Canadian Journal of Insurance Law

General Editor: Neo J. Tuytel, Bernard & Partners
Associate Editor: Krista Prockiw, Alexander Holburn Beaudin + Lang, LLP

VOLUME 32, NUMBER 1 Cited as 32 Can. J. Ins. L. JANUARY 2014

• REGULATORY OFFENCES IN THE DISTRIBUTION OF INSURANCE PRODUCTS: A CALL FOR DILIGENCE •

Marc Beauchemin, Jean Martel, Evelyne Verrier, and Leïla Yacoubi
Lavery, De Billy

• In This Issue •

On November 21, 2013, the Supreme Court of Canada issued its judgment in the case of *La Souveraine, Compagnie d'assurance générale v. Autorité des marchés financiers*,[1] a decision that is now critically important in the context of the distribution of insurance products in Quebec. Indeed, the judgment sheds light on the extent to which insurers operating in Quebec may incur penal liability for regulatory offences committed by financial services firms that they authorize to distribute their products.

In this case, the highest court of the land found an insurer guilty of the offence stipulated at s. 482 of the *Act respecting the distribution of financial products and services* [*ADFPS*][2] for having provided its consent to a Manitoba damage insurance brokerage firm that was not registered with the Autorité des marchés financiers (AMF) to provide Quebec merchants with the opportunity to participate in a master insurance policy issued by the insurer to cover the inventories financed by a third-party institution.

CANADIAN JOURNAL OF INSURANCE LAW

The **Canadian Journal of Insurance Law** is published bi-monthly by LexisNexis Canada Inc., 123 Commerce Valley Drive East, Suite 700, Markham, Ontario L3T 7W8

ISBN: 0-409-91088-0 ISSN: 0822-1090
ISBN: 0-433-44377-4 (Print & PDF)
ISBN: 0-433-44645-5 (PDF)
Publications Mail Registration No. 185906

Subscription rates: $440/year (Print or PDF)
$505/year (Print & PDF)

Please address all editorial inquiries to:

Boris Roginsky, Journals Editor
LexisNexis Canada Inc.
Tel. (905) 479-2665; Toll-Free Tel. 1-800-668-6481
Fax (905) 479-2826; Toll-Free Fax 1-800-461-3275
E-mail: cjil@lexisnexis.ca

Section 482 of the *ADFPS* provides that

> [e]very insurer that helps or, by encouragement, advice or consent or by an authorization or order, induces a firm or an independent representative or independent partnership through which it offers insurance products […] to contravene any provision of this Act or the regulations is guilty of an offence.[3]

Although the case involved a situation of non-compliance with the registration rules of a firm located in Quebec pursuant to the *ADFPS*, it is important to note that an offence that may have resulted in the filing of a penal complaint against an insurer pursuant to its s. 482 may extend to the violation of any supervisory rule prescribed under the *ADFPS* by a firm, an independent representative, or an independent partnership.

The court confirmed that s. 482 of the *ADFPS* creates a strict liability offence for the insurer—that is, an offence for which the prosecution is not required to prove the culpable intent of the insurer. In turn, the physical element of the offence does not require evidence to the effect that the insurer has taken positive action to encourage the violation of the Act by the firm. For the insurer, to simply fail to oppose in due course to the illegal distribution of its insurance products is regarded as consent or an authorization to such distribution.

However, the court noted that a due diligence defence is available to the insurer and the insurer may be found not guilty if it demonstrates that it has committed an error in fact (which leads it to believe, on reasonable grounds, in a mistaken set of facts that if true, would have rendered his or her act or omission innocent) or proves that it had taken all reasonable precautions to avoid the violation being committed. This being said, an insurer cannot rely on an error in law as a defence since "ignorance of the law is no excuse". In the case under review,

the insurer in question was therefore unable to validly defend itself by arguing that it did not believe that the complex distribution operations to which it was a party and which extended to several other provinces required that brokers not based in Quebec who were offering the product to persons or entities from Quebec were required to be registered in Quebec with the AMF. The insurer could not defend itself on the basis of an erroneous interpretation of the *ADFPS*.

In this respect, the court noted that as participants in a regulated industry, insurers agree to submit to strict standards that they are required to know and comply with.

This decision of the Supreme Court therefore brings back to the forefront the obligation for any insurer conducting business in Quebec to ensure strict control and monitoring of the regulatory compliance of the activities related to the distribution of its products, which are conducted on its behalf in Quebec by persons regulated under the *ADFPS*. In this respect, insurers must be proactive and demonstrate diligence. They cannot just obtain the opinion of inexperienced third parties, including their distributors, or rely on the silence of the AMF to efficiently mitigate the risk to their reputations brought about by having penal proceedings instituted against them.

This new interpretation of Quebec regulatory penal law constitutes a good reason for insurers to adopt policies and procedures to better assess compliance with the process for the distribution of their products in Quebec by brokerage firms subject to registration and, above all, to comply with the exculpatory standard that they are required to meet should they face proceedings arising from regulatory violations of brokers who distribute their products.

[*Editor's note*: **Marc Beauchemin** is a partner at Lavery, de Billy. Mr. Beauchemin devotes his practice to commercial law and has specifically developed a solid expertise in financial institution law. Canadian and foreign banks, savings banks, credit unions, trust companies, insurance companies, and securities brokers regularly call upon his expertise, particularly when embarking on business combinations, mergers or restructurings.

Jean Martel is a partner at Lavery, de Billy. Mr. Martel practises mainly in the field of financial law—securities, corporate financing, regulation and governance of financial institutions, financial services, and securities markets—on the national and international scenes. Prior to joining the firm, Mr. Martel held several strategic positions, including acting as head of the legal services department at the Ministère des Finances du Québec, acting as Assistant Deputy Minister of Finance for the Province of Quebec, and acting as the Chairman and CEO of the Quebec Securities Commission.

Evelyne Verrier is a partner at Lavery, de Billy. Ms. Verrier is a graduate of Laval University in both Actuarial Science and Law. Her practice is primarily focused on civil litigation and insurance. She drafted several opinions in the area of the distribution of financial products and services discussing the compliance of various insurance products marketed by Quebec and foreign insurers and the issues related to their method of distribution. She coordinates the firm's distribution of financial products and services practice group.

Leïla Yacoubi is an associate at Lavery, de Billy. Ms. Yacoubi is a member of Lavery's Business Law Group. Her practice focuses on securities and the distribution of financial products and services. More specifically, she deals with matters involving the regulation and

governance of the major players in the financial sector. During her law graduate studies at Université de Montréal, she worked as a research assistant and was primarily interested in the regulation of the Canadian financial system and the regulatory framework for investment funds.]

[1] [2013] S.C.J. No. 63, 2013 SCC 63.
[2] *ADFPS*, CQLR, c. D-9.2.
[3] *Ibid*., s. 482.

• *BOYCE v. CO-OPERATORS GENERAL INSURANCE CO.* •

Erin Farrell and Heather Gray,
Gowling Lafleur Henderson LLP

The Supreme Court of Canada has dismissed the plaintiff's appeal in *Boyce v. Co-operators General Insurance Company*[1] on the question of whether the contractual limitation period in a commercial insurance policy can override a statutory limitation period.[2]

The plaintiff owned a clothing boutique, which was closed down for a period of time in order to address a foul odour emanating from the store. The odour resulted in clean-up costs and a loss of inventory. The plaintiff believed the store had been vandalized and filed a proof of loss claim within two months of the closure. The insurer took the position that the odour was caused by a skunk and denied the claim. The plaintiff commenced an action challenging the denial just over one year after the incident.

The insurer moved for summary judgment on the basis that the action was statute barred by operation of the one-year limitation period in s. 148 of the Ontario *Insurance Act*[3] which had been incorporated by reference into the terms of the policy. The insurer relied on s. 22(*b*) of the *Limitations Act*, which allows parties to a "business agreement" to vary the applicable statutory limitation period. A "business agreement" is understood to be an agreement made by parties "none of whom is a consumer as defined in the Consumer Protection Act, 2002".[4]

Under the heading "statutory conditions" the policy read (as many policies do):

> Action
> Every action or proceeding against the insurer for recovery of any claim under or by virtue of this contract is absolutely barred unless commenced within one year next after the loss or damage occurs.

What the plaintiff did not argue—and what may have saved them on appeal—was that an insurer who denies coverage has repudiated the policy and can no longer rely upon its technical terms.[5]

The motion judge dismissed the insurer's motion, reasoning that the policy lacked the specific language necessary to override the applicable statutory limitation period of two years and that, in any event, the policy was not a "business agreement". The insurer appealed.

On appeal, the court considered the foundational question of whether the policy did in fact provide for a one-year limitation period and, if it did, whether it was capable of overriding the otherwise applicable two-year limitation period. The Court of Appeal answered all questions in the affirmative and found in favour of the insurer.

The court held that the one-year limitation in the policy was written in clear and unambiguous language and that the policy qualified as a "business agreement" as neither party was a consumer acting for personal, family, or household purposes—the policy was capable of overriding the *Limitations Act*.

The Court of Appeal's decision is significant for any commercial insured but—in our view—