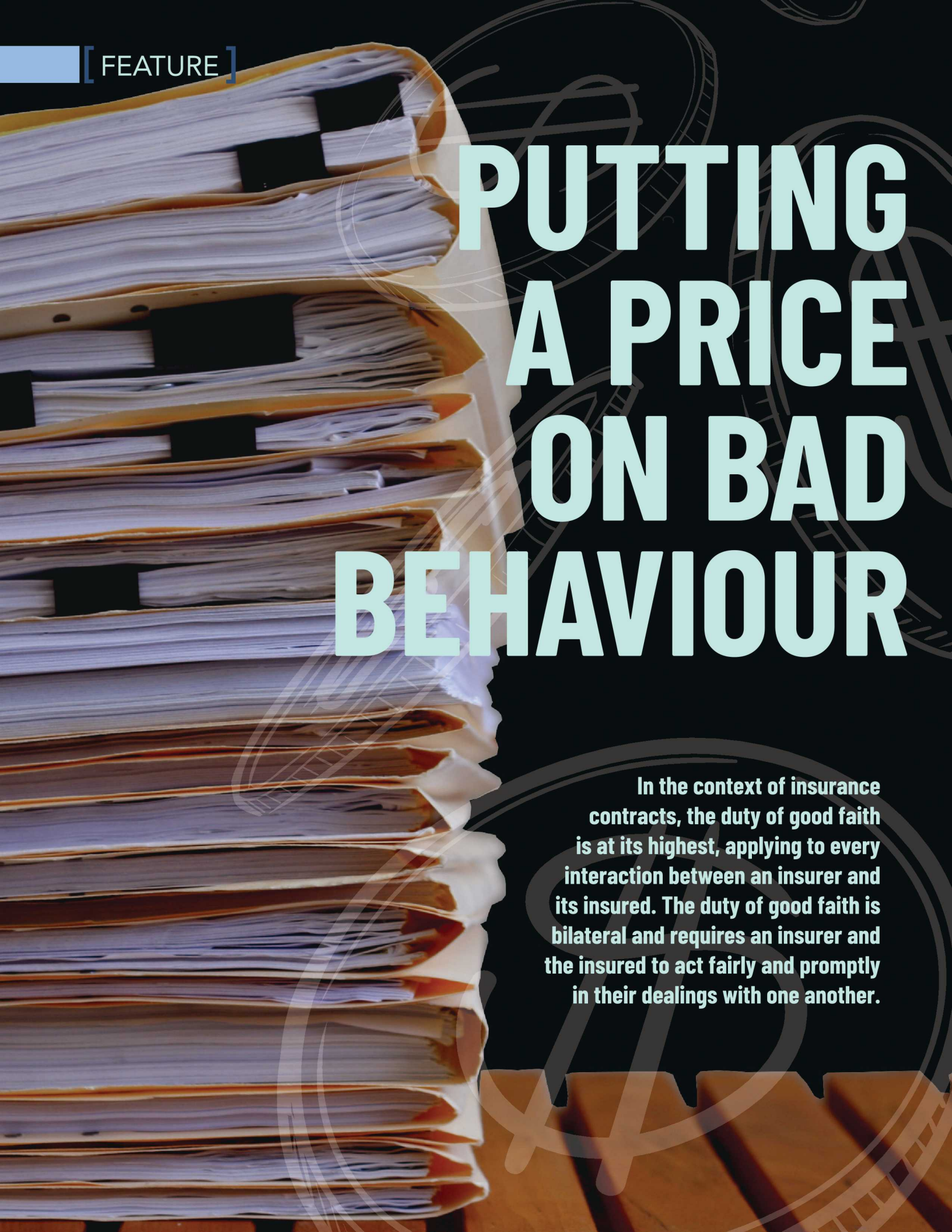

PUTTING A PRICE ON BAD BEHAVIOUR

In the context of insurance contracts, the duty of good faith is at its highest, applying to every interaction between an insurer and its insured. The duty of good faith is bilateral and requires an insurer and the insured to act fairly and promptly in their dealings with one another.

BY STEPHEN BIRMAN AND ANNA KIRALY

Lessons From Recent Case Law on Bad Faith, Punitive Damages, and Jury Trials in Canada

Introduction: The Good, The Bad, and the Punitive

What happens when someone's behaviour requires punishment to ensure it is not repeated but not so bad it constitutes a crime? Civil courts are often tasked with answering this question as not all undesirable conduct amounts to a level worthy of the *Criminal Code*. Often, such behaviour, seen as detrimental to society, will be punished using "punitive damages." Punitive damages can arise from various situations such as intentional torts like sexual assault and battery, negligent conduct, or decisions made in "bad faith".[1] For the purposes of this article, bad faith as it arises in insurance contracts will be our focus as it represents one of the most frequent triggers for a punitive damages award in Canada.

In the context of insurance contracts, the duty of good faith is central to how the contractual relationship is formed, carried out and terminated. A breach of good faith can occur when an insurer acts unfairly in the way it investigates and assesses a claim and/or makes its decision whether to pay a claim. In assessing a claim, an insurer must always act in a balanced and reasonable manner and a failure to do so will amount to bad faith. It is important to note that a denial of an insurance claim is not in and of itself bad faith. Rather, bad faith requires something more – such as a delay in payment to take advantage of an insured's economic vulnerability, or a refusal to make payment based on an unreasonable interpretation of the insurer's obligations under an insurance contract.

This article will trace the connection between bad faith and punitive damages awards in Canada. Ultimately, we will consider "best practices" on how to approach a bad faith claim against an insurance company and what circumstances may result in a punitive damages award.

Good Faith

In Canadian common law, the Supreme Court of Canada (the "SCC") has recognized that in contract law there is an "organizing principle" of good faith that requires parties to a contract to perform their contractual duties honestly and reasonably, not capriciously or arbitrarily.[2] This understanding led to the emergence of a duty of honest performance of one's contractual rights and obligations.[3] Canadian courts will therefore consider whether a party to a contract has exercised their contractual power in good faith throughout the life of the contract, including whether they acted honestly, when making bad faith determinations.[4] Notably, what constitutes "appropriate regard" of the other contracting parties' interest will vary depending on the type of contract and the relationship in question.[5]

In the context of insurance contracts, the duty of good faith is at its highest, applying to every interaction between an insurer and its insured. The duty of good faith is bilateral and requires an insurer and the insured to act fairly and promptly in their dealings with one another. The duty of good faith continues throughout the contractual relationship and endures even through litigation.[6] The Ontario Court of Appeal ("ONCA") decision in *702535 Ontario Inc. v. Non-Marine Underwriters Members of Lloyd's London* remains the leading case on good faith in insurance contracts and described the source of the duty as follows:

> "In addition to the express provisions in the policy and the statutorily mandated conditions, there is an implied obligation in every insurance contract that the insurer will deal with claims from its insured in good faith."[7]

An assessment of whether a breach of the duty of good faith has occurred is highly contextual and will depend on the facts of the case at hand. In the 2019 case, *Sky Solar (Canada) v. Economical Insurance ("Sky Solar")*, the Court described the assessment of bad faith as follows, citing *Non-Marine Underwriters:*

> "The duty of good faith requires an insurer to act with reasonable promptness at each stage of the claims process, and that the duty applies both to the manner in which the insurer investigates and assesses the claim and to the decision whether or not to pay the claim. What constitutes bad faith will depend on the circumstances in each case and a court in considering whether the duty has been breached will look at the conduct of the insurer throughout the claims process to determine whether in light of the circumstances, as they then existed, the insurer acted fairly and promptly in responding to the claim…"[8]

Assessing an insurer's bad faith requires understanding the insurer's behaviour and choices as well as their impact on the insured. The insured tends to be vulnerable as the insurer typically controls the terms of the insurance contract and holds power to determine whether and when the insured will receive necessary funds. As such, bad faith claims require information regarding the insurer's decision-making process that the insurer uniquely possesses.

To establish bad faith in the insurance context, the insured must gain access to the insurer's internal communications, files, and records to assess how claims decisions were made, what information was considered (or was omitted from the claims handling), and whether bad faith occurred.[9] To be successful, one must be able to point to moments in time where decisions were made, or actions were taken that constitute a breach of good faith. An insured needs to be able to peer behind the curtain and examine the insurer's conduct for themselves. As such, obtaining production of an insurer's files will almost always be required at the discovery stage to allow the Court to eventually assess the merits of a bad faith claim at trial.

We observed the importance of obtaining the insurer's files as trial counsel in *Baker v. Blue Cross Life Insurance Company of Canada ("Blue Cross").* Our client, Sara Baker was denied long-term disability benefits by her insurer, Blue Cross, on three occasions. At trial before a jury in 2022, Ms. Baker was awarded full payment of her retroactive benefits, damages for mental distress, and the jury found that Blue Cross acted in bad faith by denying Ms. Baker's claims and ordered that Blue Cross pay $1.5 million dollars in punitive damages. The bad faith finding and punitive damages awards were upheld on appeal.

In *Baker,* a finding of bad faith was made because of Blue Cross' systematic misconduct in handling the claim, which was established through the actions taken by Blue Cross and documented in its file. Rather than assess Ms. Baker's claims fairly, the evidence showed that in Ms. Baker's case, Blue Cross would (1) deny benefits first and ask for documentation later, (2) relied on medical opinions it ought to have known were incorrect, (3) selectively relied on evidence to support its position to deny coverage

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while ignoring evidence that supported the Plaintiff's claims, (4) distorted the conclusions of its own medical assessors, and more.[10] The decision to deny Ms. Baker's claims was not simply a matter of Blue Cross reaching the wrong conclusion in good faith. The ONCA noted that to find that Blue Cross acted in good faith in this case, the jury would have "had to ignore the coincidence that every time Blue Cross erred in handling the [Ms. Baker's] file, it was to her detriment and to the benefit of Blue Cross."[11] In assessing the totality of Blue Cross' misconduct, the Court described that it "at best, shows reckless indifference to its duty to consider [Ms. Baker's] claim in good faith and conduct a good faith investigation, and at worst, demonstrates a deliberate strategy to wrongfully deny her benefits".[12]

As observed in *Baker,* in determining whether bad faith occurred, courts will consider how the insurer made its decisions in relation to the claim – was there a basis for the claim the insurer ignored? Did the insurer systematically ignore key information to reach their desired conclusion? The courts will also consider the parties involved and whether the vulnerable insured was taken advantage of.[13] The insurer's corporate records are required to make these determinations. For a further discussion on the productions that the Plaintiff should seek to establish a bad faith claim (which is beyond the scope of this article) see the recent decision of Justice W.D. Black in *Nordik Windows et al v. Aviva Insurance Company of Canada,*[14] where the Plaintiffs successfully obtained all internal records in relation to an insurer's coverage decision in a class proceeding.

Punitive Damages: Quantum and Context

Punitive damages allow civil courts to address the objectives of "retribution, deterrence, and denunciation" in situations where someone's conduct is so reprehensible that it cannot be allowed to happen again.[15] These damages are society's way, through our justice system, of penalizing bad behaviour that is not otherwise caught by the criminal justice system. In *Whiten v. Pilot Insurance Co.,* the SCC determined that punitive damages will be awarded only in exceptional cases where there is "high-handed, malicious, arbitrary, or highly reprehensible misconduct that departs to a marked degree from ordinary standards of decent behaviour."[16]

In *Whiten,* a family's home was destroyed in a devastating fire. The insurance company accused the family of arson and forced them through a long trial to establish their claims. The jury found that the insurer had acted in bad faith and punitive damages were awarded. *Whiten* established criteria for assessing an appropriate quantum of punitive damages. Among other considerations, a punitive damages award must be proportionate to the harm caused, the degree of the misconduct, the relative vulnerability of the plaintiff and any advantage or profit gained by the defendant, while also considering any other fines or penalties the defendant is subject to.[17] The award cannot be more than necessary to accomplish the objectives of deterrence, denunciation and retribution.

The more reprehensible the conduct, the higher the "rational limits" are for the potential award.[18] There is no "ceiling" on a punitive damages award in Canada. Typically (and at least until *Baker*), Canadian Courts have made relatively conservative punitive damages awards. For example, in *Plester v. Wawanesa Mutual Insurance Co.*[19] the jury found that Wawanesa's unfounded arson accusations resulted in non-payment of insurance funds and awarded $350,000.00 in punitive damages. The ONCA affirmed this decision. In *Truong v Jeweler's Mutual Insurance Company,* the Plaintiffs sued their insurer for the value of stolen jewelry, but the insurer refused to pay due to an alleged (but unreasonable and unfounded) lack of evidence provided by the Plaintiffs.[20] In *Truong,* the judge awarded $45,000.00 in punitive damages which was upheld on appeal. In *Khazzaka o/a E.S.M. Auto Body v. Commercial Union Assurance Company of Canada,* the ONCA affirmed a jury award of $200,000.00 in punitive damages after an independent

adjuster hired by Commercial Union acted in bad faith by making unfounded arson accusations.[21] In *Brandiferri v. Wawanesa Mutual Insurance, et al.,* Wawanesa accused the Plaintiff of fraudulently claiming losses after a fire destroyed their garage and its contents. The judge found that the fraud allegations only surfaced after the litigation had started, found that Wawanesa was a "repeat offender" of bad faith claims handling and awarded $100,000.00 in punitive damages.[22] Even in the pre-*Baker* long-term disability context, a trial Judge's decision that an insurer had acted in bad faith and taken an adversarial approach to an insured's claim resulted in a punitive damages award of $200,000, upheld by the ONCA.[23] While these are but a few examples, there was a noticeable and unexplained gap in 7 figure punitive damages awards following *Whiten* and before *Baker.*

The *Baker* decision represents the new high-water mark for punitive damages in Canada. Six years after the lawsuit began, the ONCA upheld a jury award of 1.5 million dollars in punitive damages resulting from Blue Cross' bad faith and misconduct.[24] At the time this article is written, Baker remains the record for punitive damages awarded against an insurance company in Canada.[25] It is hoped that with this precedent, we will continue to see punitive damages awards at or exceeding seven figures when an insurer acts in bad faith.

The few cases involving large awards for punitive damages after a finding of bad faith tend to have one thing in common: a jury. We discuss this feature further below.

Bad Faith, Good Outcome

The presence of a jury appears to be the common theme through the most significant punitive damages awards in Canada to date from *Whiten* to *Baker.* Perhaps, this is because juries are more likely to express outrage and shock at the misconduct of insurance companies than judges who more frequently observe such companies' conduct. This could also be a function of juries (unlike judges) not being aware of prior punitive damages awards. In fact, it is improper for a trial judge to suggest a punitive damages range to a jury.[26] Additionally, once a jury arrives at its decision, its findings are much harder to overturn on appeal that a judge's reasons.

In *Baker,* the ONCA addresses the steep threshold an insurer will have in attempting to overturn a jury award.

While judges provide lengthy written opinions about why they chose to make a certain determination that can be scrutinized, juries don't give reasons, making it more difficult for an appellate court to interfere with their findings. This reality is discussed by Hourigan J.A., in *Baker*:

> "Because juries do not provide reasons, an appellate court generally has a more limited basis to interfere with their verdicts. We are not in a position where we can scrutinize the jury's chain of reasoning. That is why, generally, appellate courts take a deferential approach to reviewing jury verdicts."

When it comes to bad faith claims, the standard of review for a punitive damages award is whether the damages serve a rational purpose. For an appellate court to overturn a punitive damages award, the award, together with any compensatory damages awarded, must be so "inordinately large" that it exceeds what is necessary to punish the defendant.[27]

Jurors represent the conscience of the community and their findings on bad faith and the quantum of punitive damages should be respected where they are rationally supported by the evidence. The potential divide between how judges and juries may assess a fact pattern is described by Justice Binnie in *Whiten*:[28]

> "I would not have awarded $1 million in punitive damages in this case but in my judgment the award is within the rational limits within which a jury must be allowed to operate. The award was not so disproportionate as to exceed the bounds of rationality…"

Conclusions

The broad duty of good faith can capture a variety of issues and conduct in many different circumstances. The way courts evaluate bad faith claims will continue to evolve over time as the duty of good faith represents an evolving concept in Canadian law.

Counsel should be emboldened in pursuing bad faith claims based on the findings and award in *Baker.* From *Whiten* to *Baker,* juries are the common through line in Canada's most significant bad faith claims. Indeed, as litigators, we ought not forget the power of a simple jury notice in both helping our clients achieve desirable outcomes and in occasionally achieving broader societal objectives.

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NOTES

[1] For examples of punitive damages in the context of sexual assault: See *MacLeod v. Marshall,* 2019 ONCA 842 (CanLII), <https://canlii.ca/t/j31bt>; Hockley v. Riley, 2007 ONCA 804 (CanLII), <https://canlii.ca/t/1tvjd>). For an example of punitive damages in the context of negligence: See *McIntyre v. Grigg* (2006), 2006 CanLII 37326 (ON CA).

[2] See *Bhasin v. Hrynew,* 2014 SCC 71 (CanLII), [2014] 3 SCR 494 at para 63 https://canlii.ca/t/gf84s.

[3] See *C.M. Callow Inc. v. Zollinger,* 2020 SCC 45 (CanLII), [2020] 3 SCR 908, <https://canlii.ca/t/jc6vt>

[4] See *Wastech Services Ltd. v. Greater Vancouver Sewerage and Drainage District,* 2021 SCC 7 (CanLII), [2021] 1 SCR 32, <https://canlii.ca/t/jd1d6> at paras 68-69.

[5] *Bhasin* at para 65.

[6] See *Khazzaka v. CGU Insurance Company of Canada,* 2002 CanLII 45018 (ON CA), <https://canlii.ca/t/1cskr> at para 15.

[7] *702535 Ontario Inc. v. Non-Marine Underwriters Members of Lloyd's London,* 2000 CanLII 5684 (ON CA), <https://canlii.ca/t/1cwws> at para 27.

[8] *Sky Solar (Canada) Ltd. v. Economical Mutual Insurance Company,* 2019 ONSC 4165 (CanLII), <https://canlii.ca/t/j1cwc> at para 115..

[9] See *Nordik Windows Inc. et al, v. Aviva Insurance Company of Canada,* 2025 ONSC 633.

[10] *Baker v. Blue Cross Life Insurance Company of Canada,* 2023 ONCA 842 (CanLII), <https://canlii.ca/t/k1wkf>at para 28 [*Baker*].

[11] *Baker* at para 29.

[12] *Baker* at para 30.

[13] *Whiten v. Pilot Insurance Co.,* 2002 SCC 18 (CanLII), [2002] 1 SCR 595, <https://canlii.ca/t/51vn> at para 115 [*Whiten*].

[14] See *supra* note 9.

[15] *Whiten* paras 43 and 94.

[16] *Whiten* paras 43 and 94.

[17] *Whiten* at para 71 and 94.

[18] *Whiten* at paras 112-113.

[19] See *Plester v. Wawanesa Mutual Insurance Company,* 2006 ONCA 17918 (CanLII), https://canlii.ca/t/1ndrx at para 102-103.

[20] See *Truong v Jeweler's Mutual Insurance Company,* 2023 ONSC 4006 (CanLII), <https://canlii.ca/t/jz0xq> at paras 1-9.

[21] See *Khazzaka.*

[22] *Brandiferri v. Wawanesa Mutual Insurance, et al.,* 2012 ONSC 2206 (CanLII), <https://canlii.ca/t/frsvg> at paras 213-214

[23] *Fernandes v. Penncorp Life Insurance Company,* 2014 ONCA 615 (CanLII), https://canlii.ca/t/g8svh

[24] *Baker* at paras 34-37.

[25] See *National Steel Car Limited v. City of Hamilton,* 2024 ONSC 4120 (CanLII), <https://canlii.ca/t/k604x> at para 272 and *Forefront Electric v. Dutchies,* 2024 ONSC 4898 (CanLII), <https://canlii.ca/t/k6mpl> at para 27

[26] *Eynon v. Simplicity Air Ltd.,* 2021 ONCA 409 (CanLII), https://canlii.ca/t/jgc9l,at para 16.

[27] *Rutman v. Rabinowitz,* 2018 ONCA 80, 420 D.L.R. (4th) 310 at para 58.

[28] *Whiten* at para 128.