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SUBROGATED CLAIMS: COMMON MISCONCEPTIONS DISPELLED *GALAN V. FINCH* [2015] O.J. No. 2275 (S.C.J)

When is the doctrine of spoliation applicable? How does a ruling of "undetermined" as to the cause of fire under the NFPA 921 affect a subrogated action? Should a subrogating insurer expect its claim for rebuilding a dwelling to be reduced on account of betterment?

In his recent decision in *Galan v. Finch (Finch's Heating)*,[1] where our firm acted for the subrogating insurer, Justice Koke answered these and other questions, and in doing so, dispensed with a number of widespread misconceptions surrounding subrogated actions. By examining Justice Koke's decision in *Galan*, this article aims to assist both subrogating insurers and defending liability insurers in handling subrogated claims.

1. When does the doctrine of spoliation apply?

The doctrine of spoliation allows the Court to draw an adverse inference against the spoliator. In subrogated cases, this typically involves an allegation against the plaintiff (and thus, the subrogating insurer) that by reason of their conduct some evidence is no longer available for inspection, and that the defendant has suffered injustice as a result.

There are two common misconceptions surrounding this doctrine. The first is that prejudice sufficient to trigger the doctrine can be established simply by showing that the defendant or his expert have not been afforded equal opportunity to inspect physical evidence at the scene. The second is that prejudice, in-and-of-itself, is sufficient for an adverse inference to be drawn.

In *Galan,* Justice Koke clarified what "prejudice" means in the context of the spoliation doctrine, rejecting the argument that the doctrine applied merely because the defendant's expert did not have the opportunity to examine physical evidence at the scene of the fire. (In *Galan,* the site had been demolished before the defendant's expert had been retained). Since there was

[1] *Galan v. Finch (Finch's Heating)*, [2015] O.J. No. 2275 (S.C.J) and [2015] O.J. No. 3313.

other evidence, including photos and diagrams as well as other experts' reports prepared with the benefit of first-hand observation – there was sufficient evidence available to the defendant's expert to conduct his analysis as to the cause of the fire. So although his inability to conduct a first-hand investigation undoubtedly left the defendant's expert at a disadvantage, that disadvantage was insufficient to trigger the doctrine of spoliation.

The ruling in *Galan* confirms that for the doctrine to apply, a party will be required to show more than a lack of equal opportunity to conduct a first-hand site investigation. While every case will turn on its own facts, a finding of prejudice will be unlikely unless there is a complete lack of available evidence to perform an investigation – a scenario which will be exceedingly rare in today's technological age.

More importantly, the court went further to hold that prejudice alone will be insufficient to trigger the doctrine of spoliation: for an adverse interest to be drawn, a party will be required to establish an ***intent to destroy evidence for the purpose of influencing the outcome of litigation***. Relying on the leading Canadian case of *St. Louis v. R.*(1896), 25 S.C.R. 649 and the Alberta Court of Appeal decision in *McDougall v. Black & Decker Canada Inc.* 2008 ABCA 353, Justice Koke emphasized that, as a matter of law, the spoliation doctrine will not apply unless the following three factors are made out:

1. there was an intentional destruction of relevant evidence;
2. the destruction occurred when litigation was existing or pending; and
3. it is reasonable to draw the inference that evidence was destroyed to influence the outcome of litigation.

Justice Koke's ruling emphasises the underlying purpose of the spoliation doctrine – that is, to penalize deliberate, intentional destruction of evidence carried out with the goal of obstructing the proceedings or influencing the outcome of litigation.

The court's decision confirms that the doctrine was never intended to apply to situations where potentially relevant evidence was either inadvertently or negligently destroyed, or otherwise became unavailable to the defendant. From a practical standpoint, this means that where destructive testing has been carried out or a site has been demolished for the purpose of repairs without all stakeholders having been present or put on notice, this – without more – will not support a finding of spoliation and the associated negative inference. Indeed, anything less than the intentional destruction of evidence for the purpose of influencing litigation will be insufficient.

2. What is required to prove the cause of the fire?

Under the NFPA 921, unless the investigator can eliminate every possible source of ignition in the area of origin, the cause of the fire must be ruled "undetermined". However, as clarified by Justice Koke, a fire investigator's ruling that the cause of fire is "undetermined" under the NFPA 921 neither ends the analysis, nor automatically precludes the insurer from establishing causation and succeeding in a subrogated action.

This is because the test for causation at law is *not* whether the cause of fire can be determined under the NFPA 921. Nor does the legal test for causation require the insurer to establish cause with absolute certainty. Notwithstanding the NFPA 921, at law, there could be more than one possible cause of the fire, but if one of those possibilities is more probable than the other – causation is established. Accordingly, to succeed in an action, the subrogating insurer must only establish that, on the balance of probabilities, the fire was caused by the negligence of the defendant.

As was the case in *Galan,* it is not uncommon for defendants in fire cases to retain experts to try and raise a number of other potential "possibilities" for the cause of the fire, which then, according to the NFPA 921, leads to the cause being labelled "undetermined". Justice Koke's decision is an important reminder that it is insufficient for a defendant to merely raise other "possible" causes (whether in the same or a different area of origin) and rely on NFPA 921 to argue that the cause of the fire cannot be determined.

In addition, while a fulsome discussion regarding expert witnesses is beyond the scope of this article, the *Galan* decision serves as a reminder to subrogating insurers of the importance of properly instructing fire investigators in preparing their reports. In this way, the ruling in *Galan* is consistent with the recent findings of the Ontario Court of Appeal in *Moore v. Getahun* that "expert witnesses need the assistance of lawyers in framing their reports in a way that is...responsive to the pertinent legal issues in a case".[2] In *Moore*, the court underscored the importance of communicating with experts for the purpose of explaining their role in the litigation process, as follows:

> Consultation and collaboration between counsel and expert witnesses is essential to ensure that the expert witness understands [his/her] duties ... ***Counsel need to ensure that the expert witness understands matters such as the***

[2] *Moore v. Getahun et. al.* (2015), 124 O.R. (3d) 321 at para. 62 (C.A.).

> ***difference between the legal burden of proof and scientific certainty*** ... .
>
> ***Counsel play a crucial mediating role by explaining the legal issues to the expert witness and then by presenting complex expert evidence to the court. It is difficult to see how counsel could perform this role without engaging in communication with the expert as the report is being prepared***.[3]

Although the above statements refer to dialogue between expert witnesses and counsel, they apply with equal force to communications between the experts and adjusters and/or examiners that typically take place when experts in fire investigations are initially retained by the insurer, often long before counsel is retained or an action is commenced. Thus, it is crucial that any expert retained by the insurer is provided with clear instructions, from the outset, regarding the legal issues in the case, and the distinction between determining cause pursuant to the NFPA and the burden of proof for establishing causation at law. The appropriate question to be asked in that context is whether, irrespective of the NFPA 921, the expert being retained is able to form an opinion as to the ***cause of the fire on the balance of probabilities***.

3. Is there a deduction to the claim for cost of rebuilding the premises?

Justice Koke also rejected the long-standing misconception that a subrogating insurer's claim for the cost of rebuilding a premises following a fire must be reduced on account of depreciation and betterment caused by replacing the old with the new. His ruling is the first decision of an Ontario Court to apply *Nan v. Black Pine Mfg*. [1991] B.C.J. No 910 (C.A.) where, after an exhaustive review of the law, the B.C. Court of Appeal held that where a building is destroyed through the negligence of a third party, the claim for the cost of rebuilding is ***not*** to be reduced on account of betterment.

In *Galan,* Justice Koke recognized that the new house was an improvement over the destroyed dwelling, but nonetheless held that the subrogating insurer was entitled to the full cost of rebuilding. To hold otherwise would, in theory, require the plaintiff to go into the marketplace and borrow money to rebuild a house which has been destroyed through no fault of his own.

This reasoning raises the question as to whether the principle would apply if, unlike the fact-specific scenarios in *Galan* and *Nan* where the defendant was 100% responsible, the plaintiff was found to have been partially at

[3] *Moore, supra* at paras. 63-64.

fault. In our view, the answer to that question is “yes”. Even if the plaintiff in a subrogated action was partially at fault, any deduction in the subrogating insurer’s recovery would be determined through a discount on account of the plaintiff’s contributory negligence, and not a discount for betterment. The principle that the cost of rebuilding should not be reduced to account for betterment would still apply, even if some contributory negligence on the part of the plaintiff is established.

4. Lessons Learned

By dispelling a number of commonly held misconceptions, Justice Koke’s ruling in *Galan* provides subrogating insurers and liability insurers with the clarity needed to successfully advance and defend subrogated claims. The key principles elucidated by the *Galan* decision include the following:

1. Prejudice alone does not trigger the doctrine of spoliation. Deliberate intent to destroy evidence to influence the outcome of existing or pending litigation is required for the doctrine to apply.
2. In any event, to establish prejudice, for this purpose, it will be insufficient for the defendant to simply show that his expert did not have equal opportunity to examine physical evidence at the site. If other evidence (such as photographs or diagrams) is available, prejudice will not be made out.
3. A finding that a cause of fire is “undetermined” under the NFPA 921 is in no way determinative of the outcome in a court action. To succeed in its subrogated claim, the insurer need not eliminate every possible source of ignition in the area of origin. Rather, the insurer must meet the ***legal test*** for causation – that is, that a fire was caused by the negligence of the defendant ***on a balance of probabilities***.
4. A subrogating insurer’s claim for the cost of rebuilding a premise following a fire will not be reduced on account of betterment.
5. While future cases will examine this issue further, it is our view that this principle applies irrespective of any contributory negligence on the part of the successful plaintiff.

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