LIABILITY OF INSURANCE AGENTS FOR FAILURE TO OBTAIN EFFECTIVE COVERAGE: FINE'S FLOWERS LTD. v. GENERAL ACCIDENT ASSURANCE CO.[1]

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[I]f an insurance agency holding itself out as competent in its field of enterprise to service the needs of the plaintiff were not found liable under our general laws of negligence, there would be a genuine basis for disquietude with the ability of the law to refine and develop its concepts coincident with the ever changing realities of commerce.[2]

So you think you're covered[3] reads the title to a recent American book on insurance. As the title implies, and as many Canadians have much to their disappointment come to realize, there are many situations where individuals think they are protected by insurance but in fact are not. The reasons for this divergence between reasonable expectation and reality are many; some are fundamental to the present nature of the insurance industry,[4] while the rest arise from a variety of bases. However, it appears from recent cases on the topic, that one significant reason for ineffective coverage is the misplaced faith in the insurance agent who arranges, or more correctly in these cases who fails to arrange, the coverage. The "insured" must therefore seek recovery from the agent rather than the "insurer." The alternative bases for the agent's liability were explored in *Fine's Flowers*[5] and will be considered in this comment. In order to appreciate the extent of the duty imposed upon the agent in this case, it is necessary to set out the facts in some detail. Then the three bases of liability invoked in the case — breach of contract, negligence, and breach of equitable duty — will be considered.

Fine's Flowers Ltd., Harry Fine president and principal owner, ran a number of retail stores and garden centres in Ottawa. Mr. Fine "believed in insurance."[6] He began insuring through Frank Ault, an insurance agent, in the 1920's and dealt with him or his successors thereafter. At all relevant times the successor company was Ault,

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1. (1974), 5 O.R. (2d) 137, 49 D.L.R. (3d) 641 (H.C.); aff'd, (1977), 17 O.R. (2d) 529, 81 D.L.R. (3d) 139 (C.A.) (hereinafter referred to as *Fine's Flowers*).
2. (1977), 17 O.R. (2d) 529, at 534; 81 D.L.R. (3d) 139, at 144-45 (C.A.), per Estey, C.J.O., as he then was.
3. S. Leinwoll, *So you think you're covered: A consumer's guide to home insurance* (1977).
4. It seems that one of the principal reasons is that in a competitive insurance industry, the marketers of insurance must package the risks they agree to cover so as to provide attractive and yet reasonably priced offerings. It is to be expected that they will thus exclude certain risks that might otherwise have been included. The consumer however may not inquire as to just which risks are covered and which ones are not until a time when the issue has become much more important to them — after a loss. It is frequently only then that the insured finds out what it is that he has in fact purchased.
5. *Supra* n. 1. *See generally* R. Shibley, "Actions against Agents and Brokers" (1962), L.S.U.C. Special Lectures 241.
6. *Supra* n. 2, at 536; 81 D.L.R., at 146, per Wilson J.A.

Kinney, Campbell and Gallichan Ltd., which had been purchased by Campbell in 1958. Mr. Fine dealt directly with Mr. Campbell.

On January 10, 1968, the heating system in some of Fine's greenhouses failed and the horticultural crops were destroyed. Thinking that he was covered by insurance, Fine contacted Campbell. Campbell in turn notified General Accident Assurance Company of Canada with whom he had placed Fine's insurance. When General refused to pay, Fine sued both General and Ault.

The insurance policy was a boiler and machinery policy covering loss from an "accident" to an "object," both terms being defined. The evidence disclosed that the heating system had failed when two water supply pumps which were connected to the boilers failed. The pump failure occurred when the bearings of the electric motor on one pump burned out, the pump seized, and a resulting short circuit tripped the circuit breakers and the electricity was cut off to both supply pumps. The boilers, in turn, were shut down by an automatic safety device triggered by the inadequate water supply and thus the heat went off. The bearing had burned out as a result of ordinary wear. The definition of "accident" in the policy excluded loss from "wear and tear." Moreover the pumps were not "objects." The only objects identified were the boilers. On this basis, the plaintiff's claim against the defendant General was dismissed.[7] However, the claim against the defendant agents, Ault, Kinney, Campbell and Gallichan Ltd., was successful.

The evidence indicated that Fine had relied on Campbell to make sure that he had adequate insurance coverage. Fine did not give explicit instructions on what he wanted; he simply indicated he wanted everything covered. Having done that, Fine relied on Campbell to secure coverage against any risks that could reasonably be anticipated. As the trial Judge stated, the reasonable inference from the evidence was "that there was a contractual agreement binding on. . . [Campbell to] keep the plaintiff covered for all foreseeable, insurable and normal risks. . . ."[8] Moreover, the agent had known Fine wanted and expected full coverage and thus, he had undertaken the responsibility of providing it.

The liability of the agent was based on three different grounds by the various judges who heard the case. Mr. Justice Fraser at trial and Madame Justice Wilson (Blair, J.A., concurring) in the Court of Appeal based liability on breach of contract and breach of equitable duty. Chief Justice Estey, concurring in the result, based liability on

7. (1974), 5 O.R. (2d) 137, at 140; 49 D.L.R. (3d) 641, at 644 (H.C.). This aspect of the case was less than satisfactorily dealt with; it was conceded at trial that the plaintiff had no claim against the insurer. *Id.*

8. *Id.*, at 146; 49 D.L.R., at 650.

negligence and breach of equitable duty.[9] Each of the three bases of liability will be considered in turn.

The basis of the claim in contract was that the agent, in failing to procure coverage for the loss, was in breach of his contract to acquire and maintain full coverage. The defence position was that no such contract had been undertaken and in any event the coverage necessary could not have been obtained from any insurer. The trial Judge, as stated earlier, found a contract to insure "all foreseeable, insurable and normal" risks[10] and since the loss was foreseeable, held that there was a breach of contract.

On appeal, Madame Justice Wilson agreed that there was a breach of contract. However, the problem she encountered was in determining what the contract to provide "full coverage" really required. The defendant argued that coverage against what took place could not have been obtained. Although this was not proved, it was still necessary to decide what full coverage meant. Was it just coverage against ordinary risks, *e.g.*, accident, or did it also include extraordinary risks, including ordinary wear and tear? It was submitted that a reasonable interpretation was that coverage only against ordinary risks was required and that an agent who acted according to a reasonable interpretation of his agreement was not in breach of duty. Had the agents insured the pumps and motors against accident there would still have been no coverage on these facts. Therefore, could the agents be held in breach of contract for doing nothing, when if they had acted according to this reasonable interpretation, it would have made no difference in the result? In essence, did their breach cause any damage? But that defence was held not to be applicable on the facts of the case. The defendants did not misconstrue their instructions as requiring only insurance on the motors and pumps against accident. They claimed there was no need to insure motors and pumps at all. Their only defence would have been that "full coverage" did not involve the pumps and motors at all; but "full coverage" required coverage against all foreseeable insurable risks and this risk was both foreseeable and insurable. In fact, the evidence disclosed that about four years before the loss, the insurer had conducted an inspection of Fine's premises and quoted a

9. By allowing recovery in negligence without deciding the issue of whether there was a contract which had been breached, Chief Justice Estey would seem to be at variance with the Supreme Court of which he is now a member. The decision of the Supreme Court of Canada in *J. Nunes Diamonds Ltd. v. Dominion Electric Protection Co.*, [1972] S.C.R. 769, 26 D.L.R. (3d) 699 appears to indicate that a tort suit is only permissible, where parties are governed by a contract, if the negligence can properly be described as an independent tort unconnected with the performance of the contract. The negligence here did clearly relate to the performance of a contract if one existed and thus according to the Supreme Court the action should not have been allowed. However, since this comment is limited to Insurance law and Estey, C.J., did not mention this matter I will not pursue it here.

10. *Supra* n. 8.

premium to the agent for insurance on the pumps and motors. Apparently no discussion of this matter took place with Mr. Fine nor was any reply ever sent. If Campbell had not realized the potential for loss due to a failure of the pumps and motors before that correspondence, he must have known after it. On this basis, Wilson, J.A. found a breach of contract and concluded that this breach had caused the loss.

Estey, C.J.O., felt it "possible to circumvent the complex line of reasoning necessary to lead to liability in contract. . ."[11] and found liability in negligence as well as in equity. The negligence claim arose in Chief Justice Estey's view out of the undertaking to provide the plaintiff with insurance against foreseeable losses. The defendant did not procure coverage on the pumps and motors and did not draw this fact to the attention of the plaintiff. It was the agent's duty to do one or the other; having done neither, the agent was liable in negligence. Again, the possible defence of carrying out his duty according to a reasonable interpretation was not open. The agent had not obtained any coverage against what Estey characterized as "the most obvious and fundamental of all risks"[12] *i.e.*, failure of the heating system in winter. Since the agent obtained no coverage whatsoever, he could not use the defence that even if he had procured normal risks coverage it would not have been sufficient. In fact, they did neither and were negligent in that respect and also in failing to so indicate to the insured. If Campbell had indicated the gap in coverage to Mr. Fine, a decision could have been taken as to the next step: either to discontinue all insurance, or to make other arrangements for heating, or to obtain full coverage at whatever that might cost. Proper performance of his duty would have required the agent to act in some way other than he actually did. The agent's breach prevented Fine's Flowers from having even an opportunity to protect themselves. The agent's negligence therefore caused the loss.

All the judges also found liability in equity. They held that in certain circumstances equity imposes a special duty by reason of the relationship of the parties, a duty which is not necessarily dependent on a contractual provision but which imposes fiduciary duties and obligations.[13] Where the relationship exists, it creates a special duty in making statements and giving advice. The claim is essentially one "for dereliction of duty by a person occupying a fiduciary relation."[14]

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11. *Supra* n. 2, at 532; 81 D.L.R., at 143.
12. *Id.*, at 533; 81 D.L.R., at 144.
13. This approach was based on *Nocton* v. *Lord Ashburton*, [1914] A.C. 932 (H.L.) and *Laskin* v. *Bache & Co.*, [1972] 1 O.R. 465 (C.A.).
14. *Nocton* v. *Lord Ashburton*, *Id.*, at 943, per Jenkins, K.C. in argument, cited with approval in *Laskin* v. *Bache & Co.*, *Id.*, at 472, per Arnup J.A.

The approach was used as an alternative argument by all three judges in their reasons. They were all of the opinion that the relationship was such as to impose a special duty toward the principal: a duty which in this case had not been performed. The relationship between them caused this special duty to arise, but the agent had been "neither competent nor careful in advising as to insurance coverage or in placing. . .insurance. . .and negligent in failing to inform the plaintiff as to the respects in which he was not covered."[15] The failure to perform properly the fiduciary duties and obligations in the placing of the insurance or in informing the plaintiff as to the respects in which he was not covered had caused the principal to suffer and was therefore an alternative basis for allowing recovery.

The implication of this case and many others like it in recent years[16] 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. As Estey, C.J.O., pointed out "The present-day practices in commerce are in no way offended by the. . .[agents] . . .exposure to liability in these circumstances."[17] While the case may be heartening to consumers, and indicates that reasonable expectations may ultimately be realized in most circumstances, there are still a number of situations in which the person dealing with an insurance agent must remain wary.[18] Nevertheless, the 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.

15. *Supra* n. 7, at 147; 49 D.L.R., at 651.
16. Numbers obviously do not tell the complete story, but it might be noted that the *Canadian Abridgement* includes about twice as many cases involving actions against agents reported since 1970 as it does cases reported prior to 1970.
17. *Supra* n. 2, at 534; 81 D.L.R., at 144.
18. The famous "Newsholme rule" is one situation. Based on *Newsholme Brothers* v. *Road Transport and General Insurance Co.*, [1929] 2 K.B. 356 (C.A.) it may be summarized as follows: where an applicant for insurance gives the details of his application to an agent who records them on the written form incorrectly, the applicant who then signs the form verifying the contents is bound by the agent's mistake in later dealing with the insurer. The insurer is not bound by the information communicated to the agent. In a recent English case *O'Connor* v. *B.D.B. Kirby & Co.*, [1972] 1 Q.B. 90; [1971] 2 All E.R. 1415 (C.A.) the applicant then sued the agent. The Court held the cause of the loss of insurance was the insured's own breach of duty in failing to rectify the form and thus dismissed the claim.