2000 CarswellOnt 3093, 22 C.C.L.I. (3d) 1, 138 O.A.C. 28, [2000] O.J. No. 3309

Fellowes, McNeil v. Kansa General International Insurance Co.

Fellowes, McNeil, (Appellant) and Kansa General International Insurance Company Ltd. and Kansa Canadian Management Services Inc., (Respondents)

Ontario Court of Appeal

Weiler, Rosenberg, Goudge JJ.A.

Heard: February 29, 2000
Judgment: September 11, 2000[FN*]
Docket: CA C30847

Proceedings: reversing in part (1998), 9 C.C.L.I. (3d) 17 (Ont. Gen. Div.); additional reasons at (June 30, 1999) (Ont. S.C.J.)

Counsel: *Wendell S. Wigle, Q.C.* and *Mario R. Pietrangeli* , for Appellant.

A. Burke Doran, Q.C. and *Clive Elkin* , for Respondents.

Subject: Torts

Barristers and solicitors --- Negligence — Miscellaneous issues

Company was not estopped from denying coverage to lawyer as it did not have information on which to make decision before file was transferred to firm.

Barristers and solicitors --- Negligence — In conduct of action — General

Even if firm was negligent in handling contaminant claim, no damages resulted.

Insurance --- Actions on policies — Commencement of proceedings — Obligations of insurer — To defend — Interpretation of policy

Even if firm was negligent in handling claim, no damages resulted, because company would still have incurred expense of providing defence.

Insurance --- Actions on policies — Commencement of proceedings — Obligations of insurer — To defend — Allegation of insured's policy breach

Had firm advised company of coverage issue, company would not have been exposed to payment of judgment.

Cases considered by *Weiler J.A.* :

Alberta (Workers' Compensation Board) v. Riggins (1992), (sub nom. *Riggins v. Alberta (Workers' Compensation Board)*) 5 Alta. L.R. (3d) 66, 131 A.R. 205, 25 W.A.C. 205, 95 D.L.R. (4th) 279 (Alta. C.A.) — referred to

Confederation Life Insurance Co. v. Shepherd, McKenzie, Plaxton, Little & Jenkins (1992), 29 R.P.R. (2d) 271 (Ont. Gen. Div. [Commercial List]) — considered

Fasken Campbell Godfrey v. Seven-up Canada Inc. (2000), 47 O.R. (3d) 15, 182 D.L.R. (4th) 315, 128 O.A.C. 249 (Ont. C.A.) — considered

Fisher v. Guardian Insurance Co. of Canada, 3 B.C.L.R. (3d) 161, [1995] 5 W.W.R. 576, 28 C.C.L.I. (2d) 74, 123 D.L.R. (4th) 336, (sub nom. *McKay v. Guardian Insurance Co. of Canada)* 57 B.C.A.C. 161, (sub nom. *McKay v. Guardian Insurance Co. of Canada)* 94 W.A.C. 161 (B.C. C.A.) — referred to

Godonoaga (Litigation Guardian of) v. Khatambakhsh (Guardian of) (2000), (sub nom. *Godonoaga (Litigation guardian of) v. Khatambakhsh)* 49 O.R. (3d) 22 (Ont. C.A.) — referred to

Gouzenko v. Harris (1976), 13 O.R. (2d) 730, 1 C.C.L.T. 37, 72 D.L.R. (3d) 293 (Ont. H.C.) — referred to

Hopkins (Committee of) v. Wellington (1999), 68 B.C.L.R. (3d) 152 (B.C. S.C.) — referred to

Laurencine v. Jardine, [1988] I.L.R. 1-2292, 30 C.C.L.I. 187, 64 O.R. (2d) 336 (Ont. H.C.) — referred to

Lumbermans Mutual Casualty Company v. Plantation Pipeline Company (1994), 447 S.E.2d 89 (U.S. Ga. Ct. App.) — considered

Major v. Buchanan (1975), 9 O.R. (2d) 491, 61 D.L.R. (3d) 46 (Ont. H.C.) — referred to

Midland Bank Trust Co. v. Hett (1977), [1979] Ch. 384, [1978] 3 All E.R. 571, 121 Sol. Jo. 830, [1978] 3 W.L.R. 167 (Eng. Ch. Div.) — considered

Montreal Trust Co. of Canada v. Birmingham Lodge Ltd. (1995), 46 R.P.R. (2d) 153, 125 D.L.R. (4th) 193, 24 O.R. (3d) 97, 82 O.A.C. 25, 21 B.L.R. (2d) 165 (Ont. C.A.) — referred to

Moore v. Canadian Lawyers Insurance Assn., (sub nom. *Canadian Lawyers Insurance Assn. v. Moore)* [1993] I.L.R. 1-2981, 105 D.L.R. (4th) 258, 123 N.S.R. (2d) 414, 340 A.P.R. 414, 18 C.C.L.I. (2d) 1 (N.S. C.A.) — considered

Murphy v. Sun Life Assurance Co. (1964), 50 W.W.R. 581, 49 D.L.R. (2d) 412, [1965] I.L.R. 1-142 (Alta. C.A.) — considered

Murphy Oil Co. v. Continental Insurance Co., 33 O.R. (2d) 853, [1981] I.L.R. 1-1409 (Ont. Co. Ct.) — considered

Nichols v. American Home Assurance Co., [1990] I.L.R. 1-2583, 45 C.C.L.I. 153, 39 O.A.C. 63, 107 N.R. 321, 68 D.L.R. (4th) 321, [1990] 1 S.C.R. 801, 72 O.R. (2d) 799 (note), [1990] R.R.A. 516 (S.C.C.) — considered

Northern Life Assurance Co. v. Reierson (1976), [1977] 1 S.C.R. 390, [1976] 3 W.W.R. 275, [1976] I.L.R. 1-749, 8 N.R. 351, 67 D.L.R. (3d) 193 (S.C.C.) — distinguished

R. v. Fisher, [1961] O.W.N. 94, 34 C.R. 320, 130 C.C.C. 1 at 2 (Ont. C.A.) — considered

Rosenblood Estate v. Law Society of Upper Canada, *(*sub nom. *Rosenblood v. Law Society of Upper Canada)* [1989] I.L.R. 1-2416, 37 C.C.L.I. 142 (Ont. H.C.) — referred to

Rosenblood Estate v. Law Society of Upper Canada (1992), 16 C.C.L.I. (2d) 226 (Ont. C.A.) — referred to

Sansalone v. Wawanesa Mutual Insurance Co., *(*sub nom. *Non-Marine Underwriters, Lloyd's of London v. Scalera)* 2000 SCC 24, 75 B.C.L.R. (3d) 1, 18 C.C.L.I. (3d) 1, *(*sub nom. *Non-Marine Underwriters, Lloyd's of London v. Scalera)* 185 D.L.R. (4th) 1, 50 C.C.L.T. (2d) 1, [2000] 5 W.W.R. 465, *(*sub nom. *Non-Marine Underwriters, Lloyd's of London v. Scalera)* [2000] I.L.R. I-3810, *(*sub nom. *Scalera v. Lloyd's of London)* 253 N.R. 1, *(*sub nom. *Scalera v. Lloyd's of London)* 135 B.C.A.C. 161, *(*sub nom. *Scalera v. Lloyd's of London)* 221 W.A.C. 161, *(*sub nom. *Non-Marine Underwriters, Lloyd's of London v. Scalera)* [2000] 1 S.C.R. 551 (S.C.C.) — referred to

Sayle v. Jevco Insurance Co., 9 C.C.L.I. 54, 58 B.C.L.R. 122, [1984] I.L.R. 1-1836 (B.C. S.C.) — considered

Sayle v. Jevco Insurance Co. (1985), 16 C.C.L.I. 309, 28 B.C.L.R. (2d) xxxi (note) (B.C. C.A.) — referred to

Schwartz v. R., 17 C.C.E.L. (2d) 141, *(*sub nom. *Minister of National Revenue v. Schwartz)* 193 N.R. 241, *(*sub nom. *Schwartz v. Canada)* 133 D.L.R. (4th) 289, 96 D.T.C. 6103, 10 C.C.P.B. 213, [1996] 1 C.T.C. 303, *(*sub nom. *Schwartz v. Canada)* [1996] 1 S.C.R. 254 (S.C.C.) — referred to

State Of New York v. Travellers Indemnity Company of Rhode Island (1986), 506 N.Y.S.2d 698 (U.S. N.Y.A.D. 3rd Dept.) — considered

Wong v. 407527 Ontario Ltd. (1999), 26 R.P.R. (3d) 262, 179 D.L.R. (4th) 38, 125 O.A.C. 101 (Ont. C.A.) — applied

Statutes considered:

Condominium Act, R.S.O. 1990, c. C.26

Generally — referred to

s. 7(9) — considered

s. 7(10) — considered

APPEAL from judgment reported at (1998), 9 C.C.L.I. (3d) 17 (Ont. Gen. Div.), allowing counterclaim for loss arising from solicitor's negligence in solicitor's action for payment of unpaid accounts; ADDITIONAL REASONS decided at (June 30, 1999), Doc. 94-CU-78160CM (Ont. S.C.J.), dealing with costs.

The judgment of the court was delivered by *Weiler J.A.*:

Overview

1 Fellowes, McNeil, a law firm expert in insurance defence litigation, appeals the decision of Macdonald J. awarding damages against it for negligence in respect of two separate and distinct matters. The law firm acted for the respondent, Kansa, a general liability insurance company, between 1979 and 1993 on hundreds of files.

2 In November of 1993, Mr. McNeil ("McNeil") had a disagreement with Kansa over the conduct of the impending trial respecting a file not before this court. As a result of this disagreement, Kansa retained new counsel on the file and withdrew most of its files from Fellowes, McNeil.

3 In June 1994, Fellowes, McNeil sued Kansa for unpaid fees. Kansa counterclaimed alleging negligence in the handling of four separate files. Fellowes, McNeil's claim for fees came to trial in November 1997 and Macdonald J. granted judgment on the firm's claim for unpaid legal fees. Macdonald J. then heard Kansa's counterclaim for negligence. Four mini-trials were conducted. In one of the mini-trials, known as the "Fruitman" matter, the claim was discontinued before evidence was called; in a second, known as the "Cabaret" matter, the claim in negligence was dismissed. In the two remaining mini-trials, known as the "Little" matter and the "Uniroyal" matter, the claim for negligence was allowed. In the *Little* mini-trial, Fellowes, McNeil was held liable for $5,299,838.00 plus prejudgment interest. In the *Uniroyal* mini-trial, the firm was held liable in the amount of $593,146.25 plus prejudgment interest. This appeal relates to the *Little* and the *Uniroyal* mini-trials.

4 In this case as in all negligence actions, the plaintiff must prove that the defendant's acts or omissions fell below the generally accepted standard of care that the defendant owed to the plaintiff and caused foreseeable damage.

5 With respect to liability in negligence, the standard of care respecting McNeil is that of a reasonably competent lawyer who is expert in insurance litigation: See *Confederation Life Insurance Co. v. Shepherd, McKenzie, Plaxton, Little & Jenkins* (1992), 29 R.P.R. (2d) 271 (Ont. Gen. Div. [Commercial List]) at p. 17 (Montgomery J.) (appeal as to liability and damages dismissed but allowed with respect to the award of pre and postjudgment interest at

(1996), 88 O.A.C. 398 (Ont. C.A.) .)

6 With respect to damages, the plaintiff must show that, but for the lawyer's negligence, the matter on which the lawyer was retained would likely have been successfully concluded. The burden of proof is on the plaintiff to show what was actually lost as a result of the lawyer's negligence. See *Alberta (Workers' Compensation Board) v. Riggins* (1992), 5 Alta. L.R. (3d) 66 (Alta. C.A.) per Major J.A., as he then was, at p. 5; *Gouzenko v. Harris* (1976), 13 O.R. (2d) 730 (Ont. H.C.) , at 744-745. In order to make a determination as to what was actually lost the trial judge is required to scrutinize the matter on which the lawyer was retained and to decide what the likelihood of success would have been. The procedure has been called a trial within a trial.

7 As part of the "trial within a trial" the trial judge was required to examine the *Little* matter and McNeil's conduct as counsel. The initial issue before her was whether the policy of error and omissions insurance issued by Kansa to Little's law firm, Shepherd McKenzie, was void because a potential claim against Little for lawyer's negligence was not disclosed on the application for insurance. The trial judge found that a material misrepresentation was made when Little declared on his application for insurance that he had "no reason to anticipate any claims being brought" by a client for "any negligent act, error omission".

8 Kansa was not aware of any misrepresentation by Little at the time he was sued under the policy and did not specifically instruct McNeil to advise it concerning the issue of coverage. On Little's examination for discovery, however, Little made a number of admissions including the admission that he realized he had a "problem" in August of 1983 prior to the firm's application for claims based insurance with Kansa. The trial judge found that when McNeil read Little's examination for discovery, McNeil should have realized Little's evidence raised an issue of coverage to which Kansa should have been alerted. At that time, Little's defence was being conducted by the primary insurer, American Home. McNeil represented Kansa as the excess insurer. It was seven months later that Fellowes McNeil went on record as representing Little and assumed his defence. Little was ultimately found liable in negligence by Montgomery J. in *Confederation Life Insurance Co. v. Shepherd, McKenzie, Plaxton, Little & Jenkins* , *supra* .

9 After reading the decision of Montgomery J., Kansa alleged that McNeil should have advised Kansa to deny coverage under the E & O policy prior to going on record for Little and that McNeil's failure to do so amounted to negligence. The trial judge agreed with Kansa.

10 The trial judge found that, had Kansa been alerted to Little's admission, Kansa could have successfully refused to indemnify Little's firm when the latter was found to be negligent. The trial judge's ultimate conclusions were that because of the negligence of Fellowes, McNeil, Kansa lost the opportunity to deny coverage under the errors and omissions policy to Little and that it would likely have been successful in denying coverage. The appellant challenges the findings and conclusions of the trial judge.

11 The general standard by which a lawyer's conduct is measured is a question of law. The translation of that general duty into the particular obligation imposed on a defendant and

the decision as to whether the defendant has met that obligation is a question of fact: *Wong v. 407527 Ontario Ltd.* (1999), 179 D.L.R. (4th) 38 at 47 (Ont. C.A.) . Providing that the trial judge applied the correct standard, the trial judge's decision is essentially fact-driven and there is support for her conclusions in the evidence. Similarly, the assessment of damages is a fact-drive exercise once the approach by which damages are to be measured is ascertained. I am of the opinion that the trial judge did not err in her application of the standard of care or in the manner in which she approached damages. Bearing in mind the deference owed to a trial judge's findings of fact I would dismiss the appeal in the *Little* matter.

12 The main issues in the *Uniroyal* case turned on whether Kansa would have been obligated to provide a defence to its insured Uniroyal but for McNeil's actions. The trial judge found that McNeil filed a defence on behalf of the insured before examining the insurance policies to see if liability was excluded under the pollution exclusion clauses in the policies. If, as Fellowes McNeil contends, the loss claimed was potentially covered under the policies, then Kansa was obliged to defend Uniroyal and anything McNeil did or did not do that resulted in an order that Kansa defend Uniroyal is irrelevant. If, as Kansa submits, and the trial judge held, the exclusion clauses in the policies clearly excluded the damage caused, the question is whether McNeil should have advised Kansa to refuse to defend Uniroyal. The trial judge concluded that but for McNeil's actions, Kansa could have refused to provide a defence to Uniroyal. She again held Fellowes, McNeil liable in negligence for not advising Kansa with respect to a coverage issue.

13 The interpretation of a policy of insurance is basically a question of law and I would respectfully differ with the trial judge's interpretation and conclusion that the loss was clearly excluded under all of the policies. Consequently, even if Fellowes, McNeil fell below the required standard of care nothing was actually lost. Kansa could not have successfully refused to defend the action on behalf of its insured because the loss was potentially covered under the policy.[FN1] As a result, I would allow the appeal in the *Uniroyal* matter. My reasons follow.

The Little mini-trial

14 Kansa was the excess errors and omissions (E & O) insurer of the Shepherd McKenzie Plaxton Little & Jenkins law firm ("Shepherd McKenzie"), pursuant to a claims-based policy of insurance for the period January 29, 1984 to December 20, 1984. The policy was renewed for a further year from January 1, 1985 to December 31, 1985. Under a claims-based policy, claims that are made during the existence of the policy are insured regardless of when the acts giving rise to the claim took place.

15 When an insurance company relies on misrepresentation in an application for insurance to void a policy, it must establish 1) that the misrepresentation was material in that it affected the risk and 2) that there was a misrepresentation or inaccuracy in the information supplied by the insured: *Sayle v. Jevco Insurance Co.* (1984), 58 B.C.L.R. 122 (B.C. S.C.) , affirmed,(1985), 16 C.C.L.I. 309 (B.C. C.A.)

16 The issue as to whether the misrepresentation was material turns on what Kansa would have done had Little indicated that there was a potential claim against him at the time the ap-

plication for insurance was made. Kansa's representatives did not testify as to what they would have done. The trial judge held, however:

> As part of my consideration of these issues, I have assessed whether or not a denial of coverage to Mr. Little would have been warranted in the circumstances. This leads me to review the applications for coverage of the firm effective January 1, 1984. This application for coverage is dated December 30, 1983. There is a further application for coverage dated December 28, 1994, for coverage effective January 1, 1983. After both applications were made, Kansa extended coverage to the firm for the periods January 20, 1984 to January 1, 1985 and for January 1, 1985 to January 1, 1986.
>
> Based on the manner in which Kansa responded to the declaration of other potential claims it is reasonable to conclude that Kansa, after it assessed the risk in respect of the potential for the Confederation Life claim, would either have refused to extend coverage or, in the alternative, would have excluded the claim from a policy that they may have chosen to issue.
>
> I now turn to the application for insurance dated December 28, 1984.
>
> . . . . .
>
> It [question 13] reads as follows:
>
> > Does the Applicant Firm know of any circumstance which may result in any Professional Liability claim being made against the Applicant Firm, its predecessors in business or any past or present Partners?
>
> In answer to this question the word "yes" was typed into the form and reference was made to a schedule "B" which does not mention the Confederation Life problem or any other matter involving Mr. Little.
>
> It is important, for purposes of my overall assessment of these issues, that in response to the disclosure about a potential claim, thought to be ultimately unsuccessful, Kansa excluded coverage for such claim. Undoubtedly, this endorsement came as a result of the disclosure about a potential claim and resulted in a refusal by Kansa to assume risk for this potential claim.

17 The trial judge considered the conduct of Kansa in excluding a potential claim when it renewed the policy as circumstantial evidence of what Kansa would have done had it been aware of a potential claim against Little. She was entitled to consider this evidence and to draw the inference from this evidence that, had Kansa been aware of the Little matter, Kansa would similarly have excluded the claim. See *Montreal Trust Co. of Canada v. Birmingham Lodge Ltd.* (1995), 24 O.R. (3d) 97 at 108 (Ont. C.A.) .

18 Although the trial judge indicated that she did not rely on it, the trial judge received expert opinion evidence respecting whether nondisclosure of the claim was material. Mr. Gilbertson ("Gilbertson"), an expert called by Kansa, testified that, if proper disclosure had been

made, a reasonable insurer would have excluded or declined the risk or stipulated for a higher premium. The appellant submits that this was not a proper subject for opinion evidence because it was a question of fact and law to be decided by the trial judge. Expert evidence on matters in the expert's particular field and not within the common stock of knowledge is admissible where it will be helpful to the trier of fact and the trier of fact cannot draw the necessary inferences without it. *R. v. Fisher* (1961), 34 C.R. 320 (Ont. C.A.) . As an example of this principle, in *Fisher* , *supra* , Aylesworth J.A. stated at 95:

> In many instances opinion evidence is received upon the very issue the Court has to decide, as for example, where the issue is the materiality of a representation in an application for insurance: *Yorke v. Yorks. Ins. Co.*, [1918] 1 K.B. 662 , *Sun Ins. Off. v. Roy*, [1927] S.C.R. 8 at p. 13.

19 Expert evidence respecting the materiality of nondisclosure was also accepted in *Murphy v. Sun Life Assurance Co.* (1964), 49 D.L.R. (2d) 412 (Alta. C.A.) . The trial judge did not err in receiving expert evidence on this issue.

20 The next question is whether the declaration on the original application of insurance was a misrepresentation or inaccuracy. Resolution of that issue depends largely on whether the trial judge properly appreciated the evidence. There is no real dispute as to the background facts.

21 Little, a specialist in real estate law, acted on behalf of both Confederation Life, the lender, and the borrowers, Mr. Khoury and his company 511666 Ontario Ltd., (both referred to as "Khoury"), with respect to the placement of a mortgage on an apartment building the company purchased. The mortgage secured a loan from Confederation Life of $7,167,294 at 18.25% interest for a twenty-year term with no prepayment privilege. It was important to Confederation Life that Khoury not be allowed to prepay the mortgage before the twenty-year term was up because it had "matched" the funds needed. In other words, Confederation Life had borrowed the funds to advance under the mortgage from a pension fund and had promised to pay the pension fund a rate of return that was only slightly less than the amount Confederation Life was to receive over the same twenty year term. There is no issue that Little was aware of the importance to Confederation Life that Khoury not be able to prepay the mortgage.

22 After receiving the commitment letter from Confederation Life, Khoury proposed some changes to the commitment letter including a change to convert the apartment building into a condominium known as the "condominium clause." Confederation Life agreed to the changes Khoury had made to the commitment letter only after a conversation with Little.

23 The effect of ss.7(9) and (10) of the *Condominium Act* , is to allow the mortgage to be discharged when an apartment building is converted into condominiums A clause can be inserted into a mortgage to prevent the mortgage from being discharged but Little omitted to insert such a clause when he redrafted the document to insert the condominium clause. When interest rates fell, Khoury converted the building into condominiums and requested a discharge of the mortgage. Confederation Life refused to discharge the mortgage.

24 On June 15, 1983, Confederation Life's representative met Khoury. Khoury advised that he had an opinion from the firm of McCarthy & McCarthy that he was entitled to a discharge. Confederation Life's representative contacted Little and asked him to write a letter of opinion respecting whether Khoury was entitled to prepay the mortgage in the event the project was registered as a condominium. On June 17, 1983, Little replied but he did not answer the question asked of him. The same day Little prepared documentation on behalf of Khoury to convert the building into a condominium and forwarded it to Confederation Life. Little then prepared documentation on behalf of Confederation Life in response. Mr. Little was questioned on discovery by Mr. Lorne Morphy, acting on behalf of Confederation Life, as to whether in June 1983, he considered himself in a big conflict. He replied at p. 129 as follows:

I can't recall my specific memory: I would expect myself to have considered the conflict.

25 At p. 130 of his discovery transcript, Mr. Little said that he could not recall whether he had declared the conflict of interest to either of his clients.

26 On August 1, 1983, Khoury stopped payment on the mortgage. Little's examination for discovery also revealed that, on August 3, Little had a conversation with Chris Ahlvik, the in-house solicitor of Confederation Life, who referred him to ss.7(9) and 7(10) of the *Condominium Act* . After that conversation, Little read ss.7(9) and (10) of the *Condominium Act* . He then spoke to one of his partners, Mr. Plaxton. On August 25, Little spoke with Khoury's lawyer at McCarthy's and Little's note of the conversation indicates "McCarthy's have instructions to commence litigation next week if there is no consent as is." That is, unless Khoury was given a discharge of the mortgage upon payment of the accelerated principal and interest owing to the date of payment, he would commence litigation. Following this, Khoury commenced a declaratory action against Confederation Life in October 1983.

27 By November 30, 1983, Little knew that his services were no longer required and he forwarded a final account to Confederation Life.

28 In December 1983, Little's firm signed an application for E & O excess insurance effective January 1984. A contract of insurance is a contract that requires the utmost good faith on the part of the insured. Disclosure on the application is key to the granting of coverage.

29 In her reasons discussing the application for insurance, the trial judge stated:

Question 7 on the application for coverage reads as follows:

> Have any claims or suits been made in the past and are any pending or to the Proposer's knowledge contemplated against the Named Insured or against the present Owner, Partners or Officers or employees, either individually or otherwise?

This question was answered in the negative, and because as at December 30, 1993 there were no claims or suits pending, the answer to this question does not constitute a misrepresentation.

On page 2 of the application there is a declaration which reads as follows:

> I/We hereby declare that the above statements and particulars are true, and I/we have not suppressed or mis-stated any material facts, that at the present time *I/we have no reason to anticipate any claims being brought against me/us for any negligent act, error or omission* on the part of any member or employee of this Insured or their predecessors in business, and agree that this declaration shall be the basis of the Insurance between me/us and the Insurer. [Emphasis added.]

The application is signed by a partner in the firm on behalf of the firm. The application contemplates answers and declarations to be those of all of the partners and members of the firm. In the context of the declaration which was answered without reference to Mr. Little's "problem" with Confederation Life, one has to ask the question of whether or not Mr. Little would have had any reason as of December 30, 1983 to anticipate any claim being brought against him and his firm as a result of the problem.

I have concluded that by then it is reasonable to conclude that Mr. Little would probably have had reason to anticipate that as of December 30, 1983 a claim might be brought against him and his firm based on his failure to advise and consider the effect of s.7(9) and (10) of the *Condominium Act* on Confederation Life's intent to keep in place a twenty year mortgage with no right of prepayment.

30 Confederation Life commenced an action against Khoury for arrears under the mortgage on March 15, 1984. On September 25, 1984 Little met with Confederation Life's in-house counsel about his conduct and the provisions of the *Condominium Act* that provided for discharge of the mortgage upon conversion of an apartment building. He was asked questions about his position of conflict.

31 On December 20, 1984, Shepherd McKenzie signed an application to renew its excess E & O policy with Kansa. The application contained a declaration again stating, "that at the present time I have no reason to anticipate any clams being brought against us for any negligent act, error or omission on the part of any member or employee of this insured." The firm did not mention the Confederation Life problem although, as I have indicated, another potential claim was disclosed and excluded from coverage under the policy.

32 On January 31, 1985, Confederation Life told Little to notify his E & O insurer. In February 1985, Little gave notice of the intended claim to the Law Society of Upper Canada and to Kansa's adjusters, F.C. Maltman & Co. American Home, the firm's primary insurer was also notified. The Law Society's solicitor, Mr. Murray, advised there was "... no evidence to suggest that Confederation ever consulted" Little on the effects of the condominium clause. Doner, the adjuster for Maltman's advised, "We have neither seen nor heard anything that suggests Little knew or should have known of a claim before 1985."

33 Confederation Life settled its dispute with Mr. Khoury and the mortgage was discharged on March 28, 1985. In December 1985, Confederation Life sued Shepherd McKenzie for negligence claiming as damages the difference between what would have been received under the mortgage and the amount for which it was able to invest the funds.

34 Little's defence was that his retainer was a limited one. In his statement of defence he said he was not asked to express an opinion as to the effect of the condominium clause or the terms of the commitment letter. On his examination for discovery, Little waivered. The exchange is as follows:

> And when Mr. Boddy (of Confederation Life) gave you clause 16 on the 27th did he ask whether you had any comments concerning it?
>
> I expect he asked me what I thought of it and I just told him we could use it. It would work in the documentation.
>
> Q. And when he gave you the clause 29, did he ask for your comments?
>
> A. I think he probably asked me about both of them at the same time.
>
> Q. What did you say about clause 29 (the condominium clause)
>
> A. I answered them both the same way, I expect.
>
> Q. All right. And did you at the time he gave you this clause 29 refer him to or alert him to the provisions of the Condominium Act in particular s. 7 (9) and s. 7(10)?
>
> A. No
>
> . . . . .
>
> Q. And did Boddy ask you on that occasion as to whether...there would be any difficulty with Confederation Life in regard to the mortgage if this clause 29 was inserted therein?
>
> I made no note of it. I have no recollection of it.
>
> Q. But you are not saying he didn't?
>
> A. No

35 The trial took place in October and November 1992 before Montgomery J. He released his reasons finding Little negligent on December 4, 1992. In his reasons, *supra* , at 300, he concluded that:

- It was the condominium clause that gave Khoury his leverage to pressure Confederation;
- Confederation consulted Little about the condominium clause before approving the commitment letter;
- Little approved the condominium clause in principle and in form;
- Little drafted clause 28A of the mortgage, the clause his own expert Cowan said was not a very good clause;
- If Confederation had received the advice it was entitled to, there would have been no

condominium clause, or at the least a proviso of the type referred to by Feinstein (one of the experts who testified); and

• Confederation relied on Little's advice to its detriment.

36 The negligence alleged against McNeil in this case is that he should have been alerted to the fact that Kansa could probably deny coverage under the policy after reading Little's examination for discovery. In dealing with this issue the trial judge stated in her reasons:

> I have concluded that reading this transcript raises concerns about issues of coverage under the Kansa policy. Before excerpting the relevant and controversial portions of the discovery transcript I comment as follows. Mr. Little acknowledged in the examination for discovery that he was retained in August, 1982 by Confederation Life to act in the mortgage transaction. He acknowledged as well, that he was aware of Confederation Life's desire to preserve the twenty year term of the mortgage. Confederation Life had asked him to redraft the condominium document to achieve this objective. He was acting on both sides of the transaction in that he had acted for Mr. Khoury and 511666 Ontario Limited. He had been retained for these purposes by a Toronto law firm under cover of a letter dated July 5, 1982. At his discovery, Mr. Little acknowledged he was aware that Khoury and 511666 Ontario Limited were taking a position contrary to the interests of Confederation Life. This conflict of interest would ultimately have a very negative impact on the assessment of Mr. Little's liability. Its existence exasperated (sic exacerbated) Mr. Little's position as he attempted to solve the problems created by the omission to include in the mortgage documentation reference to the *Condominium Act* .

37 On Mr. Little's examination for discovery, Mr. Morphy questioned Little with respect to his failure to alert Confederation Life to the impact of s.7(9) and (10) of the *Condominium Act* . At question 1189, Mr. Morphy asked:

> When did you realize it was going to be a problem?

Mr. Little replied:

> I believe it was on the 3rd day of August, 1983.

38 The context of the admission noted by the trial judge is as follows:

> Q. And at any time, in August or September of 1982, or before the final advance in December of 1982 of the mortgage money, did you advise anyone from Confederation Life of the effect of Section 7(9) and 7(10) of the *Condominium Act* ?
>
> A. I don't think so.
>
> Q. Well, the fact is they didn't come to your attention, sir. You didn't even, they weren't in your mind, were they?
>
> A. Relative to this mortgage, no.

Q. No. When did you first realize, sir, it was going to be a problem?

Mr. Dermer: 7(9)? You mean 7(9)?

By Mr. Morphy: Q. Yes.

A. I believe it was on the 3rd of August, 1983.

Q. You're looking at what, sir?

A. I'm looking at —

Mr. Dermer: A handwritten note that's part of 241, production 241.

By Mr. Morphy: Q. The one that's dated —

A. The 3rd of August, 1983.

Q. In discussion with Mr. — is that your partner, Mr. Plaxton?

A. No. The next note, the next page.

Q. I'm sorry. And is there reference to it, sir?

A. A telephone conversation with Chris Ahlvik.

Q. He is a solicitor with?

A. Confederation Life. I've spelled it wrong there and the section is ...

Q. Referred to there.

A. Referred to there.

Q. And after that did you get the Act off your library shelf and read it?

A. I certainly read those sections.

Q. And you went in and discussed it with Mr. Plaxton the next day?

A. I assume I did, yes.

. . . . .

Q. Okay. So the issue was squarely before you at that point?

A. Yes.

Q. You went to see Mr. Plaxton?

A. I did.

Q. Why?

A. I wanted to discuss what I was thinking with someone else.

Q. And were you telling your partner that you had overlooked Section 7(9)?

A. No.

Q. Did you tell him at that time that you may have a problem?

A. No.

Q. You didn't consider any problem at that point?

A. I thought there was a problem that we had to solve, which was how do we enter, how do we deal with a consent of the condominium in those terms.

Mr. Dermer: Is your problem meaning a potential errors and omissions problem?

By Mr. Morphy: Q. Yes.

A. No.

. . . . .

Q. Did you tell Mr. Plaxton at that time that you were as of the 4th of August, 1983, also acting for Mr. Khoury in trying to get the condominium registered?

A. Well, I don't believe I was acting for Mr. Khoury after Confederation Life came to me and said this problem exists.

Q. Oh really.

A. From that time he was represented by McCarthy and McCarthy.

Q. What date do you take that to be when Confederation Life came to you and ...

A. Sometime around the 3rd of August.

Q. Did you tell Mr. Khoury that you couldn't act for him any more?

A. I don't recall.

Q. Because I would have thought that you, your retainer from him was to prepare and register this condominium declaration.

A. Yes.

. . . . .

Q. Yes. And, sir, turn to your 241 please.

> And your note of your conversation with Mr. Plaxton on the 4th of August, did you following your conversation with Mr. Plaxton and the deliberations that you gave at that time, did you think that it was possible at that time to rescue the situation and avoid the effect of 7(9) and 7(10)?
>
> A. I did.
>
> Q. How?
>
> A. By refusing to consent on reasonable grounds until satisfactory arrangements were reached to protect the closed nature of the mortgage.
>
> Q. What would those reasonable grounds be?
>
> A. The ones which were presented.
>
> Q. Presented where, sir?
>
> A. In the amendment to the declaration and in the agreement.
>
> Q. The agreement being?
>
> A. An agreement prepared and submitted by me to Confederation Life and appearing —
>
> Mr. Dermer: 286. Is that the document?
>
> The Deponent: At tab 286.
>
> By Mr. Morphy: Q. And have you still got tab 241 there?
>
> A. Yes.
>
> Q. Turning to your 3/8/83 note, the bottom of the second page you posed the question, I guess in a sense to yourself, did you? "Can we agree to a consent subject to an agreement amending the mortgage which stipulates the amount required to discharge in the event of fracturing"?
>
> A. Yes.

39 Fracturing is a term used to mean the prepayment of a mortgage that has a non prepayment clause in it.

40 The appellant submits that the trial judge misapprehended the evidence of Little on his examination for discovery. Little's admission, it is submitted, is that Little realized Confederation Life had a problem, not that he realized he had an errors and omissions problem. The question asked on discovery is when Little realized "it", referring to s.7(9) of the *Condominium Act* , was going to be a problem. The omission of a clause to deal with s.7(9) was Little's omission. It created a problem for Confederation Life. I cannot agree with the appellant's sub-

mission that this transcript shows that Little considered his omission to be a problem only for Confederation Life and not for himself. The appellant's submission overlooks the history of the transaction which Morphy took Little through, including the fact that on his examination for discovery Little wavered on the issue of whether he was asked his advice respecting the condominium clause. Little admitted that as of June 1983, he would have expected himself to consider he had a conflict of interest as a result of having acted for both parties. Little also knew that one of his clients was suing the other on the basis of the condominium clause. The concluding portion of the passage I have quoted indicates that Little certainly hoped the dispute arising from his omission could be resolved by an agreement between Khoury and Confederation Life that would allow an amount to be paid to "fracture" the mortgage. Little would not, however, have been ignorant of what would happen if an agreement were not reached.

41 The trial judge found that when Mr. Little did not answer the questions asked of him by Confederation Life, "...by June, 1983 the legal problems presented by the wording of the relevant covenants in the mortgage were apparent to Mr. Little." Similarly she found, "The reality is that Mr. Little acknowledged that he knew of 'a problem' created by the mortgage drafted by him for Confederation Life prior to the date of the application for insurance...." This is a finding that Little had actual knowledge of the circumstances of his omission or negligent act. It was open to the trial judge to make this finding and she did not misapprehend the evidence in that regard.

42 On the issue of whether Little knew he had an E & O problem, the trial judge expressed herself in a variety of ways. She stated:

> I have concluded that by then it is reasonable to conclude that Mr. Little would probably have had reason to anticipate that as of December 30, 1983 a claim might be brought against him and his firm based on his failure to advise and consider the effect of s.7(9) and (10) of the *Condominium Act* on Confederation Life's intent to keep in place a twenty year mortgage with no right of prepayment.

43 At another point in her reasons, the trial judge concluded that Little "probably would have known that he was potentially exposed to a claim for professional negligence by Confederation Life." I read this to mean that, on a balance of probabilities, Little subjectively realized he was potentially exposed to a claim for professional negligence. At another point, however, the trial judge stated that Little, "probably knew or ought to have known of circumstances giving rise to a potential claim against him prior to December 30, 1983, the date on which the firm applied for excess coverage with Kansa." and she repeated this phrase in another portion of her reasons. The use of the phrase "ought to have known" indicates that the trial judge may have used an objective test to determine whether Little had reason to anticipate a claim and to report it.

44 When a lawyer is aware of circumstances constituting a negligent act or omission in acting for a client, an objective approach has been adopted with respect to whether the lawyer had reason to anticipate a claim against him. In *Moore v. Canadian Lawyers Insurance Assn.* (1993), 18 C.C.L.I. (2d) 1 (N.S. C.A.) at 5 the court held that to prove a breach of the reporting requirement under a policy of insurance where a claim has not been made against an in-

sured lawyer, the insurer must prove three things:

> First that the insured lawyer had actually become aware that he had likely breached a duty to his client in the performance of legal services. Otherwise, it could not be said that he had "learned" of such a circumstance. A court could infer such knowledge from the evidence. Secondly, after learning of his probable breach of duty, a lawyer must measure up to the standard of a reasonably prudent lawyer in assessing whether his deficient conduct will likely give rise to a claim; at this stage an objective test applies. The insurer must adduce evidence from which a court could conclude that the lawyer did not meet this test. *The lawyer cannot be absolved from the contractual responsibility of reporting as soon as practicable simply because, although he had learned of his probable breach of duty to his client, he did not believe a claim was likely; such a belief must be a belief that would be reasonably held by a prudent solicitor under the circumstances* . Thirdly, the insurer must prove the insured failed to report as soon as practicable. If the delay in reporting, after learning of an apparent breach of duty is lengthy, as in this case, the lawyer, as a rule, must adduce some evidence that would support a finding that he acted as a reasonably prudent solicitor would have under the circumstances. [Emphasis added.]

45 The facts giving rise to the decision are the following. Moore, a lawyer, was hired to place a mortgage on real property as security for a loan. The property was owned by the infant of the borrower and court approval for the loan was required. Moore did not obtain court approval. He certified that a valid charge had been obtained to the financial institution advancing the money. When the error came to light as a result of an inquiry from an officer of the financial institution, Moore believed that the error could be rectified. Hallett J.A. on behalf of the court, held, reversing the trial judge that a reasonably prudent solicitor would have realized that it would be unlikely that a court would grant the approval required because there was no benefit to the infant from the loan. Upon learning that the mortgage was invalid, the court held that a reasonably prudent solicitor would have realized that unless he could rectify the problem he would be liable to the financial institution as a result of his failure to secure the loan. At pp. 8-9 of his reasons, Hallett J.A. stated:

> While an insured can be given some leeway in reporting so as to allow him to take action to correct a problem he has created through his breach of duty to his client so as to avoid a claim he must act immediately and decisively. The lengthy delay in reporting that occurred in this case was without any justification considering the nature of the error and the unlikelihood of it being corrected by court order.
>
> . . . . .
>
> A reasonably prudent solicitor would not have concluded that a claim was unlikely given that the mortgagee did not have security for the loan coupled with the unlikelihood of obtaining retroactive approval of the mortgage given the use of the proceeds.

46 *Sayle v. Jevco Insurance Co.* , *supra* , is another decision that takes an objective approach. The comments of McLachlin J., as she then was, encompass both innocent misrepresentation as well as deliberate misrepresentation. There, the issue was whether a real estate

agent failed to report the likelihood of a claim on his application for insurance .The real estate agency was joined in litigation as a stakeholder in two lawsuits for a period of ten months but neither lawsuit claimed damages against the agency. The agency applied for insurance and answered "No" to the question whether the partners/principal/staff were aware of "any circumstance which is likely to give rise to a claim against the firm". McLachlin J. held at 127 that to answer the issue of whether the question had been answered accurately an objective test should be applied. She stated:

> Resolution of that issue depends on whether there were circumstances of which the petitioners knew *or ought to have known* which might give rise to a claim. Again, the test is objective. *It is not enough that the persons responsible for completion of the application acted honestly in the belief that there were no circumstances which were likely to give rise to a claim. The question is what a reasonable person in the applicant's position would have concluded. As stated in Wright v. Engineers Ltd. v. U.S. Fire Ins. Co. (1983), 48 B.C.L.R. 37 at 48, 2 C.C.L.T. 32 (S.C.), "The responsible officers or executives of the corporation cannot, through willful blindness or stupidity, ignore the evidence of a claim or potential claim* ." See also *Stevenson v. Simcoe v Erie Gen Ins. Co.* at 488. ([1981] I.L.R. 1-1434 at 495 (Alta. Q.B.))
>
> It emerges from the authorities to which I have been referred that an applicant for insurance answering a question such as that posed by cl.7 of the respondents' application form is not obliged to inform the insurer of every complaint or suggestion of incompetence which has been raised against him. For example, in *Stevenson v. Simcoe 7 Erie Gen. Ins. Co.* the insured's right to coverage was upheld notwithstanding its failure to advise of complaints of improper quality control and site supervision, because at the time the application was made the complainant had conceded that the applicant was not at fault. It is obvious that the insurer's concern must be with the risk of future claims. It follows from this that what must be reported are claims or potential claims, not fanciful possibilities: see *Wright Engineers Ltd. v. U.S. Fire Ins. Co.* at p. 48; see also *Soole v. Royal Ins. Co.*, [1971] 2 Lloyd's Rep. 332 at 337 (Q.B.).

47 The trial judge's reference to "ought to have known" is supported by the jurisprudence quoted above. As previously indicated, however, I read the trial judge's finding to be that, when the initial application for insurance was made in December 1983, Little had actual knowledge of his omission with respect to s. 7 (9) and (10) of the *Condominium Act* . That would bring him within the test of knowing or, at the very least, being wilfully blind to the reporting requirement.

48 In her reasons, the trial judge, after finding that Little knew he had a problem, referred to a further meeting between Little and in house counsel for Confederation Life in September 1984. The meeting resulted in a four page internal memorandum by Confederation Life summarizing the meeting. The trial judge stated, "The fact that the meeting occurred and the contents of the discussions at the meeting as disclosed in the memorandum can reasonably lead to the conclusion that after that meeting, Little probably would have known that he was potentially exposed to a claim for professional negligence by Confederation Life." The appellant submits that because there was no evidence that Little saw the internal memorandum the trial

judge erred in referring to it as support for her conclusion that Little had reason to anticipate a claim. The memo indicates that, at the meeting, representatives of Confederation Life asked Little questions respecting his conflict of interest. Little did not testify and, as a result, there was no evidence from him as to whether the memo accurately reflected what transpired in his presence.

49 The trial judge had already found that Little knew of the problem created by the mortgage at the time the original application for insurance was made in 1983. The important finding is the trial judge's finding of Little's actual knowledge concerning his error in relation to s7(9) and (10) of the *Condominium Act* in 1983. The date when Little realized he might be sued by Confederation Life is a factor to consider with respect to Little's decision not to report the potential claim to Confederation Life. As I have indicated, an objective test is appropriate with respect to the reporting requirement. The reference to the 1984 meeting with Confederation Life is but a surplus comment indicative that, in the face of mounting evidence, Little did not report the potential claim when the 1984 application was made for excess E & O insurance. In order to disturb the trial judge's findings of fact an appellate court must come to the conclusion that the error made by the trial judge was overriding and determinative in the assessment of the balance of probabilities with respect to that factual issue: *Schwartz v. R.*, [1996] 1 S.C.R. 254 (S.C.C.) . The trial judge had already found that Little was actually aware of the circumstances of his omission in December 1983. She also concluded Little knew or ought to have known of a potential claim at that date. While the trial judge should probably not have accepted the 1984 memo for the truth of its contents unless it had been admitted as a business record, the error was not determinative of her assessment as to what happened in 1983. In any event, the test as to whether the negligence is likely to give rise to a claim so as to trigger the reporting requirement is objective.

50 I now turn to the issue of whether McNeil was negligent in failing to conclude that there was an issue of coverage under the policy when he read Little's examination for discovery. The duty to advise a client of a risk associated with litigation only arises when an ordinarily competent and prudent solicitor would have issued a warning. *Fasken Campbell Godfrey v. Seven-up Canada Inc.* (2000), 47 O.R. (3d) 15 (Ont. C.A.) at pp 6-7. The scope of the solicitor's retainer is a factor in determining whether an ordinarily competent and prudent solicitor would have realized there was a risk associated with the litigation. *Fasken* , *supra* . All of the surrounding circumstances constitute another consideration. In this case, one of the surrounding circumstances is whether new and important information that affected Kansa's risk in the litigation emerged on Little's examination for discovery and whether McNeil should have realized this upon reading the discovery. Even if the issue of coverage is not within the scope of the solicitor's retainer, if important information comes into a lawyer's hands that the client does not have and that affects the client's risk in the litigation, the lawyer cannot ignore this information: *Major v. Buchanan* (1975), 9 O.R. (2d) 491 (Ont. H.C.) , at 514.

51 The appellant's first submission is that the question of coverage was not within the scope of McNeil's retainer.

52 The scope of a solicitor's retainer is a factual one and the findings of the trial judge are entitled to great deference: *Fasken* , *supra* . The trial judge found that, although Kansa's in-

structions to McNeil did not include a specific request to consider coverage, McNeil should not have excluded the issue of coverage from consideration.

53 One of the surrounding circumstances that the trial judge considered in coming to her conclusion was that McNeil had raised the issue of coverage on his own initiative when acting for Kansa in the past. More importantly, McNeil admitted on his examination for discovery that, at this stage of the litigation and at this time, McNeil was "... retained to protect Kansa's interests, as opposed to the insured's interests until [it] undertook the defence of the insured." Kansa's interests at this time included not just the question of liability but coverage as well. McNeil's acknowledgement put the question of coverage within the scope of his retainer.

54 Assuming, however, that the issue of coverage was not within McNeil's retainer, would an ordinarily competent and prudent solicitor have realized that Little's examination for discovery contained important information that Kansa did not have that affected Kansa's risk in the litigation?

55 Little's examination for discovery was conducted on September 23, 1986. McNeil was retained by Kansa in February 1987 and he received the discovery sometime in October 1987. By September 1990, he had read Little's examination for discovery. On McNeil's examination for discovery, which was read in at trial, McNeil was asked questions about Little's examination for discovery. In relation to Little's denial that he realized as of August 3, 1983 that he had an errors or omissions problem, McNeil opined that the test to be applied was not subjective but objective. In saying this, McNeil acknowledged that Little's denial did not have to be accepted. McNeil denied, however, that anything that happened in 1983 would have given Little reason to anticipate that a claim might be made against him. The corollary of McNeil's position is that there was no new information arising out of Little's examination for discovery that would have caused McNeil to consider that there was an issue of coverage under the policy. The trial judge reached the opposite conclusion.

56 Mr. McKeon ("McKeon"), an expert called by Kansa, testified that, up until McNeil read the examination for discovery of Little, McNeil was entitled to take the position that he did not have a duty to advise Kansa on coverage issues. In other words, he could rely on Maltman's opinion that Little was not aware of a possible claim until January 1985. McKeon stated, however, that McNeil was required to consider coverage if evidence emerged that was "new and very substantially different" from that previously known to Kansa.

57 McNeil's evidence respecting what the discovery would reveal to an experienced insurance litigator was contradicted by McKeon, one of two experts who testified on behalf of Kansa. McKeon's evidence on this point is as follows:

> Well, from the — from the insurance standpoint, Mr. McNeil was reviewing the Examinations for Discovery, and reviewing Mr. Little's Examination for Discovery. It becomes apparent that in August of 1983 Mr. Little was approached again by Confederation who actually drew these two sections [sic. of the Condominium Act] to his attention. And he went along the hall and spoke to Mr. Plaxton about it. I don't know Mr. Plaxton, but I gathered he was a more senior member of the firm. Whatever it was, it's quite clear to me that Mr.

> Little at that time had been made aware of the fact that there were some serious problems about this mortgage; that the interest rates had changed, and if it could be paid off Confederation's expectations were going to be dashed. He knew there were lawyers involved, and the possibility of — of an attack on the mortgage. He knew that he had committed a very simple and fundamental — say omission, when he expressed his opinions on the mortgage, and when he finally registered it. *And I would have thought that it would have been quite clear to him that they were in serious trouble. Now, when that happened Mr. McNeil was faced with certain problems too* .
>
> . . . . .
>
> Q. And do I take it ... as I understood your evidence to be that on reading the Examination for Discovery of Mr. Little, Mr. McNeil should have realized that Mr. Little must have realized that he was negligent in overlooking those sections of the *Condominium Act* . Is that correct?
>
> A. It's correct ...
>
> Q. ... As I understood it, you really didn't have much complaint with Mr. McNeil until he got to the point of reading those transcripts, and in particular this meeting of August, 1983 with Mr. Plaxton that he then should have realized he had missed these sections of the *Condominium Act* and was negligent?
>
> A. More than that, the client [Confederation Life] had drawn it to his attention. But that ... that's the time, yes.

58 The trial judge accepted the evidence of McKeon and Gilbertson. Kansa's representatives were not given a copy of the examination for discovery. They did not know about Little's admissions on discovery. These admissions included the admission that Little did not deny Confederation Life had consulted him about the condominium clause, that he admitted he had not responded to Confederation Life's request for an opinion on the condominium clause in June 1983, that he had a conflict, that Confederation Life's in-house solicitor had alerted him to the existence of ss.7(9) and (10) of the *Condominium Act* in August, that he knew he had a problem and that he had spoken to his partner but not disclosed his conflict of interest. The trial judge concluded:

> Mr. McNeil fell below the standard of care expected of competent, experienced and specialized counsel by reason of his failure to canvass with and advise Kansa that Mr. Little probably knew or ought to have known of circumstances giving rise to a potential claim against him prior to December 30, 1983, the date on which the firm applied for excess coverage with Kansa.

59 There was ample expert evidence for the trial judge to conclude that, as a result of the information in the discovery, McNeil should have realized there was an issue of coverage raised by the discovery and the fact that he did not was negligence.

60 Having upheld the trial judge's finding of liability concerning McNeil's negligence, the question becomes what was lost as a result? The appellant submits that nothing was lost and advances three arguments in this regard. Firstly, the appellant submits that McNeil owed a duty to the insured Little as well as to Kansa. Consequently, it would have been inappropriate for McNeil to tell Kansa of Little's misrepresentation and to advise Kansa to deny coverage. Secondly, the appellant submits that the trial judge's conclusion that Kansa could have successfully denied coverage is flawed because she relied on expert evidence to reach this conclusion and she was not entitled to do so. Thirdly, the appellant submits that Kansa probably would not have been successful in denying coverage because Kansa was estopped by this time from denying coverage. I will address each of these arguments in turn.

61 In order to deal with the appellant's submission that McNeil could not have advised Kansa of any information relating to coverage because it would have put him in conflict with the duty owed to Little and his firm, it is essential to consider the state of the litigation. The primary insurer of Shepherd McKenzie, American Home, was representing the interests of the insured Little and had done so since it had been notified by Little of the claim against him in February 1985. Borden and Elliot were the law firm of record for Little. McNeil had been retained by Kansa in February 1987. Although McNeil had recommended to Kansa that it consider taking over the defence of Little, at the time McNeil read Little's examination for discovery, September 1990, Kansa was not directing Little's defence. That defence was only undertaken some seven months later in April 1991 when McNeil replaced Borden and Elliot.

62 As I have indicated, on his examination for discovery, McNeil admitted that Fellowes, McNeil, "...was retained to protect Kansa's interests, as opposed to the insured's interests up and until [it] undertook the defence of the insured." McNeil's admission prevents him from asserting that he had a legal duty to Little at that time. McNeil's admission supports the trial judge's conclusion that, at the time McNeil read Little's examination for discovery, he should have realized that it raised an issue of coverage and, given his unlettered duty to the insurer, should have reported this to Kansa.

63 The decisions cited by the appellant such as *Laurencine v. Jardine* (1988), 64 O.R. (2d) 336 (Ont. H.C.) , and *Hopkins (Committee of) v. Wellington* (1999), 68 B.C.L.R. (3d) 152 (B.C. S.C.) are not relevant because they deal with the situation when a coverage issue arises after an insurer has retained a law firm to defend an insured. The information received from the insured in such circumstances is privileged information because it arises in the course of the solicitor-client relationship. That is not the situation here. McNeil had not been retained to defend Little at this time. The information that McNeil obtained did not arise as a result of confidential or privileged information that Little gave to American Home that, impressed with a confidentiality, had been passed on to McNeil. The information arose from Little's examination for discovery and the opposing party had the information. McNeil was not in a position of conflict. A reasonably competent insurance litigator in McNeil's position would have been unconstrained in bringing to Kansa's attention the coverage problem, and would have done so.

64 McNeil's negligence in failing to do so resulted in Kansa losing the opportunity to further question the issue of coverage and to deny coverage.

65 The appellant's second submission is that the trial judge erred in accepting the opinion evidence of Gilbertson as evidence on the question of whether Kansa could have successfully denied coverage to its insured. Gilbertson was called as an expert witness by Kansa. He had been an insurance adjuster for one of the biggest adjustment bureaus in Canada adjusting all types of claims from 1957 until 1971 when he resigned and went to law school. In 1974, he graduated and after being called to the bar practiced in the insurance field doing primarily property and general liability cases until 1994 at which time he retired from active practice. He remained active doing some mediations and arbitrations. There was no issue that Gilbertson was qualified to give opinion evidence with respect to "the standards of what Mr. McNeil should or should not have done when he's confronted, when he receives the file, and what his obligations might be at that time." The appellant submits however that the trial judge should not have heard expert evidence on the very questions of fact and law to be decided by the court and that the reception of such evidence was contrary to the rule in *Midland Bank Trust Co. v. Hett* (1977), [1978] 3 All E.R. 571 (Eng. Ch. Div.) at 582, a solicitor's negligence case. In that case, Oliver J. stated:

> This new plea does however raise an issue of law not apparent on the original pleadings, namely what is the scope of a solicitor's duty when he is consulted about a particular aspect of a problem: is he entitled to confine himself to the particular matters for which he is retained to advise or must he consider all the circumstances affecting the underlying data including hypothetical circumstances or risks to which is attention is not directed and on which his advice is not specifically sought?
>
> As to this I have heard the evidence of a number of practising solicitors...I must say that I doubt the value, or even the admissibility, or this sort of evidence which seems to be becoming customary in cases of this type. The extent of the legal duty in any given situation must, I think, be a question of law for the court. Clearly if there is some practice in a particular profession some accepted standard of conduct which is laid down by a professional institute or sanctioned by common usage, evidence of that can and ought to be received. But evidence which really amounts to no more than an expression of opinion by a particular practitioner of what he thinks he would have done had he been placed, hypothetically and without the benefit of hindsight, in the position of the defendants is of little assistance to the court, whilst evidence of the witnesses' view of what as a matter of law, the solicitor's duty was in the particular circumstances of the case is, I should have thought, inadmissible for that is the very question which it is the court's function to decide.

66 Gilbertson did not testify about what he would have done had he been placed in the position of McNeil. He did, however, give evidence of what McNeil's duty was in the particular circumstances of the case, namely that he ought to have been aware that an issue of coverage was raised based on the transcript and that he ought to have alerted Kansa of this. In addition, Gilbertson also gave evidence as to whether Kansa would have denied coverage and whether a denial of coverage would have been successful. The appellant objects to the admission of Gilbertson's evidence on the basis it is the ultimate question the court had to decide.

67 In their text, "The Law of Evidence in Canada", Sopinka Lederman and Bryant, Butterworths Canada, 1992, state at 540:

> Wigmore has pointed out the fallacy of this reasoning (disallowing expert evidence on the issue before the court) by emphasizing that the jury has the power to accept or reject evidence as it wishes, and, accordingly, it is not obliged to take the expert's opinion on the point as conclusive.

The authors also point out, at p.542, that, historically, the rule against accepting evidence on the very issue before the court has been ignored by many Canadian and English courts. The situations where the rule has been applied recently relate to expert evidence on such matters as the assessment of credibility of a witness. Such evidence is superfluous in that the trier of fact can just as readily draw the necessary inferences without the assistance of an expert. See pp. 545-546 Sopinka, *supra* , and cases cited thereat. That is not the situation here. Section 40 of the draft *Uniform Evidence Act* in *Report of the Federal/Provincial Task Force on Uniform Rule of Evidence* (Toronto: Carswell, 1982, at 554) states:

> A witness may give opinion evidence that embraces an ultimate issue to be decided by the trier of fact where (a) the factual basis for the evidence has been established; (b) more detailed evidence cannot be given by the witness; and (c) the evidence would be helpful to the trier of fact.

68 Section 40 is really a proposed statutory formulation of the decision in *R. v. Fisher* , *supra* . The evidence of the expert met the three requisite criteria. The trial judge had found Little made a misrepresentation on his application for insurance and that McNeil was negligent because he did not appreciate that the examination for discovery raised this issue. Thus, the factual basis for the evidence was established. The trial judge ruled that she wished to hear the evidence. It appeared more detailed evidence was not otherwise forthcoming. Obviously, as the trier of fact, she felt it would be helpful. The trial judge did not err in receiving expert evidence on the ultimate issue of whether Kansa would have successfully denied coverage.

69 The appellant's third submission is that Kansa's conduct amounted to a waiver of any right to deny coverage and that Kansa was estopped from denying coverage to Little's firm. With respect to estoppel, there must first be a finding that the insurer had knowledge of facts giving rise to a lack of coverage for estoppel to apply: *Rosenblood Estate v. Law Society of Upper Canada* (1989), 37 C.C.L.I. 142 at 155 (Ont. H.C.) aff'd (1992), 16 C.C.L.I. (2d) 226 (Ont. C.A.) . Until the file was transferred to Fellowes, McNeil and McNeil read the examination for discovery, Kansa did not have the information on which to make a decision about whether or not to deny coverage. In addition, there is no evidence from Little of detrimental reliance on Kansa defending him as Little did not testify. As a result, Kansa would not have been estopped from denying coverage. Before one can find waiver by conduct, the conduct must be express and unequivocal: *Northern Life Assurance Co. v. Reierson* (1976), [1977] 1 S.C.R. 390 (S.C.C.) at 398. That is not the situation here. There was no such conduct by Kansa of its rights under the policy to deny coverage if appropriate. The trial judge carefully analyzed the facts of the events prior to 1991 when McNeil formally became solicitor of record for Little and concluded that a denial of coverage would have been successful. Again, there is evidence to support the findings of the trial judge and I would not interfere with them.

70 The appellant submits that, even if coverage could have been denied to Little, the trial

judge erred in holding that coverage could have been denied to Shepherd McKenzie. This issue does not appear to have been argued at trial. The trial judge found that the declaration made by the firm's applicant was made on behalf of all the members of the firm. This is not a case of fraud as in *Fisher v. Guardian Insurance Co. of Canada* (1995), 3 B.C.L.R. (3d) 161 (B.C. C.A.) . I am not aware of any wording in the application or the policy that would lead me to conclude the policy is void only as against Little and not the other members of the firm.

71 Finally, the appellant submits that Kansa was contributorily negligent. This submission is without merit and can also be summarily dismissed.

72 I would dismiss the appeal with respect to the Little matter.

The Uniroyal v. Sundor mini-trial

73 In 1990, the presence of the chemical nitrosodimethylamine ("NDMA") was found in juice manufactured by Sundor. On July 13, 1990, Sundor issued a statement of claim against Uniroyal, a rubber manufacturer, which alleged that the discharge of the chemical from Uniroyal's Elmira manufacturing plant had contaminated the ground water system used by Sundor to manufacture its juices. Uniroyal was added as a third party to a related action commenced by N.T.C. foods against Sundor. Uniroyal forwarded the claim to Kansa, one of its many insurers who had been on risk for a three-year period, under two standard Comprehensive General Liability ("CGL") policies #200 2867 and #250 3150 as well as two umbrella policies.

74 The statement of claim alleged, in paragraph 3:

> The defendant Uniroyal Chemical Ltd. (Uniroyal) owns property and operates a chemical plant (collectively the 'Uniroyal Plant') located in Elmira Township. During the course of its manufacturing processes, the Uniroyal Plant produces and has produced NDMA. The NDMA so produced is being deposited, discharged, emitted, spilled or otherwise escapes or has escaped ...from the Uniroyal Plant into the groundwater system in the Region. (the "Groundwater System"). Uniroyal is and was the owner and person having charge, management or control of the NDMA immediately before it was discharged into the Groundwater system.

75 Kansa was of the opinion that the loss was clearly excluded under the insurance policies it had issued and instructed McNeil to defend the claim on a basis that would preserve its right to deny coverage to its insured. McNeil did not deliver a reservation of rights letter saying that the insurer's acts were not an acknowledgement of liability.

76 During the course of the litigation, the Supreme Court of Canada handed down its decision in *Nichols v. American Home Assurance Co.*, [1990] 1 S.C.R. 801 (S.C.C.) . That case held that the duty of an insurer to defend under a contract of insurance is independent of the duty to indemnify and arises when the claim alleges acts or omissions which may fall within the policy coverage. The duty to defend is, however, restricted to claims for damages that might fall within the scope of the policy. In *Nichols* , the only damages sought against the insured were with respect to fraudulent acts or omissions and, as such, damages were excluded

under the policy. Accordingly, the Supreme Court held that the requirement to defend did not apply.

77 Kansa took the position that it was not obliged to defend its insured, Uniroyal. Uniroyal brought an application for a separate defence at Kansa's expense. The application was granted on the basis that the pleadings framed factual issues which might give rise to coverage under the Kansa policies. This conclusion was based in part on an admission in an affidavit signed by Kansa's claims supervisor. That affidavit had been drafted by McNeil.

78 Eventually, the litigation was resolved without Kansa having to make payment under the policies as the Ministry of the Environment took responsibility for Sundor's loss. Kansa was, however, left with Uniroyal's legal fees. In the *Uniroyal* mini-trial, Kansa sued McNeil to recover the cost of these fees.

79 The trial judge concluded that, but for McNeil's negligence, Kansa could have successfully refused to defend Uniroyal on the basis that coverage was clearly excluded as a result of the pollution exclusion clauses in the policies. In her reasons, she stated:

> The wording contained in the language of the relevant policies was examined in detail in the evidence at this trial. I have come to the conclusion, having regard to the general and specific allegations against Uniroyal contained in Sundor's Statement of Claim when read together with the wording of the exclusions that, on the balance of probabilities, Sundor's claim as framed would have probably been excluded from coverage under Kansa's policies and that a simple denial of coverage would be an appropriate response. I accept as correct the probability of an absence of coverage was so high that his would have been the correct response. I do not agree with Mr. Webb that the denial of coverage in the coverage in the circumstances of this case would have exposed Kansa to the risk of allegations of bad faith. Inasmuch as the duty to defend is only triggered with respect to insurance as it is afforded by the policy, the obligation to defend cannot exist if it is clear that the insurer can deny indemnity coverage at the early stages of litigation on the basis of the clear application of the exclusions. In coming to these conclusions, I have analysed and considered, with the benefit of expert opinion, the state of the law with respect to pollution exclusion clauses in mid 1990 when this claim first came to Kansa's attention and in mid 1991 at the time when Kansa was embroiled in motions respecting the application for intervenor's status and motions to compel Kansa to pay for the defence of Sundor's claim by Uniroyal.
>
> I have concluded that the claims set forth in this Statement of Claim could be traced to an excluded event that being a discharge of a contaminant with the result that on the balance of probabilities the exclusions contained in the policies could reasonably be expected to apply.
>
> . . . . .
>
> I have concluded that Mr. Gilbertson and Mr. McInnis are correct in their reasoning that the outcome of the *Nichols* case when matched with the absolute pollution exclusions contained in the relevant policies are such that Kansa would have had sufficient grounds to deny any indemnity obligations and therefore any defence obligations from the outset of

the matter.

80 The appellant submits that Kansa would have been obligated to provide a defence to Uniroyal under the 1987 umbrella policy. As a result, the appellant submits that even if Fellowes, McNeil was negligent in its handling of the Uniroyal claim, no damage was caused by Kansa having to pay for a separate defence for Uniroyal. Fellowes, McNeil would have been obliged to provide a defence under the umbrella policy in any event. Kansa's position is that liability was excluded under the 1987 umbrella policy as well as the other insurance policies.

81 An umbrella policy is a type of excess policy that provides coverage above the limits of a primary policy. An umbrella policy may also "drop down" and become a primary policy where the claim is excluded by the primary policy but not by the excess. The umbrella policy includes a duty to defend as well as to indemnify.

82 The 1986 umbrella policy, like the 1986 and 1987 primary policies, contained a clause excluding coverage in the event of damages arising from the discharge of pollutants into "*any water of any description no matter where located or how contained or into any watercourse drainage or sewer system* ." The 1987 umbrella policy, however, contained a slightly differently worded clause. The 1987 umbrella policy only excluded "*property damage arising out of the discharge of ... pollutants into or upon land, the atmosphere or any watercourse or body of water* ."

83 The overarching question is, therefore, whether the trial judge was correct in concluding, as she appears to have done implicitly, that the difference in the wording of the 1987 umbrella policy, was of no import

84 The appellant submits that the words "property damage arising out of the discharge ... of pollutants into or upon land, the atmosphere or any watercourse or any body of water" do not exclude pollution from groundwater. In support of its submission, the appellant relies on *Murphy Oil Co. v. Continental Insurance Co.* (1981), 33 O.R. (2d) 853 (Ont. Co. Ct.) , at 859; *State Of New York v. Travellers Indemnity Company of Rhode Island*, 506 N.Y.S. 2d 698 (U.S. N.Y.A.D. 3 Dept. 1986) ; and *Lumbermans Mutual Casualty Company v. Plantation Pipeline Company*, 447 S.E. 2d 89 (U.S. Ga. Ct. App. 1994) . In the *Murphy Oil Co.* case, supra, Fogarty J. concluded that the words "watercourse or any body of water" applied only to surface water and did not include a well. He adopted a definition of watercourse at 859 as "... a natural flow of water along a distinct channel which it forms. It is immaterial whether the origin of the water be a spring or springs or the rain or snowfall...". He also held that a body of water:

> ... is that which lies with defined limits (such as a lake or a pond) and although it might form part of a watercourse it is distinguished from it in that the water is not subject to the same degree of continuous flow which is usually observed within the banks of a river or stream. As in the case of a watercourse, it would not include that water which is outside its boundaries, whether from underground sources or surface run-off drainage. I hold that "watercourse" and "body of water" refer to water which is non the surface of the earth and that these terms do not include subterranean water passages, watersheds, springs or that water

feeding into or collected by a man-made well.

85 Accordingly, he held that the insured's damages were covered under the policy and that the insurer had not cause to refuse to defend the action and refuse to pay on the basis that coverage was excluded. In coming to his conclusion, however, Fogarty J. noted:

This clause does not refer to emission of the pollutant into and upon land — .

86 The decision in *State of New York v. Travelers Indemnity* , *supra* , deals with an exclusion for damage arising out of "any emission, discharge, seepage, release, or escape of petroleum or petroleum derivatives into 'any body of water'". In that case, the soil and underground water of the area were contaminated and the court held that the exclusion clause did not apply. Again, the clause did not refer to emission of any pollutant into and upon land. Similarly, the decision in *Lumbermens Mutual Casualty v. Plantation Pipeline Company* , *supra* , holds that groundwater is not a "body of water" for purposes of exclusion from coverage the discharge of oil. He defined the words "body of water" at 93 as "an aggregate of water having defined boundaries". The court also found that the term "body of water" was ambiguous and that numerous cases in other jurisdictions had held that groundwater could be a body of water if it came from major aquifers. Overall, there was, however, persuasive authority that a body of water did not necessarily include groundwater. A separate exclusion clause excluded damage from pollutants into or upon land but the exclusion clause stipulated that the exclusion did not apply where the discharge was sudden or accidental. Because the leak was sudden and accidental, that exclusion clause was held not to apply.

87 In the case before us, the parties had, by agreement, deleted the exception stating that the exclusion clause would not apply where the discharge or emission was sudden and accidental. The exclusion clause does not just exclude damage arising out of the discharge of pollutants into a body of water but the discharge of pollutants "into or upon land".

88 The respondent submits that, because none of the exclusion clauses in the cases I have discussed contained the words "into or upon land", these cases have no application to the case before us. I note, however, that the wording of the clause in question excludes *damage* arising out of the discharge ... of pollutants into or upon land. Here, it is at least arguable that the damage was not caused by the discharge of a pollutant into land. The damage was caused by the discharge into groundwater. Groundwater is defined in *Webster's Encyclopedic Unabridged Dictionary* , Grammercy Books, New York, 1989, as:

The water beneath the surface of the ground, consisting largely of surface water that has seeped down: the source of water in springs and wells.

89 In my opinion, coverage was not unequivocally excluded under the 1987 umbrella policy. I would respectfully disagree, therefore, with the trial judge's conclusion that, on the balance of probabilities, the exclusion clauses contained in the policies could reasonably be expected to apply. As a result, even if Fellowes, McNeil was negligent in the manner in which it handled the Uniroyal claim, no damage resulted because loss due to groundwater was not clearly excluded under the 1987 umbrella policy.

90 Accordingly, I would allow the appeal with respect to the *Uniroyal* mini-trial, set aside the judgment and dismiss the claim for damages.

Conclusion

91 I would dismiss the appeal in the *Little* mini-trial. I would allow the appeal in the *Uniroyal* mini-trial. Bearing in mind the result, I would allow the respondent two-thirds of its costs of this appeal.

Appeal allowed in part.

FN* Additional reasons at (November 9, 2000), Doc. CA C30847 (Ont. C.A.).

FN1 The Supreme Court of Canada has recently clarified the law respecting an insurer's duty to defend. Where the plaintiff's claims could not trigger coverage under the policy the insurer has no duty to defend: *Sansalone v. Wawanesa Mutual Insurance Co.*, 2000 SCC 24 (S.C.C.) ; *Sansalone v. Wawanesa Mutual Insurance Co.* (2000), 74 B.C.L.R. (3d) 21 (S.C.C.) ; see also *Godonoaga (Litigation Guardian of) v. Khatambakhsh (Guardian of)* (2000), 49 O.R. (3d) 22 (Ont. C.A.) a decision of the Ontario Court of Appeal, June 12, 2000.

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