Are you protected against phishing email? What the Court of Appeal said in insurance matters

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Phishing fraud is a rampant problem that causes major losses throughout the world. It consists in bad actors sending emails in which they falsely claim to be a trusted third party or legitimate company in order to obtain confidential information from the recipient for the purpose of committing fraud[1].

In *Co-operators c. Coop fédérée*[2], the Court confirmed the insurer's obligation to indemnify its insured for losses resulting from such fraud, thereby confirming that the insurer was precluded from raising a new defence at trial. The Court of Appeal also addressed the notion of specific insurance provided for in article 2496 of the *Civil Code of Québec* (hereinafter "C.C.Q.") in the presence of a plurality of insurance.

Facts

In August 2014, La Coop fédérée (the "Coop") was the victim of phishing fraud. Due to false pretenses, its comptroller sent a payment order to the Coop's bank (the "Bank"), which complied with the order and transferred the sum of $4,946,355.26 in U.S. dollars to a foreign company. On August 23, 2014, the Coop became aware of the fraud, but the Bank was unable to stop the transaction or recover the funds.

At that time, the Coop's account was overdrawn by $3,386,361.80, to which was added the amount of the transfer. The Coop contested the validity of the fraudulent transfer and the resulting additional overdraft with the Bank. It also informed its insurers of the losses incurred. However, The Co-operators General Insurance Company ("The Co-operators") denied the claim on the basis that the increase in the overdraft was not a property covered by the policy, that the misappropriated money belonged to the Bank and, incidentally, that the Coop had not suffered a compensable loss. As for Liberty International Underwriters ("Liberty"), which had issued an insurance policy against fraud and embezzlement, it accepted the claim subject to the rules of contribution between multiple insurers.

The Coop therefore went to the Superior Court to force The Co-operators to indemnify it for the loss suffered. At the same time, Liberty claimed from The Co-operators the reimbursement of part of the indemnity that it had paid to the Coop.

Superior Court

As for liability for the loss, the trial judge first concluded that the Bills of Exchange Act ("BEA") does not apply to electronic funds transfers ("EFT"), that is, transfers without the exchange of paper

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documents. He then concluded that the overdraft on the Coop's bank account constituted a loan, that the Coop had become the owner of the misappropriated sum in accordance with article 2327 of the C.C.Q., and that it thus had to bear the loss.

This conclusion led the judge to, in particular, dismiss the application filed by the Co-operators to amend its defence so that it could argue that the Coop's refusal to raise the invalidity of the payment order could not be set up against it and constituted a reason for non-coverage. Instead, the judge agreed with the Coop and Liberty, which argued that The Co-operators could not invoke new grounds for denying coverage at such a late time. According to the Court, The Co-operators had sealed its fate upon the initial denial of coverage.

As for The Co-operators' insurance coverage, the judge pointed out that a contract for "property and business interruption insurance" existed, and as it was considered as a negotiated policy, the intention of the parties had precedence. However, no evidence of this intention was filed. In the absence of a specific exclusion on fraud, the judge ruled that the loss suffered by the Coop constituted a risk covered by this insurance policy.

The trial judge found that the loss suffered was covered by both insurance policies, namely that of the Co-operators and that of Liberty. According to the trial judge, the Liberty insurance policy was not a specific insurance policy in that it covered all of the insured's property and all the risks that could affect it, as did the Co-operators policy. Given that both insurance policies covered the same risks, the Court concluded that there was of a plurality of insurance and apportioned the contributions of each of the insurers in proportion to their respective share of the total coverage, while taking into account the applicable deductibles.

Quebec Court of Appeal

The judges of the Court of Appeal dismissed the appeal except for the conclusion on the nature of the Liberty insurance policy.

Like the Superior Court judge, the Court of Appeal held that the BEA does not apply to a payment order because an EFT is not a bill of exchange within the meaning of the BEA. In addition, the Court of Appeal further distinguished the two by the fact that an EFT does not include a procedure for presenting payment, is immediate and final and, unlike a bill of exchange, beneficiaries of an EFT have no title or written document that enables them to claim payment should the transaction fail.

Regarding The Co-operators' application to amend its defence, the Court reiterated that the decision to grant an application for an amendment belongs to the trial judge. That judge must base this decision on three principles:

> An amendment is permitted if it does not delay the proceedings or is not contrary to the interests of justice;
> If it does not constitute an entirely new application;
> The lateness of the application cannot be the only justification for dismissing the application.

The Court of Appeal also found that The Co-operators had sealed its fate by failing to mention these grounds upon the initial denial of coverage.

In addition, the Court of Appeal confirmed that the misappropriated sum was indeed the Coop’s property. As a result, the trial judge did not err in determining that the policy covered all property of any kind and all risks, including a loss resulting from computer fraud. The policy was not ambiguous and no exclusions applied.

The Court ruled that there was indeed of a plurality of insurance within the meaning of article 2496 C.C.Q. Also, the Co-operators policy and the Liberty policy contained excess clauses, resulting in the effect of such clauses having to be cancelled in order to prevent the insured from finding itself in a no-compensation situation, in accordance with the teachings of *Family Insurance Corp*[3]. In this

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case, the Court of Appeal determined that the Liberty policy was in fact specific insurance, as it covered a particular category of risks, namely fraud and embezzlement. As a result, this insurance became the primary insurance.

On the basis of the foregoing, the Court of Appeal did not rule on the calculation method the Superior Court applied to apportion the insurers' contributions when insurance penalties of the same rank exist.

Conclusion

This judgment contains many noteworthy points. Among other things, it is important for insurers to make sure, when denying coverage, that all the reasons for refusing to pay benefits are fully stated.

Also, with regard to a plurality of insurance, we note that even if an insurance policy includes an excess clause, it may not apply if the insured has another insurance policy with the same type of clause.

Ultimately, the Court of Appeal confirmed that qualifying an insurance policy as specific should not be unduly limited to only cases where certain and determinate property is covered, and that the insurance granted for a particular category of risk may, depending on the context, constitute such specific insurance.

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1. Canadian Anti-Fraud Centre, *Phishing*.
2. *Compagnie d'assurances générales Co-operators c. Coop fédérée*, 2019 QCCA 1678.
3. *Family Insurance Corp v. Lombard Canada Ltd.*, [2002] 2 SCR 695.

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