

EDITOR'S INTRODUCTION

Borden Ladner Gervais LLP (BLG) is pleased to present this twenty-second edition of the *Canadian Insurance Law Newsletter* for the benefit of our clients and others interested in this constantly evolving area of law. Our objective is to keep you abreast of recent trends and developments of significance on a wide variety of insurance law related topics.

This edition canvasses the issue of whether the new *Rules of Civil Procedure* pertaining to experts in Ontario govern accident benefit assessors and considers recent Canadian appellate decisions concerning the scope of "property damage" coverage, and the absolute pollution exclusion, found in standard commercial general liability policies. This edition also includes a discussion of class actions in the insurance industry as well as case comments on two recent Ontario Court of Appeal decisions: *Wellington v. Ontario* which precludes the right of victims and their family members to bring civil actions in negligence against criminal investigators, and *Muskoka Fuels v. Hassan Steel* which considered spoliation of evidence and liability under the *Sale of Goods Act*.

We invite your comments and suggestions with respect to questions, topics or concerns of special interest that you would like to see addressed in future editions.

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CLASS ACTIONS AND THE INSURANCE INDUSTRY

Class Action! The words hardly raise the spectre of asbestos, mould or historical abuse, but they are a risk that will not be legislated out of existence or solved by technology. In fact, class action litigation is still expanding in Ontario and many other provinces led by a more developed practice in the Province of Québec.

This article will provide a brief overview of the state of development or maturation of class actions, the issues that drive them and the lines of insurance that may be implicated.

After some celebrated false starts in the 1970s that demonstrated the inadequacy of the rudimentary rules of practice permitting class proceedings, the Province of Ontario followed the lead of the Province of Québec and enacted the *Ontario Class Proceedings Act, 1992*, which came into force on January 1, 1993.

Simply, the legislation permits a representative plaintiff to ask the court to certify an action as a class proceeding, to appoint the plaintiff to represent the class and to appoint and instruct counsel and to permit the court to decide certain issues in dispute as common issues affecting the entire class. These common issues must be significant enough to move the litigation forward in a meaningful way. For example, common issues may investigate whether a defendant owes a duty of care to a class of plaintiffs or whether a defendant's actions meet the prevailing standard of care.

The class action is designed to provide access to justice for those that would not be able to seek redress because, for example, individual claims are small and the issues are complex and expensive to litigate, to provide judicial efficiency and to achieve behaviour modification.

The motions requesting certification orders from the court are hotly contested, often with legal fees for each of plaintiff and defendant of several hundred thousand dollars. If a representative plaintiff is successful in its certification motion request, the action proceeds to the liability phase with the common issues determined at a common issues trial and the remaining issues, such as individual damages, assessed at a later phase of individual trials or assessments.

The bulk of class action litigation in Ontario has been contested motions for certification. There have been fewer class action trials to judgment. Denials of certification motions usually terminate liability claims, whereas successful certification decisions often result in settlements which must be approved by the courts in what is akin to a fairness hearing.

However, in the last several years, Ontario courts have tried significant class actions to judgment with \$36 million awarded in *Smith v. Inco* (2010) and \$455 million awarded in *Jeffery v. London Life Insurance Co.* (2010), with appeals expected. In *Andersen v. St. Jude Medical, Inc.* the trial recently passed its one year anniversary and is expected to conclude this year.

These trials represent the next stage of development of the class action practice in Ontario. Insurers have developed an understanding of the cost of defending certification motions and the extraordinary costs that may be engaged in class action settlements such as notice campaigns and claims administration costs. Insurers are now able to assess the cost of defence of class action trials and the indemnity payments that may be required at judgment.

Class actions have also been responsible for the development of novel causes of action or remedies. For strategic considerations, plaintiffs have brought waiver of tort claims as an alternative to damage claims. These claims seek restitution of revenues or profits earned by a defendant on a block of business, such as on the sale of an allegedly defective product. Defence accounting costs to calculate the revenue or profit earned on the block of business can amount to several hundred thousand dollars or more. The viability or existence of the waiver of tort claim is still under legal review. At a minimum, the claim requires significant defence costs and has attracted insurer interest.

Many class actions are brought by an increasingly entrepreneurial plaintiff bar as a result of developments in the United States. For example, the prospect of large scale settlements in class actions or in multidistrict litigation in the United States often results in the initiation of copycat class proceedings in Canada. Regulatory investigations in the United States or product recall in the United States or Europe has also led to the initiation of class proceedings in Canada.

The *Canada Consumer Products Safety Act* (2010), came into force on June 20, 2011. The *Act* empowers the Minister of Health to order recalls of consumer products that are a danger to human health or safety and imposes certain incident reporting obligations on manufacturers, importers and sellers of consumer products. Experience in the United States predicts that more class actions

will result if the Minister of Health is proactive and the legislation is actively enforced.

The range of actions brought as class actions before the courts is extremely wide, including recent claims for unpaid overtime, claims for property damage or bodily injury from pharmaceutical products, medical devices or consumer products, claims for economic losses including loss of value or claims for extended warranty coverage on consumer products, claims resulting from environmental issues or contamination, claims for price fixing under competition legislation, claims for abuse in schools and custodial institutions, and claims for improper fees and charges against insurers, financial institutions, colleges and universities.

Some of these claims can touch a long list of possible insurance coverages, including commercial general liability, environmental impairment and directors and officers policies (D&O).

Securities claims continue to attract considerable publicity. These claims generate significant exposure for directors and officers who then turn to their D&O policies for defence and indemnity.

As of the end of December, 2010 there were 28 outstanding securities class actions in Canada. NERA Economic Consulting reports that these actions represent approximately \$15.9 billion in outstanding claims, inclusive of punitive damage claims. Half of these 28 cases have been filed in the last two years.

The insurance industry itself has been an early target of class actions with mixed results. Class proceedings resulted in settlement of some vanishing premium cases in the life insurance industry. Insurers were successful in ultimately resisting certification of claims for deductibles under automobile policies. Other disputes considered the quality of repair parts replaced under automobile policies. Other actions sought

certification of claims for overcharging of management fees on life policies, and most recently, a dispute concerning transactions involving PAR accounts of life insurers.

Of interest to insurers, many claims arise from a discrete event but often claims arise from a course of conduct over an extended period. Examples include products manufactured over seven or eight years, initially undetected, but with progressive property damage over many years, operation of a care facility for a decade or more, or environmental pollution over decades. Claims may be advanced by claimants in a province, across Canada or North America or throughout the world. These claims can implicate insurance policies over many years, multiple policies for the same year, as well as excess policies, and can raise territorial coverage issues and issues of jurisdiction of the courts.

Crisp management and direction of the defence, particularly at the early important stage of an action when decisions concerning the defence of a certification motion must be made, can be hampered by coverage issues preventing insurers from taking final positions on the engagement of cover or defence obligations. Coverage considerations can be particularly complex where multiple policies are implicated.

Insurance broker responsibilities can be complex and are beyond the scope of this brief article. However, insurers and brokers alike will be interested in developments affecting a company or industry, both in Canada and outside Canada, and in considering not only the risk of the importation of a copycat class action into Canada against a

Canadian insured, but also the issues of available insurance coverage for what are often novel or innovative claims. Apart from any other coverage considerations, the potential magnitude of judgments or settlements in class action suits raise obvious issues as to the adequacy of available insurance limits, particularly in industries or sectors susceptible to class action activity, and brokers should clearly be addressing this potential risk in the advice and counsel provided to insureds.

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BRITISH COLUMBIA COURT OF APPEAL BROADENS CGL COVERAGE FOR DEFECTIVE PRODUCTS

On April 12, 2011, the British Columbia Court of Appeal released its decision in *Bulldog Bag Ltd. v. AXA Pacific Insurance Co.* (2011) [*Bulldog Bag*]. The case is significant in that it was the first appellate decision in Canada dealing with a commercial general liability (CGL) policy since the Supreme Court of Canada's decision in *Progressive Homes v. Lombard General Insurance Co. of Canada* (2010) [*Progressive Homes*], and appears to have substantially broadened the scope of CGL coverage in terms of loss of use of the insured's product.

Bulldog Bag Ltd. (**Bulldog**) was a manufacturer of plastic and paper packaging in British Columbia. In late 2007, an order was placed by Sure-Gro Inc. (**Sure-Gro**) for a significant volume of printed plastic bags that Sure-Gro was going to use to package soil and manure for sale to Canadian Tire. For the 2008 season, Bulldog supplied Sure-Gro with over 1.1 million printed bags. Sure-Gro began to fill the bags, but quickly discovered that the ink from the bags came off the packaging, not only rendering the bags unreadable but also mixing with the soil and manure, making that product potentially unusable as well.

Bulldog manufactured new bags for Sure-Gro and Sure-Gro used the replacement bags in time to meet its contractual commitments to Canadian Tire. Sure-Gro then claimed against Bulldog for \$784,221.34 for losses arising from removing the materials from the defective packaging, disposing of the defective packaging, and the loss of about 10% of the raw material in the salvage process. Bulldog settled the action with Sure-Gro and then sought indemnity from its insurer, AXA Pacific Insurance Company (**AXA**).

Bulldog's CGL policy was relatively standard. It provided that Bulldog had coverage for "property damage" due to an accident or occurrence and defined "property damage" as "physical injury to or physical destruction of tangible property, including loss of use thereof, or loss of use of tangible property that has not been physically injured or destroyed". The trial judge ruled that the policy covered only the value of the lost contents, specifically the 10% of soil and manure not salvaged by Sure-Gro, which amounted to approximately \$12,000. Bulldog appealed that decision.

In between the trial decision and the appeal being heard, the Supreme Court of Canada issued its reasons in *Progressive Homes*, which stated that there was nothing in the terms "property damage" or "occurrence" in CGL policies that restricted their application to third party property, rather than property supplied and/or constructed by the insured. As a result of that decision, it is clear that "property damage" may include damage to any tangible property, including the insured's own product.

As a result of the decision in *Progressive Homes*, AXA conceded that Bulldog's claim constituted "property damage" because Bulldog's faulty bags were "injured" and Sure-Gro lost the use of them. As well, AXA conceded that the faulty workmanship that led to the defective bags was an "accident" or "occurrence" within the meaning of the policy and resulted in property damage to 10% of Sure-Gro's product.

Despite these concessions, AXA argued that the policy's work and product exclusion applied to exclude Bulldog's claim. That exclusion stated that the insurance did not apply to claims for property damage to "goods or products manufactured or sold" by Bulldog. AXA argued that the losses suffered by Sure-Gro occurred solely as a result of Sure-Gro's loss of use of the damaged bags and that the exclusion of Bulldog's claims was consistent with the general purpose of liability coverage and the own product exclusion.

The Court of Appeal rejected this argument, finding that while the clause operated to exclude claims for damage to Bulldog's bags, it could not be extended to compensation for Sure-Gro's costs in separating those bags from its product, repackaging it in different bags and salvaging the old product some months later. The Court found that the exclusion clause did not exclude coverage for "claims that flow from" the plaintiff's defective work or product and excluded only coverage for property damage to goods supplied by Bulldog, i.e., the bags themselves. The Court noted that this was consistent with the agreement of the insurer to cover damages "because of property

damage" and that to hold otherwise would be a "perversion" of the decision in *Progressive Homes*.

AXA also argued that the "work performed" exclusion in the policy, which stated that there was no cover for claims arising from the loss of use of tangible property that was not physically injured or destroyed resulting from the failure of Bulldog's products or work performed, operated to deny Bulldog's claim. However, the Court of Appeal rejected this argument, finding that it was clear that the 10% of the product that had remained stuck to the defective bags was physically injured or destroyed, at least in the sense that it had ceased to be useable for its intended purpose, such that the requirements of the exclusion were not satisfied.

The decision of the Court of Appeal with regard to the work and product exclusion appears to broaden the coverage for damages flowing from defective products supplied by insureds. In the event that the damaged or defective product results in costs related to replacing and repairing the product, and any resulting damage to other property, it appears likely that the work and product exclusion will not operate to bar coverage and the insurer will be required to indemnify the insured for these amounts.

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ONTARIO COURT OF APPEAL REINVIGORATES ABSOLUTE POLLUTION EXCLUSION

On April 26, 2011, the Ontario Court of Appeal rendered its decision in *ING Insurance Company of Canada vs. Miracle*, overturning the lower court and adopting a contextual approach to its interpretation of the application of the absolute pollution exclusion.

In *Miracle*, ING appealed the application judge's decision finding that its Commercial General Liability (CGL) policy was liable to respond to a claim for damages from the migration of gasoline from a retail fuel service station, as reported in our Spring, 2011 newsletter. The neighbouring property owner had brought a claim for \$1.85 million against the insured, the party that installed the fuel facilities and the fuel supplier. In the Statement of Claim, the plaintiffs alleged that the escape of petroleum hydrocarbons in and onto its land required it to incur expenses in investigating, testing, monitoring and rectifying the contamination. The claims were brought in strict liability, nuisance and negligence.

The application judge interpreted the Court of Appeal's earlier decision in *Zurich v. 686234 Ontario Limited* (2002) as standing for the principle that the absolute pollution exclusion did not apply to cases where negligence was pleaded and the insured was not in the business of active industrial pollution. The application judge further held that a reasonable insured would expect the exclusion to apply to industrial pollution and not to a gas leak from a retail service station.

The *Zurich* decision pertained to a leak of carbon monoxide from a malfunctioning furnace in a residential apartment building. Although the Court of Appeal in that case had cautioned against an

overly literal approach to coverage, its comments that the absolute pollution exclusion applied only to active industrial polluters had been applied literally by counsel and courts.

The Court of Appeal in *Miracle* clarified that the *Zurich* decision had to be read in its context. In *Miracle*, the insured was engaged in an activity that carried an obvious and well-known risk of pollution and environmental damage. Regardless of the allegations of negligence, the damages claimed were based on harm to the natural environment due to contamination of soil. The court explained that the claim fit entirely within the historical purpose of the pollution exclusion which was to preclude coverage for the cost of government mandated environmental clean up.

Significantly, the court did not accept that "active industrial polluter of the natural environment" should be read to apply only to activities that necessarily result in pollution as those insureds would already be excluded from coverage because of the fortuity principle. The court reasoned that such an interpretation, if correct, would render the absolute pollution exclusion without meaning.

The court further rejected the distinction between active versus passive polluters of the environment. It was noted that a majority of courts in the U.S.

have held that claims against gas stations for damages caused by leaking gasoline are unambiguously excluded by the standard “absolute pollution exclusion.”

Finally, the court rejected the argument that applying the exclusion would effectively nullify coverage since there were a variety of risks that would still be covered by the CGL policy.

While the court’s decision requires a fact based approach to the activity in question, it provides

direction for a more sensible approach to application of the absolute pollution exclusion.

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DO THE NEW ONTARIO CIVIL PROCEDURE RULES CONCERNING EXPERTS GOVERN ACCIDENT BENEFIT ASSESORS?

The proper application of the new *Rules of Civil Procedure* (the **Rules**) on expert evidence is a matter of some controversy at the moment, reflected by the recent conflict between the decisions in *Beasley v. Barrand* (2010) and *McNeil v. Filthaut* (2011), which leaves undecided the question of whether accident benefit assessors are subject to the new Rules.

In *McNeil v. Filthaut*, the trial judge considered the question of whether the new requirements outlined in Rules 4.1.01 and 53.03 relating to expert witnesses apply to individuals retained by non-parties to the litigation, namely, the accident benefit assessors of the plaintiff. The defendant was seeking to call as expert witnesses a number of the professionals retained by the plaintiff’s accident benefits insurer to give both factual and opinion evidence at trial.

The action arose out of a motor vehicle accident on June 23, 2001. The plaintiff claimed to be permanently disabled and unable to work because of the injuries she suffered in the accident. Following the accident, the plaintiff applied for and received statutory accident benefits from her insurer for medical and rehabilitation expenses and income replacement. To establish entitlement, the accident benefits insurer retained various medical experts to assess the

plaintiff. These experts provided reports to the insurer, which included factual findings as well as opinions, such as whether the plaintiff was able to return to work. It was agreed by both the plaintiff and the defendant that the information in these reports was highly relevant to the issues.

The plaintiff, however, objected to the accident benefit assessors giving expert opinion evidence at trial, as their reports did not strictly comply with the requirements of Rule 53.03. The defendants argued that the requirements of Rule 53.03 only apply to experts engaged by parties to the litigation, and do not apply to experts engaged by non-parties. The plaintiffs asserted that Rule 53.03 applies to all experts, regardless of whether they have been engaged by non-parties to the litigation.

The trial judge decided that the requirements outlined in Rules 4.1.01 and 53.03, as they relate to expert witnesses, do not apply to individuals retained by non-parties to the litigation such as accident benefit medical experts. In her view, the key factor triggering application of the expert rules is found in the clear language of the Rules, namely, when an expert is “engaged by or on behalf of a party to the litigation”. Thus, the Rules were not intended to apply to experts retained by or on behalf of non-parties to litigation.

The conclusion in *McNeil v. Filthaut* that Rule 53.03 applies only to litigation experts contradicts the earlier decision in *Beasley v. Barrand*. In the view of the trial judge in that case, it did not make sense to apply a higher standard to consulting medical experts hired by parties to the litigation and a lower standard to consulting medical experts hired by a non-party but whose opinions might assist.

Addressing this conflict, the trial judge in *McNeil v. Filthaut* stated that she could not concur with the *Beasley v. Barrand* approach. Based on both her reading and interpretation of Rules 4.1.01 and 53.03, their application is limited to

experts “engaged by or on behalf of a party.” She highlighted that the ultimate purpose of the new Rules is to limit and control the proliferation of experts retained by litigants by imposing on

those experts a duty of fairness, objectivity, and non-partisanship to the court, which prevails over any other obligations owed by the expert to a party. The introduction of the new Rules is an effort to eliminate the use of “hired guns” or “opinions for sale” in civil litigation, the use of which has resulted in potentially biased expert evidence being given at trial. In her view, the Rules were not drafted or intended to catch experts not hired by parties.

Unfortunately, the *Beasley v. Barrand* approach has caused a significant proliferation in litigation where parties have scrambled for direction as to whether the expert intended to be called is a treating expert or litigation expert, guidance on the difficult task of straining opinions out of treating expert’s anticipated evidence leaving only facts, and whether the proposed expert ought to be granted relief from non-compliance with the strict requirements of Rule 53.03 and allowed to give opinion evidence nonetheless. As long as the law is in flux and parties and their counsel need to be concerned about the *Beasley v. Barrand* approach, this will continue.

The interpretation of Rules 4.1.01 and 53.03 is important and will affect every party, counsel, and trier of fact involved in litigation where expert evidence is a critical part. Hopefully, resolution of the issue will be soon in coming from the Court of Appeal.

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FAMILY MEMBERS OF APPARENT VICTIMS OF CRIME CANNOT SUE CRIMINAL INVESTIGATORS IN NEGLIGENCE

On April 8, 2011, the Ontario Court of Appeal released its decision in *Wellington v. Ontario*. The Court dismissed a negligent investigation claim brought by the estate and family members of a man shot by police against the Special Investigations Unit (SIU), an independent civilian agency responsible for investigating incidents of serious injury or death that may have resulted from criminal offences committed by police. The Court unanimously held that the SIU investigators did not owe the victim and family a private law duty of care in conducting their investigation.

The Courts below had allowed the claim to proceed on the basis that the law was unsettled and should be developed with the benefit of a full evidentiary record. The Ontario Association of Chiefs of Police (OACP) intervened in support of the SIU to argue that criminal investigators should not be held to owe a private duty of care to the apparent victims of the crimes they are investigating. In part, the OACP argued that, although perhaps well-intentioned, the recognition of such a duty of care risked privatizing the public function of criminal investigation.

In dismissing the claim, the Court of Appeal held that while criminal investigators may owe a duty of care to suspects they are investigating (*Hill v. Hamilton*) or to warn a narrow and distinct group of potential victims of a specific threat (*Jane Doe*), they do not owe a duty of care to victims of crime and their families in relation to the investigation of the alleged crimes. The Court held that when the SIU investigates

allegations of criminal misconduct its duties are “overwhelmingly public in nature.” In this regard, the Court opined that “(w)hile victims of crime and their families understandably may feel that they have a specific and particular interest, in the end, their interest in knowing and understanding the circumstances of an alleged crime ... is shared with all members of the public.”

More generally, the Court noted that there is a well-established line of cases that stand “for the general proposition that public authorities, charged with making decisions in the general public interest, ought to be free to make those decisions without being subjected to a private law duty of care to specific members of the general public.” The Court held that criminal investigations are “not aimed at or geared to the protection of the private interests of specific individuals and do not give rise to a private law duty sufficient to ground an action in negligence.”

The Court accepted the argument of the OACP that there is “an inherent tension between the public interest in an impartial and competent investigation and a private individual’s interest in a desired outcome of that same investigation...” Imposing a private law duty of care would be “seriously at odds with the fundamental role of (criminal investigators) to investigate allegations of criminal misconduct in the public interest.”

The Court followed its 2001 decision in *Norris v. Gatien* in which the Court had previously addressed whether police investigators owed a private law duty of care to victims of crime. The plaintiffs and their supporting intervener, Aboriginal Legal Services of Toronto, had argued that the Supreme Court of Canada decisions in *Odahvji v. Woodhouse* (2003) and *Hill v. Hamilton* (2007) had effectively overruled the Court of Appeal’s earlier decision. The Court disagreed and, in doing so, limited the application of the *Odahvji* and *Hill* decisions.

Finally, and in contrast to the majority decision of the Divisional Court, the Court of Appeal disagreed that the refusal to recognize a private law duty of care in relation to police investigations left the families of victims without appropriate and viable legal recourse. The Court noted that victims of crime may apply for compensation under the *Compensation for Victims of Crime Act*, may obtain standing in Coroner’s inquests, may sue the perpetrators of the crime and have a voice in sentencing through victim impact statements.

The Court of Appeal’s decision is significant as it places a clear limit on the scope of police liability

for negligent investigation. Had the Court recognized a private duty of care in favour of victims of an alleged crime and their families, the potential exposure of investigators and police forces to lawsuits would have been significantly expanded. As the decision highlights the distinction between public and private duties, it may have a more general impact on claims in negligence raised against public authorities performing public functions.

The Wellington family, supported by the intervener, Aboriginal Legal Services of Toronto, has sought leave to appeal to the Supreme Court of Canada and we will keep you abreast of further developments in that regard in future editions.

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***SALE OF GOODS ACT* DEFENDANTS HAVE SOME EXPLAINING TO DO: DEFECT INFERRED, EVEN IN THE FACE OF SPOILIATION**

Some recent decisions from the Ontario courts in *Muskoka Fuels v. Hassan Steel Fabricators Limited* serve as reminders that liability can be found under the *Sale of Goods Act* even without the cause of the defect in the subject product being proven, and even though the plaintiff had lost the defective product before the defendant had an opportunity to inspect it.

The case involved a leaking 500 gallon fuel tank and liability for the resulting environmental cleanup costs. The tank was manufactured by the defendant who sold it to the plaintiff. The tank had an expected service life of at least 10 years. Less than five months after the tank was put into service, diesel fuel leaked out of it through a 3/16" diameter hole in the bottom of the tank caused by internal corrosion.

SPOLIATION

The defendant brought a motion at the opening of trial to strike the Statement of Claim or, alternatively, to preclude the plaintiff's expert from testifying and to preclude the filing of the expert's report, on the grounds that the plaintiff spoliated evidence.

The leak was discovered in January, 2002. In September, 2002 defendant's counsel advised that he was in the process of retaining an engineer to

inspect the tank. By June, 2005 the defendant still had not retained an engineer but was invited to attend an inspection of the tank where samples of steel would be removed for analysis.

The defendant's representatives were unable to attend that inspection. In July, 2008 the defendant served an expert's report, which was prepared without an inspection of the tank or the steel samples taken therefrom. The action was set down for trial and was scheduled to be heard in October, 2008. The defendant obtained an adjournment in order to consider new information that had recently arisen concerning the possible cause of the tank failure, and to obtain further expert reports. The defendant attempted to arrange an inspection of the tank and steel samples, but was told that the plaintiff's expert had not kept the tank and was unable to locate the steel samples taken from it.

The trial judge referred to the leading cases in *McDougall v. Black & Decker*, *Cheung v. Toyota*,

and *St. Louis v. R.* and found that he ought not to strike the plaintiff's claim "unless spoliation had been proven [it is the defendant's onus], in that it is beyond doubt that this was a **deliberate act done with the clear intention of gaining an advantage in the litigation, and the prejudice is so obviously profound that it prevents the defendant from mounting a defence.**"

The plaintiff's expert offered no explanation as to how or why the evidence came to be lost, but the trial judge would not accept the defendant's suggestion that an inference of deliberate destruction ought to be made from the lack of explanation. It is interesting that the spoliator therefore benefited from remaining silent and not explaining the loss of evidence.

The trial judge also held that the defendant had failed to establish profound prejudice. The defendant apparently did not do a good enough job of explaining why an inspection was necessary, especially since it had already delivered an expert report without having an inspection. The trial judge held that a further evidentiary record was required. She dismissed the motion without prejudice to the defendant's right to bring it back on as a mid-trial motion, or to seek rulings relating to remedies for the loss of the items at the conclusion of the trial, after a complete evidentiary record had been established. The trial decision notes that the defendant did not renew its motion at anytime during, or at the conclusion of, the trial. The trial judge further found that the defendant had not been prejudiced by the loss of the evidence because:

- (a) the plaintiff was unable to prove during the course of the trial that there

was any fault in the steel used in the tank; and

- (b) the defendant's own expert was able to opine, without analyzing the composition of the steel used in the tank, that the hole was caused by internal corrosion, which the trial judge accepted.

It seems the defendant was unable to establish that an inspection of the tank was necessary in order for it to defend itself, which will distinguish this case from others where the prejudice resulting from spoliation is much more severe.

SALE OF GOODS ACT LIABILITY AND INFERENCES OF DEFECT

The case also highlights the common quandary concerning how to properly characterize the "defect" that must be proven to establish liability: is the "defect" the manner in which the product failed (i.e., the hole in the tank) or the cause of that failure (i.e., the lack of internal corrosion protection)? The trial judge did not accept that the defect in the tank was the hole itself because there was no evidence that the hole existed at the time of purchase. Instead, the trial judge found that the defect was the absence of a protective interior coating. The Court of Appeal disagreed and implicitly held that the "defect" was the appearance of the hole within the 10-year service life of the product. It was noted that the expert witnesses were unable to identify what caused the internal corrosion that led to the tank's failure. However, relying on the Supreme Court of Canada judgment in *Schreiber Brothers Ltd. v. Currie Products Ltd.* (1980), the Court of Appeal held:

- “while the buyer bears the onus of proving the existence of a defect on a balance of probabilities, the **actual cause of the defect need not be proven.**”
- Once the buyer proved that the defect ... was not attributable to anything that he did or failed to do, **an inference could be drawn** from the evidence as a whole **that the defect existed** at the time the product was delivered to him.”
(NB: *Schreiber Brothers* could also be read as requiring the plaintiff to go further and show that there was no alteration of the product after it left the defendant’s hands, or that there were no alternative causes for the damage other than the alleged defect in the product, before a defect will be inferred.)

The trial judge had found that the tank was only used as intended, that it had not been used prior to being placed into service by the plaintiff, that it was properly installed, that it was not damaged during or after installation by some external mechanism, and that it did not fail due to improper maintenance. Those findings, combined with the facts that the tank was bought by description and that an examination of it at the time of its

purchase would not have revealed the then unknown defect, allowed the Court of Appeal to find that the defendant had breached the implied condition of merchantability in s. 15(2) of the *Sale of Goods Act*, making it 100% liable for the cleanup costs.

A defendant facing liability under the *Sale of Goods Act* better be able to explain a cogent theory as to how the alleged damages were caused, other than by a defect that existed in the subject product at the time of delivery, in order to avoid liability. Such a defendant would be well advised to obtain an inspection of the product as soon as possible after notification of the claim. Otherwise, the information necessary to build that theory might be forever lost, and the defendant should not expect Canadian courts to help them out of that predicament.

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