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A New Category of Contractual Breach in Auto Insurance: Statutory "Default"

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A NEW CATEGORY OF CONTRACTUAL BREACH IN AUTO INSURANCE: STATUTORY "DEFAULT"

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In a recent judgment, *Halifax Insurance Co.* v. *Judgment Recovery (N.S.) Ltd.*,[1] the Nova Scotia Court of Appeal has demonstrated again the vigour of the common law, sustained by unlimited judicial ingenuity. The best summary of the case is this first sentence from the judgment delivered by MacKeigan C.J.N.S.: "This appeal is on a simple question of law: Does the appellant, insurer under a motor vehicle liability policy, have to respond to the claim of a third party injured by the insured, where the insured had replaced the automobile specified in the policy without notifying the insurer within 14 days of having done so?"

If the question is simple, the answer is not. It involves the complex and refined distinction between restrictive definitions of risk in insurance contracts and breach of a policy condition, and it involves analysis of the elaborate statutory scheme to protect automobile accident victims by imposing a form of strict liability on the tortfeasor's insurer.

At trial the question posed above was answered adversely to the insurer by Cowan C.J.T.D.[2] In an earlier note,[3] I criticized Cowan C.J.'s judgment for failing to observe the difficult but fundamental distinction between risk definition and breach of condition, and for relying upon *General Security Ins. Co. of Canada* v. *Highway Victims Indemnity Fund*[4] which, though an excellent Supreme Court of Canada judgment on a similar set of facts, was an inapt authority because of the different wording of the Quebec and the Nova Scotia statutes.

The Halifax Insurance Company's appeal has now been dismissed. The judgment is much harder to criticize, except by observing that it creates a new category of contractual breach, which apparently falls nicely in the middle between the two old categories which were so nearly indistinguishable that one can only marvel that there is any room between them to fit anything.

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1 (1977), 77 D.L.R. (3d) 107.

2 *Re Judgment Recovery (N.S.) Ltd. and Halifax Ins. Co.; Lane* v. *Young* (1977), 73 D.L.R. (3d) 445.

3 J. Rendall, *The Distinction Between Breach of Condition and Restrictive Definition of Risk in Automobile Insurance Policies: Lane v. Young* (1978), 2 Can. Bus. L.J. 320.

4 [1976] I.L.R. 2703.

The Facts of the Case:

The Halifax Insurance Company issued an owner's policy of automobile insurance to Avery Young; the described automobile was a 1969 Pontiac. Young sold the Pontiac and bought a 1969 Ford, but did not inform the insurer. Twenty days later Young collided with, and injured, Rickey Lane.

It is true that the question can be formed very simply: was Halifax Insurance Company obliged to respond to Rickey Lane's claim? If it was not, then the public fund, Judgment Recovery (N.S.) Ltd., was obliged to answer the claim.

The Basic Insurance Doctrine:

In contrast to the simple fact pattern, the doctrinal context is complex, for the case involves the tension between the insurer's right to control its risk selection and the public interest in guaranteeing an insurance recovery for automobile injury victims.

Prior to this case, questions of risk selection and control fell to be considered under four heads,

(i) duty of disclosure;

(ii) material change in the risk;

(iii) breach of condition;

(iv) definition of risk.

A review of these four categories which, it was thought, subsumed all cases of the nature presently under discussion, requires reference to two sections of the *Insurance Act*, to one of the statutory conditions, and to a definition provision in the standard owner's policy of automobile insurance.

(i) Duty of Disclosure: Section 79 of the Nova Scotia *Insurance Act*[5] avoids the policy, *as against the insured*, if the insured has given "false particulars of the described automobile . . . to the prejudice of the insurer" or has "knowingly misrepresented or failed to disclose in the application any fact required to be stated therein."

At trial, Cowan C.J. noted that the Pontiac and the Ford were both standard types of vehicle, so the premium for public liability cover would be the same. Thus, if Young had obtained his policy from Halifax Insurance Company by describing his car as a 1969 Pontiac, when it was in fact a 1969 Ford, it is not clear that this inaccuracy would avoid the policy. Although the description might be "false," it could hardly be said to be "to the prejudice of the insurer." Whether the insurer would have a defence based on a "knowing misrepresentation" depends upon the meaning of "required to be stated." If that phrase implies a materiality test, then again the description of the car as a Pontiac instead of a Ford would give the insurer no defence.

In any event, such a misdescription of the car would give the insurer no defence to a claim by the third party injury victim. Subsection 98(1)

confers on the third party judgment creditor a direct right of action against the insurer,[6] and subsection 98(5) says that it is no defence that "an instrument issued as a motor vehicle liability policy . . . is not a motor vehicle liability policy."[7] This obliquely worded provision has consistently been interpreted to prevent an insurer from defending against the third party claim on the basis of a misrepresentation leading to the issue of the policy.

(ii) Material Change in the Risk: Statutory Condition #1 of the standard schedule of statutory conditions relating to automobile insurance[8] obliges the insured to "promptly notify" the insurer "of any change in the risk material to the contract and within his knowledge." Avery Young notified his insurer that he had traded cars twenty-one days after the trade and one day after the accident. On first impression, whether or not this notification was "prompt" enough, it would seem that he was not obliged to give it in any event since the change in vehicles was not material to the risk.

However, this overlooks Statutory Condition #1(2), which makes every sale of the insured vehicle a material change that must be reported to the insurer. This point will be developed at considerable length toward the end of this note.

Even if Young offended Statutory Condition #1, the insurer would have no defence as against Lane. As we shall note in a moment, breaches of condition afford the insurer no defence to the third party's claim.

(iii) Breach of Condition: The insured's conduct may amount to a breach of a condition imported into the insurance contract by statutory prescription (i.e., a "statutory condition") or a condition agreed to by the parties (i.e., a "purely contractual condition"). In either case, the breach would give the insurer a defence to any claim brought under the policy by the insured, but would afford no defence against a third party judgment creditor of the insured. Paragraph 98(4)(b) of the *Insurance Act*[9] provides that "the right of a person who is entitled under subsection (1) to have insurance money applied upon his judgment or claim is not prejudiced by . . . any act or default of the insured before or after [the event giving rise to the claim] in contravention of this part [of the Act] or of the terms of the contract."

(iv) Definition of Risk: Although their purpose is the same, to restrict the risk being assumed and to refine the statement of the risk assumed, insurance law has treated very differently two devices: the policy condition and the restrictive definition.

A breach of condition is incurable. If the insured breaches a condition,

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[5] R.S.N.S. 1967, c. 148, as amended by S.N.S. 1966 c. 79, proclaimed Jan. 1, 1969. The equivalent provision in Ontario is s. 204 of *The Insurance Act*, R.S.O. 1970, c. 224.

[6] *Id.* The Ontario equivalent is s. 225(1).

[7] *Id.* The Ontario equivalent is s. 225(5).

[8] See: the Schedule to Part VI of the *Insurance Act*, R.S.N.S. 1967, c. 148. See also: s. 205 of the Ontario Act, R.S.O. 1970, c. 224.

[9] The Ontario equivalent is s. 225(4), R.S.O. 1970, c. 224.

his policy may be avoided when the insurer learns of the breach, and the only cure is waiver by the insurer. By contrast, an insured may be able, unilaterally, to cure a failure to comply with a definition of the risk. For example, in *Re Morgan and Provincial Ins. Co.*,[10] a truck was insured pursuant to a proposal form which stated that the truck would be used to transport coal, and a recital in the policy purported to incorporate all the answers in the proposal as the basis of the contract. The truck was used temporarily to transport timber, no harm occurring during this time. Later the truck was damaged in a collision while carrying coal. Had its use to carry timber been a breach of condition, the policy would have been thereby avoided even though the breach was temporary and unrelated to the loss. However, it was held that the statement as to use of the truck was definitional of the risk; in the result, the insured was off cover whenever the truck was used for a purpose other than transportation of coal, but was covered whenever the truck was transporting coal.

Although a failure to comply with the risk as defined in the policy is less serious in that it may be cured by the insured, such a failure is more dangerous to the insured in another way. In response to the insurance industry's zealous use of policy conditions, legislatures have long since developed devices to control their application. In the Automobile Part of the *Insurance Act*, a schedule imports into every policy a set of nine statutory conditions[11] and section 80[12] prohibits the insurer from varying, omitting or adding to the statutory conditions. Moreover, although a breach of condition will avoid the policy as against the insured, it does not give the insurer a defence to a claim by a third party judgment creditor except insofar as that claim exceeds the statutory minimum limits of liability.

In contrast to this rigorous supervision of policy conditions, the *Insurance Act* leaves virtually untouched the insurer's freedom to control its risk by careful definition thereof. Section 82[13] prescribes that an owner's policy, as well as covering all named drivers, must insure against loss caused by anyone driving the described vehicle with the owner's consent. Apart from this important prescription, the Act leaves virtually unfettered the parties' freedom to make their own contract so far as agreement on the risk is concerned. Thus, the insurer, by carefully stating the risk undertaken in its policy, may be able to give itself a defence to later claims by the insured or by a third party in a way which it could not do through the device of a policy condition.

The Standard Owner's Policy:

When the vehicle described in an owner's policy is disposed of, the policy does not lapse, but continues in force to insure his third party liability

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[10] [1932] 2 K.B. 70 (C.A.), aff'd [1933] A.C. 240 (H.L.).

[11] See: Schedule to Part VI of the Nova Scotia Act, R.S.N.C. 1967, c. 148, and s. 204 of the Ontario Act, R.S.O. 1970, c. 224.

[12] The equivalent in Ontario is s. 205(1), R.S.O. 1970, c. 224.

[13] The equivalent in Ontario is s. 207, R.S.O. 1970, c. 224.

in respect of any loss caused by driving a vehicle he does not own; in effect, the owner's policy becomes a non-owner's policy.[14]

When the insured disposes of the described vehicle and replaces it with another, in theory this situation could be treated as a potential material change in the risk to be dealt with by Statutory Condition #1. If the risk was increased the policy would be avoided unless the insured "promptly notified" the insurer. If, as Cowan C.J. said was the case when Avery Young replaced his 1969 Pontiac with a 1969 Ford, the risk was not affected, then the policy would continue and would cover the new vehicle.

However, the law does not seem to follow this theory. Apparently conceding the insurer's right to know what vehicle it is covering, and to restrict its coverage to that vehicle without reference to materiality, the law applies very stringent restrictions to vehicle changes. First, Statutory Condition #1 requires the insured to notify his insurer of any sale of the described vehicle. Secondly, as a matter of basic insurance doctrine, the policy description of the vehicle appears to be treated as a restrictive definition of the risk. Just as a fire insurance policy issued without rectifiable error to cover the house at No. 10 Cedar Street would not cover an identical house at No. 11 Cedar Street, an auto policy describing a 1969 Pontiac as the insured vehicle does not cover a 1969 Ford, a 1969 Dodge nor even a 1969 Pontiac other than the one specifically described in the policy by reference to engine and body numbers.

The insurer's right to restrictively define its risk appears to be endorsed even by those provisions of the *Insurance Act* that operate to give statutory extended coverage and to give top priority to protection of automobile injury victims. Section 82 causes an owner's policy to insure in respect of losses caused by someone driving with the owner's consent if he "drives an automobile owned by the insured . . . *and within the description or definition thereof in the contract.*"[15] Subsection 98(1) gives the third party direct action against the insurer to "[a]ny person who has a claim against an insured, *for which indemnity is provided by a contract.*"[16]

However, motor vehicle owners will, in the ordinary course of things, frequently trade vehicles in the middle of an insurance policy year. To solve the numerous serious problems that would result, the insurance industry took the initiative in adding to the standard owner's policy the following clause to give extended coverage:

> AUTOMOBILE DEFINED—In this Policy except where stated to the contrary the words "the automobile" mean:
>
> . . . .
>
> (b) A Newly Acquired Automobile—an automobile, ownership of which is acquired by the insured and, within fourteen days following the date of its delivery to him, notified to the Insurer . . . .

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[14] *Minister of Transport for Ontario* v. *Economical Mutual Insurance Co.* (1973), 40 D.L.R. (3d) 651; 1 O.R. (2d) 459; [1974] I.L.R. 761 (H.C.J.); aff'd 43 D.L.R. (3d) 27*n*; [1974] I.L.R. 991 (C.A.), without written reasons.

[15] Emphasis added.

[16] Emphasis added.

Thus, if Avery Young had notified the Halifax Insurance Company of his trade of the Pontiac for the Ford within two weeks after the trade, the Ford would have been an insured vehicle under the policy and there would have been no dispute as to the insurer's obligation to answer Rickey Lane's claim.

Young did not give that notice, and MacKeigan C.J.'s deceptively simple question becomes more complex: into which of the four categories of contractual breach does Young's conduct fall? Clearly, it does not fit within category (i), *failure of disclosure.* That concept is reserved for dealings between the parties at the time of application for the insurance, and does not touch upon matters arising after the insurance contract is on foot.

Young's conduct could be viewed as falling into category (ii), *a change potentially material to the risk,* or into category (iii), *a breach of condition.* As will be discussed below, the judicial comments at trial and on appeal rest largely on those two categories, though neither judge put Young's conduct into either category and neither relied on either concept as the real basis for decision.

Before discussing the two judgments, it must be noted that the position taken by the Halifax Insurance Company was that the incident fell within category (iv), *definition of risk.* The policy described a 1969 Pontiac; through a definitional clause in the policy it would extend also to any replacement vehicle, acquisition of which was notified to the insurer within fourteen days. Young did not notify the insurer within that time; in the result, the Ford was simply outside the risk as defined in Young's policy and, accordingly, the Halifax Insurance Company was not liable either to Young or to any third party victim of his.

Judicial Gerrymandering at Trial:

Cowan C.J.T.D. noted that the change in vehicles did not adversely affect the insurer's risk and called in aid a proposition stated by Pigeon J., in a case involving similar facts,[17] that the insurer should not, as against the injury victims, be entitled to set up a failure to give notice of a vehicle change which did not prejudice the insurer when it could not set up as a defence failure to notify it of an accident, a failure which could be extremely prejudicial to the insurer.

This proposition has two important attributes in its favour. It seems logical, and it seems to reflect good public policy. However, we are dealing with an area of insurance law which, as has been illustrated, is characterized not by logic but by rather arbitrary distinctions.

Cowan C.J., too good a judge to leave his judgment dependent solely on logic and public policy, sought some kind of solid doctrinal base. It is worth noting that he did not treat Young's conduct as falling into category

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[17] *General Security Ins. Co. of Canada* v. *Highway Victims Indemnity Fund,* [1976] I.L.R. 2703 (S.C.C.).

(ii). To say that substitution of the Ford for the Pontiac was merely a change relating to the risk, but in the circumstances immaterial in that it in no way increased the risk, would involve the conclusion that the change did not have to be reported and failure to report would give the insurer no defence either against the insured or against his victim.[18] It is quite clear from the trial judgment and the judgment on appeal that there was no judicial sentiment in favour of Avery Young. Both Cowan C.J. and MacKeigan C.J. sought to fix the Halifax Ins. Co. with responsibility for Rickey Lane's loss, while leaving the insurer free to raise its defences against Avery Young and to recoup itself from Young if it wished.

Cowan C.J. went about this by considering the insurance position during the fourteen days immediately following the trade of the Pontiac for the Ford. For many years the only Canadian authority on this point was *Pascoe* v. *Provincial Treasurer of Manitoba*[19] in which the trial judge, Monnin J., had stated that a newly-acquired vehicle is automatically covered for the first 14 days, the coverage lapsing if notice is not given to the insurer within that time. Tritschler J.A., pointing out that there was no duty on the insured to take action to cause his insurance policy to cover the new vehicle, concluded that the new car would not be insured, even within the first 14 days, unless and until the insured gave the requisite notice. The point was not determinative of the result in *Pascoe*. The accident having occurred 20 days after acquisition of the new vehicle, a majority of the Court of Appeal was content to say that whatever may have been the case during the first 14 days, there was no insurance coverage at the time of the accident.

Cowan C.J. preferred Monnin J.'s view of the 14-day clause and concluded that Avery Young's Ford was insured for 14 days and the coverage then lapsed. By itself, this conclusion gets Rickey Lane and Judgment Recovery (N.S.) Ltd. nowhere in their contest with the Halifax Ins. Co. When a motor vehicle policy lapses for failure to pay a renewal premium, the vehicle is off cover and the insurer is responsible neither to the insured nor to his victims. However, Cowan C.J. cited the Supreme Court of Canada judgment in *General Security Ins. Co. of Canada* v. *Highway Victims Indemnity Fund*[20] as authority for the different treatment of a "lapse" which results from failure to comply with the 14-day clause. It is true that Pigeon J. took the view that a newly acquired vehicle was covered for 14 days and that failure to notify the insurer produced a lapse. It is also true that the Court held that a lapse in those circumstances afforded the insurer no defence to a claim by the third party injury victim.

It is vitally important to note that the *General Security* case arose under the Quebec Act, which expressly prohibits an insurer from setting up against

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[18] As will be pointed out later, this is the conclusion one would draw on first impression, but closer analysis of the *Insurance Act* suggests that it is incorrect.

[19] (1958), 16 D.L.R. (2d) 300; 26 W.W.R. 640; [1958] I.L.R. 469 (Man. Q.B.); aff'd 17 D.L.R. (2d) 234; 27 W.W.R. 393; [1959] I.L.R. 552 (Man. C.A.).

[20] [1976] I.L.R. 2703.

third parties "the causes of nullity *or of lapse* that might be set up against the insured."[21]

By contrast, the Nova Scotia Act says nothing about a lapse. Subsection 98(4) says that a third party's claim

> . . . is not prejudiced by
> . . . .
> (b) any act or default of the insured . . . in contravention of this Part or of the terms of the contract.

Indeed, Pigeon J. noted that this was the language of the Manitoba Act under which *Pascoe* was decided, and he drew attention to the different wording of the Quebec Act which he described as wider in scope.

In short, by relying on Pigeon J.'s judgment in *General Security*, Cowan C.J.T.D. seems to have rested on an inapplicable authority.

Judicial Gerrymandering on Appeal:

The point in *Lane* v. *Young* was very important to the entire auto insurance industry. An appeal was taken in the Halifax Ins. Co.'s name, but sponsored by the Insurance Bureau of Canada. The Court of Appeal sustained Cowan C.J., but on somewhat different grounds.

MacKeigan C.J.N.S. concluded that the 14-day clause could not be a condition of the insurance contract, else it would be struck down by section 80, which incorporates into the policy the statutory conditions and prohibits any "variation or omission of or addition to" them.

The Chief Justice also refuted the insurer's contention that the 14-day notice requirements formed part of the definition of the risk:

> I do not look upon the 14 days' notice phrase as part of the description. It is not needed to identify the subject. The rest of the definition is part of the insuring agreement. The notice phrase does not change or refine the definition or make the subject-matter either wider or narrower; it is thus not an exception to or exclusion from the insuring agreement.[22]

If the notice clause is neither a condition nor part of the definition of the risk, what is it? According to MacKeigan C.J. it is "merely a term of the policy which, if the insured failed to observe it by giving the insurer notice within 14 days of acquiring the replacement car, would cause a lapse in the collision coverage on that car which began the moment it replaced the previous car."[23]

Thus it will be noted that his Lordship adopted the view taken by Monnin J. in *Pascoe*, and approved by Cowan C.J.T.D. in the present case, that the extended cover under the "Newly Acquired Automobile" clause attaches automatically to the new vehicle without any necessity for notifica-

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[21] *Highway Victims Indemnity Act*, R.S.Q. 1964, c. 232, s. 6. (Emphasis added)
[22] (1977), 77 D.L.R. (3d) 197 at 109.
[23] *Id.* at 110.

tion. The only significance of the notice is that failure to give it causes the coverage to lapse after 14 days.

However, as has already been remarked, a lapse of coverage normally involves the result that the insurer is off the risk and responsible neither to the insured nor to his victims, and unlike the Quebec counterpart, the Nova Scotia subsection 98(4) says nothing about preserving the third party's claim in the face of a lapse.

Nevertheless, MacKeigan C.J.N.S. managed to jam the situation into paragraph 98(4)(b) as a "default."

> Here the only possible defence by the insurer is that the insured did not comply with the 14 days' notice term. That was, in my opinion, clearly a "default of the insured . . . in contravention of the terms of the contract" and thus not available to the insurer as a defence.[24]

Thus, judicial ingenuity has given us a fifth category of contractual breach to add to the list discussed above. In the title to this note I have, for brevity's sake, referred to the new category as "statutory default." Actually, of course, MacKeigan C.J. asserts that the failure to give notice is a "default," not in a duty imposed by statute, but in contravention of the contract. Thus, it would be more apt to style the new category "contractual default as contemplated by s. 98(4)(b)."

As will now be discussed, this new category involves us in some difficulties.

Criticism of the MacKeigan Judgment:

The first criticism of this new category is that it is one more indistinct distinction to add to a list which was already long enough and was giving rise to problems of characterization.

Perhaps a more forceful criticism is that the language of paragraph 98(4)(b), "act or default . . . in contravention . . . of the contract," seems clearly to contemplate a failure by the insured to perform some duty cast upon him.

In *Pascoe*, Tritschler J.A. pointed out that the insured is under no duty to take any action to cause his auto insurance policy to apply to a newly acquired vehicle:

> . . . he was free to do as he pleased and for any reason which seemed sufficient to him could elect to take advantage or otherwise of the provision under consideration. Just as any other motorist may decide to insure or not to insure or may forget to insure, so also might this insured.[25]

There is in Nova Scotia today a rather vague statutory duty to insure in that the *Motor Vehicle Act* makes it an offence to drive a vehicle unless

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[24] *Id.* at 110.

[25] (1959), 17 D.L.R. (2d) 234 at 238; 27 W.W.R. 393 at 397; 66 Man. R. 367 at 375; [1959] I.L.R. 552 at 554 (C.A.).

either the vehicle or the driver is covered by a liability policy. It is notorious that even this requirement is finessed by obtaining a pink card and then cancelling the policy without surrendering the pink card. What is important to our discussion, however, is that neither the *Insurance Act* nor the contract of automobile insurance contains any statement requiring a vehicle owner to insure.

It is to be noted that MacKeigan C.J. did not assert a "default . . . in contravention of" the *Insurance Act*. He held that Avery Young had committed a default which contravened the terms of the contract. But the "Newly Acquired Automobile" clause of the contract appears to operate precisely in the manner suggested by Tritschler J.A., in that it gives the insured an option to bring his new vehicle within the cover by notifying the insurer, or to leave it uninsured by refraining from giving the notice. Indeed, the entire matter seems to involve definition of the risk exactly as the Halifax Ins. Co. argued. A newly acquired vehicle is within the risk if its acquisition is notified to the insurer; it is not within the risk if notice is not given.

MacKeigan C.J. is surely wrong in saying that "[t]he notice phrase does not change or refine the definition or make the subject matter either wider or narrower; . . ."[26] It is true that all the inherent attributes of the vehicle are the same in either case and that the risk is not materially affected by giving or withholding notice. But the point is that "definition of risk" and "materiality to the risk" are separate concepts. In *Re Morgan and Provincial Ins. Co.*[27] it would have been useless for the insured to prove that transporting timber did not increase the risk, or even that it was a lower risk activity than carrying coal. The risk was defined in terms of use of the truck to carry coal; when it was carrying timber it was outside the risk. This analysis is sustained by *Renshaw* v. *Phoenix Ins. Co. of Hartford, Conn.*[28] where a cottage and its contents were insured "while located and contained as described herein and not elsewhere." A schedule to the policy fixed the cottage as located on a specifically numbered lot on Stanley Island in the St. Lawrence River. The Ontario Court of Appeal held that, by moving the cottage to the mainland, the insured had taken it outside the risk. It was pointless to argue that the risk was not materially affected; even if the risk were improved, the cottage was off cover because it was outside the defined risk. The vast importance to the insurer of the distinction between "materiality" and "definition of risk" is that the insurer can, by carefully couching the language in which the risk is defined, exclude activities which might not be regarded as "material" by a reasonable insurer. Nor is this necessarily reprehensible. As we have noted above, although replacing a 1969 Pontiac with a 1969 Ford was immaterial to the risk, none of the judges involved with the dispute between the Halifax Ins. Co. and Judgment Recovery denied that the insurer was entitled to insist on being informed of the change. It was the desire to allow the insurer to raise the failure of the insured to give this information as a defence against

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[26] *Supra* note 22, at 109.

[27] *Supra* note 10.

[28] [1943] O.R. 223; [1943] 2 D.L.R. 76; 10 I.L.R. 92 (C.A.).

the insured,while at the same time disqualifying it as a defence against the third party, that led MacKeigan C.J.N.S. to invent the new category of breach —the paragraph 98(4)(b) "default."

I think the new category is an unfortunate additional cyst on an already heavily encrusted insurance doctrine, and I think its basis as propounded by MacKeigan C.J. is very doubtful, but I cannot disagree with the underlying philosophy that guided Cowan C.J.T.D. and MacKeigan C.J.N.S.

After a brief survey of the policy considerations prompting the two decisions, I will suggest an alternative analysis by which the same result might have been reached.

The Fundamental Merits as Between Halifax Insurance Co. and Judgment Recovery Ltd.:

Both Nova Scotia judgments quoted, and apparently were influenced by, the following remarks of Pigeon J. in the *General Security*[29] case:

> [W]hy should the insurer be entitled to set up against the victims the failure to notify him of a change of car, which causes him no prejudice, when he certainly cannot set up the failure to give notification of an accident, which could be extremely prejudicial to him.
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> [NOTE that in the above paragraph "him" refers to the insurer, and in the paragraph below Pigeon J. uses the pronoun "he" when referring to the insurer.]
>
> It should be borne in mind that, under the Act of Quebec, the insurers, as a group, maintain the Fund by assessments on premiums. The purpose of s. 6 is clearly to prevent an insurer from passing on to the group a risk for which he has collected a premium. Having to bear the consequences when a false statement by an insured results in his taking a lower premium than he would otherwise charge, *a fortiori* he should not be allowed to pass the liability on to the Fund because of an omission that caused him no prejudice. In the case at bar, the real dispute is between the insurer and the Fund. I see no reason for obliging the latter rather than General Security to indemnify the victims or their legal representatives.[30]

I cannot disagree with this judicial sentiment. The same result as in the *General Security* case could be reached in Nova Scotia through an appropriate statutory amendment. Paragraph 98(4)(b) could be varied to refer to "lapses" as does section 6 of the Quebec Act. There might be an objection to this in that such a statutory provision could be taken as applying also to lapses of coverage for non-payment of a renewal premium.

An alternative would be to introduce prescriptive coverage for undescribed vehicles in the way we presently deal with unnamed drivers. Section 82 makes the insurer liable for loss caused by the described vehicle while it is being driven by anyone with the named insured's consent. It would be quite feasible to introduce a similar provision prescribing coverage whenever the named insured was driving any vehicle, whether or not described in his policy. This would introduce some statutory control into the matters which are now dealt with by the extended cover clause of the auto insurance policy under the heading, "Automobile Defined."

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[29] *Supra* note 20.

[30] [1976] I.L.R. 2703 at 2707-08.

There are some objections to any suggested statutory solution. The nine common law provinces attempt to maintain uniformity in their respective insurance statutes, and so the above proposal is really a proposal for change in nine statutes. In fact, significant differences presently exist as some provinces have adopted a system of no-fault benefits and others have not.

In any event, leaving aside the problems involved in any attempt to obtain a uniform amendment throughout the common law provinces, it is frustrating enough to contemplate the likely legislative process in Nova Scotia. A legislature which has not bothered to correct an obvious error in the subrogation provision of the Auto Insurance Part of the Act, a correction which could be made by changing one digit,[31] is unlikely to tackle the kind of significant statutory amendment suggested. Cowan C.J.T.D. and MacKeigan C.J.N.S. are to be commended for attempting a judicial solution rather than leaving the problem to be dealt with by a statutory amendment that is unlikely to be forthcoming.

However, I will suggest a judicial solution which I think preferable to the ones adopted by Cowan and MacKeigan C.JJ.

Materiality and Statutory Condition #1:

We have noted several times the judicial observation that substituting a 1969 Ford for a 1969 Pontiac does not materially affect the risk. In the first instance, therefore, there is some inclination to treat the entire problem of substituted vehicles as simply a question of change in the risk and materiality. I suggested that the judges avoided this analysis out of a concern that a finding that the replacement of the named vehicle was not a material change in the risk would lead to a conclusion that the insurer would have no complaint and no defence against its own insured for failure to give notice of the transaction. Everyone seems to agree that, regardless of its materiality, the insurer is entitled to insist on knowing what vehicle is covered by its policy, and it is reasonable to allow the insurer to treat as a breach the failure by its insured to give notice of an exchange of vehicles.

What seems to have gone unnoticed is that Statutory Condition #1 is nicely worded to achieve exactly this result.

> 1(1) *Material Change in Risk*—The insured named in this contract shall promptly notify the insurer, or its local agent, in writing, of any change in the risk material to the contract and within his knowledge.
>
> (2) Without restricting the generality of the foregoing the words "change in the risk material to the contract" include:
>
> (a) any change in the insurable interest of the insured named in this contract in the automobile by sale, assignment or otherwise, except through change of title by succession, death or proceedings under the Bankruptcy Act (Canada);
>
> . . . .

[31] Section 100M(4) of the Nova Scotia Act, S.N.S. 1966, c. 79, refers back to subsection (2). The reference should be to subsection (3). The Ontario equivalent is s. 240(4). R.S.O. 1970, c. 224.

Statutory Condition #1(1) is virtually identical to Statutory Condition #4 in the Fire Insurance Part of the Act.[32]

It has been held that Statutory Condition #4 only obliges the insured to give notice of changes which affect the risk adversely. At common law, a change in the risk after the policy was issued did not have to be reported at all. There was no opportunity for the insurer to get off the risk. Thus, it would be harsh to read the statutory condition as avoiding the insured's cover if he failed to give notice of changes which materially improved the risk.

Nevertheless, Statutory Condition #1(2) is worded so as to include in those material changes which must be reported "any change in the insurable interest . . . in the automobile by sale, assignment or otherwise."

Applying this strictly to Avery Young we could say that he breached the statutory condition by failing to notify the Halifax Ins. Co. of his sale of the 1969 Pontiac. (This assumes that notification 20 days later, and after an accident, was not "prompt notification.") The result would be a breach of condition giving the insurer a defence against Young but not against his victims.

This would be the same result which MacKeigan C.J. reached; indeed, it would be quite correct to call Young's conduct a "default" within the meaning of paragraph 98(4)(b). However, I emphasize that it would be a "default of the insured . . . in contravention of this Part [of the *Insurance Act*]," *not* a "default . . . in contravention . . . of the terms of the contract." The proposed analysis has two advantages: it uses existing categories of contractual breach instead of adding a new one; it also seems to involve less violence to the statutory language. Statutory Condition #1(2) is quite aptly worded to achieve the interpretation proposed whereas, I submit, MacKeigan C.J. has seriously strained the language of paragraph 98(4)(b).

It must be noted that the analysis I have suggested would produce a breach of the statutory condition whenever the insured parts with the vehicle described in his policy and without reference to whether he acquires a new vehicle.

It may at first be thought that this is unnecessarily harsh in view of the likelihood that the insured has improved his insurer's risk inasmuch as he no longer has any vicarious liability for losses caused by the described vehicle. Whether the risk is improved or increased may depend upon whether the insured now makes increased use of borrowed vehicles, perhaps uninsured and in worse mechanical condition. This is a matter which could be left to be proven whenever the issue arises. However, it does not seem unreasonable to give Statutory Condition #1(2) a strict reading and to justify it by saying that, irrespective of materiality, the insurer is entitled to know, not only about replacement vehicles, but about every transaction purporting to affect the insured's ownership of the vehicle named in his policy.

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[32] See: the Schedule to Part VII of the Nova Scotia Act, R.S.N.S. 1967, c. 148. Similarly, in Ontario compare Statutory Condition 4 with s. 122 with Statutory Condition 1 under s. 205.

The Minister of Transport for Ontario v. *Economical Mutual Ins. Co.*[33] involved just such an issue. The insured, McNaughton, sold his "described vehicle," a Fargo pick-up truck, and later bought an Oldsmobile, without any notice of either transaction to his insurer. Later still, he injured Elsey while driving an uninsured Pontiac borrowed from Webb. Elsey was compensated by the Ontario Unsatisfied Judgment Fund and, as in *Halifax Ins. Co.* v. *Judgment Recovery* and as in the *General Security*[34] case, the dispute was between the Fund and the tortfeasor's insurer.

The factor distinguishing the *Economical Mutual*[35] case from the other two was that about a month elapsed between sale of the Fargo truck and purchase of the Oldsmobile. The insurer argued that McNaughton's policy lapsed when he sold the Fargo. This argument was based, not on the statute, but on the contention that insurable interest in the object of the insurance is a necessary condition for the continued existence of the insurance and that the entire policy lapses when the insured parts with his interest in the described automobile.

Lerner J. distinguished a line of English cases and held that Section A of an auto policy, the third party liability cover, is an independent insurance, not requiring any insurable interest in the described vehicle. In effect, by disposing of his Fargo truck, McNaughton had converted his owner's policy into a non-owner's policy.

On the point which is of interest to our analysis of *Halifax Ins. Co.* v. *Judgment Recovery*, Lerner J. asserted that McNaughton breached Statutory Condition #1 by selling the Fargo without notifying his insurer, but this was exactly the kind of breach which could not be raised against the third party victim by reason of subsection 223(3) of the Ontario Act as it then was.[36]

Thus, Economical Mutual Ins. Co. was liable to reimburse the Ontario Minister of Transport, and following the same analysis the Halifax Ins. Co. would be liable to Rickey Lane and Judgment Recovery (N.S.) Ltd. would not.

This reaches the same result as the Nova Scotia Court of Appeal but, it is submitted, by a line of analysis which is to be preferred.

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[33] (1973), 40 D.L.R. (3d) 651; 1 O.R. (2d) 459; [1974] I.L.R. 761 (H.C.J.).

[34] *Supra* note 20.

[35] *Supra* note 33.

[36] Now s. 225(4) of the Ontario Act, R.S.O. 1970, c. 224, and s. 98(4) of the Nova Scotia Act, S.N.S. 1966, c. 79.