

# Insurers: Two-headed hydras

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On January 30, 2023, the Court of Appeal of Quebec rendered a decision in *Commission scolaire De La Jonquière c. Intact Compagnie d'assurance*.<sup>1</sup> The key issues in this case are the potential for conflicts arising from liability insurance policies and the obligation to disclose documents where insurers' duty to defend conflicts with their duty to indemnify insureds.

### The facts

This case is part of a class action in which all Quebec school boards—now referred to as school service centres (SSCs)—were accused of violating the right to free elementary and secondary education. As part of this class action, the SSCs brought an action in warranty against their insurers, seeking compensation for any amount they may be required to pay.

The insurers acknowledged their obligation to defend the appellants in the main proceedings; however, they argued that the claim was not covered by the insurance contract.

Following negotiations, the parties to the class action reached a settlement. The action in warranty against the insurers is still pending.

At the examination for discovery stage of the action in warranty, the insurers asked to obtain a copy of all communications exchanged between the appellants and their counsel since the beginning of the main proceedings. The SSCs objected to this request on the basis of professional secrecy and litigation privilege. The Court therefore had to rule on the merits of the objection.

### The trial

Drawing on the decision in *Domtar*<sup>2</sup>, the Superior Court dismissed the SSCs' objection, holding that they had waived their right to assert solicitor-client privilege regarding anything relating to the reasonableness of the settlement. It appears that the Court inferred this waiver from certain allegations made and from the disclosure of certain documents as part of the action in warranty.

The Court concluded that the appellants had to provide the insurers with the documents, risk analyses, letters, exchanges with the appellants and expert opinions having related to the reasonableness of the settlement since the beginning of the main proceedings. However, according to the Court of Appeal, the Court failed to provide a framework for such disclosure of information and to grant the SSCs the right to raise new objections in relation to said documents.

## **The appeal**

The Court of Appeal considered the conflicts that may arise from the dual responsibility of insurers: their duty to defend insureds and their duty to indemnify them. In this regard, it described liability insurers and their role as follows:

[20] The liability insurer is effectively a two-headed hydra: A type of two-headed creature with a single corporate identity, but where one head handles the insured's defence and the other protects the insurer's financial interests by ensuring that it only pays out for covered losses.

[21] Each head must base its decisions on the interest it is defending and the information available to it. The two heads must remain separate in order to give effect to the insurance contract. [...] The risk of a conflict of interest is therefore very real, which is why the insurer must put measures in place to ensure that it complies with the coverage provided by the policy, while also ensuring the full and complete defence of the insured.]

As for the ethical obligations of the lawyer mandated by the insurer to represent the insured, the Court stated that the lawyer becomes the insured's counsel in all respects and owes the insured absolute loyalty. As such, the right to professional secrecy in the insured's relationship with the lawyer can be set up against the insurer.

That being said, the lawyer must report on the progress of the case to the head of the hydra handling the insured's defence. The Court then stated that it was essential in this context that the information thus obtained be accessible only to that head, and that the insurer put in place the necessary measures to keep the two heads separate.

The Court of Appeal found that the trial judge did not err in concluding that the SSCs were required to provide the evidence necessary to examine the reasonableness of the settlement reached with the insurers. However, in order to do so, an exemption mechanism could be implemented, giving the SSCs the possibility to object to the disclosure of certain information.

The Court also confirmed that there was no basis for concluding that the appellants had waived solicitor-client or litigation privilege with respect to all of their exchanges with their counsel. This information must remain protected by professional secrecy and therefore cannot be disclosed to the person at the insurer's office in charge of the compensation file. The same goes for the accounts for fees, reports, opinions and other documents sent to the person at the insurer's office handling the defence, unless the insured waives this right.

## **Conclusion**

This case highlights the conflicts that can arise from the duality of insurers' responsibilities and the distinction between insurers' obligation to defend insureds and their obligation to indemnify them. Although the Court ruled that evidence aimed at verifying the reasonableness of a settlement from a qualitative and quantitative standpoint should be disclosed, it concluded that certain information and documents that are strictly relevant to insureds' defence need not be disclosed. In so doing, it reiterated insurers' dual responsibility and the importance of keeping the two heads separate when an insurer agrees to take on an insured's defence, but maintained its refusal to indemnify the insured.

1. *Commission scolaire De La Jonquière c. Intact Compagnie d'assurance*, 2023 QCCA 124.
2. *Chubb Insurance company of Canada c. Domtar*, 2017 QCCA 1004.