as set out in this case, is a fairly stringent one for the agent. Moreover, given the general situation of the principal relying very heavily on the expertise of the agent, it does not seem to be an unreasonable burden for an insurance agent to bear. [Emphasis added.]
>
> **55** The duty of care owed by an insurance agent was further elaborated in *G.K.N. Keller Canada Ltd. v. Hartford Fire Insurance Co*. (1983), 1 C.C.L.I. 34 (Ont. H.C.) (conf. on appeal (1984), 4 C.C.L.I. xxxvii (Ont. C.A.)). It was held in that case that where the customer adequately describes the nature of his or her business to the agent, the onus is then on the agent to review the insurance needs of the customer and provide the full coverage requested. Should an uninsured loss occur, the agent will be liable unless he or she has pointed out the gaps in coverage to the customer and advised him or her how to protect against those gaps.
>
> **56** It is clear that within the insurance industry, as also within the courts, private insurance agents and brokers are viewed as more than mere salespeople. The Continuing Legal Education Society of British Columbia's 1985 Seminar on Insurance Law focused on the services they provide, (at p. 6.1.03):

> The services of a competent agent or broker will include, in addition to advice on insurance, and the brokering or placing of insurance on behalf of the client, an active interest and involvement in loss prevention and a claims supervisory service to assist your client in the satisfactory settlement of the claims.
>
> **57** In my view, it is entirely appropriate to hold private insurance agents and brokers to a stringent duty to provide both information and advice to their customers. They are, after all, licensed professionals who specialize in helping clients with risk assessment and in tailoring insurance policies to fit the particular needs of their customers. Their service is highly personalized, concentrating on the specific circumstances of each client. Subtle differences in the forms of coverage available are frequently difficult for the average person to understand. Agents and brokers are trained to understand these differences and to provide individualized insurance advice. It is both reasonable and appropriate to impose upon them a duty not only to convey information but also to provide counsel and advice. [*Emphasis added*]

[285] Marsh says the above authorities establish that an insurance broker must exercise a reasonable degree of care and skill in carrying out his or her responsibilities, and the standard of care will depend upon the sophistication of the insured. The more sophisticated the insured, the less a broker must explain to that insured. The broker's responsibilities include reviewing the insurance needs of the customer, arranging for the appropriate coverage, and identifying any gaps in coverage.

[286] In this case, however, Grafton Connor's loss was not the result of a failure by Marsh to arrange proper coverage. It was the result of the voiding of its Policy due to material misrepresentations contained in the information provided to Underwriters. What duty, if any, does a broker owe an insured with respect to the accuracy of the information provided to the underwriter?

[287] Marsh says the broker owes no duty to the insured in this regard. The broker is not responsible for the independent investigation and verification of information provided by the applicant for insurance. In Marsh's view, then, the broker's responsibilities begin only after the insured has filled out the application form or otherwise provided the broker with all of the material facts. Even if the broker makes an error recording the information, the insured is responsible to ensure all of the information is accurate before signing the application.

[288] In its post-trial brief, Marsh summarizes its position as follows:

> Consistent with the standard set forth by the Supreme Court of Canada in *Fletcher*, *supra*, the duty of the broker is to review the needs of the assured and to ensure that the full coverage requested is obtained – **the customer first having adequately described the nature of his business to the agent**. To require a broker to interrogate and independently verify the information supplied by the insured in an application for insurance would place upon the broker a duty that is not recognized in law and would relieve the insured of the obligation to be truthful and candid in its representations about itself and the risk it is presenting.
>
> [*Emphasis in original*]

[289] Marsh relies on a number of English and Canadian authorities which it says establish that a broker has no duty to the insured for the accuracy of the information it forwards to the insurer. In *Biggar v Rock Life Assurance Company*, [1902] 1 KB 516 (KB), an insurance agent completed an insurance application with answers that he knew were false. The applicant signed the document without reading it. Wright, J. found that the applicant was under a duty to ensure that the information on the form was accurate:

> … I agree with the view taken by the Supreme Court in that case, and apparently in other cases which are there cited, that if a person in the position of the claimant chooses to sign without reading it a proposal from which somebody else filled in, and if he acquiesces in that being sent in as signed by him without taking the trouble of reading it, he must be treated as having adopted it; and business could not be carried on if that were not the law. On that ground I think the claimant is in a great difficulty. (p 524)

[290] In *O'Connor v BDB Kirby & Co*, [1971] 2 All ER 1415, the English Court of Appeal considered a claim by an insured who had consulted a broker in order to apply for an auto insurance policy. The insured supplied the broker with the necessary information to complete the application form. In answer to one question, the insured stated that he had no garage and that the car was kept in the street. Through a slip or misunderstanding, the broker filled in the answer so as to suggest that the car was kept in a garage. The insured quickly glanced at the form, failed to notice the error, and signed it. The insurers accepted the application, but when a claim was made and the mistake came to light, they denied liability. The insured then brought an action against the broker.

[291] The Court of Appeal held that the duty of the applicant for insurance was to make sure that the information contained in the proposal form was accurate and not to sign it if it was inaccurate, and that the applicant could not be heard to say that

he had not read the form properly or was not told of its contents. Davies LJ stated at 1420:

> It is argued by counsel for the brokers that the failure of the insured properly to read the form was the cause of this loss, the cause of putting the insurance company in a position to repudiate liability. I think counsel for the brokers is right in that regard. We have been referred to a couple of authorities from which I do not think it is necessary to quote, as they are concerned with a rather different subject matter: *Biggar v Rock Life Assurance Co* and *Newsholme Brothers v Road Transport and General Insurance Co Ltd*. They were cases in which an assured sued an insurance company, and in each case the proposal form had been falsely or inaccurately filled out by an insurance agent or broker who was held in each case in that respect to be acting as an agent of the proposer, the assured, and not an agent of the insurance company; and in each of those cases it was emphasised that it is the duty of the proposer for insurance to see and make sure that the information contained in the proposal form is accurate and not to sign it if it is inaccurate, and that he cannot be heard to say that he did not read it properly or was not fully appraised of its contents. That, of course, as I have said, is a different subject-matter from that with which we are presently concerned; but I think the principle applies with equal force in this case. Of course, it would be different if the insured was unable to read or was in some degree illiterate; but there is no suggestion of that in this case and there is nothing in the judge's note of the evidence to suggest any such thing. The insured was fully able to read this proposal form (though perhaps he could not have been able to read the copy we have), and there had been this discussion about the garaging of the car and its relevance to the amount of the premium, and it was there staring him in the face. If he did not read it properly then I think he has only himself to blame.

[292] Turning to Canadian authorities, in *Wolfe v Western General Mutual Insurance*, [2000] OJ No 2673, 2000 CarswellOnt 2541 (Sup Ct), the insured, Mr. Wolfe, signed an application for property insurance that represented that his home was heated by a propane furnace. In fact, the furnace was disconnected, and the house was heated by space heaters. The house was subsequently destroyed by fire, and coverage was denied by the insurer. Mr. Wolfe sued the insurer and the broker.

[293] Mr. Wolfe initially spoke to a representative of the broker by telephone on August 29, 1994, about insuring the property. The representative asked him the pertinent questions and they completed the application over the phone. She filled out the form. Mr. Wolfe told the representative that the property was heated by a wall-mounted propane furnace, and she ticked off the box "Furnace (central)." He also told her that the unit was not hooked up, because there were no propane tanks

yet. When she asked him when it would be hooked up, he told her he intended to hook it up in the near future. Mr. Wolfe signed the application in the broker's office a few weeks later, on September 19, 1994.

[294] The court accepted that the broker knew of the disconnected furnace, but nonetheless dismissed the claim against her:

> 26 The pertinent issue in determining the broker's liability for alleged breaches of duty in this case seem to me to be this. To whom does the broker owe a duty in relation to the accuracy and completeness of the information in the Application: to the plaintiffs? or to the insurer?
>
> 27 The Court of Appeal considered this issue in *Salata v. Continental Insurance Co.*, [1948] O.R. 270 (Ont. C.A.), 279, a case which on its facts is not dissimilar from this case. Chief Justice Robertson said:
>
> > The appellant (the insured) says further that at the same time when the application for insurance was procured by the agent, Cowan, he made full disclosure of the facts in relation to the condition of the barn in so far as the absence of any means for conditioning the tobacco was concerned, and told the agent of this plan to install oil-burning equipment. He says there was a discussion of these matters, in the course of which Cowan gave him advice as to how he should proceed. Not only is there no contradiction of appellant's evidence on these matters, but the agent's statements that I have already quoted from his report on the back of the application strongly support appellant's evidence. Appellant says that the answers appearing in his application were written there by Cowan. I have not been able to find in his evidence any statement as to whether or not he read the answers, or had them read over to him. He admits that he signed the application, and he says that Cowan signed it as witness. He did not get a copy of the application, and there is no copy of it attached to the policy. The agent, Cowan, was not called to challenge the appellant's evidence, nor was any explanation given for not calling him. In the circumstances I can see no ground upon which the appellant's evidence in regard to the taking of his application for insurance, can be rejected. **The application is, however, the appellant's application, for he signed it, and left it with the agent to be sent in. (Emphasis added)**
>
> The concluding words of this passage clearly indicate that the agent or broker who prepares an application for insurance for signature by the applicant for insurance is not under a legal duty to the applicant for its contents.
>
> ….
>
> 29 I agree with the submission of counsel for the insurer and the broker that any duty upon the broker in the circumstances of this case for the accuracy and completeness of the application for insurance is owed solely to the insurer and not

> to the plaintiffs. That being so, there is no breach of duty upon which the plaintiffs may rely as a foundation for their alternative claim against the broker in contract or tort.

[295] Marsh also relies on *Goodbrand v Pearson Insurance Brokers Ltd*, [2001] OTC 295, [2001] OJ No 1522 (Ont Sup Ct), which adopted the reasoning in *Wolfe*. In *Goodbrand*, the insured was denied coverage for a stolen motor vehicle on the basis of material misrepresentation, as he had not informed the insurer that his vehicle was to be used for commercial purposes. The insured alleged that he had informed his broker of his intended use of the truck. The insured argued in the alternative that the broker knew what kind of work he did and that he used his truck to do this work, so the broker should therefore have probed him more as to the proper coverage required for his truck. The court found that the insured had misrepresented the intended use of the vehicle to the broker in order to obtain a lower premium. On the issue of the broker's alleged duty to "probe", Mossip J wrote:

> 9 I was referred to several cases by counsel for each party. I find the case referred to by the defendant, *Wolfe et al. v. Western General Mutual Insurance et al.*, [2000] I.L.R. I-3851, Ontario Superior Court, to be the most relevant and helpful in deciding the case before me.

[296] After quoting from *Wolfe* at length, Mossip J concluded:

> 12 I adopt entirely Justice Sedgwick's reasoning and find that the same legal principles are applicable in the case before me, and that therefore the defendant is not liable to the plaintiff for any damages he may have suffered when his truck was stolen.
>
> 13 The type of case that was before Justice Sedgwick and that is before me, is not similar to those situations such as in *Fine's Flowers Ltd. et al. v. General Accident Assurance Co. of Canada et al.* (1977), 17 O.R. (2d) 529 (Ont. C.A.) or *Dueck v. Manitoba Mennonite Mutual Insurance Co.*, [1992] M.J. No. 294. These cases involved situations where insurance brokers or agents were specifically relied upon for their expertise in commercial insurance coverage, for example, where agents were asked to obtain and provide an insured with proper insurance coverage to cover "all risks" or "full coverage". In those cases, the agent was relied on to choose appropriate insurance coverage to meet the requirements of an insured, and the agents' failure to do so would be at his or her peril. Obviously, those cases are quite different from the one before me, where an insured applies for insurance coverage and fills in the application requesting coverage of his truck for a certain use, and obtains exactly what he applied for. In my view, the agent in this latter case is not a private detective who is required to cross-examine his own

> client as to the answers given on an application. The agent is merely a "scribe or secretary" of the insured in completing the application for insurance.
>
> 14 As to the obligation of the insured to read the application and ensure its accuracy, I find that *Wolfe et al.*, above,. and *Fraser Jewellers (1982) Ltd. v. Dominion Electric Protection Co. et al.* (1997), 34 O.R. (3d) 1, stand for the proposition that it is the insured's responsibility to read and ensure the accuracy of both the application for insurance, and the insurance policy itself. It is simply no defence to an inaccurate application and subsequent inadequate policy, for the person seeking to escape the provisions of the contract, to allege that they did not read it.

[297] Finally, Marsh cites *Edwards v Kent General Insurance Corporation*, 1986 CarswellNB 66, a decision of the New Brunswick Court of Queen's Bench. In that case, the insured, Mr. Edwards, had signed an application form for motor vehicle insurance containing answers that had been filled out by the insurance agent, Lynn Chase. The answers filled in by the agent were essentially guesses based upon the previous insurance carried by Mr. Edwards. Mr. Edwards was in a hurry and did not read the application form before signing it. One of the answers on the form misrepresented whether the insured had a previous licence suspension. In dismissing the insured's claim against the insurer, Turnbull J stated:

> 10 But I do not believe that this case turns on that point. I believe that this case turns on its peculiar facts that Lynn Chase did not put these questions to the insured — to the plaintiff and he himself has no recollection of the matter, he does not recall signing the application. I make a finding of fact that he did in fact sign Ex. 5(e). As Lynn Chase says, he was in a hurry, he left for Nova Scotia, she didn't want to give him the application either in blank or with her answers and have him just pro forma sign without reading them. She filled it in assuming her answers were correct based on the low rate he had with his previous insurer. The plaintiff knew or ought to have known that she was not writing down answers he gave and should have taken the trouble to read the question and answers. When he signed it, he was adopting the answers as his own.

[298] Not all of the authorities relieve an insurance broker of any duty to make additional inquiries in order to verify information provided by the insured. In *Sotiropoulus v. Bernard Freedman Insurance Ltd.*, [1982] NBJ No 402, 1982 CarswellNB 259 (QB), fire destroyed the Belmont Hotel in Saint John, including the restaurant and tavern housed within it. The restaurant was operated by the plaintiffs, Louis and Theodore Sotiropoulus, while the tavern was operated by the plaintiff Paul Daeres, who, through a company, owned the building and operated the hotel. The restaurant and tavern were both mentioned in an insurance policy taken out on the premises, but the insurer refused to pay any loss relating to either

because Mr. Daeres and the Sotiropoulus brothers were not named as insureds in the policy. The plaintiffs brought an action in negligence against the insurance agent, Mr. Freedman.

[299] The court accepted that the agent had been supplied with documentation that clearly indicated that the restaurant and tavern were operated separately from the hotel. For this reason, Mr. Freedman was found negligent for not obtaining the required coverage. However, even if Mr. Freedman had not been given that information, Hoyt J would have found liability on an alternative basis:

> 23 The plaintiffs relied on the defendant to arrange coverage which would naturally include naming the correct insured.
>
> 24 Additionally, and entirely apart from the above finding, it is my view that in circumstances such as this, even if I accept Mr. Freedman's version of his questioning of Mr. Daeres before placing the coverage, that the defendant was obliged to make additional inquiries to verify the basic facts.
>
> 25 The vital importance of naming the correct insured is well known. Casual questioning is not always sufficient. The agent must make sufficient inquiries, perhaps in some cases from an independent source or by inspection, to satisfy himself that the answers given are indeed correct. This inquiry would vary in each situation. Factors to be considered include the nature and complexity of the coverage requested, the sophistication of the insured, whether the coverage was new or the renewal or extension of existing coverage, previous dealings between insured and agent, and whether or not the insured was suffering from any disability. … [*Emphasis added*]

[300] He went on to cite Wilson J's remarks in *Fine's Flowers* (quoted above), adding, "[w]hile these remarks are directed to specialty coverage, they have equal, if not greater, application to a more usual commercial situation, such as existed here."

[301] A further example is *Strougal v Coast Capital Insurance Services Ltd*, 2008 BCSC 17, 2008 CarswellBC 116. In that case, Evelin Strougal insured her house and its contents under a policy issued by Canadian Northern Shield Insurance Company. The policy was arranged by Coast Capital Insurance Services Ltd., an insurance brokerage. Ms. Strougal's home was subsequently destroyed by fire, and she brought an action against the broker and the insurer for failing to ensure that she had adequate coverage for the contents of her home.

[302] Until 1999, Ms. Strougal obtained her house insurance through H.W. Dickie. Coast Capital bought out H.W. Dickie in 1999, and from March 2000 until the fire

on November 4, 2004, Ms. Strougal obtained her insurance through Coast Capital. The insurance coverage for the house was set at $186,000 based on an estimate by Coast Capital of the property's replacement cost. Since it was the insurer's practice to provide the same coverage for personal property as for the house, the limit of coverage for the contents was also set at $186,000. The policy contained a "guaranteed replacement cost endorsement" designed to cover any excess replacement costs for the home if certain conditions were met. This endorsement did not apply to the contents.

[303] The actual replacement cost of the home was $357,000, which was paid by the insurer under the endorsement. The personal property in the home was determined to have a replacement cost of $357,655.99. Ms. Strougal brought the action to recover the value of the personal property that exceeded the $186,000 coverage limit.

[304] Ms. Strougal alleged that Coast Capital used incorrect information to estimate the house replacement cost. She claimed Coast Capital breached its duty to her by failing to take reasonable steps to correct the false information in its files. Expert evidence was presented which was alleged to establish that if correct information had been used, the replacement cost estimate would have been set at over $300,000, which would have resulted in the same amount of coverage for personal property.

[305] Coast Capital denied that it was negligent, and asserted that all of the incorrect information it relied on to calculate the replacement cost of the house had been provided by Ms. Strougal to H.W. Dickie, and that she failed to correct that information when it was repeated in the renewal documents every year thereafter. Coast Capital also argued that Ms. Strougal did not rely on its estimated replacement cost of the house in deciding what amount of insurance coverage she wanted to purchase for her personal property.

[306] Halfyard J was satisfied that Coast Capital owed a duty to Ms. Strougal to exercise reasonable skill and care in estimating the replacement cost of her house. As to the standard of care, he held that an insurance broker of reasonable competence in the position of Coast Capital would have reviewed with Ms. Strougal the information in its files concerning all relevant characteristics of her home, item by item, before issuing the renewal policy.

[307] Halfyard J found that Coast Capital did receive false information from H.W. Dickie concerning Ms. Strougal's home. Coast Capital printed out this information

on a document and sent it to Ms. Strougal for her review. This document was entered at trial as Exhibit 7. Ms. Strougal attempted to correct three items before signing the document below an endorsement certifying that all of the statements made in the document were complete and accurate. As it turned out, the document still contained several significant errors. It listed the area of the ground floor as being 1200 square feet when it was considerably larger. It represented that there was no balcony or deck, when there was a deck. It said there were no extra bathrooms, when the house had two and one-half bathrooms. The court found that Coast Capital sent out renewal letters and other written materials to Ms. Strougal in the years from 2000 to 2004 which, except for 2003, included a one-page document which repeated the erroneous information that remained in Exhibit 7. Ms. Strougal failed each year to detect the errors.

[308] The court found that a Coast Capital employee was mistaken in her belief that she reviewed all of the relevant characteristics of Ms. Strougal's home with her, item by item, on April 16, 2004. It was more likely that she asked Ms. Strougal whether any significant changes had been made to the home. Halfyard J concluded that Coast Capital should have made further inquiries of Ms. Strougal to verify the information it had with respect to her home:

> 35 I find that Ms. Strougal did not knowingly convey any false information to either H.W. Dickie Ltd. or to Coast Capital. I further find that Ms. Strougal did not know that Coast Capital was relying on false information when it estimated the replacement cost of her house. I find that Ms. Strougal gave correct information about her house, whenever she was asked by any employee of Coast Capital about any characteristic of her house. I am not satisfied that Ms. Strougal was negligent in giving information about her house to H.W. Dickie Ltd.
>
> 36 In my opinion, Exhibit 7 is a confusing document which is difficult to understand. I think Coast Capital should have taken steps to ensure that Ms. Strougal understood exactly what was being asked of her before requesting that she certify the truth of the information. Perhaps Ms. Strougal should have made detailed inquiries about the information contained in this document. Certainly she should have paid closer attention to the renewal material sent out to her each year. She may have been negligent in these respects, but that is a different matter.
>
> 37 Accordingly, I find that Coast Capital failed to make adequate inquiries of Ms. Strougal to ensure that they had the correct information about the relevant characteristics of her house. I find that, if this had been done, the false information about those characteristics would have been discovered and corrected. I find that, if the correct information had been used to estimate the replacement cost of Ms. Strougal's house, Coast Capital would have estimated the replacement cost to be about $254,600, in 2004.

[309] Although Halfyard J determined that Coast Capital breached its duty of care with respect to insurance coverage for the house, he was not satisfied that this breach was the cause of the loss incurred by Ms. Strougal. In the event that he was wrong on this point, Halfyard J noted that he would have found Ms. Strougal fifty percent at fault:

> 60 In February or March 2000, Coast Capital sent out renewal material which included Exhibit 7. In the renewal letter, Ms. Strougal was asked to review the material
>
> > . . . carefully to ensure that the information is correct and you are satisfied with the limits and coverages. Please call your branch if you wish to discuss your coverages or amend this information.
>
> 61 Similar wording was contained in the renewal letters sent to Ms. Strougal in the years 2001, 2002, 2003 and 2004. In addition, except for 2003, the letters were accompanied by a sheet containing a printout of the information on file about the characteristics of Ms. Strougal's house. Those sheets were easier to read, and to understand, than Exhibit 7. Ms. Strougal failed to detect most of the errors pertaining to her house, in the materials sent to her. Moreover, she failed to inquire of Coast Capital to ask questions about what any of the statements or entries meant, notwithstanding that they were not easy to understand and may have confused her. She knew or ought to have known that Coast Capital was relying on the information in the materials that they sent her each year, in arranging the insurance coverage for her house.
>
> 62 In my opinion, Ms. Strougal failed to exercise the care that would have been exercised by a reasonable homeowner in similar circumstances. Had she done so, the erroneous information, or most of it, would have been discovered and corrected. I would have found that Ms. Strougal should be held 50 percent at fault, if I had concluded that she suffered a loss by reason of Coast Capital's breach of duty.

[310] Whether expert evidence is necessary to determine the standard of care for an insurance agent or broker will depend on the circumstances: see, for example, *Keizer v Portage LaPrairie Mutual Insurance Co*, 2013 NSSC 118, [2013] NSJ No 289 at para 94. In my view, I need not rely on or adopt the conclusions of either expert in the circumstances of this case. The standard of care can be ascertained through the jurisprudence and the evidence given by the witnesses at trial.

[311] When Blake Miller obtained the Grafton Connor business in 1999, Ed Raymond assumed it was the broker's responsibility to visit the properties and review the company's files in order to gather the necessary information to place coverage. Mr. Miller, on the other hand, believed his only responsibility with

respect to collecting information from Grafton Connor was to hand over eight blank application forms. As is often the case, the standard of care lies somewhere between these two extremes.

[312] As Marsh points out in its submissions, the content of a broker's duties will vary depending on the sophistication of the client. According to Marsh, Ed Raymond, a former lawyer, and Steve McMullin, an accountant, were sophisticated clients, and Marsh was therefore entitled to assume that they needed little in the way of counsel and advice. I have heard no evidence, however, that a representative of Marsh ever made inquiries of either man to ascertain his experience placing commercial property insurance, or the degree of confidence each had in his respective ability to provide accurate answers to the questions required to secure coverage. That such inquiries were never made of Mr. Raymond is patently obvious, since he believed, despite multiple meetings with Blake Miller, that Mr. Miller had gathered all of the information for the initial application and ensured its accuracy.

[313] As I indicated in my findings of fact, I do not accept that either Mr. Raymond or Mr. McMullin was a sophisticated insurance client. The mere fact that a person is a professional does not mean that he or she has the knowledge or skill required to walk into a commercial building and, without assistance, collect the information required to complete a property insurance application. Indeed, the complexity of the task was apparent from Blake Miller's own testimony. Mr. Miller has worked in the insurance industry for close to twenty years. When asked if he had ever independently inspected a client's property in order to verify the answers provided on an application form, Mr. Miller responded that he had not, because he personally did not have "any training in terms of property inspection or engineering." Yet he made no inquiries to satisfy himself that Mr. Raymond had the necessary training or experience to collect the information for eight separate commercial properties.

[314] Grafton Connor was Marsh's largest hospitality client under the Molson Business Edge Program. In 1999, its properties were worth almost $10 million. By 2006, that number had grown closer to $20 million. I am satisfied that an insurance broker of reasonable competence, taking on a client like Grafton Connor in 1999, would have made inquiries of Mr. Raymond to satisfy himself that he was capable of completing the application forms accurately. He would have asked if there had been inspections done on the properties in the past from which Mr. Raymond could glean the relevant information. If not, he would have discussed

the benefit of inspections with the client, and the consequences of a failure to provide accurate information. I find that Marsh's failure to make these inquiries constituted a breach of its duty to provide appropriate counsel and advice.

[315] The obligation on the part of the broker is not a particularly onerous one. If, despite the broker's advice, the client declines to proceed with inspections or any other means of obtaining accurate information, he does so at his peril. There is no duty on the broker to cross-examine or interrogate the insured with respect to the individual responses he or she eventually provides. Should a denial of coverage occur, the broker's notes of his advice and the client's response will serve as evidence that he has competently discharged his duties.

[316] If Mr. Miller had asked Mr. Raymond about his experience placing property coverage and his ability to provide accurate answers to the questions on the application, Mr. Raymond would have realized that he could not rely on Mr. Miller to compile the information for him. Based on the evidence of the reliance Mr. Raymond placed on Marsh, I am satisfied that he would have arranged for property inspections if this course of action had been recommended to him. If inspections had been conducted, proper coverage would have been in place for the North End Pub at the time of the fire.

[317] Whether the standard of care will require the insurance broker to make inquiries of the nature described above will depend on the complexity of the risk. The decisions in *Biggar*, *O'Connor*, *Wolfe*, *Goodbrand*, and *Edwards* involved basic life, home and auto insurance applications. The information required to obtain these types of coverage would be within the personal knowledge of the applicant, regardless of his or her experience with the placement of insurance. In such a situation, there would be no obligation on the broker to make inquiries as to the applicant's ability to accurately respond to the questions being asked.

[318] Where the risk is significantly more complex, the broker must make additional inquiries, *before* the application form is completed or the information otherwise compiled, to ensure that the applicant either has the necessary skill to provide accurate information, or is aware of the options available, including property inspections, to obtain it. Once this obligation has been fulfilled and the information reduced to writing, the cases cited by Marsh will apply, and the applicant will be responsible for reading it over and correcting any inaccuracies.

[319] In my view, Marsh's opportunity to avoid the losses that occurred in this case was likely limited to the initial three years of coverage. Once Steve McMullin

took over responsibility for the insurance and Ed Raymond left Grafton Connor, questions by Marsh about Mr. McMullin's ability to provide accurate information about the properties may not have changed the outcome. Mr. McMullin would have no reason to doubt the accuracy of the pre-existing information. He would have assumed that Marsh had done its due diligence in dealing with his predecessor. That said, if Marsh had reviewed the file and advised Mr. McMullin that the previous information should be verified by an inspection, I am confident that he, like Mr. Raymond, would have followed this advice.

[320] I will now consider Grafton Connor's allegations of negligence with respect to the TRS report. Grafton Connor says Marsh was negligent for not obtaining and forwarding the TRS inspection report for the North End Pub to Underwriters in 2003. In the alternative, it says Marsh was negligent for not reviewing all of the closed ECI files prior to renewal in 2006 to ascertain whether they contained any information relevant to current Marsh clients.

[321] Beginning with the alternative argument, I do not accept it. Grafton Connor provided no authorities to support its position, and I am not satisfied that Marsh had any reason to suspect that the ECI files contained information that would be helpful to current clients. I am not prepared to impose such an onerous obligation on Marsh without any evidence or authorities to support it.

[322] As I indicated in my findings of fact, however, I am satisfied that Eric Bourque was aware of the TRS inspections of the Grafton Connor Building and the North End Pub in 2003. A reasonably prudent insurance broker would have taken the necessary steps to obtain the Pub report from ECI and forward it to Underwriters. In making this finding, I recognize that an insurer will rarely agree to provide a broker with a copy of an inspection report. In the unique circumstances of this case, however, Zurich was not in a position to renew coverage, and ECI was willing to provide Marsh with copies of its reports. After receiving the TRS report for the Grafton Connor Building, a reasonably prudent broker in Mr. Bourque's position would have followed up with ECI to obtain the report for the North End Pub, and forward it to Marsh UK to give to Underwriters.

[323] That said, I am not satisfied that both misrepresentations would have been avoided if Underwriters had been in possession of the TRS report prior to renewal of the Policy in 2006. As discussed earlier, the TRS report contains an incomplete description of the construction of the North End Pub. Martin Pope testified that the description in the report was consistent with masonry construction. As a result, if

Underwriters had reviewed the TRS report, it would have realized that the Pub was not sprinklered, but the masonry misrepresentation would have persisted.

[324] Could Underwriters still have voided the Policy? I concluded earlier in this decision that construction type is an objectively material fact. I found, however, that if the North End Pub had been sprinklered, the masonry misrepresentation, on its own, would not have been subjectively material to Underwriters. I arrived at this conclusion based on the evidence that the Esquire, a property described as being of frame construction and 100 percent sprinklered, was added to the policy in 2004 without an increase in premium. There is no evidence before the court, however, as to whether Underwriters would have charged a higher premium if the Grafton Connor account included an unsprinklered property of wood frame construction rather than an unsprinklered property of masonry construction. As a result, I have no basis on which to find that Mr. Bourque's negligence caused Grafton Connor's loss.

[325] In sum, I find that Marsh breached the standard of care of a reasonable broker by failing to make inquiries of Mr. Raymond to ascertain whether he had the necessary training or experience to accurately complete the insurance applications, and, if not, to discuss the benefits of property inspections with him. While I find that Marsh also breached the standard of care by failing to obtain the TRS report for the North End Pub from ECI and provide it to Underwriters, I am not satisfied that this breach caused the loss. Subject to a finding of contributory negligence, Marsh is therefore liable to Grafton Connor for the value of the claim under the Policy.

[326] I wish to add that the evidence disclosed many examples of careless and imprudent conduct by the Marsh representatives handling the Grafton Connor account. These include: (1) failing to ensure that corrections made by Grafton Connor to the applications were entered into the Marsh system; (2) failing to ensure that business interruption worksheets were completed; (3) failing to keep accurate notes; (4) failing to respond to Mr. McMullin's inquiry about the FourM wording; and (5) failing to review with Grafton Connor the e-mail from James Brown of Marsh UK.

[327] Nevertheless, a breach of the standard of care will result in liability only where the breach caused the plaintiff's loss. I am not satisfied that any of these failures by Marsh caused Underwriters to void the Policy for misrepresentation. To

be clear, such behaviour could put Marsh at risk of liability where the causal link to the client's loss is established. That is simply not the case here.

Contributory Negligence

[328] Having found liability on the part of Marsh, I must decide whether Grafton Connor was contributorily negligent. In my view, Grafton Connor, like Marsh, was far too lackadaisical in its approach to insuring commercial properties worth millions of dollars.

[329] Grafton Connor's failure to act prudently in the management of its own affairs began in 1996, when Gary Hurst departed for Florida and left Mr. Raymond in charge of placing insurance on the properties. Mr. Hurst appears to have been the only person at Grafton Connor who was aware that the North End Pub was mixed construction and had no sprinklers. Before leaving, Mr. Hurst did not ask Mr. Raymond about his experience with placing insurance, or inquire as to his knowledge of the individual properties. He did not sit down and review previous policies with Mr. Raymond, visit the locations with him, or otherwise provide him with information about the relevant features of the properties. It appears Mr. Hurst provided Mr. Raymond with no instructions at all. If he had reviewed the salient features of the properties with Mr. Raymond, the misrepresentations concerning the North End Pub could have been avoided.

[330] Mr. Raymond was also negligent. He testified that when he reviewed the 1999 Molson Business Edge Master Application Form for the North End Pub, he assumed that Mr. Miller had taken steps to obtain and verify the information provided therein. He did not, however, ask Ms. Henderson or Mr. Miller whether that was indeed the case. This was not reasonable behaviour.

[331] Mr. Raymond noticed that the property was listed as being 100% sprinklered, and he "didn't see anything wrong with it." At the same time, he testified that he did not actually know whether the building was sprinklered. He saw that the building was described as being of masonry construction. He thought the building also had a wood component, but he told himself that every building probably had a wood component. At no point did Mr. Raymond pick up the phone and call Gary Hurst, or anyone else who might know, and ask whether the property had sprinklers, or whether masonry was an appropriate description of its construction.

[332] By the time Mr. McMullin took over responsibility for placing the insurance, the misrepresentations had subsisted for three years. While Mr. McMullin was careless in his handling of other aspects of the insurance, I am not satisfied that his failure to verify the accuracy of the construction and sprinkler representations amounted to negligence.

[333] In my view, Grafton Connor is as blameworthy as Marsh for the former's loss of the value of its claim under the Policy. I therefore apportion liability equally between the two parties.

The Value of the Claim

[334] In its submissions, Underwriters argues that any indemnity under the Policy is limited in two ways. First, the Policy is a scheduled policy, not a blanket policy, and coverage is limited to the values for the North End Pub provided in the Location Details Summary. Second, Grafton Connor grossly undervalued the property, triggering the co-insurance provision. Although I have found no liability on the part of Underwriters, these issues must be resolved in order to determine the value of Grafton Connor's loss under the Policy.

Blanket vs. Scheduled Policy

[335] Grafton Connor says the Policy was clearly a blanket, not a scheduled, policy. A blanket policy, also called an open policy, is one that insures a number of different locations and provides a global maximum limit of insurance available for any particular loss. A scheduled, or valued, policy is one in which the maximum available for any one loss is the amount stated with reference to that specific location.

[336] Underwriters says the Policy was clearly a scheduled policy, and points out that in the Market Submission provided to Underwriters in 2006, Grafton Connor, through Marsh, stated:

> Limit of Liability: $17,616,000 any one Occurrence and in the annual aggregate in respect of Earthquake and Flood/Sewer back-up separately
>
> *(Please refer to attached schedule for individual values)

[337] According to Underwriters, the reference to the schedule confirms the parties' intention that the individual declared values of each location would be the maximum amount recoverable in case of a loss at that location.

[338] Whether a policy is a blanket or scheduled policy depends on the words of the policy. In *General Principles of Canadian Insurance Law*, 2nd ed. (Markham: LexisNexis Butterworths, 2014) Barbara Billingsley writes at p 266:

> Whether a policy is properly characterized as valued or open is determined by applying the standard interpretation principles to the wording of the insurance contract. Although a valued policy must, by definition, assign a dollar value to the property insured, the assignment of value alone does not mean that a given policy is a valued policy. The inclusion of an assigned value for insured property is a necessary, but not sufficient, criterion of a valued policy. The central question is whether the parties intended the contract to be a valued policy or an open policy. This question must be answered with a specific reference to the policy wording as a whole.

[339] Grafton Connor relies on *A Melchior & Son Ltd v Insurance Corp of Ireland Ltd*, [1987] OJ No 321 (Ont HCJ), *Re Freesman and Royal Insurance Co of Canada*, [1986] OJ No 674 (Ont HCJ) aff'd [1988] OJ No 3020 (Ont CA), and *Sunburst Skylight Ltd v Lloyds Underwriters*, 2010 BCSC 714, [2010] BCJ No 963.

[340] In *Melchior*, the Bay Moorings marina was extensively damaged by fire in 1982. It was insured under a policy of fire insurance that covered 12 separate premises. The insurance policy included a "Schedule of Premises", which listed the location of the properties covered by the policy. Opposite each location was an amount for the building and its contents. The total amount for all of the properties was almost $27 million. The amount listed for the marina and its contents totalled $600,000. The fire caused damage to the building and contents in an amount of $1,300,000. The insurer acknowledged liability under the policy to the extent of $600,000, and the issue before the court was whether the policy was a blanket or scheduled policy.

[341] The policy contained a "Summary of Coverages", which stated there was $26,642,000 coverage "[o]n Property of Every Description as per schedule", for a premium of $16,710. On the next page, under "Section I", appeared the following language:

> PROPERTY INSURED: $26,642,000.00 on "PROPERTY OF EVERY DESCRIPTION"
>
> (except as hereinafter excluded), consisting but without limiting the generality of the foregoing, principally of buildings and all structures pertaining thereto, including tunnels, equipment and stock pertaining to the business of the Insured,

> the property of the Insured or for which the Insured may be held responsible or for which the Insured may have assumed responsibility, while at the premises of the Insured included in the schedule attached to and forming part of this policy.

[342] The Schedule of Premises followed. The values appeared underneath the heading "Amounts of Insurance or Limits of Liability." The bottom of the schedule indicated:

> … Nothing herein contained shall be held to vary, alter, waive or extend any of the Agreements, Conditions, DECLARATIONS, Exclusions, Limitations, Provisions or other items of the Part and of the Policy to which this Schedule is attached other than as above stated. [*Emphasis in original*]

[343] There was evidence before the court that when the policy was first written in 1975, it had been written on a blanket basis. Three subsequent renewals were also written on a blanket basis. In 1979, the insurer asked for a schedule of values to be used to calculate a premium quote. The Schedule of Premises then appeared in the 1979-1980 policy. Upon reviewing the policy, the broker became concerned that the document was intended to change the policy from blanket to scheduled coverage and called the insurer. The insurer indicated that the form was used for both blanket and scheduled policies, and if it had been intended to change the coverage, there would likely have been some communication between the insurer to the broker to that effect. There was no evidence of such communication. Subsequent renewals continued to include the schedule.

[344] Concluding that the policy was a blanket policy, Gray J wrote:

> 33 The conclusion I have reached is that the material policy of insurance, to which reference has just been made, is a blanket policy. No explanation has been tendered to me to explain the words "Amounts of Insurance or Limits of Liability". Nor has any submission been made really as to any difference in meaning between them, joined as they are in the disjunctive by the word "or". This policy is an ICI form and in or about 1979 policies of insurance were issued by ICI which had by way of format the "Schedule of Premises" document identical to that issued in 1979 by ICI wherein amounts were set opposite each location, which policies were admitted to be blanket policies
>
> …
>
> 35 I agree with the submission that it is necessary to look at the whole policy to determine its meaning. The words appearing on p. 1 under the heading "Summary of Coverage", to which reference has been previously made, and the portion of the policy on p. 2 under the heading "Section I", appear on every policy and are consistent with a blanket policy and inconsistent with a scheduled policy.

[345] He went on to state that even if he was wrong in his conclusion and there was true ambiguity, "it should be construed against the insurer" (para 40).

[346] Grafton Connor relies on *Re Freesman* for the proposition that a policy must contain express language of intent before it will be deemed to be a valued policy. In the following lengthy, but instructive, passage, the court reviewed several American authorities on valued policies:

> **3** Is it a "valued" policy? I believe it can be fairly stated that a valued policy is one which specifies the agreed value of the subject-matter insured, with the intention that, in the event of loss, the agreed valuation is conclusive upon both parties without further inquiry …
>
> **4** The policy to be interpreted herein is described as a select homeshield policy covering a residence, contents and miscellaneous items. The coverage for the residence, additional buildings and some other items refers to "Limits Of Your Coverage". Additional coverages include "Jewellery, Special Individual Coverage". Under that last-mentioned heading various items of jewellery are listed (including the diamond ring in question) as being "Insured For". In the case of the diamond ring, it was "Insured for $13,886.00".
>
> **5** Subject to certain exceptions not applicable herein, the normal rules of construction apply to a contract of insurance; that is, it must be construed according to the intention of the parties to be ascertained from the words they have used: *Re Art Gallery of Toronto, supra*, and *MacGillivray & Parkington on Insurance Law*, 7th ed. (1981), para. 1066.
>
> **6** As I understood the submission of counsel, the meaning or purpose of a "valued" policy (as outlined above) was not controversial; but the Canadian and English authorities relied on by counsel were not of much assistance in the construction of this particular contract of insurance. However, in insurance cases, American authorities are frequently reviewed and accepted by Canadian courts …
>
> **7** In *Houston Fire & Casualty Ins. Co. v. Nichols* (1968), 435 S.W. 2d 140 at p. 142, the Supreme Court of Texas (on an appeal from a Court of Civil Appeals) adopted the following statement from Appleman, *Insurance Law and Practice*, vol. 6 (1942):
>
> > In determining whether a policy is open or valued, the contract must be viewed in its entirety to give effect to the mutual intentions of the parties at the time of its execution and the policy must contain express language showing such an intent, before it will be deemed to be a valued policy. So, a policy without the words "valued at" or other equivalent language is not valued.
>
> **8** In *Naiman v. Niagara Fire Ins. Co.* (1955), 140 N.Y.S. 2d 494 (Supreme Court, Appellate Division), the following statement is found at p. 497:

> [6] Ordinarily the amount of insurance set forth in the policy is the measure of coverage rather than of damages. "[T]he mere statement of the amount of insurance does not create a valued policy". *St. Paul Fire & Marine Ins. Co. v. Pure Oil Co.*, 2 Cir., 63 F.2d 771, 772. In the leading case of *Lee v. Hamilton Fire Ins. Co.*, 251 N.Y. 230, 167 N.E. 426, the Court of Appeals set great store by the necessity for inclusion of precise words of valuation in the policy: "A valued policy is one in which the words 'valued at' appear and the amount at which the property insured is 'valued at' definitely fixes the liability of the insurer and is conclusive on the parties." 251 N.Y. at page 234, 167 N.E. at page 426.

...

10 Also in *Naiman* it was held that providing appraisals for insured items is not sufficient evidence that the insurance policy was meant to be a "valued" policy. The court dealt with the issue at p. 498 as follows:

> Plaintiff contends that an agreement to fix value before loss may be spelled out of the fact that defendant required her to submit an appraisal of each article before insuring it and that the amounts of insurance allocated to the items on the schedule correspond in each instance to the appraised values. In accepting risks of this nature an insurance company may require an appraisal for too many good and prudent reasons to permit that circumstance to override the clear and well- grooved meaning of the language employed in the policy.
>
> It must be borne in mind that each of the twenty-three items is insured separately, for a stated, specific amount -- just as though twenty-three small policies of insurance had been issued in various amounts. Appraisals by a reputable expert gave some assurance to defendant that the articles insured were in existence, helped identify them by expert description and afforded some confirmation that the values of the articles bore a reasonable ratio to the amounts for which they were insured. Since blanket risk policies of this nature are peculiarly vulnerable to fraudulent claims, the information procured from reliable appraisals becomes a potent protective measure. Such information also tends to establish the reasonableness of the premium collected by defendant, because premiums are charged on a basis of loss exposure.

11 As indicated in the agreed statement of facts, the endorsement for special items provides that each item (which includes the diamond ring) is "insured ... for its replacement value, but not for more than the amount shown on the Coverage Summary".

12 In my opinion, the parties have agreed that the ring is insured for its replacement value; not that it is valued at $13,886 in the event of loss. Also that the recommendation as to appraisals under the word "Caution" is not evidence that the policy was meant to be a "valued" policy: *Naiman*, *supra*. Such an

> interpretation is consistent with the fundamental rule of insurance law that a policy of insurance is a contract of indemnity and that an insured should not be entitled to recover more than the actual value of a loss as measured at the time of the occurrence: *Castellain v. Preston et al.* (1883), 11 Q.B. 380 (C.A.). Of course the parties to a contract of insurance may agree otherwise (as in the case of a "valued" policy); but such an intention should be clearly expressed.

[347] Finally, in *Sunburst*, the court considered whether a Statement of Values signed by the plaintiff insured, but not expressly made a part of the policy, limited the insured's recovery. The plaintiff was in the business of manufacturing skylights and had three business locations, including 1210 Industrial Way in Parksville, British Columbia. In July of 2006, Mr. Paffen and Mr. Polz, principals of the plaintiff, had discussions with Mr. Brendon of HUB International Barton Insurance Brokers regarding insurance coverage. On July 28, 2006, Mr. Brendon sent Mr. Paffen and Mr. Polz a fax which identified the three locations at which the plaintiff conducted business, and ascribed values to the property at each location. It also identified a global premium amount of $3,419. The premium was not broken down by specific location.

[348] On August 9, 2006, Mr. Brendon sent Mr. Paffen and Mr. Polz a fax with a number of enclosures, including a cover note listing the three locations and confirming the values of the properties. The cover note confirmed the global premium amount and stated that the document was "intended for use as confirmation that insurance described above has been effected" and "shall automatically be terminated and voided when replaced by policies issued by the insurers."

[349] On August 24, 2006, Mr. Brendon sent the principals a further letter enclosing the policy and a Statement of Values. The letter stated:

> The attached Statement of Values requires your signature and to be returned to our office as soon [*sic*] possible.

[350] The Statement of Values identified the policy, and the fact that the plaintiff did business at three locations. It attributed values which mirrored those identified in the July 28, 2006 fax for each of the three locations. The total amount of the values was $1,439,500. The total value for the property at Industrial Way was $1,080,000.

[351] Mr. Polz signed the Statement of Values on August 30, 2006 and returned it to Mr. Brendon. On November 20, 2006, a fire broke out at the Industrial Way location.

[352] The parties agreed on a number of facts, including:

- The co-insurance percentage under the policy was ninety percent;
- The value of the property at risk at the 1210 Industrial Way location was $1,596,776.41;
- The value at risk at all three locations insured was $1,955,776.41;
- The inflation adjustment provision in the policy increased the limits by $78,482.00;
- The plaintiff suffered a loss of property having a value of $1,226,552.48;
- Lloyd's had paid Sunburst a total of $992,507.51.

[353] Under "Limit(s) of Liability" in Part I, the policy provided a single value - $1,439,500", across from which was stated "Property of Every Description Building and Business Personal Property – Subject to a Deductible of $1,000." Under "Property Insured", the policy stated:

> Property of Every Description
>
> If Property of Every Description is indicated on the Schedule of Part I, the limits of liability for Building and Business Personal Property as insured per each individual location are combined to provide one single limit of liability per location, hereinafter referred to as Property of Every Description (POED).

[354] Finally, the co-insurance clause provided that it "applies separately to each location or division of the property insured …" and "[y]ou will maintain insurance concurrent with this form on the property insured to the extent of at least the amount produced by multiplying the replacement cost value of the property by the co-insurance percentage set out on the Schedule of Part I." Voith J noted that there was no "Schedule of Part I" to the policy, and concluded that this likely referred to the portion of the policy entitled "Part I – Property Insured", which was discussed above.

[355] The value of the Industrial Way property, as noted above, was determined to be $1,596,276.41. If that figure was used, the co-insurance clause required it to be insured to at least $1,436,648.77. The parties also agreed that the value of all three locations was $1,955,776.41. If that figure was used, the clause required that $1,760,198.77 of insurance be maintained. Voith J described the parties' positions and the main issue as follows:

> 34 If the plaintiff "maintained" the requisite level of insurance, the Co-Insurance Clause is not engaged any further. The question is how much insurance did Sunburst "maintain". As noted earlier, the inflation adjustment provisions in the Policy increased the limits by $78,482. Sunburst asserts that it maintained insurance in the amount of $1,439,500, the figure found under "Limit(s) of Liability" in "Part 1 - Property Insured", adjusted upwards by $78,482 to yield $1,517,982.
>
> 35 Lloyd's disagrees. Lloyd's says Sunburst maintained insurance at 1210 Industrial Way in the amount of $1,080,000 adjusted upwards by $78,482 to $1,158,482. The $1,080,000 figure relied on by Lloyd's is not found in the Policy. Indeed, that specific figure is not found in the Statement of Values signed by Mr. Polz on August 30, 2006. Instead, as I have said, that figure is generated if one adds up the various line items and dollar amounts on the Statement of Values which are referable to "Location 1" - the 1210 Industrial Way property.
>
> 36 Thus, the central issue before me is the significance of the Statement of Values to the proper interpretation of the Policy. Though both parties advance various arguments in support of their respective positions, those positions can be simplified. Sunburst argues that an analysis of the Policy and the application of relevant interpretive tools leaves no place for the Statement of Values. Lloyd's says the Co-Insurance Clause, in stipulating that it "applies separately to each location ... of the property insured", necessarily applies to the 1210 Industrial Way location separately and to the insurance maintained for that location as expressed in the Statement of Values. Applying Sunburst's interpretation would have the court combine the available limits of insurance across the three locations and apply that aggregate result to the 1210 Industrial Way location.
>
> …
>
> 39 Lloyd's assertion that the Policy is unambiguous is not tenable. Its interpretation relies on the incorporation of a document, the Statement of Values, into the Policy. The Statement of Values is not referenced in the Policy and indeed was not yet signed when the Policy was issued. Instead, if one has regard to the "Limit(s) of Liability" portion of the Policy, accepted to be the "Schedule of Part 1" referenced in Item 2(c), Property of Every Description, there is simply no reference to individual locations or properties. Lloyd's cannot succeed unless the Statement of Values is made part of the contract between the parties or is used to inform its interpretation.

[356] In Voith J's view, there were multiple discrete factors that militated against the Statement of Values being a part of the policy, including:

- The Statement of Values was delivered to Sunburst after the policy had become valid and operative (para. 41);
- Neither the policy declarations nor the policy wordings referred to the Statement of Values (para. 43);
- Expert evidence confirmed that Statements of Values are used in different ways in different circumstances, and there was "no evidence of any trade practice regarding the use of a Statement of Value that is sufficiently certain and notorious and so generally acquiesced in that it might be presumed to form a part of the contract made between the parties" (para. 44);
- Nothing in the Statement of Values suggested that it was part of the contract between the parties:

> The language of the Statement of Values is prospective in nature. It is a document which, in the normal case is intended to preceed [*sic*] the issuance of a policy. The Policy itself consists of the two parts I have described earlier and has a physical appearance or formatting which bears no relationship to the Statement of Values. The Statement of Values appears to simply be a document in which the insured certifies, to the best of its knowledge and belief, the values of property insured. … (para. 45)

- To the extent any ambiguity was created in the policy because no specific properties were identified in "Part I – Property of Every Description," or because the Property of Every Description and the Co-Insurance Clause refer to "individual location(s)", such ambiguity was to be interpreted against Lloyd's (para. 75).

[357] For these reasons, Voith J concluded that "the agreement of the parties is found within the Policy and is not supplemented or further informed by the Statement of Values" (para. 77).

[358] Underwriters, for its part, cites one Canadian and two American decisions. In its written submissions, Underwriters stated at p 30:

> Although the Policy does not contain an explicit "margins clause", i.e. a clause which specifically limits liability to the individual values in the Statement of Values or Summaries, nevertheless recent Canadian jurisprudence is persuasive that a Policy such as this one should limit liability to the stated values – in this case, the values for the Pub stated by the Plaintiffs in 2006.
>
> The leading case on this issue is *Bell Pole Co. v. Commonwealth Insurance Co.*, [2003] B.C.J. No. 8 (BCCA) …..

[359] In *Bell Pole*, the insured, Bell Pole, had various locations at which it treated poles with preservatives. These locations had been insured under a subscription policy, renewal annually, with annual Statements of Value. The only limit set out in the wording of the policy was a $7 million per occurrence limit. It was common ground that the Statement of Values formed part of the policy, and listed numerous assets and corresponding values, including a full length pole-treating tank, valued at $450,000. The treatment tank was destroyed by fire. Replacement of the tank on the site was not feasible, however, because the ground beneath the tank had become degraded from the preservative solutions, and the authorities would have required expensive remediation of the site before reconstruction. In addition, the structure of the tank was not up to modern standards and authorities would have required an up-to-date system that would not allow chemical spillage. As a result, Bell Pole constructed a treatment tank of modern design at a different site at a cost of $4 million. The cost of the new tank, its replacement cost, was slightly over $1.3 million.

[360] While a direct replacement of the former tank would have cost $450,000, Bell still claimed the balance of the cost of the new facility, arguing that the environmental regulator would not have permitted a direct replacement, and, as a result, the cost was covered under the policy's bylaw provision.

[361] Bell Pole's broker had negotiated with the insurer that there would be no sub-limit with respect to bylaw coverage on the condition that the insured would estimate the approximate exposure under the bylaw coverage provision in the event of a loss, and declare such value in the Statement of Values. While Bell Pole represented that the exposure under the bylaws coverage was $250,000, it argued that the disclosure on the Statement of Values was irrelevant and it was entitled to full cover up to the $7 million limit.

[362] The trial judge limited Bell Pole's recovery to $450,000 for direct replacement of the destroyed tank, plus $250,000 on account of increased cost to comply with current environmental regulations. The decision was upheld by the

Court of Appeal, but for different reasons. The trial judge held that the Statement of Values created sub-limits, at least with respect to the bylaw cover. The Court of Appeal disagreed, noting that the insured "could not create a 'sub-limit', sub-limits being contractual terms, in the absence of some provision in the contract permitting it to do so. A contracting party may not create a term in pectore" (para 25).

[363] The Court of Appeal focused its analysis on the question of good faith. It was satisfied that the insured deliberately declared a grossly inadequate value for bylaws in order to keep its premium down. Southin JA, for the Court, concluded:

> 29 To put it another way, the appellant is saying to the insurers, "It is true that we only paid a premium for $250,000 of insurance although we knew the risk far exceeded that, but you must pay the $1.3 million because you did not put into the policy any express provision requiring us to tell the truth in the Statement of Values."
>
> 30 The word which best describes this approach of the appellant is a word with no precise equivalent in English - the Yiddish word "chutzpah".
>
> …
>
> 32 It has been said that it is a principle of universal application to all types of insurance contracts that such contracts are based on the utmost good faith of both parties. See Halsbury's Laws of England, 4th ed., Vol. 25, para. 349.
>
> 33 It is unnecessary in the case at bar to examine the exact limits of that proposition or what the remedy for a breach of that duty may be in any given case.
>
> 34 So far as this case is concerned, it is my opinion that the act of the appellant in deliberately understating the "by-law" risk was a breach of its duty of good faith to the insurers. But it does not follow that the breach should disentitle the appellant to recover anything under the by-law coverage. The insurers took the appellant's money, they are better off than if the appellant had paid a premium for by-law coverage of $1,000,000.00 and it ill-becomes them to resist paying the $250,000.00.

[364] Underwriters also relies on brief statements in *Fair Grounds Corp v Travelers Indemnity Company of Illinois*, No 99-301 (La App 5 Cir 09/28/99), 742 So2d 1069, 1999 La App Lexis 2650, and *Vernon Fire and Casualty Co v Sharp*, (1976), 254 Ind 603, 349 NE 2d 173. In its submissions, Underwriters cited the following passage from *Fair Grounds*:

> There is no question here that the insurance contract at issue is a "scheduled" rather than a "blanket" policy. Underwriters' liability for any covered losses is

> limited to the value of the lost property appearing in the itemized list of values sent to it by the insured. [*Emphasis by Underwriters*]

[365] In *Vernon Fire*, the insured had two fire insurance policies which contained a schedule of values for individual items of real and personal property belonging to the business. A fire damaged the business and caused itemized losses in the amount of $94,108.09. Losses on some of the individual items exceeded the particular value assigned to them in the schedules. The court noted:

> The plaintiff's losses exceeded the amount of the insurance provided under the two contracts, and under 'blanket' policies he would have been entitled to reimbursement for the stated policy limits of $31,250.00 upon each contract. However, these were not 'blanket' policies but were 'scheduled' policies, i.e. the property insured was separately scheduled and valued in the contracts. The liability of the insurers under such policies is limited as to each scheduled item, and a portion applying to one item but unused may not be transferred to another item which was under-valued and thus underinsured.

[366] The authorities cited by Underwriters are not persuasive. I agree with the observation of Voith J in *Sunburst* that, when considering whether a statement of values forms part of an insurance policy, the decision in *Bell Pole* is of no relevance (para 74). While the Court of Appeal in *Bell Pole* restricted the insurer's indemnity obligation to the values set out in a statement of values that was not incorporated into the policy, it did so on the basis that the insured breached its duty of good faith to the insurer by deliberately understating the risk.

[367] As for the American authorities, they are equally unhelpful. In *Fair Grounds*, the insurance policies in question explicitly limited liability to the values set out in the statement of values on file with the insurer. Indeed, the court noted that it was "undisputed here that the above references to 'statements of values on file with us' mean that these were scheduled, rather than blanket, policies" (p 4). In *Vernon Fire*, the schedule was clearly part of the policy, set out beneath the following language: "This policy being for $31,250 covers its pro-rata proportion of and on the following amounts: …"

[368] In deciding whether the Policy provides scheduled or blanket coverage, I am satisfied that I must consider the policy wording as a whole in order to determine whether the parties intended the contract to be a scheduled or a blanket policy. The first page of the Policy, under the heading "THE SCHEDULE", lists, *inter alia*, the policy number, named insured, address of insured, premium, inception

date, expiry date, and limits of liability. The limit of liability is described as follows:

LIMITS OF LIABILITY:	CAD 17,616,000 any one Occurrence and in the annual aggregate in respect of Earthquake and Flood/Sewer back-up separately.

[369] There is no breakdown of the individual locations covered by the Policy, or their respective values. The Policy makes no reference to the Location Details Summary or any other schedule of values. There is nothing about the format or the content of the Location Details Summary to suggest that it was intended to form part of the Policy. For these reasons, I conclude that the Policy is a blanket policy.

[370] Even if I am wrong on this point, I would impose liability on Marsh for the balance of the replacement value of the property in any event, on one of two alternative bases. First, I would find that Marsh negligently failed to explain the concepts of blanket and scheduled coverage to Grafton Connor and failed to ensure that it obtained a blanket policy from Underwriters.

[371] Gary Hurst testified that when he was responsible for placing the insurance, he purchased blanket coverage. When he transitioned responsibility to Mr. Raymond, however, Mr. Hurst did not tell him that he wanted a blanket policy. Although Mr. Raymond agreed that Mr. Hurst had not told him to obtain blanket coverage, the documentary evidence confirmed Mr. Raymond's recollection that he had purchased blanket coverage from Bell & Grant. According to Mr. Raymond, no one at Marsh ever discussed blanket and scheduled coverage with him, but he assumed he was purchasing the same kind of coverage as in the past.

[372] When Mr. Raymond delegated responsibility for insurance to Mr. McMullin, he did not discuss the concept of blanket coverage with him. Mr. McMullin testified, however, that he also believed he was purchasing blanket coverage. The foundation for his belief was not clear from his evidence.

[373] Indeed, Marsh shared Grafton Connor's position that the Policy provided blanket coverage. Mr. Miller and Ms. Stone testified that they understood the Policy to be a blanket policy. After the fire, Len Costello, the adjuster, wrote to Gary Muise at Grafton Connor on March 19, 2007 as follows:

> We have been advised by the broker that the limit of liability for the building would be the blanket policy amount. This is a Broadform property policy. Please refer to the actual policy wording for review of specific details of the contract.
>
> (p 5)

[374] Mr. Maloney confirmed in his testimony that he was the broker who told Mr. Costello that the Policy provided blanket coverage.

[375] I am satisfied that Grafton Connor intended to purchase blanket coverage. If, contrary to my conclusions on this point, the Policy is actually a scheduled policy, I find that Marsh's failure to explain the two types of coverage to Grafton Connor and to ensure that it obtained blanket coverage was negligent. While Grafton Connor could have raised the issue, I am not satisfied that its failure to do so in the circumstances amounted to contributory negligence.

[376] In the alternative, I would find that Marsh negligently failed to advise Grafton Connor that replacement cost values were required for each of the properties. Even if the Policy was a scheduled policy, Grafton Connor would have been indemnified for the full replacement cost of the North End Pub if Marsh had communicated this information. Moreover, Marsh failed to respond to clear signs that Grafton Connor was not providing replacement cost values. This was negligent.

[377] The evidence regarding replacement cost values is as follows. On the second page of the 1999 Molson Business Edge Master Application Form was a space for "Building Value." At the top of the page were the following words, in bold:

> **Replacement Values on Property (indicate full replacement cost values)**
>
> **SUBJECT TO CO-INSURANCE CLAUSE**

[378] After coverage was bound in 1999, Mr. Miller sent a form letter to Grafton Connor similar to those sent to all Marsh clients to remind them of important things to consider with respect to their coverage. This letter, dated July 9, 1999, indicated that "Business Property" generally includes buildings, computers, stock, equipment, tenants improvements, office contents and all other property not specifically excluded, and that "[c]overage limits should be based on replacement value."

[379] The 2000 Molson Business Edge Renewal Form, like the master application form, required the applicant to provide the "Building Value" for each location, and included the same notation that the applicant was to "indicate full replacement cost values." The 2001 Benson & Hedges Business Edge Master Application Form was essentially identical to the 1999 Molson Business Edge Master Application Form. The note regarding replacement cost values appeared at the top of the second page.

[380] Mr. Miller testified that replacement value on a property policy "is a bit unique to the insurance world" and is something that, as a practice, he would always talk about with his clients. He said that Marsh brokers would explain the need for accurate replacement values, but would rely on clients to provide those values.

[381] During his testimony, Mr. Miller was shown an article prepared by Marsh in 2004. The article, entitled "At Risk: Rise in Building Materials Costs Means Properties May Be Under-Insured" stated, in part:

> A rise in the cost of building materials such as cement and steel, as well as other commodities used in the construction process, such as petroleum, may mean that many commercial and residential properties are under-insured. This can have significant implications if an insured's policy is subject to coinsurance or margin clause provisions. With a more than 10 percent increase in the cost of building materials over the past 12 months, owners who simply renewed last year's policies without reviewing their coverage for replacement costs could find themselves under-insured in the case of a loss. While spikes can come into play in the short-term, the long-term impact of rising construction and material costs must also be considered.
>
> …
>
> … To properly calculate replacement values of buildings, it is essential to seek the services of construction industry professionals, who can review a site and provide detailed replacement values using construction-industry estimating techniques. If you have multiple facilities, it may be most cost-effective to review a representative sample of properties.
>
> …
>
> Professionals in Marsh's Forensic Accounting and Claims Practice help ensure you have sufficient coverage. With experience in engineering, forensic accounting, and insurance claims, Marsh professionals provide accurate and up-to-date property valuation and business interruption calculations.

> For property damage values, Marsh's Construction Consulting professionals calculate replacement costs using methods certified by the Association for the Advancement of Cost Engineering (AACE),the industry's leader in cost estimating, cost control, business planning, project management, planning, and scheduling. And Marsh's forensic accountants and claims specialists bring a deep knowledge of insurance losses and how to account for them.

[382] Mr. Miller conceded that Marsh representatives, as brokers, would "definitely" have been aware that building costs can rise over time. He admitted that he did not offer Grafton Connor any of the services discussed in the article while he was account manager.

[383] When Mr. Miller transitioned into his new role as risk placement specialist, Eric Bourque took over the Grafton Connor account. He testified that he would have discussed the need for replacement cost values with Grafton Connor, but he did not recall a specific conversation. On May 29, 2002, Mr. Bourque sent Grafton Connor the same form letter that Mr. Miller sent in 1999, which indicated that coverage limits should be based on replacement value.

[384] Michael Maloney, the account manager for Grafton Connor at the time of the fire, initially testified that he would have explained the need for replacement cost values for the building and contents. He admitted on cross-examination, however, that he never actually told Mr. McMullin or Mr. Muise that the reference to "Building Value" on the Location Details Summary meant replacement cost. He said he was asking to be provided with replacement cost numbers and he simply assumed that what he was getting from Grafton Connor were replacement cost numbers.

[385] Replacement costs were raised, however, in an e-mail from Lynn Stone to Mr. McMullin on July 14, 2006, after coverage was bound:

> Hi Steve
>
> As you know, I had forwarded Montrose Mortgage Corporation a copy of the renewal binder for your property & CGL insurance (as per your request). After reviewing the Property coverage, Montrose advised that they have a requirement whereby there must not be a "co-insurance clause" in your policy (there is currently a 80% co-insurance clause in existance [*sic*], which requires that your buildings, etc. be insured to at least 80% of their Replacement Cost in order for the Insurers to provide the full replacement value in the event of a loss (to rebuild, etc). I've gone back to the underwriter and advised him that Montrose wants the Co-Insurance Clause removed, and the underwriter said he would require recent appraisals on the buildings in order to do this. Please advise as to what you

> currently have with respect to appraisals (ie. For which buildings, and how current they are, etc.).

[386] Mr. McMullin responded several minutes later, noting that "[t]he most recent Real Estate appraisal was Mar/01" and they "have scheduled a re-appraisal of the building for appx Aug/Sept of 2006, as part of a business valuation exercise." Ms. Stone replied in part:

> Which building(s) are you referring to below? (ie. all buildings?)
>
> Will these appraisals be based on "Replacement Cost" or "Market Value"? For insurance purposes, we would be looking for replacement cost appraisals.

[387] Mr. McMullin responded that the main building downtown was the only one Montrose had an interest in, and he was unsure which approach the appraisal would take. Ms. Stone thanked him, said she would advise Montrose, and "hopefully they will be okay with waiting a couple of months."

[388] For his part, Ed Raymond testified that he didn't focus much on the individual "Building Value" listed for each location on the applications, or the Location Details Summary. He explained that there are several different types of building values – book value, assessment value, market value and replacement value, and he never specifically asked Marsh which value they wanted. For this reason, when he saw the building value for the North End Pub listed as $600,000, it did not occur to him that this figure could not possibly represent the replacement cost of the property. He did not consider building value and replacement cost as being one and the same.

[389] Instead of focusing on the individual values, Mr. Raymond focused on the figure for the total amount insured, which in 1999 was about $8 million. He did not realize that this figure was supposed to represent the aggregate of the replacement costs for building and contents for all of the insured locations. Mr. Raymond did not know how Marsh arrived at the $8 million figure, and he did not ask. He understood only that Grafton Connor was purchasing blanket replacement coverage and he was satisfied that the total amount would be sufficient to replace any of Grafton Connor's properties.

[390] Mr. Raymond was never corrected by anyone at Marsh. According to his evidence, no one at Marsh ever explained the concept of replacement value to him, and he never asked about it.

[391] As to where the $600,000 building value came from, Mr. Raymond testified that the replacement values on the application form originated with Marsh. On cross-examination, he was shown a letter that he wrote to John W. James and J. De Conde at Marsh on April 22, 1996. The letter stated, in part:

> Dear Sirs:
>
> Further to our meeting last week, I now enclose the following:
>
> 1. Statement of Replacement Cost Values based on an appraisal of J.W. Lindsay Enterprises.
>
> ….

[392] Mr. Raymond admitted that according to this letter, he was providing replacement cost values to the broker in 1996.

[393] Mr. Raymond was also shown a Renewal Proposal prepared by A.J. Bell & Grant on May 25, 1998, one year before Marsh obtained Grafton Connor's property insurance business. The Schedule of Values included in the proposal listed the building at 2774-2778 Gottingen Street, the address of the North End Pub, as having a value of $600,000.

[394] Steve McMullin took over the insurance in 2003, and it was then that he first saw the Location Details Summary. He was never told that "Building Value" meant the building's replacement value. He assumed it meant the amount that a person would be prepared to pay for the property on the open market. As to "Contents Value", he assumed it meant the market value of the contents at the time.

[395] The only time Mr. McMullin updated the building value for the North End Pub on the Location Details Summary was prior to renewal in 2006. He increased the value from $600,000 to $650,000. He explained that he had received an assessment notice for the Pub stating that its value had gone up $50,000 over the previous two years, so he adjusted the building value by that amount. He denied, however, that he understood "Building Value" to mean tax assessment value.

[396] Mr. McMullin also increased the building value of the Five Fish/Little Fish Rental from $1,200,000 to $1,300,000. He said Grafton Connor had made some capital improvements to the building over the course of the year that would have raised its value. He had adjusted the building value of the Joint Venture by $100,000, but could not now remember why. Finally, he increased the building

value of the Esquire restaurant from $500,000 to $600,000 because an addition had been made to the back of the restaurant. Mr. McMullin admitted that 2006 was the first time he had made any changes to any of the building values on the Location Details Summary.

[397] Based on the above evidence, each Marsh representative understood the importance of explaining replacement cost values to clients. Nevertheless, I find that none of them ever made it clear to Grafton Connor that "building value" meant "replacement cost." I am also satisfied that Grafton Connor did not review the insurance applications and correspondence with the appropriate degree of care.

[398] I find, however, that a reasonably prudent insurance broker in Marsh's position would have recognized that Grafton Connor was not providing replacement cost values long before the fire, and would have corrected the misapprehension. I say this for two reasons: (1) Grafton Connor did not increase the building value for the North End Pub at any time between 1999-2006, and (2) the declared value was far too low to accurately reflect the cost to replace a building of its size in the north end of Halifax.

[399] Every year, Marsh provided Grafton Connor with the values it had on file from the year before, and asked for updates. Every year except 2006-2007, the building value of the North End Pub remained $600,000, a far cry from its actual replacement cost of over $2 million. These factors should have put Marsh, the largest insurance broker in the world, on notice that Grafton Connor was unaware of its obligation to provide replacement cost values. Indeed, Marsh's own literature warned of the need to update replacement cost values regularly, and cautioned against carrying over the same values year after year.

[400] If Marsh had met the standard of care of a reasonably prudent broker in these circumstances, Grafton Connor would have been covered for the full replacement cost of the North End Pub whether the Policy provided blanket or scheduled coverage. For this reason, if I had not found the Policy to be a blanket policy, I would have attributed liability for the balance of the replacement cost value to Marsh.

Does the Co-insurance Provision Apply?

[401] It is common ground that the declared replacement value of the North End Pub on the Location Details Summary was $980,000: $650,000 for the building, $180,000 for the contents, and $150,000 for business interruption. According to

the proof of loss submitted by Grafton Connor, the actual replacement cost for the property was $2,740,869.16: $2,174,514.02 for the building, $411,357.61 for the contents, and $154,997.53 for business interruption. Underwriters says this gross undervaluation by Grafton Connor triggered the co-insurance provision.

[402] The co-insurance provision of the Policy is found in the second half of Endorsement 10:

> … in the event of any error or omission including a declaration of the Insured's total insurable values being less than (80%) eighty percent of the actual insurable values at the time of declaration, any loss payable in respect of the property involved or other insurable interests in the loss shall be reduced in the proportion that the said actual insurable value bears to the declared insurable value provided that this provision shall only apply when the actual building(s) or individual property(ies) or other insurable interests involved in the loss are the subject of an incorrect declaration of values.

[403] I will review the evidence concerning the co-insurance clause. As discussed earlier, the 1999 Molson Business Edge Master Application Form included the following notation at the top of the second page:

> **Replacement Values on Property (indicate full replacement cost values)**
>
> **SUBJECT TO CO-INSURANCE CLAUSE**

[404] The same notation appeared on the 2000 Molson Business Edge Renewal Application Form and the 2001 Benson & Hedges Business Edge Master Application Form. The application form for 2002 is not in evidence.

[405] Blake Miller testified that, as with replacement costs, it was his general practice to "always" explain the concept of co-insurance to his clients. According to Mr. Raymond, however, no one at Marsh ever talked to him about co-insurance, and he never asked. He said he did not know what co-insurance meant until after the fire. Since Mr. Miller admitted that he had no specific recollection of his interactions with Grafton Connor, I prefer the evidence of Mr. Raymond on this point.

[406] Like Mr. Raymond, Mr. McMullin testified that no one from Marsh ever explained co-insurance to him. That said, the term was mentioned in correspondence between Mr. McMullin and Marsh on two occasions. On May 7, 2003, Mr. Bourque sent an e-mail to Mr. McMullin requesting that he review and update the values and limits in the Location Details Summary, review and update

the receipts for each location, and provide an updated claims listing. The e-mail concluded as follows:

> Steve, regarding the Co-Insurance clause. The upcoming property portion will include a 90% Co-insurance clause for sprinklered locations, and an 80% Co-insurance clause for non-sprinklered locations.
>
> If you have any questions or concerns please do not hesitate to contact me.

[407] Mr. McMullin responded to the e-mail, but did not mention the co-insurance clause. He testified that when he received this e-mail, he had no understanding of what co-insurance meant, and he never asked.

[408] Mr. McMullin was exposed to the term again on July 14, 2006, after coverage had been bound for the 2006-2007 term, when Lynn Stone sent him the e-mail reproduced at para 385. Again, Mr. McMullin replied without asking any questions about co-insurance.

[409] Mr. Maloney initially testified that when he took over the account and met with Grafton Connor, he would have explained co-insurance to Mr. McMullin and told him that a failure to properly insure the buildings to full value could result in a loss greater than the deductible. As with replacement costs, Mr. Maloney's evidence changed on cross-examination. He admitted that he never actually discussed the meaning of the co-insurance clause with Grafton Connor before the fire. I accept that co-insurance was never explained to Mr. McMullin prior to coverage being bound in 2006.

[410] There was no dispute as to the proper interpretation of the co-insurance clause in this case. If the total insurable value declared by Grafton Connor in 2006 is less than eighty percent of the actual insurable value in 2006, the loss payable will be reduced in the proportion that the actual insurable value of the Pub bears to the declared insurable value of the Pub. The total insurable value declared by Grafton Connor in 2006 was $17,596,263. After the fire, Grafton Connor retained Tudor Valuations to perform replacement cost valuations of each of the other properties. Based on these valuations and the SPEC valuation of the North End Pub, the actual insurable value of the properties in 2007 was $19,705,018.16. Dividing the declared insurable value by the actual insurable value in 2007 yields a result of 89 percent.

[411] According to Underwriters, the clause requires evidence of the actual insurable value in 2006, not 2007. Since Grafton Connor has provided no evidence

of the actual insurable value in 2006, it has not established that it should avoid the co-insurance penalty.

[412] Grafton Connor relies on s. 170 of the *Insurance Act*, which requires that a policy containing a co-insurance clause be stamped in red ink, on its face, with a warning to that effect. In the alternative, it says the Tudor valuations provide sufficient evidence to enable the court to make a finding that the actual values for 2006 would have been equivalent to the valuation performed in 2007, or at least no greater.

[413] Section 170 of the *Insurance Act* states:

> 170 A contract containing
>
> (a) a deductible clause;
>
> (b) a co-insurance, average or similar clause; or
>
> (c) a clause limiting recovery by the insured to a specified percentage of the value of any property insured at the time of loss, whether or not that clause is conditional or unconditional,
>
> shall have printed or stamped upon its face in red ink or in bold print of not less than twelve-point size the words: "This policy contains a clause which may limit the amount payable", and unless these words are so printed or stamped the clause shall not be binding upon the insured.

[414] Subsection 161(1) of the *Act* limits the application of Part VII to "insurance against loss of or damage to property arising from the peril of fire *in any contract made in the Province*" [*emphasis added*].

[415] Section 170 (then s. 125 of the *Insurance Act*, RSNS 1967, c 148) has been considered in *Khoury v Constitution Insurance Co of Canada et al*, [1979] NSJ No 612 (SC), and *Maritime Drywall Ltd v Commercial Union Assurance Co Ltd*, [1980] NSJ No 541, aff'd [1980] NSJ No 540 (NSSCAD).

[416] In *Khoury*, the plaintiff claimed under a fire insurance policy issued by Constitution Insurance Co. of Canada. The policy had been arranged through George Simon, the President of Omega Insurance Limited, an insurance brokerage.

[417] In 1975, Mr. Simon began taking care of the plaintiff's insurance needs. She owned a car, a rooming house on South Street in Halifax, and a six-unit apartment building in Halifax. In 1975, 1976, and 1977, Mr. Simon arranged fire insurance on the rooming house through Continental Insurance Companies for amounts

ranging from $40,000 to $48,400. Each of the policies was subject to eighty percent co-insurance and a $250 deductible.

[418] On November 2, 1977, prior to the expiration of the policy on the rooming house, Continental advised the plaintiff that the policy would be cancelled as of November 17, 1977. Mr. Simon tried to obtain coverage in the local market without success, due to the high risk nature of rooming houses.

[419] On November 7, he called David Tune Property Underwriters Limited (Tune) of Montreal which specialized in risks turned down by other insurers. Tune had no offices or agents in Nova Scotia. Mr. Simon inquired as to whether Tune could arrange fire insurance for the rooming house. He was advised by Ted Chapman, the General Manager of Tune, that coverage could be arranged for $40,000 (the amount requested by Simon) subject to a deductible of $250 and an eighty percent co-insurance clause. The rate of premium per $100 of insurance would be $2.25, approximately four times higher than the rate the plaintiff had been paying to Continental. Mr. Chapman told Mr. Simon that if his client wanted the coverage, he should write to him.

[420] Mr. Simon advised the plaintiff of the premium rate, but she did not think she could afford the coverage. She allowed the Continental policy to lapse, but eventually told Mr. Simon to place $20,000 of insurance with Tune, rather than $40,000. On November 24, 1977, Mr. Simon wrote Tune requesting that fire insurance coverage be placed as of that date on the boarding house in the amount of $20,000. The fire insurance policy was issued for $20,000 subject to an eighty percent co-insurance clause and a $250 deductible. The policy was prepared in Tune's Montreal office. It was not stamped on its face with the warning required by s. 125.

[421] The premium was paid by the plaintiff on February 6, 1978, and the loss occurred on February 15, 1978. The parties agreed that the actual cash value of the insured building was $42,500 and the net cost of repairs after depreciation was $20,297.25. They also agreed that the amount payable under the policy, if the co-insurance clause and the $250 deductible applied to the plaintiff, was $11,690, which the insurer paid to the plaintiff. The plaintiff, however, claimed the full $20,000 on the basis that the eighty percent co-insurance and the deductible were not binding by reason of s. 125. The insurer argued that s. 125 did not apply, as the contract was made in Montreal and s. 113(1) (now s. 161(1)) limited the application of s. 125 to contracts made in Nova Scotia.

[422] Hallett J (as he then was) found, *inter alia*, that Omega was the plaintiff's agent, not the agent of the insurer, and there was no relationship between Tune and Omega. Applying basic contract principles, Hallett J held that the contract was formed in Montreal:

> 22 In order to determine where a contract was made, it is necessary to consider what constituted the offer.
>
> 23 In *General Principles of Insurance Law, Second Edition*, by Ivamy, the author states at p. 64:
>
> > "The offer to enter into a contract of insurance may, as a general rule, be considered as addressed to the insurers by the person who is seeking to protect himself by insurance against loss."
>
> 24 However, the author goes on to say at p. 64:
>
> > "Where the terms of the proposed contract are really a matter of negotiation, as in the case of special insurances falling outside the ordinary business of the insurers, greater difficulty arises, and each case must be judged by its own circumstances.... The facts may show that it is the insurers who have made an offer, from which they cannot recede, and which the proposer may turn at his option into a binding contract."
>
> 25 Considering the circumstances of this case, the plaintiff's agent sought insurance outside the province; he was quoted rates by the defendants' agent and told that if he wanted coverage he would have to put his request in writing. The plaintiff's agent subsequently discussed the coverage available with the plaintiff who eventually decided she would place $ 20,000.00 fire insurance on the property. On November 24 the plaintiff's agent requested the coverage, not for $ 40,000.00 as he had originally discussed over the telephone with Mr. Chapman, but for $ 20,000.00. Mr. Simon was the plaintiff's agent and had no working arrangement whatever with the defendants' agent, Tune. In my opinion, the letter of November 24 requesting coverage was the offer which was accepted by the defendants by the issuance and mailing on their behalf of the policy in the amount of $ 20,000.00 in accordance with the request by the plaintiff's agent, Mr. Simon. In my opinion, the first telephone call by Mr. Simon to Mr. Chapman and the quoting of rates by Mr. Chapman was not an offer by Tune on behalf of the defendants which was open for acceptance by the plaintiff, as Mr. Chapman specifically stated to Mr. Simon that if Mr. Simon wished to place insurance on behalf of the plaintiff, he would have to make a written request. Mr. Chapman testified that he often received calls for coverage but has a policy not to agree to cover any risk except on receipt of a written request as on too many occasions in the past he had agreed only to find that the insurance policy when sent out to the agent was rejected.
>
> 26 The contract of insurance between the parties was completed when the policy was mailed from Montreal to the plaintiff's agent in Halifax. Therefore, the

> contract was made in Montreal and not in Nova Scotia. The offer was accepted by the issuance of the policy and was communicated by the mailing of the same to the plaintiff's agent, all of which took place in Montreal. [*Emphasis added*]

[423] In *Maritime Drywall*, the plaintiff brought an action against its insurer, Commercial Union Assurance Co. Ltd ("CUA") to recover the unpaid portion of an insurance claim for losses to the plaintiff's inventory. The plaintiff was a building contractor specializing in erecting and finishing drywall. Its office and warehouse was located on North Street in Halifax. As part of its operation, the plaintiff maintained an inventory of building materials in the warehouse. The amount of inventory fluctuated significantly, ranging from under $80,000 to more than $150,000 worth at a time.

[424] The plaintiff's secretary-treasurer, Don Brennan, was approached by John Depew of Marsh & McLennan Limited in Halifax to discuss the general insurance needs of the company. Mr. Brennan accepted Marsh & McLennan's proposal and coverage was bound with CUA. Under the policy, Maritime Drywall had $75,000 of insurance coverage for inventory, subject to 100 percent co-insurance and monthly reports of inventory values. Mr. Brennan understood that Maritime Drywall was required to file monthly inventory reports with Marsh & McLennan. He understood that Mr. Depew would provide the forms, but when no forms were sent, he forgot about the reporting requirement. Mr. Depew had no memory of promising to supply forms. He said the normal practice was for clients to send in the monthly figure on their own letterhead.

[425] A fire took place at Maritime Drywall's warehouse on September 1, 1996. The proof of loss quantified the total amount of the loss to inventory as being $132,720.90. Maritime Drywall claimed the full $75,000. CUA paid $56,250, which was 75 percent of the face amount of coverage. CUA relied upon Clause 9 of the fire insurance section of the policy, which provided that a failure to file a monthly report of inventory values would result in payment by the insurer of not more than 75 percent of the applicable limit of liability under the policy. Maritime Drywall took the position that CUA could not avail itself of the limitation contained in the clause because the policy was not stamped to indicate that it contained a clause limiting the amount payable, as required by s. 125 of the *Insurance Act*.

[426] Maritime Drywall relied on *Martinello v Travellers Indemnity Company of Canada et al* (1976) 14 OR (2d) 66 (Ont HCJ), where Griffiths J considered a virtually identical statutory provision. In that case, the statutory caution was

stamped on the fourth page of the policy. Griffiths J observed that provisions of this nature are intended to protect the insured, and must be strictly construed. He held that the words "printed or stamped upon its face" meant that the words must appear on the front or first page of the contract of insurance.

[427] Richard J rejected the holding in *Martinello*, which he considered a "rather restrictive interpretation", and held:

> 17 The Fire section policy in the instant case contains 7 pages. Some of the pages contain writing on the back as well as on the face of the page. The policy contains the statutory warning in large bold red print running diagonally across the face of page 4. I agree with Griffiths, J., in *Martinello, supra*, that the intention of this section of the Act is to provide protection for the insured. I am of the opinion the inscription in the subject policy provides just such protection. Anyone taking even the most cursory glance at this policy would be struck by this red lettered inscription. I am satisfied that the defendant has substantially complied with section 125 of the *Insurance Act* and the plaintiff is bound by the limitation contained in clause 9.

[428] He went on to note that even if he was wrong, he would have dismissed the plaintiff's case on the alternative ground that the insurance contract was not made in the province:

> 19 According to Mr. Infantino, CUA does not have office facilities or staff in Nova Scotia. All its business is conducted through agents and brokers. In the present case, the business was transacted in Montreal between CUA and the Montreal office of Marsh & McLennan. Mr. Depew said he had no dealings with CUA and all negotiations were handled by Marsh & McLennan in Montreal. Insofar as CUA is concerned, the contract was executed and delivered in Montreal. Clearly, Marsh & McLennan, as brokers, were acting throughout on behalf of its client, the plaintiff.
>
> 20 I find that the insurance contract in dispute was made in Montreal and not in the Province of Nova Scotia. …

[429] The Court of Appeal affirmed Richard J's interpretation of s. 125, but did not comment on whether the contract was made in Nova Scotia.

[430] In the case at bar, the warning required by s. 170 does not appear anywhere on the Policy. As a result, the co-insurance clause will not be binding on Grafton Connor unless the contract was made outside the province.

[431] The facts in this case are akin to those in *Maritime Drywall*. Lloyd's of London does not have office facilities or staff in Nova Scotia. All of the business was transacted in London, between Underwriters and Marsh UK. None of the Marsh brokers in Halifax had any dealings with Underwriters, and all negotiations were handled by Marsh UK.

[432] In my view, as in *Maritime Drywall*, it does not matter whether the applicant for insurance or the insurer is considered the offeror. The result is the same in either scenario. There was no suggestion by Grafton Connor during these proceedings that Marsh UK lacked authority to act as its sub-agent in placing coverage in the London market. Accordingly, if Grafton Connor was making an offer to Underwriters through its sub-agent, Marsh UK, then the contract was formed when Underwriters accepted the offer and communicated that acceptance to Marsh UK, in London. If Underwriters was making an offer to Grafton Connor, then Grafton Connor accepted when that acceptance was communicated by its sub-agent, Marsh UK, to Underwriters, in London. As a result, I find that the contract between the parties was made in London, not Nova Scotia, and s. 170 does not apply.

[433] Even if I am wrong as to where the contract was made, this is of little consequence, since I find that the co-insurance provision is not triggered in these circumstances. In order for the total insurable values declared in 2006 ($17,596,263) to be less than eighty percent of the actual insurable values in 2006, the latter would have to be significantly higher than the actual values in 2007 ($19,705,018.16). I am satisfied that the 2007 Tudor valuations, and common sense, enable this court to make a finding that the actual values for 2006 would not have been greater than the 2007 actual values of $19,705,018.16. Therefore, the co-insurance clause does not apply.

Summary of the Value of Claim under Policy

[434] Having determined that the Policy is a blanket policy and that the co-insurance provision does not apply, the value of the claim under the Policy is $2,740,869.16: $2,174,514.02 for the building, $411,357.61 for the contents, and $154,997.53 for business interruption. Marsh and Grafton Connor are each liable for fifty percent of this amount or $1,370,434.58.

Consequential Damages

[435] In addition to its claim for the value of the Policy, Grafton Connor claims against Underwriters and Marsh for costs arising from the delay in being able to redevelop the property. The claim is based on the factual premise that if the insurance proceeds had been paid in a timely manner, Grafton Connor would have used those proceeds to carry out a redevelopment of the property.

[436] Instead of simply replacing the North End Pub, however, Grafton Connor decided to build an eight-story mixed use development on the property. The development would consist of commercial space on the ground floor, including the re-established North End Pub, and seven residential floors. Without the insurance proceeds, Grafton Connor was not financially able to incur the cost, and had to defer redevelopment pending resolution of this action.

[437] Grafton Connor says it has suffered three categories of loss as a result of the delay. First, the cost of construction has risen over the period of the delay and Grafton Connor will have to incur that additional cost when it is able to proceed. Second, it has lost the profit it could have generated from the development during the period it has been delayed. Third, it has lost the ability to obtain VLTs for a reconstructed North End Pub, resulting in the loss of the business.

[438] Grafton Connor bases its claim against Underwriters on an alleged failure to consider whether the errors and omissions portion of Endorsement 10 excused the misrepresentations Underwriters relied on to void the Policy. According to Grafton Connor, by ignoring Endorsement 10, Underwriters breached its duty to investigate the claim in good faith, making it liable for consequential damages.

[439] Grafton Connor says Marsh is liable for consequential damages because its negligence caused the Policy to be voided and a protracted legal battle to ensue, resulting in the delay in rebuilding and the loss of the VLTs. The delay and its associated damages were the foreseeable consequences of Marsh's negligence.

[440] Underwriters says it had no obligation to cite Endorsement 10 in its denial of the claim because the clause did not apply to material misrepresentations. It says any alleged financial inability to rebuild on the part of Grafton Connor was not a foreseeable consequence of any acts or omissions on its part, but was the result of unrelated business losses Grafton Connor experienced from 2006 to 2008. Furthermore, Underwriters submits that the consequential damages claimed by Grafton Connor are too remote. In the alternative, Underwriters says Grafton Connor failed to mitigate its damages.

[441] Like Underwriters, Marsh says the consequential damages claim is too remote. There is no evidence that Marsh should have been aware that Grafton Connor would use the insurance proceeds to fund a significant mixed-use development in place of the existing North End Pub, that Grafton Connor would be unable to redevelop the property without the insurance proceeds, and that Grafton Connor would lose its entitlement to VLTs. According to Marsh, if it breached a duty owed to Grafton Connor, the only foreseeable consequence of that breach was that Grafton Connor would not be indemnified in the event of a loss. Its damages should therefore be limited to the amount it would have recovered for that loss under the Policy if coverage had been in place. Like Underwriters, Marsh argues in the alternative that Grafton Connor failed to mitigate its damages.

The Claim against Underwriters

[442] Before considering the evidence of consequential damages, I will first determine whether such damages are available against Underwriters in these circumstances. I conclude that Grafton Connor has not established a breach of the duty of good faith by Underwriters that could give rise to consequential damages.

[443] In *Insurance Bad Faith*, 3d edn (Markham: LexisNexis Canada Inc., 2015), Gordon G. Hilliker explains when consequential pecuniary losses will be available against an insurer:

> In an action against the insurer pursuant to the policy the insured's remedy is not restricted to the benefits stipulated in the policy, together with any applicable interests and costs. Rather, even in the absence of a breach of the duty of good faith, the insured may be able to recover, under contract law, for certain pecuniary losses which are consequent upon the wrongful delay or denial of the policy proceeds. In addition, where there has been a breach of the duty of good faith, the insured may be able to recover in contract, and possibly in tort, for pecuniary loss resulting from the breach. The limiting factor on the recovery of such losses will be the principle of remoteness … (p 120)

[444] In this case, Grafton Connor's claim for consequential damages against Underwriters is premised on a breach of the duty of good faith. In *702535 Ontario Inc v Non-Marine Underwriters, Lloyd's of London*, [2000] ILR I-3826, [2000] OJ No 866 (Ont CA), O'Connor JA described the insurer's duty of good faith during the claims process:

> 27 The relationship between an insurer and an insured is contractual in nature. The contract is one of utmost good faith. In addition to the express provisions in

> the policy and the statutorily mandated conditions, there is an implied obligation in every insurance contract that the insurer will deal with claims from its insured in good faith: *Whiten v. Pilot Insurance Co.* (1999), 42 O.R. (3d) 641 (Ont. C.A.). The duty of good faith requires an insurer to act both promptly and fairly when investigating, assessing and attempting to resolve claims made by its insureds.
>
> 28 The first part of this duty speaks to the timeliness in which a claim is processed by the insurer. Although an insurer may be responsible to pay interest on a claim paid after delay, delay in payment may nevertheless operate to the disadvantage of an insured. The insured, having suffered a loss, will frequently be under financial pressure to settle the claim as soon as possible in order to redress the situation that underlies the claim. The duty of good faith obliges the insurer to act with reasonable promptness during each step of the claims process. Included in this duty is the obligation to pay a claim in a timely manner when there is no reasonable basis to contest coverage or to withhold payment. …
>
> 29 The duty of good faith also requires an insurer to deal with its insured's claim fairly. The duty to act fairly applies both to the manner in which the insurer investigates and assesses the claim and to the decision whether or not to pay the claim. In making a decision whether to refuse payment of a claim from its insured, an insurer must assess the merits of the claim in a balanced and reasonable manner. It must not deny coverage or delay payment in order to take advantage of the insured's economic vulnerability or to gain bargaining leverage in negotiating a settlement. A decision by an insurer to refuse payment should be based on a reasonable interpretation of its obligations under the policy.
>
> 30 This duty of fairness, however, does not require that an insurer necessarily be correct in making a decision to dispute its obligation to pay a claim. Mere denial of a claim that ultimately succeeds is not, in itself, an act of bad faith: *Palmer v. Royal Insurance Co. of Canada* (1995), 27 C.C.L.I. (2d) 249 (O.C.G.D.).
>
> 31 What constitutes bad faith will depend on the circumstances in each case. A court considering whether the duty has been breached will look at the conduct of the insurer throughout the claims process to determine whether in light of the circumstances, as they then existed, the insurer acted fairly and promptly in responding to the claim.
>
> 32 A breach of the duty to act in good faith gives rise to a separate cause of action from an action for the failure of an insurer to compensate for loss covered by the policy. …
>
> 33 A breach of the duty of good faith may result in an award of damages which is distinct from the proceeds payable under the policy for the insured loss and which are not restricted by the limits in the policy … [*Emphasis added*]

[445] Earlier in this decision, I concluded that Underwriters was entitled to void the Policy on the basis of material misrepresentation. Whether a finding of bad

faith on the part of an insurer can be made in the absence of coverage is unsettled. Some courts have held that a wrongful failure or refusal to pay benefits owing under a policy is a necessary prerequisite to a bad faith claim: see, for example, *Forestex Management Corp v Underwriters at Lloyd's*, 2004 FC 1303, 2004 CarswellNat 3344; *Wonderful Ventures Ltd v Maylam*, 2001 BCSC 775, 2001 CarswellBC 1516. Others have held that insurer bad faith may exist despite an absence of coverage: see, for example, *Baudisch v Co-operators General Insurance Co*, 2004 ABPC 229, 2004 CarswellAlta 1705; *Insurance Bad Faith*, *supra*, at p 80. For the reasons that follow, however, I need not comment on the issue.

[446] Grafton Connor says the failure by Underwriters to investigate whether the misrepresentations were excused by Endorsement 10 amounted to a breach of its duty to investigate and assess the claim in good faith. With respect, I disagree. I concluded that Endorsement 10 did not apply to material misrepresentations, and the duty of good faith does not require an insurer, in the course of its investigation of a claim, to consider irrelevant policy provisions and provide the insured with reasons why such provisions do not apply. Underwriters is therefore not liable for any consequential damages claimed by Grafton Connor.

[447] Whether Marsh is liable for the consequential damages claimed by Grafton Connor will depend on whether the delay in rebuilding and the associated damages were reasonably foreseeable at the time of Marsh's negligence. Having found that Grafton Connor was fifty percent responsible for the misrepresentations that resulted in a denial of coverage, it will be equally liable for any proven consequential losses.

Grafton Connor's Plans for Redevelopment

[448] Gary Hurst testified that Grafton Connor began to think about rebuilding within days of the fire. He wanted to replace the North End Pub, but also to consider whether there was potential for other mixed-use development.

[449] Mr. Hurst said he quickly realized that replacing the Pub as a standalone operation did not make sense from a financial perspective. He explained that he knew, based on his experience financing other food and beverage properties, that sixty percent would be the ceiling on the financing he would get from a bank or mortgage company for a standalone facility. At $100 per square foot, it would cost approximately $2.1 million to rebuild the North End Pub. With a mortgage at sixty percent, Grafton Connor would have to inject the equity capital of forty percent, or

$850,000. It would also need to purchase replacement contents, at a cost of approximately $300,000. The equity cost for contents would be about $50,000, as Grafton Connor would qualify for a business loan of $250,000. Accordingly, the cost to Grafton Connor to rebuild the standalone facility would be in the neighbourhood of $900,000.

[450] On the other hand, if Grafton Connor built a mixed-use property, with a ground floor of commercial space that would include the new North End Pub and multiple floors of residential units, it could get 85 percent financing through a Canada Mortgage and Housing Corporation ("CMHC") financing guarantee. Assuming a complete construction cost of $10 million, the equity contribution would be approximately $850,000, with an additional $50,000 for contents.

[451] Realizing that, from a financing standpoint, Grafton Connor would be in the same position whether it built a standalone facility or a mixed-use development, Mr. Hurst considered what the market was interested in for the site. He concluded that the public wanted a reincarnation of the North End Pub, with an updated theme and operating style, but that the market was also ready for apartments. He retained Andy Lynch, architect and principal of Lydon Lynch, in April 2007, to provide an opinion as to the options for a mixed-use development that would receive planning approval from Halifax Regional Municipality ("HRM").

[452] Mr. Lynch and his junior associate began by developing a number of "as of right" scenarios. In other words, developments that could be built under the zoning bylaw without going through years of contract development applications and an onerous approval process with HRM. In late 2007, when these initial plans were completed, Mr. Lynch believed that zoning bylaws limited the proposed development to four storeys. For this reason, the drawings depicted a mixed-use development with three floors of apartments above a ground floor of commercial space.

[453] In October 2007, Mr. Hurst learned that Underwriters was officially denying coverage and that any recovery would require a lawsuit. Knowing that resolution of the matter was fairly far off, he requested that Mr. Lynch put the matter on the back burner and take his time with the development work.

[454] In December 2007 or January 2008, Mr. Lynch met with city planners on a project that had many similarities to the proposed Grafton Connor development. Mr. Lynch decided to show the plans for the development to Luc Ouellet, one of the city planners, to obtain his feedback. As a result of his conversation with Mr.

Ouellet, Mr. Lynch learned of a piece of zoning legislation called Schedule Q that applied only to Gottingen Street. This legislation allowed for mixed-use developments of a greater height.

[455] Over the course of 2008, Mr. Lynch developed several scenarios under Schedule Q for a seven-story building with six residential floors, instead of three, over the same ground floor commercial layout. These drawings also added a basement parking garage level underneath the commercial level.

[456] Very little progress was made on the file during 2009 and into 2010. In late 2010, Mr. Hurst was optimistic that the legal proceeding would be resolved within a year. He asked Mr. Lynch to move the matter to the front burner, and meet with city staff with a view to finalizing the materials for the formal application. The goal was for completion of the approval process to coincide with resolution of the lawsuit.

[457] Mr. Lynch went to work developing the final scheme for the site. He commissioned traffic and engineering studies that were required for the formal application. In early 2011, he prepared several three dimensional renderings and a detailed description of the project. By this point, the building had gained a seventh floor of residential units, bringing the total number of floors to eight.

[458] In February of 2011, Mr. Lynch met with Mr. Hurst in Florida to review the plans. Mr. Lynch thought they were nearing the point of filing the formal application, but he was asked to consider other options, including the purchase of additional properties. Several different scenarios were prepared in April and May 2011 as a result of these discussions.

[459] In mid-2011, Mr. Lynch advised Mr. Hurst that he intended to retire and recommended that Mr. Hurst hire Ross Cantwell, a real estate consultant and developer, to assist with the application. Mr. Cantwell had significant experience in residential development and when he joined the team, he began asking a number of questions about the project. According to Mr. Lynch, these questions brought them back to square one, planning-wise.

[460] Mr. Cantwell conducted market studies and reported that there was a good market for the proposed development. In particular, the studies identified a demand for smaller units, and there were opportunities to rent units to people who were transitory.

[461] In late November 2011, the Acropolis property became available at the corner of Gottingen and Almon Street, creating an opportunity to increase the size of the land and the number of units. Mr. Lynch performed a study to determine whether the additional land was worth the increased cost. He concluded that the property was too expensive to make its acquisition worthwhile.

[462] Mr. Lynch continued to work with Mr. Cantwell and Mr. Hurst on the project, making revisions and updating studies, until February 2012. By that time, there was still no final decision on the plan for the site and pressure was mounting to finalize a submission to city staff. Mr. Cantwell wanted more studies, and Mr. Lynch was frustrated with the lack of progress. Mr. Lynch e-mailed Mr. Hurst on February 7, 2012, and summarized the remaining options in an attempt to bring the matter to a conclusion. A few days later, Mr. Hurst and Mr. Lynch agreed that if Mr. Lynch received payment of the outstanding balance for his work, Mr. Hurst would be free to move forward with another architect.

[463] After paying Mr. Lynch, Mr. Hurst retained Paul Skerry. Mr. Skerry came up with the final design which had 70 residential units above the ground floor of commercial space. A development agreement with HRM was finalized in September 2013. The project will move forward, without the reincarnated North End Pub, upon resolution of this action.

Grafton Connor's Capacity to Rebuild

[464] The matter of whether Grafton Connor was in a financial position to rebuild without the insurance proceeds is critical to its claim for consequential damages, and the defendants' allegations that it failed to mitigate its damages.

[465] Gary Hurst and Steve McMullin testified that when Underwriters denied the claim in October 2007, Grafton Connor's financial position was too weak to finance a redevelopment without the insurance proceeds. Between 2006 and 2008, Grafton Connor lost $1.4 million on the Thirsty Duck pub, which included $550,000 worth of capital improvements Grafton Connor had made to the premises that were surrendered when the property was liened by the owner. Furthermore, in December 2007, a brawl took place at the Dome cabaret that resulted in a week-long closure of the business. Grafton Connor suffered damage to its reputation for a period of about seven months, and lost an estimated $1 million as a result. Accordingly, when the claim was denied and Grafton Connor filed this action, it was in the midst of experiencing losses of $2.4 million.

[466] In addition to substantial business losses, Mr. Hurst and Mr. McMullin said Grafton Connor has remained unable to finance a redevelopment because the borrowing capacity on the only three properties it owns (the Grafton Connor Building, the Esquire, and the North End Pub) is, and has been, maxed out. In September 2007, Mr. Hurst refinanced the Grafton Connor Building and obtained $500,000 that was surplus to what the lender required to be spent on the property. Those funds, as well as $300,000 of cash flow Grafton Connor had accrued over the course of 2007, were used to partially offset the $2.4 million in losses. But this still left a significant shortfall.

[467] When it became apparent that Grafton Connor would be bringing an action against Underwriters, the only property that could be used to fund the proceeding was the North End Pub site. The Esquire was already above maximum borrowing capacity. Mr. Hurst used the Pub property, which had no mortgage at the time of the fire, to finance legal expenses and some of the indebtedness from the Thirsty Duck and the Dome. At the time of trial, the property had a mortgage of $1.45 million.

[468] During the period that redevelopment was on hold, Grafton Connor made several acquisitions. In 2009, the recession was under way and future economic conditions were hard to predict. Mr. Hurst was unsure if the business would survive. But the recession also yielded opportunities. Grafton Connor developed a strategy of acquiring other hospitality locations that were suffering as a result of the economic downturn. It looked for properties where the vendor would take back a mortgage as part of the purchase price, and agree to include stock and inventory that had already been paid for as part of the transfer. With stock and inventory taken care of, Grafton Connor had six weeks of cash flow free of any requirement to pay suppliers. This allowed it to make money on the cash flow in excess of what it had to pay for the acquisition. In other words, Grafton Connor was purchasing each of the businesses with the money being generated by those businesses.

[469] Grafton Connor used the "vendor take back" approach to purchase Brewster's, Kempster's, and the Redwood Grill without any outside financing. The acquisition of the True North Diner in Bedford did require financing in the form of a loan of $180,000 from Royal Bank of Canada ("RBC"), but no asset was encumbered other than the assets of the operation itself.

[470] Finally, Grafton Connor was able to purchase four Pizza Pizza locations with financing from RBC through a franchise financing program that Pizza Pizza Limited National had in place. This financing was not available for anything other than a franchise. Ultimately, three of the Pizza Pizza locations turned out to be unprofitable and Grafton Connor persuaded the franchisor to buy them back, and take over the bank loans for each location.

[471] While it was acquiring new properties, Grafton Connor also carried out some renovations to its existing establishments. In the Grafton Connor Building, it changed the Attic nightclub into a new nightclub called Taboo, at a cost of approximately $450,000. The renovation was paid for with funds obtained when the Grafton Connor Building was remortgaged in September 2007. Also in the Grafton Connor Building, the Dome was renovated to add the Auction House, another nightclub, at a cost of approximately $500,000. It was directly financed as part of a re-financing of the building in December 2012 for $500,000. In order to obtain the funds from the lender, Grafton Connor was required to build the Auction House, show proof of the build, and provide proof of payment. Finally, Grafton Connor spent $450,000 renovating Tomorrow's Lounge in Bridgewater, which it renamed the Bridgewater Local Public House. Mr. McMullin testified that no financing was available to fund the Bridgewater renovations, so Grafton Connor reallocated cash flow it would normally have used to pay vendors and the Canada Revenue Agency.

[472] In addition to the evidence of Mr. Hurst and Mr. McMullin, Grafton Connor relies on the expert report of Daniel Jennings, a chartered accountant and business valuator, formerly with Raymond Yuill Chartered Accountants and currently with BDO Canada LLP. In his report, Mr. Jennings provided, *inter alia*, an opinion on Grafton Connor's financial ability to proceed with redevelopment without the insurance proceeds.

[473] Assuming a $10.5 million project, and the availability of CMHC-backed financing, Mr. Jennings concluded that Grafton Connor would have needed fifteen percent equity or $880,000 (after contributing the value of the land) to construct the mixed-use development. Having reviewed the existing debt of the Esquire and Grafton Connor Building, Mr. Jennings opined that Grafton Connor "had little ability to further debt finance its operations": Expert Report, p 16. In his opinion, Grafton Connor would not have been able to finance the construction of the mixed-use development without an injection of new equity, like the insurance proceeds.

[474] Mr. Jennings was cross-examined. He conceded that his report focused on Grafton Connor's financial ability to proceed with the development in 2007/2008. While his report did not address Grafton Connor's ability to finance the construction from 2009 onward, he said he was asked by counsel to review the report filed by Marsh's expert, which did cover the period from 2009 to 2013, in the context of his conclusions.

[475] Marsh filed an expert report prepared by Brian Keough, a chartered accountant and business valuator with Keough & Associates Inc. Mr. Keough was qualified as an expert on loss valuation, business valuation, accounting and corporate finance. In his report, Mr. Keough also considered, *inter alia*, whether Grafton Connor would have been able to redevelop the North End Pub site without the insurance proceeds.

[476] Relying on the Jennings report, Mr. Keough started from the premise that Grafton Connor would have needed to contribute fifteen percent equity, or $1.575 million, toward the $10.5 million cost to construct the mixed-use development. Part of that equity requirement could be satisfied by contributing the value of the land. According to Mr. Keough, the North End Pub site may have been worth $1.2 million in 2009 (an offer of $1.45 million had been made on the property in 2010), "which would go a long way towards the $1.575 million equity needed": Expert Report, p 26. Mr. Keough also opined that after 2009, there may have been capacity to raise additional mortgage funds by remortgaging the Grafton Connor Building to a sixty percent ratio.

[477] Mr. Keough further noted that Grafton Connor acquired or invested in a number of new hospitality enterprises between 2009 and 2013, and "it appears GCG used cash flow from existing operations and/or additional mortgage financing on their Bedford Highway and Gottingen Street properties to fund at least part of the price": Expert Report, p 26. Mr. Keough concluded that Grafton Connor had discretion as to where to place its investment capital, and it chose not to fund the equity component needed to redevelop the North End Pub site.

[478] The materials provided to Mr. Keough by counsel for Marsh included statements of Mr. Hurst's personal net worth, but these do not seem to have influenced his opinion. He noted only that Mr. Hurst had significant personal net worth, but most of it was tied up in Grafton Connor.

[479] Finally, Mr. Keough was asked to consider whether Grafton Connor had the financial ability to reconstruct the North End Pub in its pre-existing form. Relying

on a report prepared for Grafton Connor by Hanscomb Limited, Mr. Keough assumed that the cost to reconstruct the Pub in 2009 would have been $2.854 million. Presuming that a property mortgage could be placed on the newly constructed building at 65 percent of the cost, Mr. Keough concluded that Grafton Connor would have required $424,000 cash equity to rebuild in 2009. In his opinion, that sum could have been obtained by remortgaging the Grafton Connor Building.

[480] I am satisfied that Grafton Connor did not have the financial ability to redevelop the North End Pub site prior to trial, either as an eight-storey mixed-use development, or a standalone facility. Mr. Keough concluded that Grafton Connor could have constructed the eight-story building in 2009 or 2010 if it had contributed the full value of the Pub site and remortgaged the Grafton Connor Building to a sixty percent ratio. In my view, it was reasonable for Grafton Connor to mortgage the North End Pub site in order to finance this litigation, and to help offset some of the losses from the Thirsty Duck and the Dome. Litigation is a costly business and, at the time, the Pub site was Grafton Connor's only unencumbered property.

[481] To arrive at his opinion that Grafton Connor chose to use its available resources to fund new acquisitions instead of redeveloping the property, Mr. Keough calculated the total acquisition costs from 2009 to 2012, and the total vendor and bank financing obtained by Grafton Connor during the same period. He subtracted the total financing amount from the total acquisition cost, leaving an amount that he concluded must have been financed from Grafton Connor's operating cash flow and/or incremental mortgage financing.

[482] I am not satisfied that Mr. Keough's approach provides an accurate representation of Grafton Connor's financial history. He appears to have been working with incomplete information. The data for the year 2011 is a useful example. Mr. Keough noted that the acquisition cost for the True North Diner was $401,500, and the Pizza Pizza capital investment was $250,000, for a total of $651,500 in acquisition costs. In terms of financing, Grafton Connor received $241,500 in the form of a vendor note for the True North Diner. The chart lists no other financing for 2011. Mr. Keough subtracted $241,500 from $651,500, leaving $410,000, which he concluded was financed from Grafton Connor's operating cash flow and/or incremental mortgage financing. The evidence from Mr. Hurst and Mr. McMullin, however, was that Grafton Connor financed its acquisition of the

Pizza Pizza locations through RBC as part of a franchise financing program. The 2012 calculations are similarly suspect.

[483] Finally, Mr. Keough's conclusion that Grafton Connor could have rebuilt the North End Pub as a standalone facility in 2009 is premised on its contribution of the $1.2 million value of the land. As I indicated earlier, it was reasonable for Grafton Connor to use the Pub site to fund this litigation.

[484] I accept the evidence of Mr. Hurst and Mr. McMullin that redevelopment without the insurance proceeds was not feasible. That said, Underwriters and Marsh argued at trial that even if Grafton Connor was unable to rebuild without the insurance proceeds, its impecuniosity was caused by its significant business reversals, not the denial of coverage under the Policy. Although the defendants framed the issue as one of either causation or mitigation, I consider it a question of remoteness. Losses associated with a plaintiff's impecuniosity will be recoverable where such impecuniosity was reasonably foreseeable to the defendant: see *All-Up Consulting Enterprises Inc v Dalrymple*, 2013 NSSC 46, [2013] NSJ No 80 at para 215; *Lagden v O'Connor*, [2003] HL 64, [2004] 1 All ER 277, at paras 51-61 (*per* Lord Hope).

[485] It is useful to return to basic principles and review when a loss will be considered "reasonably foreseeable." In *Mustapha v Culligan*, 2008 SCC 27, [2008] SCJ No 27, McLachlin CJ described the terms "probable" and "possible" as misleading, and explained a foreseeable harm as one which is a "real risk" and not "far-fetched":

> 13 Much has been written on how probable or likely a harm needs to be in order to be considered reasonably foreseeable. The parties raise the question of whether a reasonably foreseeable harm is one whose occurrence is probable or merely possible. In my view, these terms are misleading. Any harm which has actually occurred is "possible"; it is therefore clear that possibility alone does not provide a meaningful standard for the application of reasonable foreseeability. The degree of probability that would satisfy the reasonable foreseeability requirement was described in *The Wagon Mound (No. 2)* as a "real risk", i.e. "one which would occur to the mind of a reasonable man in the position of the defendan[t] ... and which he would not brush aside as far-fetched" …

[486] Was it reasonably foreseeable to Marsh, at the time of its negligence, that if Grafton Connor was denied indemnity under the Policy, it would not have the resources available to rebuild the North End Pub? I find that it was. Marsh was aware that Grafton Connor operated a number of hospitality enterprises in Nova

Scotia. Although Grafton Connor appeared to be relatively successful, the high risk nature of hospitality operations has been a continuous theme of this litigation. Douglas Poole, the former President and CEO of ECI, testified that hospitality enterprises, and restaurants in particular, "have the highest rate of bankruptcies of industry classes that most insurer's write." Frank Szirt noted in his report that Best's *Underwriting Guide* lists hospitality risks as carrying a "Hazard Index" of 7, which is graded as "high": Expert Report, p 10. In Mr. Jennings's report, he wrote at p 8:

> The retail food and beverage industry is a very competitive one, highlighted by a relatively high failure rate and turnover. Some studies claim that 60% of new restaurants fail within the first three years …

[487] Finally, Prem Lobo, a chartered accountant and business valuator retained by Marsh, noted at p 10 of his expert report:

> Notwithstanding the experience of GCG management and its track record in operating the old NEP and other similar enterprises, the operation of a bar/pub is an inherently risky undertaking.

[488] Losses are part of doing business in the hospitality industry, and a history of past successes does not immunize an owner/operator against them in the future. In this case, a reasonable insurance broker in Marsh's position would not have brushed aside as far-fetched the risk that Grafton Connor would not be able to rebuild the North End Pub without the insurance proceeds. I find that Grafton Connor's inability to rebuild until after the resolution of this litigation was a reasonably foreseeable consequence of Marsh's negligence.

Rise in Construction Costs

[489] Grafton Connor says that as a result of the delay, it will have to incur increased construction costs when it redevelops the North End Pub site. Hanscomb Limited was retained by Grafton Connor to prepare an estimate of the cost of building the eight-storey development as of the fall of 2009, as well as an estimate of the cost if construction had started in the fall of 2013. The latter date was used because the trial in this matter was initially set for the fall of 2013.

[490] The report prepared by Raymond Murray, Vice-President of Hanscomb Limited, stated that if Grafton Connor had proceeded with construction in the fall of 2009, the cost would have been $9,264,223. If construction had commenced in the fall of 2013, the total cost would have been $10,283,645. Based on these

estimates, the delay from 2009 to 2013 resulted in an estimated increased cost of construction of $1,019,422.

[491] Marsh argues that it was not foreseeable to either defendant that Grafton Connor would use the insurance proceeds to construct an eight-storey mixed-use building, instead of simply replacing the original North End Pub.

[492] Without offering any authority for its position, Grafton Connor says an insurer, and by extension a broker, should foresee that any redevelopment by an insured will be done on the basis of the highest and best use of the property. I disagree. Grafton Connor purchased replacement cost insurance coverage for a standalone operation, and it was reasonable for Underwriters and Marsh to assume that in the event of a loss, Grafton Connor would replace the North End Pub with a similar standalone operation. As Marsh noted in its submissions, acceptance of Grafton Connor's position would open the door to a wide variety of speculative claims.

[493] I find that any losses incurred by Grafton Connor as a result of its decision to proceed with a multi-storey mixed-use development instead of a standalone operation are too remote. Although nothing prohibits Grafton Connor from using the insurance proceeds to build a different -- and much more costly -- development, its choice to do so was not reasonably foreseeable to the defendants.

[494] That said, it was foreseeable that the cost to construct a new standalone North End Pub would increase if payment of the insurance proceeds was substantially delayed. Based on the Proof of Loss, the replacement cost of the standalone Pub in 2007 was $2,174,514.02. A second report prepared by Mr. Murray provides annual construction cost escalation figures from November 2007 to May 2013, which total sixteen percent. From June 2013 to June 2014, I will add 2.67 percent, the average annual escalation adjustment over the six year period. This results in an estimated increased cost of construction of $405,981.77.

[495] With respect to the contents, I am prepared to allow a five percent increase to the amount claimed in the proof of loss ($411,357.61), less the $104,061.46 included in that amount for the cost of debris removal. This results in an increased replacement cost of $15,364.81.

[496] If, contrary to my conclusion, it was foreseeable that Grafton Connor would build a multi-story mixed-use development with the insurance proceeds, I would accept Mr. Hanscomb's figure of $9,264,223 for the cost of construction in the fall

of 2009. To that figure, he added eleven percent to account for the rise in construction costs from November 2009 to November 2013. For the period of December 2013 to June 2014, I would add 1.56 percent. This yields a provisional award for increased construction cost of $1,163,586.41.

Past and Future Economic Losses

[497] Grafton Connor says that as a consequence of the delay, it has experienced past losses in the form of lost profit it could have generated from the development during the period it has been delayed. It also claims to have lost the ability to install VLTs in a new North End Pub, and says that, as a result, it is no longer economical to re-establish the North End Pub. Grafton Connor claims damages in perpetuity for the loss of the business.

[498] I propose to deal first with the claim for the loss of the VLTs and the business, as the evidence pertaining thereto is of relevance to the claim for loss of profits.

Loss of VLTs and North End Pub Business

[499] Prior to the fire, the North End Pub operated about eight VLTs pursuant to license agreements with Atlantic Lotto Corporation. These VLTs, which were a significant source of income to the business, were destroyed in the fire.

[500] Mr. Hurst testified that after the fire, he contacted Geoffrey Palmeter, the Regional Manager for Video Lottery at Atlantic Lotto Corporation, and asked whether the VLTs could be grandfathered so that they would be reinstated when the Pub was rebuilt. He told Mr. Palmeter that Grafton Connor intended to rebuild within two to three years. According to Mr. Hurst, he left the conversation with the understanding that the VLTs would be grandfathered.

[501] Mr. Palmeter testified that a few days after the fire, he received a call from Mr. Hurst asking whether Grafton Connor would still qualify for the VLTs if he rebuilt the North End Pub. After consulting a committee of business development managers, Mr. Palmeter told Mr. Hurst that if the North End Pub was rebuilt within "a couple years", Grafton Connor could probably have the VLTs back. He testified that he did not use the word "grandfather" in his conversation with Mr. Hurst.

[502] On April 12, 2007, Grafton Connor's licenses for the North End Pub were suspended by the Nova Scotia Utility and Review Board, at the request of the Alcohol and Gaming Division, on the basis that the building had been destroyed by fire.

[503] Mr. Palmeter left the Atlantic Lotto Corporation in 2008. Prior to his departure, Mr. Hurst did not advise him that Grafton Connor needed more time to rebuild the North End Pub.

[504] In March 2011, the government of Nova Scotia introduced the *Responsible Gaming Strategy*. This strategy was a follow-up to a 2005 strategy document in which the government attempted to strike a more appropriate balance between social responsibility and revenue generation. Under the 2005 strategy, 1000 VLTs were removed from operation, VLT hours of operation were reduced, software changes were implemented that slowed game speed by thirty percent, and the "stop button" feature was disabled. Under the 2011 strategy, the government pledged, *inter alia*, "to continue the moratorium on the addition of any new VLTs in Nova Scotia" and to "gradually reduce VLTs through natural attrition such that any electronic gambling machines available as a result of a business closing will be retired from the system and will not be transferable."

[505] Mr. Hurst admitted that he was aware of the introduction of the *Responsible Gaming Strategy* in 2011, but he did not contact the Atlantic Lotto Corporation again in regards to the North End Pub VLTs until the summer of 2013. With trial scheduled to begin in the fall, Mr. Hurst telephoned Scott Meek, Manager of Sales and Sales Support. Mr. Meek advised Mr. Hurst that he needed to pose his question in writing. To that end, Mr. Hurst e-mailed Mr. Meek as follows on June 24, 2013:

> Scott – on March 7, 2007 the North End Beverage Room was destroyed by fire. At that time we had 8 VLT machines generating $2700 net revenue per week or $140,000 per year. After the fire I sought and received assurances from Geoff Palmeter, then General Manager Atlantic Region for Atlantic Lotto that our 8 VLT machines would be grandfathered for our use when we reopened the North End Beverage Room in two to three years. We wanted then and now to rebuild an up-dated version of the North End building with a current theme North End Pub on the ground floor and apartments above ie the number of apartments depending upon the HRM approval process. Unfortunately in late 2007 our insurer, Lloyd's, denied our claim and we have been trying to get our case before the Courts ever since. After 6 and ¾ years our case will be heard beginning November 13th, 2013. We have also been seeking a Development Agreement with HRM including 70

> apartments and a rebuild of the North End Pub -6875 square feet with a strong food component/open-pizza oven/connected food and wine bar, etc. The Development Agreement is on scheduled to be approved by HRM in the Fall for completion mid 2015.
>
> The availability or not of the 8 VLT machines are [*sic*] the deciding factor for proceeding or not with the North End Pub. We have three other Pubs – Brewsters Bedford, Riverside Pub Bedford, Locals Bridgewater – all with VLT machines. As you know our focus in our pub business has been to significantly improve our food and beverage service and upgrade our VLT facilities in response to government policy.
>
> We make our case to you as the most experienced food and beverage operators in Nova Scotia, namely for 40 years. We have operated since 1973. We employ 530 people and the rebuild of the North End Pub means 30 jobs. It can also mean a boost to the attractive gentrification of the neighbourhood of north-end peninsular Halifax. We also make our case to you that the Responsible Gaming Strategy 2011 provides on page 5 that the viability of those businesses which are dependent upon VLT revenue for their existence are to be taken into account. Presumably it is also the intention that the jobs at stake are to be taken into account.
>
> We request confirmation that our 8 VLT machines will be available for the new North End Pub. With the Development Agreement and the Court case both a [*sic*] critical stages, it would [*sic*] much appreciated if this could be communicated to us soon.

[506] Mr. Meek responded to Mr. Hurst on July 4, 2013 as follows:

> Thanks for your enquiry regarding VL terminal availability for the development and rebuild of the North End Pub. The VLT program in NS has undergone some significant changes since 2007. The 2011 Responsible Gaming Strategy called for a reduction in both the number of available VLTs and retailer reliance on video lottery revenue. Retailers who experience a temporary site closure will have 12 months to have their site ready to receive terminals. Under this scenario you would not be eligible to retain your VLT's from 2007 and as such you would be considered a 'new' VL site. NSPLCC and Atlantic Lottery are currently reviewing its terminal placement policies in light of the direction set out on the strategy and are not evaluating opportunities for 'new' video lottery sites at this time.
>
> If this policy changes, I will be sure to inform you so you can plan accordingly. Please feel free to contact me should you have any questions or require clarification.

[507] Mr. Meek testified that after receiving Mr. Hurst's e-mail, he reviewed the records relating to the North End Pub, but found no evidence of an agreement

between Mr. Palmeter and Mr. Hurst. He also spoke to colleagues who worked at Atlantic Lotto in 2007 in an attempt to determine the practice at that time with respect to VLTs when a business closed temporarily. There were no written policies or guidelines that governed the situation. Based on second-hand information, Mr. Meek testified that, prior to 2011, Atlantic Lotto would return video lottery machines to customers if they were closed temporarily. As to the meaning of "closed temporarily," Mr. Meek could not say.

[508] Finally, Mr. Meek consulted with the Nova Scotia Provincial Lotteries and Casino Corporation. Applying current standards, they determined that too much time had elapsed. The North End Pub's closure would be considered a permanent one, and, as such, it would have to apply as a new retailer. Since applications by new retailers were not being accepted, the Pub would not be able to obtain VLTs.

[509] On the above evidence, I am unable to conclude that Mr. Palmeter agreed to any "grandfathering" of the North End Pub's VLT licenses. I find that Mr. Palmeter told Mr. Hurst that if the property was rebuilt within two to three years, the VLTs would probably be returned.

[510] In order for Marsh to be liable for this portion of the claim, I must be satisfied of two things. First, that it was foreseeable, at the time of Marsh's negligence, that a lengthy delay in payment of the insurance proceeds would result in the permanent loss of the North End Pub's entitlement to VLTs. Second, that without VLTs, a reincarnated North End Pub would not be financially viable. I conclude that the claim fails at the first stage.

[511] In my view, it was not reasonably foreseeable to Marsh that in early 2010, when the two-to-three year period mentioned by Mr. Palmeter was nearing expiration, Mr. Hurst would take no steps to ensure that the reincarnated North End Pub maintained its entitlement to VLTs. Nor was it reasonably foreseeable that the government of Nova Scotia would introduce a policy precluding the return of VLTs to retailers whose businesses had been closed for more than twelve months. Even if such a policy had been foreseeable, Marsh could not have foreseen that when the policy was released, a year beyond the timeframe agreed to by Mr. Palmeter, Mr. Hurst would not contact Atlantic Lotto to ensure that the reincarnated North End Pub would have its VLTs reinstated. In other words, the permanent loss of the VLTs was too remote.

[512] I would add that I have difficulty with Grafton Connor's allegation that Marsh should have foreseen the permanent loss of the VLTs, when such loss was

clearly unforeseeable to Mr. Hurst himself. Indeed, Mr. Hurst's confidence that the North End Pub's VLT licenses were not at risk was so high that he did not even contact Atlantic Lotto in 2011 when it introduced the *Responsible Gaming Strategy*. It was only in June 2013, with trial expected to begin in November, that he contacted Atlantic Lotto and learned that the Pub would not be entitled to the return of the VLTs. Almost a year later, with a month before trial, Grafton Connor moved to amend the Statement of Claim to add the claim for consequential damages.

[513] In sum, I find that Grafton Connor's permanent loss of the North End Pub's VLTs was not foreseeable. It follows that Grafton Connor is not entitled to damages for the loss of the business.

[514] In the event that I am wrong, I must decide whether a reincarnated North End Pub would be financially viable without VLTs. If not, I will provide a provisional assessment of damages.

[515] Daniel Jennings and Brian Keough, experts for Grafton Connor and Marsh, respectively, were each asked to prepare a quantification of the loss suffered by Grafton Connor as a result of its alleged inability to re-establish the North End Pub business. In order to quantify the future loss, both experts developed a forecast of the North End Pub's annual profitability for the years 2011-2013. In both cases, when one deducts the forecasted annual VLT revenues from the forecasted annual cash profits, the remaining profits are negligible. For this reason I accept that a new North End Pub without VLTs is not a viable proposition, and will provisionally assess Grafton Connor's future loss.

[516] Mr. Jennings, relying heavily on Grafton Connor's experience operating the Riverside Pub in Bedford, quantified Grafton Connor's future loss of the proposed North End Pub cash flow stream as falling within the range of $1,536,000 and $1,725,000. Mr. Keough, on the other hand, quantified the loss as falling within the range of $255,000 to $286,400.

[517] Having carefully reviewed each of the reports, I find that Mr. Jennings relied too heavily on Grafton Connor's experience operating the Riverside Pub to develop his forecasts, and, as a result, they are far too optimistic. While I accept the premise that a new or newly renovated location would attract greater sales volume than an existing operation, I do not believe the proposed North End Pub would achieve the kind of results predicted by Mr. Jennings. His forecasted gross profit percentage of 36.3 percent fails to adequately account for the significant

differences between the two operating environments. The Riverside Pub has a bigger footprint and is located in Bedford, which is larger, wealthier, and has been growing faster than the north end of Halifax. It benefits from the economies of scale of over $2.8 million in food sales earned from sharing a kitchen with the Sunnyside and the Sunnyside Too.

[518] Mr. Jennings's forecasts also fail to account for Grafton Connor's own gross profit experience operating the former North End Pub. The former operation had a history of unimpressive gross profit performance on food sales, with a blended 24.5 percent gross profit margin on sales in 2007. Mr. Jennings's forecasts yield an improvement of 87-139 percent over the track record of the former Pub. I agree with the opinion of Mr. Keough that a thirty percent gross profit margin is more suitable.

[519] For the purposes of a post-2013 forecast, I would adopt Mr. Keough's calculation of $141,000 cash profit for the year 2013. Like Mr. Keough, I find that the discount rates used by Mr. Jennings are too low. I would apply a rate of 18-20 percent. To arrive at a capitalization rate, I would use the midpoint of nineteen percent, deduct two percent for inflation and two percent for anticipated growth in sales, and I would add three percent for the anticipated continuing decline in VLT revenues. In my view, Mr. Keough's addition of five percent fails to account for the North End Pub's history of higher than average VLT profits due to its proximity to Stadacona. My calculation results in a total future economic loss of $783,333. That said, this figure includes the period of January 2014 to the start of trial in June 2014. In order to avoid double recovery, I must deduct an amount from this total for that period. I would therefore deduct $50,000 for this period, resulting in an award of $733,333.

Past Loss

[520] For its claim for past economic loss, Grafton Connor relies on the reports of Ross Cantwell, real estate consultant and developer, and Arthur Savary of the Altus Group Limited.

[521] Mr. Cantwell provided an opinion that if Grafton Connor had received the insurance proceeds immediately after the fire and proceeded with a planning application in 2007/2008, HRM would have approved a seven-to-eight story mixed-use development on the former North End Pub site. His report also stated that the most likely commencement date for building on the property would have been the fourth quarter of 2009. He estimated that construction would take about

fifteen months. With a building lease-up period of three months, occupancy would begin in the first quarter of 2011 and stabilize in the second quarter.

[522] Like all other expert reports in this proceeding, Mr. Cantwell's report was admitted by consent. It was argued at trial, however, that Mr. Cantwell was biased, and his report should be given no weight by this court. Mr. Cantwell acknowledged on cross-examination that he had been hired by Grafton Connor to assist with the planning application for the proposed development. At the time of trial, several items under his consulting contract remained outstanding. Once these tasks are completed, Mr. Cantwell will earn a further $8,000. Mr. Cantwell admitted that his role under the contract was essentially to be an advocate for the development project, but he also testified that this role did not impact the objectivity of his report.

[523] Neither defendant offered evidence to challenge Mr. Cantwell's timeline, and I am satisfied that the objectivity of his evidence was not compromised by his role as consultant for the development project.

[524] Mr. Savary was retained to provide his opinion as to the value of the loss of profit from the proposed mixed-use development. His opinion was based on the assumption that a development agreement with HRM would have been in place at commencement of construction in the fourth quarter of 2009. He noted in his report that he was advised by Mr. Cantwell that development approval at that time would most likely have been for a building with a total of seven stories, rather than eight. The building would have sixty apartments.

[525] Mr. Savary was retained in July of 2013, not long after Mr. Hurst learned that the North End Pub would not be getting its VLTs back. This may be why Mr. Savary was not directed to assume that the ground floor commercial space would be occupied by a reincarnated North End Pub. As a result, Mr. Savary included loss of commercial rental income as a component of his estimate of lost profits.

[526] The first thing Mr. Savary established was the cost of the building in the fourth quarter of 2009. He accepted the Hanscomb estimate of construction costs had the building gone ahead in 2009 ($9,264,223). He noted that the Hanscomb estimate included some "soft" costs, but not others which Mr. Savary considered necessary for the purposes of his opinion. The inclusion of these additional soft costs brought the total construction costs to $10,516,824. He then estimated total annual revenue at $1,017,324, and net operating income at $699,651.

[527] Armed with the above information, Mr. Savary applied two alternative approaches to provide an estimate of the loss of net income and profit which could have been generated from the mixed-use development. Both approaches yielded similar estimates. His net operating analysis resulted in lost income of $463,792, while the development approach resulted in a damage amount of $416,126. Mr. Savary blended the results and arrived at a total loss of profit of $440,000.

[528] As I previously indicated, any losses associated with Grafton Connor's decision to construct a multi-storey mixed-use development rather than a standalone operation are too remote to recover against Marsh. Grafton Connor's entitlement to damages for past economic loss is limited to the foreseeable consequences of Marsh's negligence. I conclude that Grafton Connor is entitled to damages for loss of the profits it would have earned from the operation of a replacement standalone North End Pub. The period of loss would begin at the time Grafton Connor would have completed construction of the new building, and conclude as of June 2014.

[529] Regrettably, the parties adduced no evidence as to the time required to construct a new standalone North End Pub. Furthermore, while Mr. Jennings and Mr. Keough did provide a quantification of past loss in their reports, they each assumed a start date of 2011 and a trial date of November 2013.

[530] Where a plaintiff establishes that a loss has occurred but the evidence is insufficient to enable a precise quantification of that loss, the court must do the best it can to arrive at an appropriate damage award: *All-Up Consulting Enterprises Inc v Dalrymple, supra,* at paras 196-197; *Penvidic Contracting Co v International Nickel Co of Canada,* [1976] 1 SCR 267, 1975 CarswellOnt 299 at paras 22-24.

[531] The North End Pub was destroyed in March 2007. If Grafton Connor had received the insurance proceeds without delay and immediately set about rebuilding the Pub, I estimate that construction would have been completed by December 2008. This results in a period of loss of 5.5 years (January 2009 to June 2014).

[532] In their reports, Mr. Jennings and Mr. Keough each developed forecasts of the annual profitability for the proposed North End Pub for the years 2011, 2012 and 2013. Mr. Jennings's low forecast was $144,000/$168,000/$167,000, and his high forecast was $213,000/$197,000/$205,000. Mr. Keough's forecast for 2011-2013 was $88,000/$122,000/$141,000.

[533] As discussed above, I believe Mr. Jennings's forecasted gross profit margin was too high. For this reason, I prefer to use Mr. Keough's forecast as a guide. For the years 2009 and 2010, I would estimate profits of $88,000 and $100,000, respectively. For 2011, I would estimate profits of $115,000. For 2012 and 2013, I adopt the figures of Mr. Keough. Finally, from January of 2014 to the start of trial, I estimate lost profits of $71,000. In the result, I find Grafton Connor is entitled to $637,000 for past loss of profit.

[534] In the event that I am wrong about the foreseeability of Grafton Connor's decision to proceed with a multi-storey mixed-use development, I have only Mr. Savary's evidence as to the appropriate quantum of past loss of rental income. Mr. Savary was not cross-examined and his evidence was otherwise unchallenged. That said, Mr. Savary calculated pass loss of rental income from 2011 until November 2013, not June of 2014. Moreover, he was not directed to assume that the ground floor commercial space of the development would be occupied by the new North End Pub. He therefore calculated net operating income from renting the commercial space at $128,436. As a result, the total net operating income figure that he used ($699,651) to arrive at his conclusion of $440,000 in lost profit is too high.

[535] To account for the period of November 2013 to June 2014, a period of nine months, I would add $110,000 to Mr. Savary's figure for a total of $540,000. I would then deduct $150,000 from the $540,000 total to account for his inclusion of commercial rental income in his calculations. This yields a total award of $390,000 for past loss of rental income from 2011 – June 2014.

[536] Assuming the reincarnated North End Pub would have commenced operations in 2011, I would adopt Mr. Keough's forecast for 2011-2013, and add $68,000 for the period of January 2014 to June 2014. This results in past loss profits from the North End Pub business of $419,000. Added to the amount for past loss of rental income, the total award for past loss of income would be $809,000.

[537] In sum, I find that Grafton Connor is entitled to an award equivalent to the profits it would have earned if it had rebuilt a standalone North End Pub, with construction being completed by December 2008. I have estimated those profits at $637,000.

[538] If Grafton Connor's decision to proceed with a multi-storey mixed-use development was foreseeable, I would make a provisional award of $809,000 for

past income loss, which includes lost income from residential rent and a reincarnated North End Pub.

Aggravated and Punitive Damages

[539] Grafton Connor claims aggravated and punitive damages against both defendants. The same conduct serves as the basis for both types of damages claimed.

[540] In *Hill v Church of Scientology of Toronto*, [1995] 2 SCR 1130, [1995] SCJ No 64, which involved an action for defamation, the Supreme Court of Canada defined aggravated damages as follows:

> 188 Aggravated damages may be awarded in circumstances where the defendants' conduct has been particularly high-handed or oppressive, thereby increasing the plaintiff's humiliation and anxiety arising from the libellous statement. …
>
> 189 These damages take into account the additional harm caused to the plaintiff's feelings by the defendant's outrageous and malicious conduct. Like general or special damages, they are compensatory in nature. …

[541] The British Columbia Court of Appeal explained the concept of aggravated damages in *Huff v Price*, [1990] BCJ No 2692, [1990] CarswellBC 267, as follows:

> 51 So aggravated damages are an award, or an augmentation of an award, of compensatory damages for non-pecuniary losses. They are designed to compensate the plaintiff, and they are measured by the plaintiff's suffering. Such intangible elements as pain, anguish, grief, humiliation, wounded pride, damaged self-confidence or self-esteem, loss of faith in friends or colleagues, and similar matters that are caused by the conduct of the defendant; that are of the type that the defendant should reasonably have foreseen in tort cases or had in contemplation in contract cases; that cannot be said to be fully compensated for in an award for pecuniary losses; and that are sufficiently significant in depth, or duration, or both, that they represent a significant influence on the plaintiff's life, can properly be the basis for the making of an award for non-pecuniary losses or for the augmentation of such an award. An award of that kind is frequently referred to as aggravated damages. It is, of course, not the damages that are aggravated but the injury. The damage award is for aggravation of the injury by the defendant's high-handed conduct.

[542] Our Court of Appeal recently summarized the principles applicable to punitive damages in *National Bank Financial Ltd. v. Barthe Estate*, 2015 NSCA 47:

> 438 The legal principles to be considered when deciding whether to award punitive damages may be gleaned from a series of cases from the Supreme Court of Canada starting with *Whiten v. Pilot Insurance Co.*, 2002 SCC 18; *Fidler v. Sun Life Assurance Co. of Canada*, 2006 SCC 30; and *Honda Canada Inc. v. Keays*, 2008 SCC 39.
>
> 439 From these and other leading authorities we know that the discretion to award punitive damages "should be most cautiously exercised" and courts "should only resort to punitive damages in exceptional cases". Punitive damages require proof of conduct that amounts to "an independent actionable wrong", typically seen as so shocking as to "depart markedly from ordinary standards of decency ... so malicious and outrageous (to be) ... deserving of punishment on their own". Punitive damages "are directed to the quality of the defendant's conduct, not the quantity (if any) of the plaintiff's loss". The aim of punitive damages "is not to compensate the plaintiff, but rather to punish the defendant". They are "the means by which the jury or judge expresses its outrage at the egregious conduct of the defendant". Punitive damages are intended to punish the wrongdoer, express the court's clear denunciation and serve as a deterrent not only to the wrongdoer, but others who may be inclined to follow the same example.

[543] Punitive damages must be proportionate to the blameworthiness of the defendant's conduct, and should only be awarded in cases where "all other penalties have been taken into account and found to be inadequate to accomplish the objectives of retribution, deterrence, and denunciation": *Whiten v Pilot Insurance Co*, 2002 SCC 18, [2002] SCJ No 19 at para 123.

[544] Grafton Connor cites three instances of conduct on the part of Underwriters that it says warrant aggravated and/or punitive damages. First, it says Underwriters failed to investigate whether it was entitled to void the Policy. Grafton Connor stated at p 116 of its post-trial brief:

> Lloyd's conduct in voiding the policy, denying liability and maintaining a defence through six years of litigation based on the justification that they were entitled to do so without at any point making any effort to assess the terms of their own Policy to determine whether they were justified in doing so cries out for compensation to Grafton Connor and a significant sanction to Lloyd's.

[545] In other words, Grafton Connor alleges that Underwriters voided the Policy without considering whether Endorsement 10 applied to excuse the misrepresentations.

[546] Second, Underwriters failed to return the premium Grafton Connor paid to insure the North End Pub from 2003 until the date of the fire. Having taken the position that the Policy with respect to the Pub was void *ab initio*, Underwriters was obligated to return the premium.

[547] Finally, Grafton Connor says the delay by Underwriters in voiding the Policy warrants exemplary damages. Notwithstanding the adjuster's discovery that the Pub was not equipped with sprinklers and not completely masonry construction, Underwriters continued to conduct itself as though coverage would be provided. It hired contractors to assess the site, demolish the remnants of the premises, and provide property evaluation. Grafton Connor says these actions by Underwriters signified that the errors in the description of the premises were immaterial and indemnity would be provided.

[548] As discussed earlier, the law is unsettled as to whether a finding of bad faith may be made against an insurer in the absence of coverage. Moreover, a finding of bad faith does not necessarily lead to an award of exemplary damages.

[549] Assuming without deciding that this court can find a breach of the duty of good faith by Underwriters notwithstanding the decision on coverage, I am not satisfied that aggravated or punitive damages are appropriate in the circumstances.

[550] If I had concluded that Endorsement 10 applied, a failure by Underwriters to consider the provision in the course of its investigation may have been a breach of the duty of good faith. Having found otherwise, there is no basis for aggravated or punitive damages.

[551] It is common ground that Underwriters, contrary to its obligation, has not returned the premium for the North End Pub to Grafton Connor. On October 8, 2007, Underwriters officially denied Grafton Connor's claim. Ian Harrison, the claims adjuster for Underwriters, drafted the denial letter which included the following paragraph:

> In light of the above, the insurers have no alternative but to void such coverage from inception and we shall take steps forthwith to return that portion of the premium that relates to the property in question, as the insurers are bound to do.

[552] Mr. Harrison testified that in the London market, the premium is collected by the broker. After deduction of the broker's commission, the balance is forwarded to Underwriters. The premium goes into a central accounting system in which Marsh UK has an account. Once the premium arrives in the Marsh UK account, it is distributed to the subscribing underwriters in relation to their proportion of the risk.

[553] In the event that a premium is returned, Underwriters would expect an endorsement from the broker. The endorsement, having been signed by the subscribing underwriters, is then entered into the central accounting system whereby the money is collected from the participating insurers on the slip and refunded as a whole amount into Marsh UK's account.

[554] Mr. Harrison explained that the denial letter was sent to Marsh UK by regular mail and by e-mail. In his e-mail to Marsh UK attaching the letter he wrote, in part:

> I assume that you will present our underwriters with an endorsement(s) to enable the appropriate refund of premium to be made to your client in due course, however if this is not the case please contact me in order that we can make the appropriate arrangements.

[555] According to Mr. Harrison, Marsh UK did not respond. Mr. Harrison then spoke to Christian Corby and asked him to follow up with Marsh UK. Mr. Harrison did acknowledge that, notwithstanding any arrangements between Marsh UK and Underwriters, it is the underwriter's obligation to return the premium to the insured. He was not sure why that did not occur, and he apologized to Grafton Connor for the omission.

[556] Like Mr. Harrison, Mr. Corby testified that the broker would normally return the premium to an insured, and that he had asked Marsh UK for the necessary endorsement. On July 9, 2008, Mr. Corby e-mailed David James at Marsh UK:

> Further to our recent conversations regarding our request for an endorsement to the above insured's policy to enable a return premium (for years of account from 2003 through to 2006) to be paid to them in respect of the North End Beverage Room property, could you advise status.

According to Mr. Corby, Mr. James never responded to his request.

[557] It is clear that Underwriters never returned the premium to Grafton Connor, despite being aware of its obligation to do so. While Underwriters did make several requests to Marsh UK for an endorsement, the responsibility to return the premium ultimately belongs to Underwriters. When Mr. James failed to respond to Mr. Corby's e-mail, Underwriters should have taken the necessary steps to return the premium to Grafton Connor without Marsh UK's assistance. Failure to do so, in my view, is a breach of the duty of good faith. In the circumstances of this case, however, I am not satisfied that the failure to return the premium was so high-handed and oppressive as to cause the degree of suffering contemplated by an award of aggravated damages. Nor do I find the failure to return the premium to be so shocking, outrageous or malicious as to merit an award of punitive damages.

[558] As to the delay in voiding the Policy, I am not satisfied that, prior to October 2007, Underwriters had the necessary information to ascertain whether it had ever been provided with information by Marsh UK that the Pub was not sprinklered.

[559] The fire occurred on March 7, 2007. On that same day, Michael Maloney retained Len Costello of Crawford Adjusters Canada to adjust the loss. He sought and obtained confirmation from Underwriters through Marsh UK that his choice of adjuster was acceptable.

[560] Mr. Costello arrived on the scene while the Pub was still burning and began his investigation. On March 13, 2007, Mr. Costello met with Steve McMullin and Gary Muise, and questioned both about the presence of a sprinkler in the Pub. Both told him that they were uncertain whether the Pub was sprinklered. Neither volunteered to call Gary Hurst.

[561] Two days later, Mr. Costello received approval from Underwriters to retain Fred Dunphy Excavating and Construction Ltd. to perform debris removal, and Michael Geislinger, a structural engineer, to do a basement consultation. He was also directed to retain SPECS for a building appraisal, and to hire site security.

[562] Mr. Costello wrote to Mr. Muise on March 19, 2007, explaining the investigation to date and providing Grafton Connor with a proof of loss. The letter contained the following express reservation of rights:

> Reservation of Rights
>
> My investigation to date, and my discussions with yourselves, relating to both damages and evaluation, and my activities to date on behalf of the insurers, should by no means be construed as having waved [*sic*] any of the rights or

> privileges available to either yourself or the insurers under the terms of the policy conditions.
>
> The insurers retain and will continue to maintain all of their rights and privileges as spelled out in the contract of insurance.

[563] By April 27, 2007, Mr. Costello was still uncertain as to whether the Pub had been sprinklered. After speaking with Mr. Muise and Mr. McMullin, he had consulted with the fire inspectors with HRM and asked if they had any record of the building ever being inspected or approved as sprinklered. He had also spoken with Fred Dunphy to ask whether he noticed any evidence of a sprinkler system when he did the debris removal. Neither inquiry was helpful. Mr. Costello then put the question to Michael Geislinger, the structural engineer. Mr. Geislinger wrote to Mr. Costello on May 25, 2007, confirming that there was never a sprinkler system at the Pub. This information was passed on to Underwriters in Mr. Costello's report of June 7, 2007.

[564] Mr. Harrison testified that it was only after receiving Mr. Costello's report that Underwriters knew for certain that the North End Pub was not sprinklered. On June 20, 2007, having been informed by Martin Pope and Christian Corby that the sprinkler information would have been material in writing the risk, Underwriters retained Canadian legal counsel.

[565] On July 17, Matthew Liben of Stikeman Elliott wrote to Grafton Connor, in care of Marsh, advising of his engagement. Noting that Underwriters had appointed an adjuster to investigate the claim, Mr. Liben emphasized that this should not be construed as an admission of coverage:

> However, you should understand that the appointment of an adjuster and the investigation in this claim are done without waiving, prejudicing, or invalidating any rights or positions of the Underwriters. The investigation and appointment of any adjuster is also done without admitting coverage or liability in any matter or manner whatsoever in connection with the investigation. In particular, the Underwriters reserve all rights to fully deny any coverage under the Policy, for any reason whatsoever, and to set up any and all defences of non coverage under the Policy should Underwriters ultimately determine that such a position is appropriate. Underwriters are not in any way representing that they will provide indemnification for any claims, losses, or damages advanced by any insured with respect to this matter.

[566] Mr. Harrison testified that Underwriters does not take declining coverage lightly, and once it knew that the Pub was not sprinklered, it wanted to be certain

that this information had never been provided to it by Marsh UK prior to the fire. Mr. Harrison explained that in the London market, the placing broker retains the submissions on the initial placement and renewals. For this reason, Underwriters had to request copies of the documents from Marsh UK. On July 4, 2007, Elizabeth Parsons of Marsh UK e-mailed Christian Corby as follows:

> As per your request to Ann attached are the Schedules for 2004, 2005 and 2006 for Grafton Connor (which were all saved in our system). We do not have the 2003 schedule electronically, however, I have attached a copy of the slip which shows the TIV and breakdown for buildings, contents and BI (page 7). I am also requesting the 2003-2006 files from archiving to see if there are any survey reports on these files.

[567] Mr. Harrison testified that the 2004-2006 schedules referenced in this e-mail were Excel versions, not the copies that had been scratched by Underwriters, and the "sprinklered" column was missing. Underwriters proceeded to ask for the scratched copies. Marsh UK eventually provided the scratched versions, but it did not confirm whether there were any engineering reports, survey reports or proposal forms in the archives until September 20, 2007.

[568] Upon receipt of this information, Underwriters was able to obtain a formal coverage opinion from Stikeman Elliott, which it received in the late September. Between the end of September and the sending of the denial letter on October 8, Mr. Harrison needed to confirm that Mr. Pope and Mr. Corby remained of their earlier view that the misrepresentations had been material to their assessment of the risk. As Mr. Pope was out of the country on business, Mr. Harrison had to wait several days to obtain his approval to issue a denial of coverage.

[569] In my view, it is difficult to criticize Mr. Costello or Mr. Harrison for the speed with which their investigations were conducted. Len Costello testified that no one at Grafton Connor or Marsh ever complained that his investigation was taking too long, and, after hearing Mr. Costello's testimony and reviewing his time records, I am satisfied that his investigation was thorough, competent, and carried out without delay on his part. As for Mr. Harrison, he was cognizant of an insurer's duty to conduct its investigation in good faith, and he prudently waited to deny coverage until he could be certain that no information had ever been put before Underwriters that the Pub had no sprinklers. While the delay on Marsh's part in obtaining the documents was unfortunate, it would have been reckless and inappropriate for Underwriters to deny coverage without having first completed its investigation.

[570] As to Grafton Connor's claim that Underwriters conducted itself as though coverage would be provided, and that its actions signified an acceptance of the obligation to indemnify Grafton Connor, I disagree. The hiring of contractors to clean up the site after the fire was in the interests and for the protection of all parties involved, regardless of the outcome of the investigation. If Underwriters had not retained Mr. Dunphy, the municipality would surely have ordered Mr. Hurst to clean up the unsightly and hazardous remains of the building. Moreover, I find that Underwriters, through Mr. Costello and Stikeman Elliott, made it clear that its conduct should not be interpreted as an admission of coverage.

[571] Against Marsh, Grafton Connor bases its claim for aggravated and punitive damages on the following: (1) the extent of negligence displayed by Marsh; (2) the failure to return the premium; and (3) the delay in responding to requests from Underwriters after the fire loss.

[572] While I am not convinced that any of these actions or omissions by Marsh amount to an independent actionable wrong upon which I can order punitive damages, it is of no consequence for the reasons that follow.

[573] Grafton Connor argued in its post-trial brief that Marsh's negligence and incompetence has been a pervading theme of the evidence, and that "no client of Marsh deserves to have their insurance, an important aspect of protecting the business, treated in such a cavalier fashion" (p 119). As I commented earlier, the evidence discloses multiple examples of careless conduct on Marsh's part. The same can be said, however, of Grafton Connor.

[574] I am not satisfied that Marsh's carelessness was high-handed, or caused Grafton Connor the increased distress essential to an award of aggravated damages. Nor was it sufficiently outrageous or shocking to justify punitive damages. Punitive damages are available only where all other penalties are inadequate to accomplish the objectives of retribution, deterrence, and denunciation. In this case, the damages ordered against Marsh as a result of its negligence are substantial enough to achieve these objectives.

[575] Like Underwriters, Marsh failed to take steps to have the premium returned to Grafton Connor. While I acknowledge that this would have been frustrating to Grafton Connor, the primary obligation to return the premium belongs to Underwriters. Having held that neither aggravated nor punitive damages are appropriate against Underwriters in the circumstances, it follows that these damages are similarly unavailable against Marsh.

[576] Finally, Grafton Connor says that its claim proceeded in a slow and protected way due to the delays caused by Marsh in failing to provide the documents requested by Underwriters. I do not accept that Marsh is solely responsible for the speed, or lack thereof, with which the claim progressed. A significant portion of the delay can be attributed to Grafton Connor's inability to conclusively advise Mr. Costello whether the Pub was sprinklered, despite Mr. Hurst's evidence that he always knew the Pub had no sprinklers. Given the uncertainty, Mr. Costello had to make other inquiries, and ultimately engaged the structural engineer to confirm that the Pub was not sprinklered.

[577] When Underwriters requested documents from Marsh UK in July 2007, it did take Marsh UK an inordinate amount of time to retrieve them from its archives. That said, I am not satisfied that this delay was outrageous or high-handed.

Marsh's Crossclaim

[578] Marsh's crossclaims against Underwriters for any damages it is ordered to pay to Grafton Connor. In the absence of a finding of liability against Underwriters, the crossclaim has no basis in law and must be dismissed.

Underwriters's Counterclaim

[579] Underwriters counterclaims against Grafton Connor for $95,000 -- the amount it paid to Fred Dunphy for debris removal. Grafton Connor alleges in its pleadings that when Len Costello obtained authorization from Underwriters to hire Mr. Dunphy, he did so with knowledge of the misrepresentations concerning the sprinklers and the construction. It says that Underwriters's failure to pay Mr. Dunphy for the work performed amounts to a breach of the duty of good faith.

[580] In order to recover his fees, Mr. Dunphy filed an action on April 4, 2008, against Grafton Connor, Marsh and Underwriters. In the fall of 2012, Underwriters settled the claim and the proceedings were dismissed by an order dated October 31, 2012. Underwriters now seeks recovery of the settlement amount from Grafton Connor.

[581] Mr. Harrison explained that unlike "adjustment costs" that are paid regardless of the outcome of the investigation, indemnity for the cost of debris removal was contingent upon a finding of coverage under the Policy. He testified that at the time Mr. Dunphy presented his invoice, Underwriters was not in a position to pay the fees because it was still investigating the circumstances of the

loss to determine whether coverage would be triggered under the Policy. If Underwriters had made such an indemnity payment under the Policy, it would have affirmed coverage prior to completion of the investigation.

[582] I do not accept that at the time he retained Mr. Dunphy, Mr. Costello had knowledge that the Pub was not sprinklered. He did not receive confirmation of that fact until he reviewed the report from Mr. Geislinger in May 2007. In my view, payment by Underwriters of the invoice prior to completion of the investigation would have been inconsistent with its position that a decision on coverage had not been made. If Underwriters had paid Mr. Dunphy in the weeks after the fire, Grafton Connor would surely have argued that its conduct signaled its acceptance of the obligation to cover the loss.

[583] Grafton Connor has been enriched by payment of the invoice, and Underwriters has suffered a corresponding deprivation. In the absence of coverage under the Policy, there is no juristic reason for that enrichment. I allow the counterclaim.

Summary of Damages

[584] I have concluded that Marsh was negligent in its handling of the Grafton Connor account, and that this negligence caused Grafton Connor to lose its right to indemnity from Underwriters under the Policy. However, I found Grafton Connor liable in contributory negligence for fifty percent of its own losses. Having determined that the Policy is a blanket policy and that the co-insurance provision does not apply, the value of the claim under the Policy is $2,740,869.16: $2,174,514.02 for the building, $411,357.61 for the contents, and $154,997.53 for business interruption. Marsh and Grafton Connor are each liable for $1,370,434.58 or fifty percent of that amount.

[585] In addition to the value of the claim under the Policy, Grafton Connor claimed damages against both defendants for consequential losses arising from the delay in being able to redevelop the property. In light of my finding that Grafton Connor contributed to its own losses, any award for consequential damages must be reduced by fifty percent.

[586] I dismissed the claim against Underwriters, finding that Grafton Connor failed to establish the necessary breach of the duty of good faith. As for the claim against Marsh, I was satisfied that Grafton Connor did not have the financial

capacity to rebuild the North End Pub prior to trial and that this inability to rebuild was foreseeable to Marsh.

[587] Grafton Connor claimed that as a result of the delay, it would have to incur increased construction costs when it redeveloped the site. I found it was not foreseeable that Grafton Connor would use the insurance proceeds to construct a multi-storey mixed-use development instead of simply replacing the original stand-alone Pub. For this reason, Grafton Connor's award was limited to the increased cost to rebuild a standalone Pub, which I estimated at $405,981.77. I also allowed an award of $15,364.81 for the increased cost to replace the contents.

[588] Grafton Connor also alleged that it lost the ability to obtain VLTs for a reconstructed North End Pub, resulting in the loss of the business. I held that it was not foreseeable to Marsh that a lengthy delay in payment of the insurance proceeds would result in the permanent loss of the North End Pub's VLTs. As a result, Grafton Connor was not entitled to damages for the loss of the business.

[589] Finally, Grafton Connor advanced a claim for the loss of profits it could have generated from the development during the period it had been delayed. Having decided that any losses incurred by Grafton Connor as a result of its decision to build a multi-storey mixed-use development were too remote, I made no award for lost rental income. I concluded that Grafton Connor was entitled to the profits it would have earned if it had rebuilt a standalone Pub, with construction being completed by December 2008. I estimated those damages at $637,000.

[590] With respect to aggravated and punitive damages, I was not satisfied that either was appropriate in the circumstances.

[591] I dismissed Marsh's crossclaim against Underwriters, and allowed Underwriters's counterclaim against Grafton Connor for $95,000 that it paid for debris removal.

Summary of Provisional Damages

[592] In the event that the loss of the North End Pub's VLTs was foreseeable, I provisionally award $733,333 for future loss of profits.

[593] In the event that Grafton Connor's decision to build a multi-storey mixed-use development was foreseeable, I provisionally award $1,163,586.41 for

increased construction costs, and $809,000 for lost profits from residential rent and a reincarnated North End Pub.

Conclusion

[594] The lesson to be gleaned from this case is that assumptions have no place in the world of insurance. Gary Hurst assumed that Mr. Raymond knew enough about the properties to handle placing the insurance. Mr. Raymond assumed that Marsh was collecting the information about Grafton Connor's properties and warranting its accuracy. Mr. McMullin assumed that all of the information that predated him was accurate. Marsh assumed that Mr. Raymond and Mr. McMullin were sophisticated in the placement of insurance and recognized that "business value" meant "replacement cost". In the end, the failure by both parties to ask a few simple questions cost them dearly.

[595] It is common ground that Grafton Connor has not received a refund of the premium it paid to insure the North End Pub from 2003-2007. Underwriters acknowledges its obligation to return the premium and I order that it do so within thirty days of this decision.

[596] Although prejudgment interest was claimed by Grafton Connor, none of the parties took a position as to the appropriate rate. I will accept submissions on this issue within 45 days of this decision.

[597] If the parties are unable to agree on costs, they may submit their positions to me within 45 days of this decision.