COURT OF APPEAL FOR ONTARIO

CITATION: Davies v. AIG Insurance Company of Canada, 2024 ONCA 509
DATE: 20240627
DOCKET: COA-23-CV-0054

Gillese, Brown and Paciocco JJ.A.

BETWEEN

John Davies and Judith Davies

Applicants (Respondents)

and

AIG Insurance Company of Canada

Respondent (Appellant)

David Vaillancourt and Ardita Sinojmeri, for the appellant

Lawrence Theall and Dylan Cox, for the respondents

Heard: April 17, 2024

On appeal from two judgments of Justice Grant R. Dow of the Superior Court of Justice, both dated December 1, 2022, with reasons at 2022 ONSC 5647.

Gillese J.A.:

I. OVERVIEW

[1] John Davies was the principal of several interrelated Ontario real estate development companies (the "Davies Companies"). AIG Insurance Company of

Canada (“AIG” or the “appellant”) issued directors’ and officers’ liability insurance policies (the “D&O Insurance Policies” or the “Policies”) to the Davies Companies.

[2] Mr. Davies and his spouse Judith Davies (together, the “Davies” or the “respondents”) are named defendants in two lawsuits alleging that Mr. Davies and his associates used the Davies Companies (and other corporate vehicles) to operate a Ponzi scheme. The claims further allege that the Davies Companies’ purported real estate developments were funded by millions of dollars in syndicated mortgages advanced by individual investors and that the Davies (and others) misappropriated those monies (the “Underlying Actions”).

[3] The Davies sought coverage under the Policies for their legal costs of defending the Underlying Actions. Initially, AIG paid their defence costs but later resiled on the basis that their applications for coverage contained a material misrepresentation because they failed to disclose that syndicated mortgages were the source of financing for the Davies Companies.

[4] The Davies and AIG brought competing applications to determine whether AIG has a duty to pay the Davies’ defence costs in the Underlying Actions. The applications judge found in favour of the Davies.

[5] AIG appeals. Its appeal raises two questions: (1) was there a misrepresentation in the Davies’ applications for the D&O Insurance Policies, and

(2) if so, was the misrepresentation material? The application judge answered "no" to both questions.

[6] In my view, the answer to both questions is "yes". By failing to disclose that syndicated mortgages were the source of financing for the Davies Companies, Mr. Davies made a material misrepresentation that triggered an exclusion under the D&O Insurance Policies. Since Ms. Davies' coverage is derivative of Mr. Davies' coverage, she too has no coverage.

[7] Accordingly, I would allow the appeals and declare that AIG does not have a duty to pay the Davies' defence costs in the Underlying Actions.

II. BACKGROUND

[8] AIG first issued the D&O Insurance Policies to the Davies Companies for the policy period July 2015 to July 2016. The Policies were automatically renewed in July 2016. The 2016-2017 Policies, under which the Davies sought coverage, included a representations and severability clause which provided that if

> "any of the statements, warranties or representations is not accurately and completely disclosed in the **Application** and materially affects either the acceptance of the risk or the hazard assumed by the **Insurer**, no coverage shall be afforded for any **Claim** alleging, arising out of, based upon, attributable to or in consequence of the subject matter of any incomplete or inaccurate statements, warranties, or representations…". [Emphasis in original.]

[9] Pursuant to the D&O Insurance Policies, AIG paid over $1 million in legal costs on behalf of the Davies in the Underlying Actions before notifying them that it was denying coverage.

[10] The denial of coverage relates back to the process followed in 2015 leading up to issuance of the Policies. That process began when Greg Markell, an insurance broker, sent an email to AIG's underwriting group to which he attached the 2013-14 financial statements of the Davies Companies (the "Financial Statements"). In the email, Mr. Markell invited someone from the AIG underwriting group to speak with him by phone once they had reviewed the "submission" so he could explain how the prospective insureds wanted to structure the policies.

[11] Michelle McQueen was assigned as the underwriter for AIG. She reviewed the email and attached Financial Statements. The latter were for companies that AIG was not familiar with. The companies were in the real estate development business and appeared to be at an early stage of that process. The Financial Statements reflected a significant amount of inter-company loans and almost $40 million in long-term debt to external lenders. However, the Financial Statements did not disclose the identity of the external lenders.

[12] Ms. McQueen knew that real estate development companies require access to a significant amount of capital to bring a project from inception through to completion. She needed information about the amount and source of the Davies

Companies' financing to ascertain whether they had sufficient funds to complete their development projects. That information was not in the Financial Statements. Without it, she was not able to provide quotes for D & O insurance policies.

[13] On May 22, 2015, Ms. McQueen emailed Mr. Markell to schedule a phone call to discuss the submission. They spoke later that day, by phone, and she identified the additional information she needed to be able to "quote the risk". She followed up with another email that day and a further email dated May 28, 2015. Mr. Markell responded by email on May 28, saying he had "spoke[n] with the client yesterday" and "they [are] working on it". In his email, he also stated that his clients were working on answering the following queries from AIG:

- Regarding the inter-company loans, [AIG] were hoping to get an understanding as to who the loan facility is that is providing to the current [Davies] companies.
- [AIG asked that the Davies] Please provide the terms of the loans from outside sources.

[14] On July 16, 2015, Mr. Markell sent Ms. McQueen an email that included the following question and answer (the "Email"):

> Question: "Regarding the inter-company loans, [AIG] were hoping to get an understanding as to who the loan facility is that is providing to the current companies".
>
> Answer: "Balfor will go shoulder to shoulder for covenants, the remaining loans provided by mezzanine and construction financing. Memorandum of understanding and term sheet from a lender on board.

> Kingset (sp?) Capital in Toronto. John Love's company.
> $500MM funds. All schedule A banks in funds."

[15] As you will see, the Email played a significant role in the applications judge's disposition of the Davies and AIG applications.

III. THE DECISION BELOW

[16] The applications judge noted the parties' agreement that, to avoid funding the Davies' defence costs, AIG had to prove the following:

1. there was a misrepresentation;
2. the misrepresentation was in the Davies Companies' applications for coverage;
3. the misrepresentation was material;
4. the Underlying Actions allege, arose out of, were based upon, were attributable to, or were in consequence of the subject matter of the alleged misrepresentation; and
5. the insured (John Davies) knew of the misrepresentation.

[17] The applications judge found against AIG on the first and third requirements.

[18] On the first requirement, the applications judge found a "complete absence of any mention of syndicated mortgages as the method of financing being used by John Davies in his real estate developments". He described the Email as lacking "detail or precision" and while "the absence of syndicated mortgages is troubling", its wording was "insufficient to conclude a misrepresentation had occurred".

[19] On the third requirement, the applications judge relied on the evidence of AIG's expert to find that the "subject of the real estate development financing is material to the decision to extend coverage". Nonetheless, the applications judge stated, the "point form" nature of the Email and its reference to a variety of financing possibilities "should have been clarified" by Ms. McQueen in some fashion beyond that which had been put forward and then commented that AIG "cannot merely rely on its interpretation of what was not clear".

[20] The applications judge concluded by granting the Davies' Application and dismissing the AIG Application.

IV. THE ISSUES

[21] AIG submits the applications judge erred in failing to find:

1. there was a misrepresentation; and
2. that the misrepresentation was material.

[22] The Davies support the applications judge's decision but submit he erred in finding that Mr. Davies knew about the purported financing misrepresentation based on agency principles.

V. THE FRESH EVIDENCE MOTION

[23] On the eve of the original hearing date of this appeal, counsel for the Davies learned that Ms. Davies was an undischarged bankrupt when she and Mr. Davies

commenced their Application in this proceeding.[1] The original hearing date was adjourned to allow the parties to consider the implications of Ms. Davies bankruptcy.

[24] The parties could not agree on the procedural ramifications of Ms. Davies' bankruptcy. AIG maintains that it rendered her application a nullity because undischarged bankrupts lack standing to bring proceedings of this nature. Thus, her application must be dismissed. Counsel for the Davies maintains that Ms. Davies "has always had standing as a party to the application".

[25] Significantly, AIG advised counsel for the Davies that it would apply this Court's insurance coverage determination for Mr. Davies to Ms. Davies despite "the absence of a properly constituted coverage application from Judy Davies".

[26] The parties attended a case conference before a judge of this court for assistance on how to proceed with the matter of Ms. Davies' bankruptcy. The case management judge directed AIG to bring a fresh evidence motion, to the panel of the court hearing the appeal, disclosing Ms. Davies' bankruptcy. That motion proceeded before this panel in conjunction with the hearing of the appeal.

[27] The parties are agreed that the *Palmer*[2] test for the admission of fresh evidence on appeal has been met. I agree and, therefore, would admit the fresh

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[1] Since then, she has been granted a conditional discharge and, subject to her having met certain conditions, Ms. Davies was to have been discharged from bankruptcy on April 27, 2024.
[2] *R v. Palmer,* [1980] 1 S.C.R. 759.

evidence. In sum: (1) AIG could not, through the exercise of due diligence, have presented the evidence at the hearing of the applications when even Ms. Davies' own lawyer on the Applications was unaware of it; (2) the evidence consists of documents created by officers of the Court and is reasonably capable of belief; (3) the evidence is relevant to a potentially decisive issue as it relates to Ms. Davies' standing in this proceeding; and (4) if believed, the fresh evidence may have affected the result in respect of Ms. Davies.

[28] However, in light of AIG's undertaking that it will apply this court's insurance coverage determination for Mr. Davies to Ms. Davies, the issue of Ms. Davies' standing is of no practical significance and I decline to decide it. Whether an undischarged bankrupt has standing in a particular legal proceeding is a question of some significance. In my view, its determination is better left for a case in which the determination matters, and where the issue has been squarely raised and argued at first instance, with any necessary findings of fact having been made at that level.

VI. ANALYSIS

The Standard of Review

[29] As I explain below, the applications judge ignored relevant evidence in deciding both whether there had been a misrepresentation and, if so, whether the misrepresentation was material. Failing to consider all the evidence relevant to

those matters, in a way that affected the applications judge's conclusions, is an error of law justifying reconsideration of the evidence by this court: *Sharbern Holding Inc. v. Vancouver Airport Centre Ltd.*, 2011 SCC 23, [2011] 2 S.C.R. 175, at para. 71.

The Misrepresentation

[30] The applications judge found there was a "complete absence of any mention of syndicated mortgages as the method of financing being used by John Davies". However, he did not consider that finding, and the evidence underlying it, when deciding whether a misrepresentation had been made. Instead, the applications judge considered only the Email and Ms. McQueen's failure to clarify its ambiguities. By failing to consider all evidence relevant to whether a misrepresentation had been made, the applications judge fell into legal error justifying this court's reconsideration of the evidence.

[31] As I discuss more fully below, the Davies Companies had an obligation to disclose that syndicated mortgages were the source of their financing. On the applications judge's finding, they failed to disclose that information. By failing to disclose to AIG all information relevant to the nature and extent of the risk AIG was being asked to undertake, the Davies Companies made a misrepresentation by omission (the "Misrepresentation").

[32] In light of this clear Misrepresentation, it is unnecessary to decide AIG's alternate submission, namely, that the applications judge erred by failing to find that the Email contained financing misrepresentations because it indicated that Kingset Capital, John Love's company, was providing financing, and that Schedule A banks were providing $500MM of financing.

The Misrepresentation was Material

[33] The applications judge's materiality determination was fatally flawed because he failed to consider the Misrepresentation when making that determination. Instead, he focused on the Email and Ms. McQueen's response to it. Because the applications judge's approach to materiality reflects legal error, this court must determine whether the Misrepresentation was material.

[34] In my view, there can be no doubt that the Misrepresentation was material.

[35] The legal framework surrounding materiality was well summarized in the following statements drawn from *Sagl v. Chubb Insurance Company of Canada*, 2009 ONCA 388, 209 O.A.C. 234, at paras. 51-52:

1. the parties to the contract of insurance are held to a standard of utmost good faith;
2. this duty places a heavy burden on applicants for insurance coverage to provide full disclosure to the insurance company of all information relevant to the nature and extent of the risk the insurer is being asked to assume;

3. a fact is material if it would influence a prudent insurer in deciding whether to issue the policy or in determining the amount of the premium;
4. there is also a subjective element to be considered when determining whether a misrepresentation or non-disclosure is material;
5. the duty to disclose all material facts applies even in the absence of questions from the insurer, although the absence of questions may be evidence that the insurer does not consider a fact to be material; and
6. the consequence of non-disclosure or misrepresentation of a material fact by the insured is that the insurer is entitled to void the insurance contract *ab initio*.

[36] The applications judge's reasons can be understood as finding that the objective component of the materiality test was met. He referred to the expert evidence that "determining the source and amount of financing is the cornerstone underwriting issue for a privately owned real estate development company" and concluded that "the subject of the real estate development financing is material to the decision to extend coverage".

[37] It may be that the applications judge was considering the subjective component when he said Ms. McQueen needed to do something more than she had after receiving the Email. However, because the applications judge failed to set out the legal test for materiality, the basis on which he was assessing her response to the Email is unclear.

[38] In any event, the applications judge had to determine the entirety of AIG's subjective response, not simply its response to the Email. On that matter, Ms. McQueen's evidence was clear and unchallenged: (1) she needed information on the amount and sources of funding because the Davies Companies had not provided that information and that information was necessary to ensure there was sufficient funding for the Davies Companies to complete their development projects; (2) without that information, she was not able to provide quotes for the Policies; and (3) she would not have placed the risk as she did had she known the true state of financing for the Davies Companies. The 2015 process leading up to the issuance of the Policies supports her testimony. Before responding to the coverage request and quoting the risk, Ms. McQueen specifically sought the financing information, a context that confirms the materiality of the requested information to AIG.

[39] The Davies Companies failed to disclose to AIG, at any point in the process culminating in the issuance of the Policies, that they were financed by way of syndicated mortgages. There is no question that was a material Misrepresentation, viewed both objectively and subjectively.

Conclusion

[40] In my view, AIG was, and is, under no duty to advance the Davies' defence costs because their claims are excluded by the terms of the representations and

severability clause in the Policies. Accordingly, AIG is entitled to a declaration to that effect and it is entitled to recover, as damages, the $1,015,418.97 advanced to date.

[41] Further, I would reject the Davies' challenge to the applications judge's finding that Mr. Davies knew of the Misrepresentation based on agency principles. I see no basis for appellate interference with that finding.

[42] On the record, that finding was open to the applications judge. In July 2015, Mr. Davies was the sole director of the Davies companies. He signed the applications for insurance for the Davies Companies. The application form clearly showed the financial information was required. And the emails from Mr. Davies' broker established that the broker sought the necessary financial information from his client to complete the application and enable AIG to process it.

VII. DISPOSITION

[43] For these reasons, I would: allow the appeal; grant the AIG application; dismiss the Davies application; declare that AIG does not have a duty to pay the Davies' defence costs; and award damages to AIG of $1,015,418.97, plus pre- and post-judgment interest, payable jointly and severally by the Davies.

[44] I would order costs to AIG as follows:

1. costs of the appeal in the agreed-on sum of $30,000, all inclusive;

2. costs thrown away for the preparation of the previously scheduled oral hearing of the appeal in the agreed-on sum of $3,000, all inclusive;
3. costs of $12,000, all inclusive, for preparation of the fresh evidence materials; and
4. costs of the applications below.

[45] If the parties are unable to agree on the costs of the applications, I would order them to file, with this court, written submissions to a maximum of three pages within seven days of the date of release of this decision (the “Costs Submissions”), and to attach to their Costs Submissions, their Bills of Costs for the applications and any attendant written submissions.

Released: June 27, 2024 “E.E.G.”

“E.E. Gillese J.A.”
“I agree. David Brown J.A.”
“I agree. David M. Paciocco J.A.”