SUPREME COURT OF NOVA SCOTIA

Citation: *Colman v. AAA Plumbing and Heating Limited*, 2020 NSSC 360

Date: 20201210
Docket: Hfx 490165
Registry: Halifax

Between:

Russell Colman and William Palander

Plaintiffs

v.

AAA Plumbing and Heating Limited

Defendant

DECISION

Judge: The Honourable Justice Jamie Campbell

Heard: December 1, 2020, in Halifax, Nova Scotia

Counsel: Cory Withrow and Kevin Quigley, for the Plaintiffs
Ian Dunbar, for the Defendant

[1] This is the decision on a motion seeking an order for the defendant to disclose documents that they claim are subject to litigation privilege. Those documents are found in the adjuster's file created by an adjuster retained by the defendant's third-party liability insurer.

Facts

[2] The case itself is about a leaking oil tank. On December 22, 2016, the plaintiffs discovered a fuel oil leak from a tank that had been installed on their property by the defendant, AAA, days before. On the same day that the leak was discovered, they contacted AAA and their own insurer, the Co-operators. The claim notes from the Co-operators state on December 29, 2016, that a letter of notice would be sent out to AAA advising them of potential subrogation. The next day, an adjuster with the Co-operators noted that he had spoken with the owner of AAA who said that he had contacted his own insurer.

[3] An insurance adjuster with the firm ClaimsPro was retained by AAA's insurer, AIG Inc. That adjuster was Shane Walker, and it is the contents of his file that form the subject matter of the dispute on the motion. On January 23, 2017, Michael Buckley, a Claims Representative with the Co-operators, wrote to Mr. Walker, with ClaimsPro. That letter does not merely say that the Co-operators was considering subrogation or investigating whether they would pursue a subrogation claim. It says, in its entirety,

> Our investigation indicates that your Insured is responsible for damages sustained to our insured's property.
>
> This letter serves as notice of our intent to recover our subrogated interest. We will forward our supporting documentation once the claim has been finalized.
>
> If you have any questions, please feel free to contact me.

[4] The Co-operators had reached a conclusion about who was responsible for the loss. They responded to the oil spill and remediated the property as the first-party insurer. In the meantime, the third-party liability insurer, AIG Inc., would have to determine whether their insured was covered, and if so, how they should respond to the subrogation claim. This was not a situation in which their insured had alerted them to a potential liability claim. Nor was it a situation in which the first-party insurer had put them on notice that it was considering or investigating the potential of a subrogation claim. As of January 23, 2017, AIG Inc. had notice

of a claim the settled intention on the part of the Co-operators to recover their subrogated interest.

[5] The Co-operators and AIG Inc. through Mr. Walker of ClaimsPro, tried to reach an agreement with respect to AAA's liability for the leak and the value of the loss. Those communications happened verbally and in writing, largely between Mr. Buckley of the Co-operators and Mr. Walker of ClaimsPro. That went on from January 2017 to June 2019. There is a dispute about the admissibility of some of those communications. But the plaintiffs, through the Co-operators, say that Shane Walker acknowledged AAA's liability several times from November 2018 through to June 3, 2019.

[6] Mr. Buckley said in his affidavit that when he received an email from Mr. Walker on November 20, 2018, he concluded that AIG Inc. had acknowledged liability for the oil leak and that only the issues related to the quantum of the claim remained open. He said that emails of December 3 and December 4, 2018 confirmed that understanding. Legal counsel had not been involved to that point, because it seemed "obvious" to him, because of the discussions with Mr. Walker, that AAA's insurer had accepted liability and were interested in settling the claim.

[7] Things changed on June 4, 2019. Mr. Buckley sent an email to Mr. Walker that day indicating that unless an offer was received by June 7, 2019, he would be recommending to the Co-operators that they retain counsel and start a subrogation action. Mr. Walker responded, saying that he had heard back from the insurer instructing him to advise Mr. Buckley that because the two-year limitation period had expired, they would not accept responsibility for the claim.

The Legal Action

[8] On July 16, 2019, the plaintiffs filed an action against AAA for the oil leak. In the Statement of Claim the plaintiffs relied on section 20 of the *Limitation of Actions Act* SNS 2014, c. 35, which renews the limitation period at the point when a party acknowledges liability in respect of a claim for a liquidated sum. The plaintiffs also pleaded that AAA was estopped from relying on the *Limitation of Actions Act* as a defence because they had acknowledged liability. AAA filed a defence that denied that the representations made to the Co-operators amounted to an admission of liability.

[9] AAA produced an Affidavit Disclosing Documents on December 23, 2019. It disclosed the existence of claim notes and correspondence between Shane

Walker and the insurer, AIG Inc. Some of those documents were close to the dates on which Mr. Walker wrote to Mr. Buckley making comments that Mr. Buckley says assured him that the third-party liability insurer was accepting liability. The disclosure is heavily redacted. The defendant claims litigation privilege.

[10] A Supplemental Affidavit Disclosing Documents was filed on March 17, 2020. That disclosure includes reference to 25 adjuster's reports. Those are also heavily redacted based on the claim of litigation privilege. The privilege log included with the disclosure identifies the particulars of the claim notes and correspondence including the date, type, and recipient. All other information remains redacted.

[11] The defendant claims litigation privilege over the adjuster's file. The defendant contends that the adjuster's file was created solely for the purpose of preparing for reasonably contemplated litigation. The plaintiffs are seeking an order compelling the defendant to disclose the entire adjuster's file from its creation up to June 4, 2019. The relevance of the documents is not disputed. They contain evidence of internal discussions about whether AAA, their insurer AIG Inc., through Shane Walker of ClaimsPro on their behalf, had admitted liability for the claim.

Issue

[12] The issue is whether litigation privilege applies to the adjuster's file.

Litigation Privilege

[13] Litigation privilege applies to disclosure of documents and communications the dominant purpose of which is the preparation for litigation. That would include, for example, communications between lawyers and witnesses or experts. The party seeking to invoke the privilege has to establish that litigation was "in reasonable prospect" when the document was produced and that the dominant purpose of the document was to conduct or aid in the conduct of the litigation. The purpose is to afford litigants a zone of privacy in which to prepare for the case.

[14] Courts are required to balance the need for a zone of privacy in preparation for litigation against the presumption of full disclosure. Both must be respected to encourage a fair and efficient system of civil litigation.

A Reasonable Prospect of Litigation

[15] The first question then is whether, when the documents were prepared, there was a reasonable prospect of litigation. That means more than that litigation is possible. But it also does not mean that litigation must be a certainty. The test is whether a reasonable person with all of the pertinent information, including information relating only to one or the other of the parties, would conclude that it would be unlikely that the claim would be resolved without litigation. Again, it is not whether litigation in a general sense was probable but whether having regard to the conduct of the parties in the circumstances, litigation was reasonably contemplated. Anticipated litigation must be real and not just a possibility, a suspicion, or a vague anticipation.

[16] The presence of a potential for a subrogated claim does not mean that litigation is reasonably contemplated. The issue is whether or when pursuing such a claim was actively considered.

[17] Michael Buckley said in his affidavit that when the Co-operators notified AAA of the oil leak and of the plaintiffs' intent to recover the loss from AAA, there was no reason for any party to have anticipated litigation. Many losses and claims are investigated, discussed, and settled by the insurers without any prospect that litigation will be required. In this case, the exchanges between Mr. Buckley and Mr. Walker suggest that the parties were working on resolution of the matter.

[18] The Co-operators say that there is no evidence to suggest that AAA had a reasonable prospect of any litigation leading up to June 4, 2019. They say that Mr. Walker, as the adjuster for AIG Inc., represented that his principals were investigating the oil leak to determine the cause, reviewing and scrutinizing the plaintiffs' documents relating to the amount of the claim and were preparing a settlement offer. While retaining counsel is not determinative of whether litigation is in contemplation, it is a factor. And in this case the defendant, AAA, did not retain counsel until July 26, 2019.

[19] Insurance adjusters' files are prepared for many reasons. Adjusters seek information to provide recommendations to their principals. At some point litigation becomes a real and reasonable prospect. It may be to assert a subrogation claim, defend liability or to deny coverage. As the defendant notes however, it is important to distinguish between first-party claims and third-party claims. First-party claims involve dealing with the principal's contractual and statutory obligations. An insurance company cannot claim that it is anticipating litigation just because the insured party wants to be paid for what they believe to be an

insured loss. Insurance companies investigate those claims without anticipating litigation.

[20] The defendant says that a third-party insurer, like AIG Inc., is in a different position. For those insurers, litigation can be said to be in contemplation once an accident occurs and notice is given. It is not essential that counsel be retained. The time when litigation privilege commences depends on the facts of each individual case, having regard to whether the insurer involved is a first-party insurer or a third-party insurer.

[21] The determination of when litigation privilege begins is fact specific. The fact that a third-party insurer is involved is a factor to be considered. It is not determinative of the issue. A third-party liability insurance adjuster's file is not automatically or presumptively subject to litigation privilege. The time for the retainer of legal counsel is a factor. But that too is not determinative. So is the nature of the loss and the relationship among the parties involved. For some kinds of claims there is the potential that the third-party insurer will be called upon to respond. For others, it is far more than just a potential. When the third-party insurer has been given formal notice of a subrogation claim involving a significant loss, there remains the possibility that the case will be settled short of litigation. But the potential for litigation comes into shaper focus.

[22] In this case, the oil leak was discovered a few days after a tank had been replaced by AAA. The leak was reported to the first-party insurer, Co-operators, and they almost immediately considered pursuing a subrogation claim against AAA. They decided to formally put AAA on notice of that on December 29, 2016 and gave that notice on January 23, 2017. At that stage, there was no way to determine whether litigation would be required. Many subrogation claims are resolved through negotiation. But in this case, it was clear, early in the process, that the plaintiffs' insurer was not only weighing the potential for a claim but was making a claim against the plaintiffs' liability insurer. This file would involve the third-party insurer. This was not a case in which it would be reasonable to suppose that the first-party insurer would just settle the claim with its insured and leave things at that.

[23] The first-party-insurer and the insured are not immediately in an adversarial relationship. There is a requirement to investigate to determine how or whether the insurer will respond. Information is gathered for that purpose. The adjuster working on behalf of the third-party insurer may investigate to see whether their

insured is covered for the liability. Their attention then turns to the loss that had been sustained. When the third-party insurer is advised of a subrogation claim the third-party liability insurer and plaintiffs, or the plaintiffs' first-party insurer, are in an adversarial relationship. They may settle the dispute without litigation. But they understand litigation will result if the case is not settled by negotiation.

[24] The purpose of litigation privilege is to afford parties a zone of privacy. That zone of privacy extends to the preparation for litigation that is reasonably contemplated between adversarial parties. The purpose of the third-party insurance adjuster's file is to provide information that would be used to assess how the third-party liability insurer should respond to the subrogation claim. That may involve gathering evidence to be used in court or gathering evidence to be used in the negotiation of a settlement. But it is gathering information to respond to a claim. Information regarding the plaintiffs' insurance coverage would usually not be relevant to the dispute about liability.

First-party and Third-party Insurers

[25] The distinction between first-party and third-party insurers was made clear in *Panetta v. Retrocom Mid-Market Real Estate Investment Trust*, 2013 ONSC 2386. That case arose from a slip and fall accident at a Walmart. The judge concluded that as soon as the plaintiff fell and was injured, she was in an adversarial position with all of those who were ultimately to become the defendant and their insurers. In third-party claims there is no preliminary investigative phase where privilege does not attach to notes, reports and files of adjusters. The only reason for any investigation on behalf of the third-party insurer was the prospect of litigation. The judge held that it would be "naïve to think otherwise". The fact that the investigation might be used to reach a pre-lawsuit settlement does not detract from that point. "The prospect of litigation inherently includes the prospect of settlement." at para. 61.

[26] The practical point seems to be that, for a third-party insurer, there would be no purpose for the creation of the documents other than for anticipated litigation, setting reserves or seeking legal advice. Settlement of litigation is part of litigation. In that case, when the adjusters were retained to investigate by the defendant, the sole purpose of the documents they created was in anticipation of litigation. The court found that litigation privilege applied.

[27] *Panetta* has raised a distinction about litigation privilege that has been adopted by other courts. In *Plenert v. Melnik Estate*, 2016 BCSC 403, the case

arose from a serious motor vehicle accident involving several vehicles. A third-party was responsible for maintenance of the section of highway where the accident happened. There were allegations that slippery conditions contributed to the accident. The company responsible for road maintenance retained an adjuster to investigate. The other parties made a motion for production of the adjuster's files.

[28] When the claim was first reported to the third-party, there was a reasonable prospect of litigation. That was based on the seriousness of the accident and the fact that another adjuster had made inquiries about road maintenance. The Master in that case determined that litigation was in reasonable prospect even though there had been no notice of a claim and legal counsel had not yet been retained.

[29] In this case, AAA was alerted early on that there was a subrogation claim going to be made. The facts of the case involved a potentially significant loss due to an oil leak, discovered some days after the defendant installed an oil tank. A person with that information would reasonably anticipate that if liability were not acknowledged, there would be a high likelihood that litigation would follow. The case may be settled, as they often are, but in a case like this, litigation was the reasonably anticipated end point.

[30] In this context, making an assessment about whether the dispute can at some point be settled without going to court fails to have regard to the significance of the "zone of privacy". Litigation may appear to go through phases during which settlement seems likely, then less likely, or not likely at all. Circumstances may change and it then is settled. The documents prepared based on those shifting prospects do not go in and out of the zone of privacy based on a retrospective assessment of the apparent likelihood of settlement at the time the documents were prepared. The settlement of litigation is part of the process of litigation.

Dominant Purpose

[31] The two issues of the reasonable prospect of litigation and the dominant purpose of the documents are separate but related. It is an important distinction in this case.

[32] Just because documents were prepared at a time when litigation is in reasonable prospect does not mean that they are subject to litigation privilege. Preparation for litigation may have been one of the predominant reasons for the

creation of a document but unless that is the dominant purpose the privilege does not apply. *Hamalainen (Committee of) v. Sippola*, [1991] B.C.J. No. 3614.

[33] The plaintiffs argue that no evidence has been put forward to establish the dominant purpose of each of the documents in respect of which litigation privilege has been claimed. They say that the defendant is required to show, on a document by document basis, that the dominant purpose for the creation of the document was the preparation for litigation. Documents may be prepared for multiple purposes, one of which is litigation, but to be subject to litigation privilege the dominant purpose to produce the document must have been litigation. And the party seeking to rely on litigation privilege must establish that dominant purpose for each document. In many cases that would either be a difficult task or a mindlessly simple one. Other than a self-serving statement to the effect that the document, the contents of which are not disclosed, was created for the dominant purpose of preparing for litigation, usually there would be not much else that could be said. It may be difficult to satisfactorily show that a document was prepared with the dominant purpose being litigation preparation, without showing the contents of the document itself.

[34] Inferences as to the dominant purpose can of course be drawn from the circumstances surrounding the preparation of the documents. In the case of a third-party insurer put on formal notice of a subrogation claim an inference may be drawn that documents prepared by the adjuster were for the dominant purpose of responding to that claim, either by litigation or the settlement of litigation.

[35] In this case, the court has been provided with the unredacted materials. The package, provided to the court, but not to the defendant, is about 350 pages long. The purpose is not to have the court do the litigant's work by determining the dominant purpose for which each document was prepared. The unredacted documents are reviewed having regard to the context within which they were created. A third-party insurer may have a reason to retain an adjuster to do an investigation for reasons that do not involve the preparation for litigation on a subrogation claim. There may be issues regarding the insured party's coverage. If that were the case, it may be reasonable to inquire as to how it would be relevant to the subject matter of the subrogation claim.

[36] The documents provided to me for review relate to the investigation of the file in preparation for the negotiated settlement or the resolution in court of the subrogation claim. The documents contain some materials that relate to the

investigation of the cause of the leak and some materials that pertain to the extent of the potential exposure of the third-party insurer. The investigation was done, and the documents were prepared for no reason other than to respond to the subrogation claim. The concept of the "zone of privacy" allows parties to prepare for litigation. They must be able to do that with the assurance of privacy, so that their internal investigations and discussions will not be turned against them by parties who were known to have adverse interests to theirs in litigation that was "in reasonable prospect". Full disclosure in that situation would be unfair to the party who would be required to disclose documents that were created to deal with litigation.

[37] When the third-party insurer, AIG Inc., was advised that there would be a subrogation claim in this case, litigation became a reasonable prospect. The nature and value of the claim was such that the notice provided by the Co-operators could not reasonably be considered an idle threat, a warning that the Co-operators were considering a claim or an opening gambit. The investigation done by the adjuster was for the dominant purpose of responding to that litigation, whether by preparing for a trial or settlement of the claim. The adjusters' investigations in this case served no other purpose. The documents provided to the court for review confirm that.

[38] The materials sought were created for the purpose of preparing for litigation and were prepared at a time when litigation was "in reasonable prospect".

Exception to Litigation Privilege

[39] The plaintiffs have argued that the adjuster's file should be disclosed even if the preconditions for litigation privilege have been met. The basis of that argument is that the information is relevant to the proof of an issue that is important to the outcome of the trial and there is no reasonable alternative form of evidence that can serve the same purpose. The plaintiffs argue that by pleading and relying upon the *Limitation of Actions Act* the plaintiffs have put the issue of their internal communications regarding liability and their state of mind about the claim before June 4, 2019 directly into issue.

[40] The plaintiffs acknowledge that the exception to litigation privilege is rarely invoked. But here the adjuster's reports to the insurer and the various communications among AAA, the insurer and the adjuster are indispensable evidence on the limitation period issue. The issue is whether the communications between the adjuster, Shane Walker and Michael Buckley, amounted to an

acknowledgement of liability so that the limitation period under the *Limitation of Actions Act* was re-set. The plaintiffs say that the evidence regarding whether Mr. Walker's emails amounted to an acknowledgement of liability is potentially dispositive to the claim.

[41] There are exceptions. The Supreme Court of Canada in *Lizotte v. Aviva Insurance Company of Canada*, 2016 SCC 52, set out the exceptions to solicitor-client privilege and litigation privilege. The scope of those exceptions is circumscribed and is not defined by a balancing exercise. The exceptions relate to public safety, the innocence of the accused in criminal matters and to criminal communication. They also include evidence of a party's abuse of process or other blameworthy conduct. The Court allowed that other exceptions may be identified in the future, but they would always be based on the narrow classes that apply in specific circumstances. Urgency and necessity might be an appealing exception when litigation privilege may delay access to documents that the other party needs to "prevent serious harm". The Court said that such an exception would be based on the need to obtain the evidence to prevent that serious harm, the impossibility of obtaining it by other means and the urgency of obtaining it before litigation privilege would otherwise lapse.

[42] The materials sought in this case do not fall within any of those exceptions. The kind of urgency to which the Supreme Court of Canada referred related to serious harm and not the success or failure of litigation. The exception to litigation privilege does not extend to circumstances in which the disclosure sought is alleged to be important to the case.

Conclusion

[43] The adjuster's file is subject to litigation privilege. It was created at a time when litigation regarding a subrogation claim was in reasonable prospect. The dominant purpose of the file was to prepare for that litigation, whether by a trial or negotiated settlement. The materials sought are not subject to any exception to litigation privilege.

[44] The defendant is awarded costs in the matter in the amount of $1,000.

Campbell, J.