Newsletter

IN THIS ISSUE

Death by a Thousand Cuts (or by Dents, Buckling, Frame Damage…)

The recent decision of *2068286 Ontario Inc. v. Jevco Insurance Company,* 2014 ONSC 3929 involved a plaintiff bringing a claim against Jevco Insurance ("Jevco") for indemnity under an insurance policy relating to the theft of a 2009 Peterbilt tractor from a storage yard, and for damages relating to alleged bad faith on the part of Jevco in it's handling of the claim.

This decision provides an interesting analysis of the obligation under Ontario's *Insurance Act* for an applicant to provide a full and fair description of the risk to an insurance company.

For the reasons described below the Court held that Jevco need not indemnify the plaintiff for the loss of the tractor and had properly taken an "off coverage" position on the basis that the plaintiff had not accurately and adequately described the condition of the tractor at the time of applying for the insurance coverage. The Court also decisively ruled that there was no bad faith whatsoever on the part of Jevco in its handling of the claim.

The Facts

The plaintiff, 2068286 Ontario Inc., purchased a 2009 Peterbilt tractor for $109,045 on September 13, 2010, insuring it with Jevco several days later. In December of that year the Peterbilt was stolen from a lot where the plaintiff parked it. It was never recovered.

The plaintiff's president testified at trial that he did not ask many questions of the vendor who sold it to the plaintiff. He checked the ownership for the brand (which was "none"), and gave evidence that there was nothing much in terms of unrepaired damage. The question of, or existence of "unrepaired damage" would in fact provide to be the main issue at trial and prove to be the undoing of the plaintiff's

FIRM AND INDUSTRY NEWS

- **Canadian Board of Marine Underwriters** Annual Golf Tournament, Richmond Hill Golf Club, August 19, 2014.
- **International Civil Aviation Organization** Seminar on "Fuelling Aviation With Green Technology" Montreal, September 9-10, 2014.
- **Rui Fernandes** will be speaking on "The Changing World of Customs Broker Risk and Liability" at the **Canadian Society of Customs Brokers** annual meeting in St. John's Newfoundland on September 15, 2014.
- **Railway Association of Canada's** Canadian Rail Summit 2014, at the Palais des congrès de Montréal (Montréal Convention Center), September 21-23.
- **International Union of Marine Insurers** Annual Meeting in Hong Kong on September 21-24.
- **Canadian Transportation Lawyers Association** Annual Meeting and Conference, Halifax Nova Scotia, September 24-27, 2014. **Kim Stoll** will be moderating the Modal Updates Panel, **Rui Fernandes** will be providing the Trucking Modal Update (Canada). **Gordon Hearn** will be attending as the Transportation Lawyers Association representative to the Canadian Transport Lawyers Association.

case. In particular, this individual relied on the safety certificate and annual inspection certificate secured by him just prior to or at the time of purchase to determine that the tractor was in good condition.

The plaintiff applied for the insurance for the Peterbilt from Jevco. It used a broker to apply for the insurance. In its signed application to Jevco, it was indicated that the vehicle had a value of $109,045.

The plaintiff was later required to sign the Ontario Application for Automobile Insurance (the OAF1 form) to finalize his application for insurance with Jevco. Most importantly, a box on the form soliciting information as to whether there was any "*unrepaired damage*" was filled in by the plaintiff to say "*no*".

However, there in fact existed the following problems or anomalies to the tractor at the time of the application for the insurance coverage as established by photographs taken by the plaintiff admitted into evidence at trial:

- the rear fender was missing;
- the right convex mirror was missing;
- there was buckling on the back panel;
- the heat shield was bent on the passenger side and was different from the one on the driver's side, with the installation being done incorrectly;
- the backup light was missing as the Peterbilt was manufactured with one;
- the seam on the bunk was not properly joined;
- empty holes on the bumper indicated that it was designed for a different truck;
- the bumper has been straightened out, resulting in buckling;
- the right headlight components showed crushing damage;
- the hood misalignment could be evidence of frame damage;
- the bonnet of the air breather was distorted;
- the lower step on the passenger side was missing and had likely "cut off", the same having been designed to be riveted to the tractor;
- the driver's side step was bent down, suggesting damage occasioned by a rollover incident, and
- the tires installed were too small given the Peterbilt's original construction.

Taken one by one in isolation, some or all of the foregoing might be said to simply evidence "wear and tear", "a degree of use" or merely cosmetic issues of the unit as opposed to "unrepaired damage". Jevco's underwriter did not see the photographs at the time of binding the risk. They were produced only in the context of the coverage litigation. Jevco's case at trial was that these items jointly or severally amounted to a unit that had been subjected to a history of trauma, neglect, abuse and shoddy repairs such that had its underwriter known of same at the time of the application being filed for the insurance coverage that it would have in fact rejected this risk. Jevco's concern, and the evidence of its underwriter (as was led at trial), was that the actual state of the tractor presented a clear "moral hazard" and potential for over-indemnification in the event of a loss (e.g. a claim being presented for pre-existing damage during the life of the policy) as well as an enhanced potential for third party liability claims (expert evidence at trial led by Jevco indicating that many of the above irregularities present a compromise to the roadworthiness and safety of the unit).

As to the plaintiff's claim for bad faith, Jevco's claims examiner, gave evidence regarding the insurer's investigation. This individual gave evidence that usual procedures were followed for theft investigations in the appointment of both an appraiser and an investigator. As the investigation proceeded, a number of "red flags" were raised leading to the off coverage position taken.

The Trial Decision

Jevco's defence relied primarily on sections 233(1)(a)(i) and (ii) of the Ontario *Insurance Act*

(and which are also mirrored in the standard form Ontario Automobile Policy). These sections state:

> ***Misrepresentation or violation of conditions renders claim invalid***
> *233. (1) Where,*
> *(a) an applicant for a contract,*
> *(i) gives false particulars of the described automobile to be insured to the prejudice of the insurer, or*
> *(ii) knowingly misrepresents or fails to disclose in the application any fact required to be stated therein;*
> *…*
> *a claim by the insured is invalid and the right of the insured to recover indemnity is forfeited.*

For subsection 233(1)(a)(i) to apply, the provision of the "false" particulars may be "innocent" (as opposed to "knowingly"), but the insurance company must prove that it was prejudiced as a result. For subsection 233(1)(a)(ii) to apply, the insurance company is not required to prove the prejudice element, but does need to prove the insured acted "knowingly" in misrepresenting or failing to disclose items in the application form.

The judge agreed with Jevco's position, accepting the evidence of its witnesses that the aforementioned defects were in fact material to both Jevco's underwriting guidelines in the acceptance of such risks, and in also accepting the trial evidence of an independent underwriter that Jevco's need for accurate and full disclosure in this regard reflected the general market practice.

The judge accepted Jevco's position that "unrepaired damage" for the purposes of the OAF1 form should include damage improperly or incompletely repaired, damage not repaired to industry standard, and items missing that are supposed to exist but do not as per the manufacturer's "build record".

The trial judge found that the lack of fair and accurate disclosure in the application caused Jevco prejudice in its decision making process as to whether or not to accept the risk, holding that:

> *Jevco was prejudiced in that it was deprived [of] the opportunity to make*

further inquiries as to the condition of the Peterbilt it was insuring. The actual condition of the tractor was not fully disclosed. The unrepaired damage was not minor.

Accordingly the judge held that Jevco was entitled to deny the claim on the basis of section 233(1)(a)(i).

Section 233(1)(a)(ii) was also considered. The trial judge noted that evidence of the plaintiff's president was that "he was completely unaware of any previous damage", and that at the time of purchase, "he noticed only little scratches and dents from normal wear and tear" was incredible. It did not help that this individual was himself a mechanic.

The trial judge concluded that the plaintiff "knowingly" misrepresented the condition of the vehicle to Jevco, and that Jevco was accordingly also entitled to deny the claim on this additional basis.

The claim in its entirety was accordingly dismissed against Jevco, which was found to have acted in good faith throughout in its dealings on the claim.

[Gordon Hearn and Kimberly Newton defended Jevco Insurance Company in this case.]

2. Marine Liability Act Limitation Period Cannot Be Extended

The recent decision of *Malcolm v. Shubenacadie Tidal Bore Rafting Park Limited*, 2014 NSSC 217 involved an infant claimant who was injured during a rafting excursion on the Shubenacadie River. The claimant brought an action against the raft operator for injuries suffered. The operator took the position that the applicable limitation period was under the Federal *Marine Liability Act* and that the action was started after that period. The operator brought a motion for summary judgment.

At issue was what is the applicable limitation period and had it expired before commencement of the action? Under the provincial law of Nova Scotia the claim would not be time barred as the limitation period would commence after the infant comes of age.

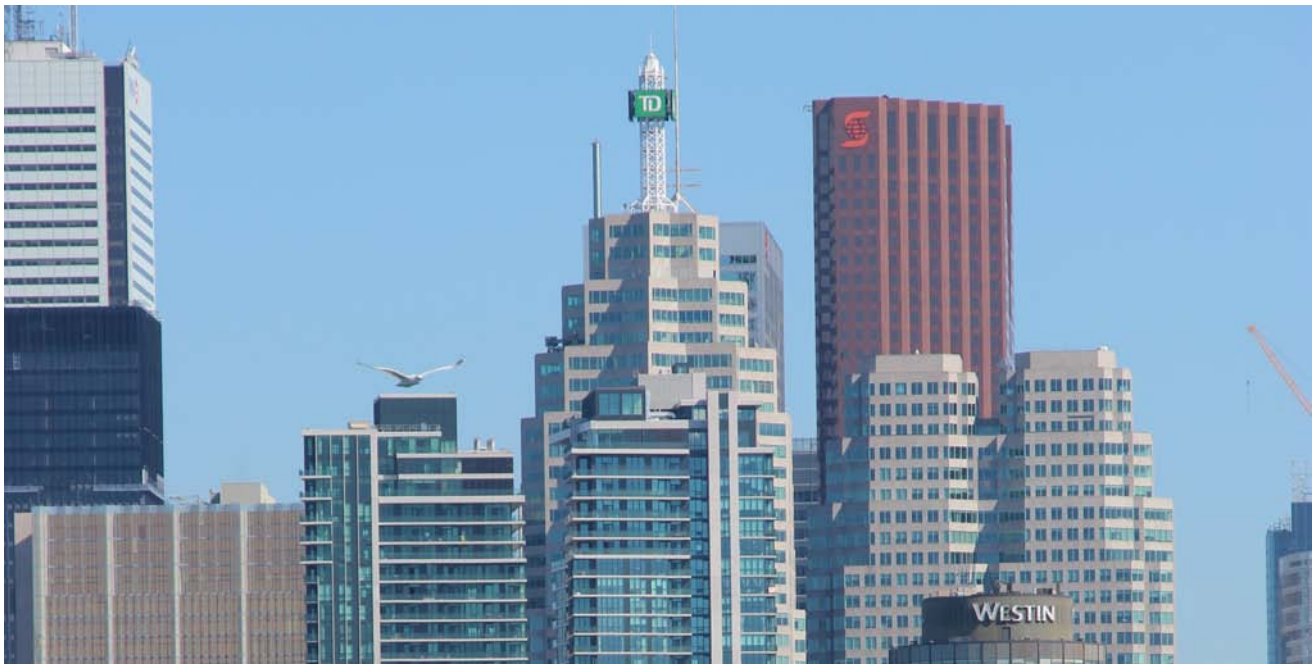
The Nova Scotia court looked at two prior decisions in New Brunswick and in Quebec in arriving at its decision.

In *MacKay v. Russell*, 2007 NBCA 55 (CanLII), 2007 NBCA 55, the New Brunswick Court of Appeal considered a claim for personal injuries suffered by a passenger on a whale watching excursion in the Bay of Fundy. The Court was asked to determine whether the claim was governed by the New Brunswick *Limitations of Actions Act,* or the provisions of the *Athens Convention* as incorporated in the *Marine Liability Act*. The Court concluded that federal law applied.

The Quebec Court of Appeal came to the same conclusion in *Frugoli v. Services aeriens des Cantons de l'Est inc.,* 2009 QCCA 1246 (CanLII), 2009 QCCA 1246. The plaintiffs in that case were the estates of two individuals who drowned while on a hunting expedition in northern Quebec. The court decided that those actions were governed by federal maritime law, including the limitation provisions of the *Athens Convention* as incorporated in the *Marine Liability Act*. Quebec limitation legislation did not apply.

The Nova Scotia court agreed with these two earlier decisions including the finding that there was no discretion in the court to postpone or suspend the running of the limitation.

The claimant also suggested that the court has an inherent jurisdiction under the *Marine Liability Act* to suspend or extend the limitation period. Alternatively the claimant argued that a failure to recognize the legal disability of a minor potentially infringed the child's right to "justice and fairness" under the *Canadian Charter of Rights and Freedoms* and that to rectify this



violation the discoverability principle should be applied to the determination of the limitation period.

The court dismissed the claimant's arguments, stating at paragraphs 19-21:

> Since limitation periods are creatures of statute, the determination of the date on which the period starts to run and when it expires must be made based upon the legislation's language. If there is no provision for postponement or suspension of the limitation found in the legislation, then no such authority exists. Where the limitation period is said to commence when the cause of action arises, courts have determined that the discoverability principle applies. The cause of action accrues when the plaintiff is aware of all of its elements, including damages. When the cause of action begins to run from a fixed event, the discovery principle does not apply.
>
> In this case, the limitation period under the *Athens Convention* starts upon disembarkation of the passenger. That is an ascertainable date and the discovery principle has no application.
>
> The *Athens Convention* and the *Marine Liability Act* do not contain any provision which says that limitation periods for infants are postponed until they attain majority. Without such language, there is no basis to apply such an interpretation and defeat the clear language of the statute.

In the result the court held that the *Marine Liability Act* governed the claim and the applicable limitation period had expired. There was no discretion to suspend or extend the period even though the claimant was an infant. Summary judgment was granted to the defendant.

Rui Fernandes

3. A Defendant's Challenge to the Jurisdiction of the Ontario Courts and Avoiding Inadvertent "Attornment"

In feudal and old English law "attornment" referred to the act of a person holding a leasehold interest in land agreeing to become the tenant of a stranger who has acquired an interest in the land.

In modern civil litigation practice, "attornment" has come to take on a different meaning that can catch the unwary defendant: a defendant in a court proceeding is said to have "attorned" to that jurisdiction by taking certain steps to defend itself in the context of that action. In so doing the unwary defendant might find that it has irrevocably submitted itself to that court forum.

A defendant who is sued in the Ontario Superior Court of Justice may wish to seek a 'stay' of that action in favour of another forum considered more appropriate for the adjudication of the dispute. Perhaps the parties to the lawsuit had bargained in the contract that the courts of another forum would adjudicate any disputes. Perhaps another forum is considered to be so much more convenient for the efficient resolution of the dispute such that the matter should not be heard by an Ontario court. Regardless of the motivation for wanting to put the "brakes" on an Ontario action – for the "merits" of a matter to be dealt with elsewhere – defendants and their counsel are cautioned to be careful in the manner in which they "appear" in the Ontario proceeding to challenge the Ontario forum. If the defendant is seen to have entered a defence on the "merits" (or lack thereof) of the action there is a risk that it will be found to have "attorned" or in effect, voluntarily submitted to the jurisdiction of the Ontario court.

The recent decision of the Ontario Court of Appeal in the case of *John Fraser v. 4358376 Canada Inc.* operating as Itravel 2000 and others (*1) offers some guidance as to what steps taken by a defendant to a law suit might be considered to have "crossed the line" from merely "appearing" (so as to contest the jurisdiction) as opposed to having actually "attorned" to the Ontario jurisdiction.

The Facts

The facts of the case, and the manner in which the law suit commenced in Ontario against the defendants came to pass, inform the analysis as to whether those steps taken by certain defendants amounted to an "attornment".

The plaintiff, John Fraser, brought a law suit for wrongful dismissal against the corporate defendants Itravel 2000, Travelzest PLC, and The Cruise Professionals Limited (the "Corporate Defendants"). The Corporate Defendants applied to the court for a "stay" of the action (or alternatively a dismissal of the action) on the basis of a "jurisdiction clause" in the relevant employment contract that required any disputes to be litigated in England.

After the filing of the Corporate Defendants' request for a "stay", but before that matter could be ruled on by the Court, the plaintiff added two individuals as defendants (the "Individual Defendants"). The claims against the Individual Defendants related to allegations that they interfered with the plaintiff's employment contract with the Corporate Defendants, bringing about or motivating his dismissal.

After the Individual Defendants were added as defendants to the action, the Corporate Defendants were placed into receivership under governing bankruptcy legislation as a result of which the action against the Corporate Defendants was stayed. Following the commencement of these bankruptcy proceedings the Individual Defendants brought an application for a stay of the action as against them until the bankruptcy driven stay (*2) of the action against the Corporate Defendants had been lifted, or until the proceedings against those defendants had been dismissed or otherwise finally resolved. In addition, the

Individual Defendants asked for an Order striking out the law suit as against them on the ground that the Court was required to deal with the issue of jurisdiction on the basis of the pleadings as they existed at the time the jurisdiction motion was first brought i.e. the action as initially brought by the plaintiff only as against the Corporate Defendants. The basis for the request for the stay pending the resolution of the bankruptcy proceedings was that the claims against the Individual Defendants were inextricably tied to the claim of wrongful dismissal against the Corporate Defendants, and that the jurisdictional issue was entirely predicated upon the terms of the plaintiff's employment contract with the Corporate Defendants. The Individual Defendants asserted that as long as the claims continued against the Corporate Defendants, the issue of jurisdiction could not be fairly resolved without their presence.

The matter came before a judge of the Ontario Superior Court, who ruled that by asking for the temporary stay of the action against the Individual Defendants (pending the lifting of the bankruptcy stay or dismissal of the claims against the Corporate Defendants), that the Individual Defendants had "attorned" to the jurisdiction of the Court.

The Individual Defendants appealed this ruling.

At the Appeal

The central issue at the appeal was whether the Individual Defendants attorned to the jurisdiction of the Ontario court by taking the specific steps they did being *above and beyond* the usual scope of a motion to stay based on jurisdiction. In particular, the question of whether the Individual Defendants' request for:

a) a temporary stay based on the status of the Corporate Defendants and
b) the amended claim (so as to include them as new defendants) be struck

amounted to an attornment.

The Court of Appeal agreed with the Individual Defendants that the judge who initially heard the matter erred in law. The Court of Appeal concluded that the above steps were more properly characterized as "procedural" steps taken *within the confines of the motion on the question of jurisdiction*. By asking for a temporary stay, the Individual Defendants were asserting their position that the proper resolution of the jurisdictional motion required that the Corporate Defendants be before the Court. The temporary stay sought was for that specific and limited purpose. The Court of Appeal ruled that when one challenges the jurisdiction of the court, it is entitled to insist on a proper jurisdictional foundation for the determination of the challenge. Provided that the party's steps request no more than that, they do not amount to 'attornment'.

The above said, the Court of Appeal found that the Individual Defendants were wrong on the second step that it took in seeking the dismissal of the claim against them. The Court of Appeal did not agree that the Individual Defendants could ask the Court to strike the new claim (as brought against them) simply on the basis that their addition as defendants came *after* the original jurisdiction motion by the Corporate Defendants. The Individual Defendants would still have to defend the matter wherever the action would proceed.

The Court of Appeal noted that it and other courts have in the past taken a broad view of the kind of steps taken in a proceeding that amount to attornment (*3). It has been held in the past that when a defendant seeks an order from the Ontario court declaring that an action is *res judicata* (*4) and an abuse of process and should therefore be dismissed or permanently stayed, that this amounts to the assertion of a defence amounting to attornment to the court. It has also been held that when a party to an action appears in court and goes beyond challenging the jurisdiction of the court based on *jurisdiction simpliciter* (*5) and *forum non conveniens*, (*6)

that party will be regarded as attorned, thus giving the court consent-based jurisdiction.

Accordingly, in this case there was no attornment. The Court of Appeal however while ruling in favour of the Individual Defendants on the attornment issue proceeded to dismiss their application for a temporary stay of the action against them pending the outcome of the bankruptcy of the Corporate Defendants. As noted by the Court of Appeal:

> It is entirely regrettable that this action has become mired in a dispute over jurisdiction involving parties (i.e. the Corporate Defendants) that almost certainly will never be brought before the court…. There is nothing in the record to suggest that there is any realistic prospect that the bankruptcy stay will be lifted or that the claims against the corporate defendants will ever proceed. We see no reason why what appears to be the purely theoretical possibility of the claims proceeding against the corporate defendants should preclude the respondent (i.e. the plaintiff) from proceeding with his claims…

Hence the matter was left to proceed against the Individual Defendants, with the jurisdiction question as to the claims against them still having to be resolved.

Conclusion

Defendants sued in the Ontario courts who wish to challenge that forum must tread strategically and carefully. While procedural steps brought within the confines of a jurisdiction motion (dealing solely with the mechanics of having the motion heard in a proper procedural setting) do not amount to attornment, it is easy for the unwary to 'step over the line' by addressing the merits of the case by engaging in a substantive response to the claim which may amount to attornment.

Gordon Hearn

Endnotes

(*1) 2014 ONCA 553 (CanLII)
(*2) It is a basic feature of the governing bankruptcy legislation that when a party becomes bankrupt that civil actions against it are stayed pending the resolution of the bankruptcy proceedings.
(*3) See for example: *Wolfe v. Pickar*, 2011 ONCA 347 (CanLII) and *Mid-Ohio Imported Car C. v. Tri-K Investments Ltd.* 1995 CanLII 2084 (BC CA)
(*4) A legal position that might be taken by one party, amounting to a defence, that the matter in dispute has already been finally determined between the parties.
(*5) *Jurisdiction Simpliciter*: a party seeking to challenge the jurisdiction of the court chosen by the plaintiff can challenge the jurisdiction on the basis that the present forum has no tenable or significant enough connection to the facts of the case to warrant the matter being litigated in that particular forum. It should be noted that the court can itself raise this concern and cite the lack of "connecting factors" for it to adjudicate the matter.
(*6) *Forum non conveniens*: a basis whereby a defendant might file a limited appearance in a court action to challenge jurisdiction on the basis that there is a forum elsewhere clearly more appropriate and convenient for the battle to be waged. On such an application the court initially seized of the matter will apply its discretion as to whether the matter should remain or be moved to the other forum.

4. A Case Study of the Admiralty Jurisdiction of the Federal Court of Canada: The Maritime Element Must Be Real and Direct

The recent decision of the Federal Court of Canada in *General MPP Carriers Ltd. v. SCL Bern AG* (*1) provides an important reminder that our Federal Court has a limited "subject matter" jurisdiction. While the Court has jurisdiction over maritime disputes, this will not extend to a dispute that only *incidentally* involves a ship. In this case, a claim was filed by the plaintiff in the Federal Court, followed by the arrest of a vessel implicated in the matter so as to provide security for the claim. The defendants (including the vessel interests) applied to the Court for an order quashing the action and the warrant for arrest on the basis that the Court lacked jurisdiction over the claim – *and they succeeded.*

The Facts

SCL Bern AG ("SCL Bern") is a company incorporated pursuant to the laws of Switzerland and is the registered owner of the vessel SCL BERN.

In August 2008, SCL Reederei AG ("SCL Reederei") and MPP Carriers Limited ("MPP") entered into a Shareholder's Agreement. This Agreement provided that these parties directly hold 100% of the shares in SCL Bern and included certain provisions concerning the right of first refusal and prohibition on the disposal of shares:

> Right of first refusal
>
> *12. Should any Party wish to dispose of their shares, it may only offer to sell its shares to the other Party. The Party which is entitled to purchase the shares shall within 30 days of the date of receipt of the offer reply in writing whether and to what extent it wishes to exercise its right of first refusal.*
>
> Prohibition on disposal
>
> *13. Mr. Talal Hallak* (an MPP officer) *shall not be entitled to dispose of his shares in SCL Bern AG to third parties. Any transfer of title for consideration or for no consideration, be it pursuant to a sale, exchange, gift, any provisions of property law, contribution or the like shall be deemed to be a disposal.*
>
> *Mr. Talal Hallik shall, however, have as exit possibility the one time right, after 5 years of owing the shares, that is to say in June, 2013, to sell his shares in SCL Bern AG to the majority shareholder (SCL Reederei AG, Bern) at a price representing 125% of his investment (5% per year), meaning here U.S. $5,000,000 + 25% = US $6,250,000. The condition for the exercise of this right is that he must give notice of 12 months (in June, 2012) to the buyer, before selling his shares to the majority shareholder as above.*

MPP alleges that notice under clause 13 of the Agreement was given, triggering the above share sale provisions, but that the payment was not received. MPP commenced debt enforcement proceedings in Switzerland. On April 25, 2014, a Swiss court granted judgment in favour of MPP in the amount of roughly U.S. $3,750,000. This judgment is currently under appeal.

The Federal Court of Canada Action

On May 28, 2014, MPP caused a Statement of Claim to be issued in the Federal Court of Canada naming SCL Reederei and SCL Bern as *in personam* defendants and the vessel SCL BERN as an *in rem* defendant. The Statement of Claim claims that the defendants breached the terms of the Shareholders' Agreement and that MPP suffered damages as a result – specifically, that the defendants had failed to pay MPP the amount owed for its ownership in SCL Bern. MPP alleged having an ownership interest in the vessel by virtue of its 40% ownership stake in SCL Bern. An alternative claim was advanced that a certain U.S. $5 million loan from MPP to

SCL Bern and SCL Reederei was secured by way of a mortgage or charge on the vessel in favour of MPP.

In support of its claim against the vessel, MPP relied on the following provisions of section 22(2) the Federal Courts Act (*2) as a grant of the requisite maritime jurisdiction:

> (a) [pertaining to]… any claim with respect to title, possession or ownership of a ship or any part interest therein or with respect to the proceeds of sale of a ship or any part interest therein.
>
> (c) [pertaining to] …any claim in respect of a mortgage or hypothecation of, or charge on, a ship or any part interest therein or any charge in the nature of bottomry or respondentia for which a ship or part interest therein or cargo was made security.

Based on the Statement of Claim and an Affidavit to Lead Warrant sworn by Mr. Hallak, the vessel SCL BERN was arrested by process of the Federal Court of Canada on May 30, 2014.

On June 5, 2014, the defendants filed a motion on an urgent basis seeking to strike the Statement of Claim and to set aside its arrest on the basis that:

- MPP's claim was a shareholder dispute that does not fall within the maritime subject matter jurisdiction of the Federal Court of Canada. The defendants accordingly sought to have the Statement of Claim struck, as being the first necessary step in order to have the arrest warrant set aside.

- the defendants asserted that SCL Bern is the registered owner of the vessel. As such, MPP cannot claim that it has title to or a registered interest in respect of the vessel.

- the defendants asserted that MPP's ownership interest concerned 40% of the shares of the SCL Bern company. Under Swiss law, a shareholder does not own the assets of the company in which it owns shares.

- the underlying claim by MPP in the Swiss courts did not involve a claim in respect of the vessel.

- the Statement of Claim was merely an action to recover money allegedly owed under the Shareholders' Agreement and was not a claim in respect to the "title, possession, ownership, mortgage, hypothecation or charge on the vessel".

- the Shareholders' Agreement is a corporate agreement inseparable from SCL Bern's Articles of Association and Swiss company law and is not an agreement pertaining to navigation and shipping. For that matter, the Agreement does not mention the vessel at all by name.

- as to the claim in respect of a mortgage, hypothecation or charge on the vessel, the Swiss Ship Registry indicates that the only mortgagee or lien holder is the Swiss Confederation.

Accordingly, the defendants asserted that no facts were alleged in the Statement of Claim so as to bring this claim within the maritime jurisdiction of the Federal Court. As no maritime cause of action had been made out, the Court had no maritime jurisdiction and accordingly the Statement of Claim must be struck out, the action dismissed and the warrant of arrest for the vessel quashed.

In turn, MPP submitted that there was sufficient maritime jurisdiction in the Federal Court of Canada to sustain the issuance of the arrest warrant for the vessel:

• there was an agreement between SCL Reederei and a management company who managed the vessel that MPP would advance U.S. $5,000,000 to assist in the financing and capitalization of the vessel, in consideration for MPP having a 40% interest in the vessel. This was implemented by SCL Reederei owning 60% and MPP owning 40% of SCL Bern – which was a "one ship" company that owns the vessel.

• Mr. Hallak's intention, and belief, was that MPP would accordingly hold a 40% interest in the vessel. Whether the 40% was of shares in SCL Bern or in the vessel itself, this was of no importance as the end result was the intention that MPP would have a 40% interest in the vessel once the right to sell was triggered.

• MPP arrested the vessel on the basis that MPP was a part owner of the vessel, that it triggered its right to sell and it had not been repaid its part interest in the vessel.

• MPP submitted on the basis of established case law that to succeed in striking out an *in rem* action, the defendants must establish that it is "plain, obvious and beyond doubt" that the *in rem* claim is so clearly futile that it did not have the slightest chance of success. Rather, as MPP submitted, the court should not be daunted by the novelty of a pleaded cause of action but should focus "on whether there is a reasonable prospect that the claim will succeed if the facts pleaded can be assumed to be true". Based on this, MPP asserted that the action should not be struck out simply because the case law had not settled whether the Court had jurisdiction over vessel ownership interests acquired by the purchase of corporate shares in a one ship company.

• MPP also submitted that it was not necessary for the claim to fall strictly under s. 22(2) (a) or another of the enumerated "jurisdiction grant" subsections of the *Federal Courts Act* to support an *in rem* action. It need only have a claim "for relief or a remedy sought under Canadian Maritime law or relating to any matter coming within the class of subject of navigation or shipping": s. 21(1). MPP asserted in this regard that the ownership and financing of vessels is integrally connected to maritime commerce and carrying out the activity of shipping. Furthermore the modern approach to Canadian Maritime law should include disputes with regard to the financing of vessels and the corporate entities which may be employed for the limited purpose of financing vessels.

• MPP argued that the fact that there is an intervening company holding the ownership of the vessel does "not make it any less a claim or question arising out of a claim to the ownership of the vessel in these circumstances".

• in essence, MPP asserted that if not the "form" that the "substance" of the matter placed it within the subject matter jurisdiction of the Federal Court that the matter involved a dispute centering around the investment into a ship, albeit through a one ship company, being a matter falling within the court's maritime jurisdiction.

Accordingly MPP argued that the motion by the defendants should be dismissed, that the action should proceed and that the arrest warrant served on the vessel should stand.

Disposition and Analysis

Madam Justice Strickland of the Federal Court ruled that "*the heart of the matter, even when viewed in whole, is a shareholder's dispute and falls outside of the jurisdiction of this court".*

In making this finding the Court noted that the Shareholders' Agreement made no reference to the vessel and that under Swiss law the owning of shares of a company does not give an ownership interest in the assets of that company. Accordingly, that MPP owned 40% of the shares of SCL Bern did not mean that it owned 40% of the assets of SCL Bern.

In its analysis the Court agreed with the submissions made by counsel for MPP that even if its claim does not fall precisely within any of the jurisdictional grant subsection of s. 22(2) of the *Federal Courts Act* that there will still be jurisdiction as long as the claim falls within s. 21(1), the enumerated claims in s. 22(2) "simply being illustrative of and do not limit the jurisdiction described in s. 21(1). S. 21(1) provides as follows:

> *The Federal Court has concurrent original jurisdiction, between subject and subject as well as otherwise, in all cases in which a claim for relief is made or a remedy is sought under or by virtue of Canadian maritime law or any other law of Canada relating to any matter coming within the class of subject of navigation and shipping, except to the extent that jurisdiction has been otherwise specifically assigned.*

Justice Strickland however proceeded to note that:

> *" I do think that it is quite clear that MPP's claims arise from the alleged breach of the Shareholders' Agreement concerning the sale of the shares of SCL Bern. The reference in the Shareholders' Agreement to the Articles of Association and company law adds to the characterization of the dispute, and therefore the claim, as one of corporate and not maritime law. It is very significant that the Shareholders' Agreement does not refer to the Vessel either directly or indirectly nor to any marine activity or connection. Nor, and contrary [to the] Statement of Claim, does it grant MPP an option to sell its interest in the vessel…. it is difficult to see [how] a dispute arising out of a Shareholders' Agreement can, without more, result in the arrest of a ship not mentioned in the agreement and which is owned by another party."*

Finding that the dispute only indirectly involved the vessel, as the principal asset of SCL Bern, the Court found that the dispute is separate from a maritime aspect relating solely to the Shareholders' Agreement and the sale of the shares in the ship owning company.

In the result, the *in rem* action against the defendant vessel was struck out, as a result of which that the arrest warrant was set aside with the vessel being released from arrest.

Gordon Hearn

Endnotes
(*1) 2014 FC 571 (CanLII)
(*2) R.S.C., 1985, c F-7

5. Surveyors and Claim Adjusters Reports and Privilege

The Federal Court of Appeal handed down a decision on May 22, 2014 which will impact how surveyors and claims adjusters should be framing their preliminary investigation reports when the cause of damage is not immediately known (*Webasto Product North America Inc. v Shasta Equities Ltd. And Lorne Shandro* (2014 FCA 135)). Based on this decision, where a fire breaks out due to unknown causes preliminary investigation reports may have to be produced in a law suit as part of 'documentary discovery' - even when counsel has been retained and has provided instruction. Surveyors and adjusters should bear this in mind when writing their initial/preliminary reports, being careful to leave out any opinions, theories, or instructions with respect to future courses of action.

On October 13, 2009 a fire broke out on the yacht "HELIOS 1" at a marina in Coal Harbour in Vancouver, spreading to nearby yachts. The vessel's insurance broker quickly learned of the incident and on the same day appointed Aegis Marine Surveyors Ltd. ("Aegis") and Sereca Fire Consulting Ltd. ("Sereca") to attend the scene and investigate the fire. Believing that the third party yachts may advance claims, he advised the adjusters that they were being retained "on behalf of counsel" who would be in touch shortly to instruct and guide them in their investigation, and that they should report directly to counsel.

The broker then immediately retained counsel, instructing him that third party vessels had been damaged in the fire and that he was to defend any claims. Defence counsel was shortly thereafter contacted by lawyers representing owners of the nearby yachts with a request for a joint inspection of the "HELIOS 1". On counsel's instructions Aegis attended the "HELIOS 1" the next day. Also present were the vessel's owner Shandro, other yacht owners, the Vancouver Police and Fire Departments, representatives of the marina and Vancouver Port, and the Canadian Coast Guard. Aegis issued a report that same day stating that the purpose of the inspection was to "ascertain the cause, nature, and extent of damage in the fire".

Defence counsel then instructed Sereca to attend another joint inspection with experts retained by the third party vessels. One week later, Sereca prepared a report addressed to defence counsel describing the inspection and proposing various causation scenarios warranting further analysis. Two and a half weeks later, Canadian Claims Services ("Canadian Claims") was retained directly by defence counsel to interview Shandro, the owner of the "HELIOS 1", to assist in defending any claims. Canadian Claims obtained a lengthy and detailed statement from Shandro. Also attached to its November 7, 2009 report were survey reports from years earlier which had been provided by Shandro.

Following the preliminary investigations, the finger of blame was pointed at Webasto Product North America Inc. ("Webasto"), the manufacturer of a diesel-fired coolant heater which may have caused or contributed to the fire. Litigation was commenced by the third party yacht owners; Webasto was third partied. Webasto then applied for disclosure of the Aegis, Sereca, and Canadian Claims reports produced shortly after the fire.

The prothonotary held that although there "may have been a prospect of litigation" when the preliminary investigations were done, the nature of any potential disputes and whether or not third party claims would

be covered was not known at that stage. It was possible that potential claims could be resolved without litigation. He found that there was more than one purpose for the adjuster's reports and that the evidence lacked precision and clarity in this regard. He therefore held that there was no privilege attached to any of the reports and he ordered them all to be produced to the other parties.

The owners of the "HELIOS 1" appealed to the Federal Court. The motions judge reversed the prothonotary's decision, holding that litigation privilege applied to the Aegis and Sereca reports and that solicitor-and-client privilege applied to the Canadian Claims report. The appropriate test was "whether or not production of the documents is vital to our fundamental sense of justice", balanced against the necessity for privilege. Litigation privilege exists to ensure that parties can prepare their positions in a "protected area" or "zone of privacy" in relation to pending or apprehended litigation. Solicitor-and-client privilege exists to promote full and frank disclosure by clients.

The motions judge applied litigation privilege to the Aegis and Sereca reports because "the only purpose of the reports was to ascertain if claims against the Helios I would succeed". He held that the only purpose of defence counsel's involvement was to defend or pursue claims. The parties were therefore in an adversarial situation before any of the reports were created. Solicitor-and-client privilege applied to the Canadian Claims report because that adjuster was retained directly by defence counsel, acting as his agent in obtaining the statement from Shandro.

The motions judge did caution however that the facts and information contained within the reports would have to be disclosed if/ when the party obtaining the reports is examined for discovery.

Webasto appealed this Order to the Federal Court of Appeal. The court agreed with the motions judge that the test for litigation privilege is twofold: 1) litigation must be ongoing or reasonably contemplated at the time the document is created, and 2) the dominant purpose in creating the document was to prepare for that litigation. Additionally, the court must consider the following factors:

1. Who authored the report, and on whose authority it was prepared;
2. The date on which the report was produced;
3. The date on which the insurers appointed counsel;
4. The identity of the parties to whom the report is addressed; and,
5. The contents of the report.

The appeal court held that the initial investigation reports had to be produced, with the exception of the Canadian Claims report. Although the possibility of litigation always exists when a loss is caused by fire, the nature of the incident was not known to the parties. The cause of the fire was being investigated and the first reports were described as "interim". Those documents arose out of an examination of what took place and the parties were only at a preliminary stage of investigation.

Although defence counsel was retained on the same day as the fire and had contact from other counsel indicating that claims would be advanced, the court held that "mere contact from the solicitors for the

third parties does not change a preliminary investigation into an adversarial situation". But by the time counsel retained Canadian Claims to take a statement from Shandro, the initial investigation had been done and litigation was reasonably contemplated. The motions court erred in applying solicitor-and-client privilege to the Canadian Claims report. The Court of Appeal instead held that litigation privilege applied to that report.

A series of follow-up reports issued by Aegis, Sereca, and Canadian Claims were all held to be privileged, since by that time the initial investigation had been done and litigation was reasonably contemplated.

Given this recent decision, when adjusters are completing initial, preliminary, or "interim" reports concerning the cause of an event, they should be cautioned that these initial reports may well be producible even when they have taken their instructions directly from defence counsel. Bearing this in mind when initial reports are produced will ensure that sensitive information or opinions as to litigation strategy are not made available to the other parties. The initial reports should remain within the four corners of a preliminary investigation as to what happened, and not stray into any other territory.

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CONTEST

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