

[...] [T]he operator of a convenience store and gas bar faces the risk of a wide range of liability claims for bodily injury and damage to property that the CGL will cover. By denying coverage for pollution liability, the court does not deprive the policy of a very significant measure of protection for the myriad other risks that the policy does cover. [...] [T]he pollution exclusion in this case is animated by a unique purpose: to preclude coverage for expensive government-mandated environmental cleanup required by legislation that makes polluters strictly liable.

The Court of Appeal's holding in the *ING Insurance* case clarifies its prior holding in *Zurich* to the effect that a pollution liability exclusion clause does not only exclude coverage for the activities of "active industrial polluters." It also excludes coverage for activities that carry "a known risk of pollution and environmental harm" engaged in by businesses that are not active industrial polluters, but the application of the exclusion continues to be highly fact-dependent. It also seems clear that if the underlying event giving rise to the claim against the insured is founded on a discharge into the natural environment (*Zurich* was not — it concerned a discharge into the air in an apartment building,

which under the *Environmental Protection Act*, R.S.O. 1990, c. E.19, is excluded from the definitions of "air" and "natural environment" since it was enclosed in a building), the courts will be more inclined to find that the exclusion applies.

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**• EXTENDED WARRANTIES AND INSURANCE, WHAT IS INSURANCE?
A HEALTHY DOSE OF COMMON SENSE
FROM THE ALBERTA COURT OF APPEAL •**

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Overview

On July 21, 2011, the Court of Appeal for Alberta released a decision in a significant case concerning the meaning of "insurance" under provincial insurance legislation and its application to retail extended warranties. In doing so it provided helpful guidance on the meaning of "insurance".

The case arose out of an extended warranty program covering repair or replacement of products sold by The Brick, a large retailer of furniture, appliances, and electronic equipment. The ex-

tended warranty program was offered by Brick Protection Corporation, a sister company to The Brick. The Court established that the extended warranties do not constitute insurance even if they are offered by a sister company of the retailer.

While the case arose in a tax context,¹ the significance of the decision extends beyond the narrow tax issue considered in that: (i) both levels of court hearing the case found that the extended warranties were not contracts of insurance; and (ii) the decision places some limits on

the very wide ambit of the definition of "insurance" under insurance legislation.²

Background

Brick Protection provided extended warranties covering products sold by its sister company, which operated The Brick, a retailer of furniture, appliances and electronic equipment. These warranties covered repair or replacement of products purchased at The Brick where such products proved defective in workmanship or materials.

The Provincial Treasurer of Alberta assessed Brick Protection for over \$700,000 in taxes that ought to have been paid by Brick Protection on the basis that it was operating as an insurance company. With interest and penalties, Brick Protection faced liability of greater than \$1,000,000.

The taxing legislation at issue in *Brick Protection Corp. v. Alberta (Provincial Treasurer)*, [2011] A.J. No. 819, applied to companies carrying on the business of insurance "within the meaning of the *Insurance Act*." Justice Côté (with Justice Costigan concurring), writing for the majority, began by noting that the "business of insurance" was not a concept having a specific defined meaning under the *Insurance Act* (Alberta), RSA 2000, c. I-3.

In these circumstances, the majority noted that it was necessary to apply a commercial common sense approach to the term "business of insurance" (at para. 18):

In deciding whether a certain business is 'insurance', we must give some weight to actual practices and commercial reality. The Legislature must be presumed to legislate with reference to what actually occurs in the real world, not to theoretical nonexistent possibilities. That is doubly so when the new taxing legislation expressly refers to an existing well-known industry plus its regulation.

Justice Côté referred specifically to two other factors that ought to guide the court in determining how to interpret "the business of insurance".

First, the judge noted that "insurance" is a well-developed and homogeneous concept having well-established conventions. Second, the judge noted that the business of providing extended warranties is a distinct business with its own history.

The Definition of Insurance

Against this backdrop, Côté J.A. proceeded to analyze the legal question of whether the extended warranties fell within the definition of "insurance" under the *Insurance Act*. The judge began by quoting the definition of insurance under the Alberta *Insurance Act*, which is substantially similar to the definition in many Canadian provinces. It provides that "insurance" means (at s. 1(aa)):

... the undertaking by one person to indemnify another person against loss or liability for loss in respect of certain risk or peril to which the object of the insurance might be exposed, or to pay a sum of money or other thing of value on the happening of a certain event ...

The judge then proceeded to note the limited usefulness of the definition, given the degree to which, in theory, it could encompass many forms of financial products that no layperson would regard as insurance (at para. 23):

That definition has a number of problems. First, it has two alternative fairly different branches (separated by a comma). Second, it is very vague and abstract. Third, if read literally, it would cover a host of things which no one in Canada would ever consider when using the word 'insurance'. That is true of any reader, lawyer or lay person, in or outside the business community. Those three problems may not be fatal when setting the scope of the particular regulatory provisions in the Insurance Act. But as a guide to language in general, or to other statutes on other topics (such as taxation), those three problems seriously degrade that definition's usefulness.

Having recognized the limited usefulness of the definition, Côté J.A. proceeded to examine the treatment of insurance by text writers and in case law. Noting that the text writers and the case law have replaced the ambiguity in the definition of insurance with "a necessary use of caution and realism," the judge noted that the

proper approach to the interpretation of the insurance definition should be consistent with the modern trend in favour of a realistic approach that is sensitive to context. This modern approach seeks "to make the words in question fit into, and faithfully advance, the overall legislative scheme and objectives of the *Act*."

The purpose of the *Insurance Act*, the judge noted, is "to regulate the traditional insurance industry and protect the public from insolvent or unscrupulous companies and from certain unfair types of policy and claims processes."

Components of Traditional Insurance

Justice Côté continued by specifically referring to the absence of any external risk against which the extended warranties were to protect the consumer (at para. 36):

Another feature of insurance is mentioned briefly in some of the definitions of insurance. Typically, insurance involves outside risks created neither by the insurer nor by the insured. Even life insurance involves such outside risks (though we will all die someday). The effect of a number of phrases or clauses very common in insurance policies is the same: the insurer does not cover risk of bad workmanship or design, nor materials supplied by the insured. (Some bonding companies issue performance bonds sometimes having that effect, but no one argues that analogy here.) Closely connected with that and overlapping is another insurance industry practice. Typically the policy is worded so as not to cover simple failure of, or loss of, the very item insured from internal causes.

The guarantees in issue here are the opposite. They cover only product failure as a result of defects in materials or workmanship of the very item sold. And they call only for repair or (sometimes) replacement.

Justice Côté therefore did not regard as material the fact that the putative "insurance" company in this case was a related company to the retailer. The focus of the inquiry was on the nature of the contract that Brick Protection was entering into.

From this perspective, the judge emphasized that the stipulations of the *Insurance Act* had to be interpreted in such a way as not to produce a

commercial absurdity. The judge noted that a great many contracts allocate risk, in some cases putting all of the risk on one party. It is not, however, for this reason alone that they are regarded as insurance. Furthermore, other components of a traditional insurance relationship were absent. The extended warranties could scarcely be described as contracts of indemnity, since they only governed repair or replacement of items purchased. Similarly, there was an absence of any individualized assessment of risk by the putative "insurer" before setting the premium and concluding the contract.

Concurring Reasons

In concurring reasons, Justice Graesser did not go so far as the majority insofar as it interpreted the definition of insurance under the *Insurance Act*, but rather confined his reasoning to the general question of what constituted the business of insurance within the meaning of the *Insurance Act*. Since the insurance regulator in Alberta had not taken the view that similar extended warranty products were insurance, and since the business of providing extended warranties does not predominantly involve insurance companies, it was appropriate to conclude in favour of the taxpayer that extended warranties were not insurance business for the purpose of the taxing.

Conclusion

Ultimately, the reasoning of the majority is a strong statement of the need to have regard to purpose and context when interpreting the definition of "insurance" under provincial insurance legislation. The mere fact that a contract transfers risk and is triggered on the happening of contingency is not to be taken as automatically indicating that the contract is a contract of insurance. Rather, it is necessary to look more deeply at the contract in question with a view to determining how much a given product resembles traditional insurance.

While the Court in *Brick Protection* focused only on certain traditional components of an insurance relationship (*i.e.* the absence of a traditional indemnity relationship, the absence of external risk, the absence of risk assessment by the insurer, the non-involvement of an insurer, and the absence of a "remote" risk), the reasoning in *Brick Protection* would permit considering other criteria such as the existence or non-existence of an insurable interest, and the element of risk-spreading among similarly-situated insureds.

By strongly signalling that the definition is to be interpreted with reference to those contracts that are traditionally regarded as insurance, the Court has taken a clear step in the direction of providing greater clarity for businesses considering marketing financial products that may fall within the literal definition of insurance.

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¹ The case arose as a result of an attempt by tax authorities to claim premium tax against a provider of extended warranties on the basis that the warranties were in effect contracts of insurance.

² The breadth of the definition of "insurance" in the insurance legislation of most Canadian provinces is so broad that they risk catching within their ambit commercial contracts that look nothing like insurance and that, as a practical matter, most would not consider to be insurance (*e.g.*, extended warranties). This lack of clarity leaves an essentially legal question to be resolved on an *ad hoc* basis by individual regulators, whose views concerning what is and is not insurance can diverge widely from province to province notwithstanding substantially identical definitions of insurance throughout provincial insurance legislation in Canada.