[FEATURE]

BY JASON KATZ AND SCOTT KASTELIC

ASSIGNMENT OF BAD FAITH CLAIMS

Insurance is marketed to the public as a vital safety net in times of crisis. It is intended to mitigate the life-altering consequences of unforeseen traumatic events. What happens though when an insured who has signed up for coverage and dutifully paid their premiums not only has their claim denied but is subjected to unfair treatment? The insurance company becomes an additional source of hardship rather than a financial lifeline. This breakdown most often occurs when insurers deny legitimate claims despite coverage, unreasonably delay payments without justification, or offer significantly lower compensatory amounts than the benefits or limits outlined in the policy. We see this conduct first-hand in our areas of practice when dealing with clients that have been wrongfully denied claims for long-term disability benefits or coverage for a property loss. The denial of a claim or termination of a benefit may have merit but the conduct of the insurance company must be scrutinized at all times to ensure they are not acting in bad faith.

What happens though when an insured who has signed up for coverage and dutifully paid their premiums not only has their claim denied but is subjected to unfair treatment?

THE INSURANCE COMPANY BECOMES AN ADDITIONAL SOURCE OF HARDSHIP RATHER THAN A FINANCIAL LIFELINE.

Despite the mistreatment that insurers may engage in, under Ontario law they are obligated to act in good faith towards their insureds due to the recognized power imbalance between the parties.[1] This inequality occurs both in terms of resources and experience in dealing with claims. As noted in *Halsbury's Laws of Canada - Insurance,* the relationship is a particularly "vulnerable one" subject to "special privileges".[2] In recognition of these vulnerabilities, insurance policies are regarded as being contracts of the "utmost good faith".[3] This principle of good faith has been in practice for over 200 years, originating from marine insurance. Ship owners and captains on dangerous voyages could not provide their insurers with sufficient objective proof about their activities. As a result, both the details of the losses sustained on these expeditions and the agreement to pay these claims were dependent on trust, good faith communication and disclosure.[4] This requirement continues today, albeit in less extreme circumstances, making it imperative that insurers, adjusters and defence counsel are reminded to remain cognizant of these obligations when dealing with policyholders.

Plaintiff's counsel are typically mindful of these concerns when dealing directly with insurance companies on first party claims where clients are seeking compensation under their own policy for covered losses. They should also remember the implications of this obligation in third party actions where accident victims are seeking compensation from a defendant's insurance company for damages caused by a negligent tortfeasor. In those cases, the defendant's insurer owes their insured a duty of good faith in the course of defending the action and indemnifying the policyholder in accordance with the policy terms, for any damages payable in a settlement or verdict. This obligation requires the insurance company to protect their insured from unreasonable financial risk which can prove challenging when a claim is potentially greater than the policy limits. When insurers fail to meet expectations, a bad faith claim may arise.

The additional risk this duty creates for insurance companies should be used as a tool by plaintiff's counsel attempting to negotiate a settlement at an amount the other side may not be willing to initially pay. The amount of liability coverage in Ontario appears to be gradually increasing but $1,000,000 is still the most popular policy limit. This amount of coverage however does not represent the same protection it once did. With a cap on general damages that is gradually increasing (now over $400,000) and annual inflation causing both a diminished perception in the value of a dollar and a significant rise in the cost of care, claims with a risk of exceeding $1,000,000 are becoming more common. As a result, there is an increased pressure on insurance companies to settle files for more than their perceived value if the amount is within policy limits and prevents exposing their insured to personal financial liability.

This inherent conflict of interest between the insurer and their insured should be top of mind on large loss cases where policy limits are at stake. The defence lawyer represents the defendant but is taking their instructions from an adjuster who is focussed on getting the best result possible for their employer. They do not owe a duty of good faith to the plaintiff. The adjusters and their lawyers are rewarded for performing well on these files with incentives ranging from positive performance reviews to promotions to additional work in the future. This approach leads to a vigorous defence of these claims and an attempt to minimize the damages paid. The problem with this aggressive mentality is it becomes counter-intuitive when a settlement that will protect their insured's personal assets is larger than their valuation of the file and prevents them from attempting to minimize the payment made by the company they are working for.

Insurers have established protocols with how they deal with these situations but it appears some companies are more stringent while others are willing take on greater risk for their policyholders in an effort to obtain a better result for the company. The frequent turnover of adjusters over the long life of a file may also lead to confusion about whether these procedures were followed by one of their predecessors. To help mitigate the conflict, it is incumbent upon insurers and their counsel to continue to consider the exposure of a defendant to a judgment beyond policy limits. Either party's refusal to accept an offer within limits for a claim worth significant damages creates an increase in the inherent tension between insurer and defendant. When a legitimate concern arises, the insurer has a duty to inform the defendant about the importance of obtaining independent legal advice to advise them on the risk of their financial exposure should a judgment exceed the policy limits. While an insurer may deem the continuity of an action worthwhile for their own self-interest, it is noted in *Halsbury's Laws of Canada* that "as part of the duty of utmost good faith an insurer is required to settle third party claims within policy limits."[5] Further still, "if the insurer breaches its good faith duty to make its best efforts to resolve the claim within policy limits, it may be responsible for paying the underinsured portions of the third party judgment."[6] Consequently, settling within policy limits must be a leading consideration for the adjuster and defence counsel regardless of any other mandate they are facing. The analysis when determining whether to risk an insured's assets in continuing to defend an action must be included in the decision-making process even if the danger is determined to be remote. Otherwise, the decision to proceed will likely be seen as preferential treatment for the insurer over the insured, leading to a potential claim for bad faith.

Finally, after years of litigation, a trial is conducted in which the court awards the plaintiff a judgment in excess of the insurance coverage available and the offers to settle which were within policy limits. After the excitement of the successful trial wears off, the plaintiff is now faced with the uncertainty of attempting to collect on the judgment. The insurance company will also inevitably appeal the verdict in part because of the financial exposure for the insured and the risk of a bad faith claim. These issues will unfortunately create significant additional delays for the compensation the plaintiff has been waiting years to receive.

Whether there are legitimate issues for appeal or not, the insurance company will file a Notice of Appeal for a number of reasons. It delays payment of the judgment and creates some risk for the plaintiff that the decision or part thereof will be overturned on appeal. During this time, defence counsel

THIS PRINCIPLE OF GOOD FAITH HAS BEEN IN PRACTICE FOR OVER 200 YEARS, ORIGINATING FROM MARINE INSURANCE.

Ship owners and captains on dangerous voyages could not provide their insurers with sufficient objective proof about their activities. As a result, both the details of the losses sustained on these expeditions and the agreement to pay these claims were dependent on trust, good faith communication and disclosure.

dealing with the appeal will likely reach out to plaintiff's counsel in an effort to resolve the action. These negotiations post-trial are quite different than prior settlement discussions as the amounts being contemplated are beyond the policy limits. The insurance company is offering these increased amounts because of their duty of good faith to their insured and the financial risk they have created for them with their conduct. The insurer will still likely not offer the full amount of the judgment and be looking for some discount due to the perceived leverage caused by the risk of the appeal and the potential difficulty in personally collecting from the defendant. To counter this strategy, plaintiff's counsel can send a letter to defence counsel indicating that writs of garnishment and of seizure and sale will be filed within a defined period unless the insurer guarantees payment of any amounts owed in excess of the policy. If the insurance company does not attempt to deny the requisition of these writs due to the appeal, they may be motivated to accept these terms as failing to do so would potentially open them up to a bad faith claim and the subsequent negative public attention that would come with such a case. This would provide the plaintiff with some solace as the full amount of the judgment would then be protected (subject to appeal) and avoid the need to pursue the defendant's assets to obtain full compensation.

However, should defence counsel refuse or be non-responsive, writs of garnishment and of seizure and sale in the jurisdictions where the defendant's income and assets are located may then be filed. The plaintiff will then have a number of options at their disposal.

Enforcing the writ is a remedy available under Rule 60 of the *Rules of Civil Procedure*. The rule provides the tools to effectively account for what assets the defendant has and how they may be encumbered. In this scenario, non-compliance with the writ is not only possible but probable. The defendant has been placed in a situation they never thought possible. They paid their insurance premiums, cooperated fully with their insurer and followed the advice of defence counsel…just to find out that their life savings and wages are now in jeopardy. When compliance from the defendant to surrender their assets is not forthcoming, Rule 60.18 provides counsel with the power to conduct an examination in aid of execution to obtain information relating to the reason for nonpayment, the defendant's income and property, and their means to satisfy the judgment. The examination will hopefully provide a better understanding on the likelihood of payment and the path to eventual collection. A settlement for some or all of the damages beyond their policy coverage is possible.

While the writs provide the plaintiff with certain rights, the expensive process is time-consuming and the outcome is uncertain. A judgment-proof defendant will limit compensation to the policy limits available despite an award worth considerably more. A viable alternative is to attempt to obtain an assignment of the defendant's bad faith claim against their own insurer. Bad faith claims emanating from personal injury matters are assignable after judgment.[7] Enforcement of the judgment will likely lead to the defendant or their counsel reaching out to discuss a resolution. Given the way they were treated, the defendant feels no loyalty to their insurance company and would be prepared to assist in the pursuit of a bad faith claim against them in order to protect their personal assets and income. After years of treating the defendant as an adversary, plaintiff's counsel would then be acting for them in an action against their insurance company. The insured would assign their rights to the proceeds from the lawsuit to the plaintiff in exchange for an agreement that the plaintiff would limit their rights under the judgment to any amount they were successful in obtaining in the bad faith claim.

The plaintiff may choose to proceed in this manner because they know the insurance company has the resources to pay the judgment. They would be trading in the uncertainty of collection from the defendant with the risk of successfully proving the bad faith claim against the insurance company. Plaintiff's counsel would have to analyze the behaviour of the insurer to determine the likelihood of proving bad faith before providing their client with advice on which path would likely lead to the best financial outcome.

If the assignment is the option chosen, a claim against the insurer is then commenced. The action will detail the elements of bad faith discussed above such as declining legitimate offers within policy limits while exposing their insured to unnecessary financial risk, placing their own interests ahead of the insured, failing to suggest obtaining independent legal advice once a conflict had formed, and unnecessarily prolonging the litigation.

Prosecuting bad faith claims is an important exercise in not only ensuring that plaintiffs receive the compensation they are entitled to, but also in protecting the rights of policyholders from improper conduct by insurers and defence counsel. With judgments increasingly exceeding policy limits, the potential for financial exposure to defendants continues to rise. The duty of good faith increases the tension for insurers between protecting their insureds from financial exposure and reducing the cost of claims. When they fail to meet these obligations, plaintiff's counsel should be prepared to pursue bad faith claims to obtain full compensation for their clients.

***Jason Katz** is an OTLA member and practices with Singer Katz LLP*

***Scott Kastelic** is an OTLA member and practices with Singer Katz LLP*

NOTES

[1] *Coronation Insurance Co. v. Taku Air Transport Ltd.*, 1991 CanLII 16 (SCC), [1991] 3 SCR 622.

[2] Knutsen, E. (2023). *HIN – 63 The Basic Principle. In Halsbury's Laws of Canada – Insurance* (2023 Reissue). LexisNexis.

[3] *Ibid.*

[4] *MacNeil (Litigation Guardian of) v. Bryan,* [2009] O.J. No. 3461, 77 C.C.L.I. (4th) 96 (Ont. S.C.J.).

[5] *Knutsen,* E. S. (2023). HIN-84 Third party claims. *Halsbury's laws of Canada - Insurance (2023 Reissue).* VI. Duties of policy holders and insurers.

[6] *Shea v. Manitoba Public Insurance Corp.*, [1991] B.C.J. No. 711, 55 B.C.L.R. (2d) 15 (B.C.S.C.); *Dillon v. Guardian Insurance Co.,* [1983] O.J. No. 2534, 2 C.C.L.I. 227 (Ont. H.C.J.). However, "the duty to investigate fairly, in a balanced and reasonable manner, is owed only to the insured, not third parties": Trial Lawyers Association of *British Columbia v. Royal & Sun Alliance Insurance Co. of Canada,* [2021] S.C.J. No. 47 at para. 35, 2021 SCC 47 (S.C.C.) Ibid.

[7] *Ma v. Ma,* 2012 ONCA 408 (CanLII).