BCICAC File No. DCA-1695

IN THE MATTER OF AN ARBITRATION PURSUANT TO
an insurance policy numbered B0753PG1301038000

BETWEEN:

FRASER CEDAR PRODUCTS LTD.

Claimant

AND:

LLOYD'S UNDERWRITERS

Defendant

INTERIM AWARD IN THE ARBITRATION PROCEEDING

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This is Exhibit" I " referred to in the affidavit of Liz Takata sworn before me at Vancouver this 13 day of September 2016

A COMMISSIONER FOR TAKING AFFIDAVITS FOR BRITISH COLUMBIA

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PART A

THE CLAIMANT'S APPLICATIONS

I. INTRODUCTION

1. The Claimant owns and operates a specialty lumber mill at Maple Ridge, BC. Since about December 2011 the Defendant has insured the mill against the risk of physical loss or damage, *inter alia*, under an all risks insurance policy numbered B0753PG1301038000 ("the Policy"). The policy was renewed from year to year for one year terms, and was renewed effective November 1, 2013.

2. On 25 October 2014, a fire occurred at the mill which destroyed a large part of it. The Defendant has denied liability to indemnify the Claimant for the loss.

3. The Policy contains an arbitration clause as follows:

> ***18. Arbitration***
>
> ...
>
> *C. Arbitration. As a condition precedent to any right of action hereunder, in the event that a good faith effort to mediate pursuant to Clause 18(B) above cannot resolve a dispute between any Insured and the Insurer hereunder involving this Policy, it is hereby mutually agreed that such dispute shall be determined by final and binding arbitration before a single arbitrator under the provisions of the provincial Arbitration Act currently in force in the jurisdiction of the Named Insured's principal address indicated in item 2 of the Schedule. If the parties cannot mutually select the arbitrator, the parties will refer the selection of the arbitrator to the final chapter of the ADR Institute of Canada Inc. operating in the jurisdiction of the applicable Arbitration Act.*

4. The Claimant has commenced these arbitration proceedings pursuant to that provision. Mediation was attempted, and proved to be unsuccessful.

5. The parties, by their counsel, have agreed to my appointment as sole arbitrator.

6. By virtue of the Arbitration clause, the Arbitration is to be conducted under the provisions of the *Arbitration Act*, R.S.B.C. 1996, c.55 (the "*Act*").

7. Pursuant to Section 22 of the *Act*, the Arbitration is subject to the Rules of the B.C. International Commercial Arbitration Centre ("BCICAC"), which in a case such as this are the "Domestic Rules". The Rules govern the conduct of the Arbitration proceedings. Rule 29

confers jurisdiction on the Arbitration Tribunal to make a broad range of orders, including the making of interim orders and awards.

8. Both parties have made applications under the provisions of those Rules for a variety of interim relief, pending the hearing of the Arbitration proper, which is set to commence in October 2016.

9. While the Defendant acknowledges the Arbitrator's jurisdiction under the Rules to make partial awards or interim awards, it emphasizes that principals of equality and fairness are critical to the arbitration process.

10. As to the Arbitrator's discretion to grant the Claimant's applications to strike pleadings, or summarily dismiss defences as pleaded, the defendant submits that the applications should be decided in accordance with the tests applicable under the B.C. Supreme Court Rules.

11. For applications to strike, this means that the "plain and obvious" test applies, and pleadings will only be struck if they are clearly without merit, or have no prospect of success. For applications to summarily dismiss pleadings, the test is whether it would be "unjust" to grant the relief sought, taking all relevant factors into account.

12. I agree with, and accept as applicable, the tests to be applied, as submitted by the Defendant, and with the legal foundation for doing so as set out in the Defendant's submission.

II. BACKGROUND OF THE CLAIM

13. About one year before the fire loss of 25 October 2014, which is the subject of the present claim, there was an earlier fire at the Claimant's mill on 30 November 2013. The Defendant denied coverage for the fire loss on 30 November 2013, and purported to void the Policy, alleging breach of, or non-compliance by the Claimant with, various terms or conditions of the Policy.

14. The Policy contained these provisions, relevant to these proceedings:

> *5. **Perils Insured***
>
> *This policy indemnifies against all-risks of direct physical loss or damage occurring during the policy period from any cause other than as hereinafter excluded.*

...

*20. **Permission***

Permission is hereby granted:

A. To alter and repair the Premises

B. To work all hours and for such use the Premises as is usual and incidental to the business and to keep and use all such appliances, articles and materials in such quantities as are usual, convenient or incidental to such business.

Endorsement #3

STATUTORY CONDITIONS
(British Columbia)

...

Material change in risk

4 (1) The insured must promptly give notice in writing to the insurer or its agent of a change that is

(a) material to the risk, and

(b) within the control and knowledge of the insured.

(2) If an insurer or its agent is not promptly notified of a change under subparagraph (1) of this condition, the contract is void as to the part affected by the change.

...

Endorsement #6
PROTECTIVE SAFEGUARD ENDORSEMENT

FAILURE TO COMPLY WITH THE PROTECTIVE SAFEGUARD CLAUSES SHALL SUSPEND THIS INSURANCE

PROTECTIVE SAFEGUARD CLAUSE(S)

In consideration of the premium at which this policy is written, based on the protection of the Premises by the protective safeguard system or systems indicated below, it is a condition of this policy that the insured shall exercise due diligence in maintaining in complete working order all Equipment and services pertaining to the system which are under the control of the insured, including any special maintenance or service requirements indicated below. It is also a condition of this insurance that the insured shall give immediate notice to their insurance agent of any impairment in or suspension of any Equipment or service pertaining to the system within the knowledge of the insured.

A. Automatic Sprinkler System.

In further consideration of the premium at which this policy is written, it is a condition of this policy that the insured shall have the automatic sprinkler system serviced by an independent contractor licensed to serve and maintain automatic

sprinkler systems in the state in which the Premises are located. It is also a condition of this policy that the insured shall have the automatic sprinkler system inspected and tested at least once per year by an independent contractor licensed to inspect and test automatic sprinkler systems in the state in which the Premises are located.

B. Automatic Fire Alarm, reporting to a public or private fire alarm station.

...

Endorsement #7
WARRANTY: HOT WORK ACTIVITIES

Definition: *Common work activities that involves the generation of flames, heat or sparks in any area where there is the potential for a fire or explosion to occur. This type of work normally involves but is not limited to the following:*

- *Welding*
- *Brazing*
- *Soldering or burning activities*
- *Cutting, pip thawing*
- *Torch-applied roofing or grinding activities*
- *Tar boiling*

Warranted that in respect of loss or damage caused by fire that:

1. ***Hot Work Permit form*** *to be used as attached (or similar)*

This permit applies to any type of 'hot work' carried out on the insured's premises whether by their own employees or by contractors.

Before ***any*** *person is allowed to commence any of the hot work activities as described above, a full and proper assessment of the hazards and risks associated with the area of work must be made by the person authorized to complete the Hot Work Permit form.*

The Hot Work Permit details additional precautions that need to be taken in the case of this type of work. The authorized person (Fire-safety Supervisor) should complete the permit and ensure that the person accepting it fully understands it.

In all cases of Hot Work a 'Fire-watch' must be appointed and named on the Hot Work Permit.

The Insured, whether by their own employees or by contracts, shall maintain a fire watch in accordance with the requirements of the relevant provincial Fire Code.

It is a Condition Precedent to the liability of the insurers that these procedures are in place and enforced at all times. Should a loss arise due to the failure of the insured to abide by this warranty, then any claim resulting from the loss will be void.

15. On or about 12 March 2014 the Defendant gave notice that it would deny coverage for the November 2013 fire loss. By its London claims service, Catlin Risk Solutions Ltd. ("Catlin"), it advised the Claimant that the Claimant was likely in breach of Endorsement #7, the Hot Works Warranty, and Endorsement #3 (Statutory Condition #4), requiring prompt notice in writing of any material change in the risk. These assertions were based upon the report of a fire investigator.

16. There followed a series of communications between various parties, including a visit by the Claimant's Vancouver insurance broker, Jason Fogal of Axis Insurance Managers Inc. ("Axis"), to Lloyd and Partners ("Lloyds"), (Fogal's "placing broker" in London), and email exchanges between Axis, Catlin, Lloyds and Maxwell Claims Services Inc. ("Maxwell"), the Defendant's insurance adjuster in Vancouver. These exchanges led to a draft Settlement Agreement.

17. On April 8, 2014, Catlin, the lead underwriter for Lloyds advised Torus, another underwriter of information relating to one clause of the draft:

> *Just spoken [sic] to Francis at Lloyd & Partners. The only other potential issue is clause 5 – the client is looking at their options because having an "external" qualified contractor may cause problems when they need work done at short notice. Apparently they are investigating whether they can get one of their own guys set up as an external company with appropriate insurance to do the work – if so, they will be able to agree clause 5, if not they will come back with a proposed alternative.* (emphasis added)

18. This email appears to reflect the discussions which took place between the Claimant and its broker, Mr. Fogal, as to how the Claimant could agree to the proposed requirement for an "external" welding contractor, and at the same time meet its own need for access to welding services, on short notice, and on a daily basis.

19. On April 10, 2014, Francis Maloney of Lloyds attached to an email to Mr. Fogal the approved wording for the new Endorsement #31. (The attachment appears on its face to have been approved by the "leading insurer" on "10/4/14" – (April 10, 2014)).

20. Endorsement #31 reads:

Endorsement #31

THIRD PARTY WELDING WARRANTY

In conjunction with endorsement 7 "Warranty: HotWorks Activities" it is warranted that any hot works as defined in endorsement 7 are only to be carried out by a qualified third party contractor, who must carry at least CAD 5,000,000 of liability insurance.

The third party welder must adhere to the conditions of endorsement 7.

It is a Condition Precedent to the liability of the insurers that these procedures are in place and enforced at all times. Should a loss arise due to the failure of the insured to abide by this warranty, then any claim resulting from the loss will be void.

All other terms and conditions remain unchanged. (emphasis added)

21. The Claimant agreed to the wording of Endorsement #31, and Mr. Fogal conveyed that agreement to Lloyds on April 11, 2014.

22. On the same date, the parties entered into a Settlement Agreement.

23. It provided for payment by the Defendant to the Claimant of CDN $1.5 million for the fire loss of November 2013. Significantly, for the purposes of the present claim, it also included this:

> *5. **The Policy**. The Insured warrants that it is not aware of any circumstances or occurrences which would give rise to a claim on the Policy which took place in the period between 10 March 2014 and the date hereof. Underwriters agree that they will withdraw the letter voiding the Policy dated 10 March 2014 and they shall be deemed to have been on risk at all times since inception pursuant to the terms of the Policy. The Policy shall remain in effect, subject to the Policy's terms and conditions, until 1 November 2014, at 00:01 local standard time at the location of the Property. The Policy will include an additional endorsement, the precise wording of which is to be agreed, which will require future hot works on the Property to be conducted by an appropriately qualified external contractor carrying liability insurance of at least Cnd $5,000,000.00 (the "Hot Works Endorsement"). The Insured will agree to and consents to the addition of the Hot Works Endorsement to the Policy.* (emphasis added)

24. At the time the terms of the Settlement Agreement were being discussed, the Claimant entered into a contract with Shellborn Maintenance ("Shellborn") as its "third party contractor" for "HotWorks". The Claimant laid off its millwright, Bobby Grewal, who had previously done the welding at the Claimant's mill, and arranged for him to be hired by Shellborn. Shellborn, in turn, assigned Mr. Grewal to work as the Claimant's millwright on a daily basis.

25. At the same time, Shellborn obtained a liability insurance policy for CDN $5,000,000.00, as stipulated in Endorsement #31. The Claimant paid the premium for that policy.

26. As provided for in the Settlement Agreement, the Defendant's policy of insurance covering the Claimant was reinstated.

27. On the evening of 25 October 2014, the subject fire occurred at the Claimant's mill. Earlier in the day, the mill had been closed for cleanup, and Mr. Grewal performed welding work to effect certain repairs to equipment. During the day the sprinkler lines had been damaged when Mr. Grewal was operating a front end loader. The Claimant notified its broker, Axis, who in turn notified Lloyd's.

28. The Claimant made a claim on its policy for the fire loss of October 2014. Defendants, via the adjuster Maxwell, denied the claim by letter of February 4, 2015. The Claimant by its legal counsel responded to the denial by letter of 19 March 2015.

29. Mediation on October 5, 2015 did not achieve settlement, as noted above.

III. APPLICABILITY OF *CONTRA PROFERENTUM*

30. Fundamental to the Defendant's position in this Arbitration is its assertion that any ambiguity in either Endorsement #31 or the Settlement Agreement should be construed in its favour. It bases this position on the proposition that Lloyds drafted Endorsement #31 and the Settlement Agreement and that in doing so Lloyds was acting on the Claimant's behalf as its agent.

31. The Defendant says that when insurance brokers approach Lloyds Underwriters to negotiate and place risks, they do so as agents of the insureds, and not as agents of the underwriters.

32. The Defendant says the documents before me on these applications show that the wording of both the policy and the endorsements were drafted by Lloyds, and it is therefore not open to the Claimant to argue that the Defendant should have insisted upon different language if, for example, the Defendant wanted to exclude Mr. Grewal from the mill, or required welding to be done only by certified or licensed welders.

33. I will leave aside for the moment the question of whether there is any ambiguity in either Endorsement #31 or the Settlement Agreement, and address that later in dealing with the specific language of the Settlement Agreement and the endorsement that may be in issue.

34. In my opinion, however, it is not open to the Defendant to argue that any doubts as to the meaning of the words used should be construed against the Claimant.

35. In its reply of June 20, 2016, to the Claimant's application, counsel for the Defendant admitted that Endorsement #31 and the Settlement Agreement were drafted by the lead underwriter, Catlin. The reply reads in part:

> *12.h. Lloyd's told Lloyd & Partners, the Insured's agent, that Lloyd's would only reinstate the Policy and settle the claim if the Insured would agree that the Policy would be amended to require that any future welding at the Mill would be performed by a qualified third party contractor carrying $5.0m. in liability insurance. Lloyd's communicated this position during telephone calls and meetings with Lloyd & Partners.*
>
> ...
>
> *28.a. On March 25, 2014, Catlin met with Lloyd & Partners to discuss the Insured's request that Lloyd's withdraw the March 10, 2014 letter voiding the Policy, and negotiate a monetary settlement of the first loss. During that meeting Catlin told Lloyd & Partners that the syndicates on risk would only consider reinstating the Policy if any and all future welding was done by external contractors as opposed to the Insured's staff. The wording that was put to Lloyd's & Partners was that "... future hot works will be carried out by a qualified external contractor carrying suitable cover."*
>
> ...
>
> *f. By April 4, 2014, Catlin had told Lloyd & Partners that the wording for Clause 5 would have to read "... an appropriately qualified external contractor..." would do the welding.*

36. These are assertions of fact which the Defendant says it will prove in this Arbitration.

37. When these assertions are read in conjunction with the communications referred to above in Part II, it is clear that the critical wording of Endorsement #31 was stipulated by the Defendant's lead underwriter, Catlin. Lloyds may have assisted in drafting or preparing Endorsement #31, but the content of that endorsement was directed by the Defendant's lead insurer.

38. Whether Lloyds owed any duties to the Claimant as the "placing broker" in London for Axis, it clearly presented the offer of coverage, including Endorsement #31, on behalf of the Defendant underwriters.

39. There is nothing before me to suggest that either the Claimant, or its Vancouver broker, Axis, had anything to do with drafting any part of either the Settlement Agreement or the Policy.

40. It follows that the Defendants purported reliance on the doctrine of *contra proferentum* is completely unfounded. The policy language was put forth by the Defendant underwriters and accepted by the Claimant. In the event of any ambiguity, coverage provisions are to be read broadly, and exclusions narrowly, with any ambiguity or uncertainty to be resolved in the Claimant's favour.

IV. THE CLAIMANT'S APPLICATION TO STRIKE OR SUMMARILY DISMISS

41. By its Statement of Defence filed 23 October 2015, the Defendants allege the election to void the October 2014 fire loss claim is based upon:

(a) The Claimant's breach of Endorsement #31 and Endorsement #7, the "HotWorks Warranty" (paras. 52-60 of the Defence);

(b) The Claimant's failure to comply with the requirements of Endorsement #7 (paras. 61-64);

(c) The Claimant's breach of the Settlement Agreement, Endorsement #31, Statutory Condition #4, and the duty of honest contractual performance (paras. 65-69);

(d) Material change in circumstances – Statutory Condition #4 and Endorsement #6, "Protective Safeguard Endorsements re Automatic Fire Alarm" (paras. 70-78).

42. The Claimant now applies for orders that:

(a) the defence of 'dishonest contractual performance' does not apply to the Policy and its Endorsements as drafted, or on the facts as pleaded;

(b) in the alternative, the defence of dishonest contractual performance does not apply in relation to Endorsement #31 based on the facts disclosed in the Fraser Cedar's own Underwriting File documents;

(c) evidence of the parties' subjective intentions regarding the purpose of Endorsements #7 and #31 is irrelevant and therefore inadmissible;

(d) Endorsements #6, #7 and #31, as drafted, are not conditions precedent to coverage under the Policy;

(e) in order for Lloyds to avoid coverage under Endorsements #7 and #31, it must prove that any alleged breach of the same caused the subject 2014 loss;

(f) the Statement of Defence discloses no breach of Statutory Condition 4, under Endorsement #3; and

(g) Lloyds in not entitled to rely upon the 2013 (sic) **"Settlement Agreement"** to avoid coverage for such Loss.

43. I will address each in turn.

V. DISHONEST CONTRACTUAL PERFORMANCE

44. The Claimant says that this defence, as alleged in paras. 66-69 of the Defence, discloses no independent defence that is distinct from the various policy breaches relied upon by the Defendant. The Claimant says that this defence is simply repetitive of the defences raised in paras. 18-30, 53-56, and 38.

45. At the heart of those defences are allegations that:

1) Mr. Grewal was untrained, unqualified, and unlicensed, could not read English, and did not understand the requirements of the fire code; and

2) the Claimant was also dishonest by failing to notify the broker of HotWorks at the mill on the day of the fire contrary to Endorsement #3, Statutory Condition #4 (para. 67 of the Defence).

46. Those allegations found the Defendant's position that the Claimant was in breach of Endorsement #31 by permitting an unqualified welder to perform its HotWorks on a regular basis, as pleaded in paras. 53-56 of the Defence.

47. Those appear to be the same allegations relied upon in support of the defence of dishonest contractual performance in paras. 66-69.

48. The Defendant's response to this aspect of the Claimant's application is set out at length in paragraphs 51-76 of its submission. It says the duty of honest contractual performance requires parties to perform agreements in good faith (para. 52(b)); and that misleading conduct is

prohibited (para. 54). The Defendant says further that defences based on good faith contractual performance should not be struck at the pleadings stage (para. 59); and that "novel issues" concerning the scope of the contractual duty of honest contractual performance should be determined on a full evidentiary record.

49. Here, the Defendant says the Claimant's failure to disclose Mr. Grewal's continued operations at the mill was a breach of its duty of honest contractual performance, and that this is a separate defence from the other defences based on breach of contract.

50. The Defendant says that "keeping Mr. Grewal away from future hot works in the mill" was the contractual benefit Defendant underwriters had bargained for (para. 63). The Defendant says that "it only agreed to reinstate the Policy after the first fire on the understanding that Mr. Grewal would no longer be performing welding at the mill (para. 66). The Defendant says that whether the Claimant was entitled not to disclose that Mr. Grewal would continue welding, should be determined on a full evidentiary record, and not decided on an application to strike the pleadings.

51. The Claimant's contractual obligations under Clause 5 of the Settlement Agreement were to:

> *Agree and consent to an additional endorsement requiring future HotWorks to be conducted by an appropriately qualified external contractor; and that such external contractor carry liability insurance of $5,000,000.00.*

52. Those duties are fulfilled by the plain language of Endorsement #31 as accepted by the Claimant. I do not see how any alleged "dishonest contractual performance" can constitute a defence with respect to the Settlement Agreement.

53. The Claimant's contractual duty under Endorsement #31 is to have HotWorks carried only by a "qualified third party contractor". The Defendant now argues that the duty of honest contractual performance required the Claimant to tell Defendant underwriters at the time the Settlement Agreement and Endorsement #31 were being negotiated that Mr. Grewal would continue to do the HotWorks at its mill.

54. With respect, I do not consider this position to be tenable. It is effectively an attempt to modify the requirements of Endorsement #31 so as to impose on the Claimant additional duties that are not reflected in the wording of the endorsement.

55. It would appear that the Defendant by this strategy attempts to import into the endorsement the "contractual benefit it bargained for" (as per the Defence submission para. 53); or "its understanding" that Mr. Grewal would no longer be performing welding at the mill (para. 66). In this way, the Defendant attempts to make relevant and admissible its subjective intentions, which are not otherwise admissible in the interpretation of contracts.

56. I agree with the Claimant's submission that paragraphs 66-69 do not raise any defence that is independent of the defence that the Claimant was in breach of Endorsement #31 or Statutory Condition #4.

57. The Claimant's obligations to the Defendant are simply those set out in the Settlement Agreement, as superseded by the reinstated policy. The Defendant cannot graft onto, or infer from, those contractual duties any other general duty as pleaded in paras. 66-69. It would be unjust to do so.

58. I would therefore grant the Claimant an order, as summary dismissal, as sought that:

a) the defence of 'dishonest contractual performance' does not apply to the Policy and its Endorsements as drafted, or on the facts as pleaded.

59. Paragraphs 66-69 of the Statement of Defence are accordingly struck out.

VI. THE PLEA OF THE CLAIMANT'S DISHONEST PERFORMANCE IN RELATION TO ENDORSEMENT #31

60. The Defendant pleads in paragraphs 52-60 of its Defence, that the Claimant was in breach of Endorsement #31 and Endorsement #7 by permitting Mr. Grewal to continue as welder at its mill when it knew that Mr. Grewal was not qualified nor licensed (paras. 30 and 55), and that neither Mr. Grewal nor his employer Shellborn had adhered to the requirements of Endorsement #7 – The HotWorks Warranty. The Defendant says it did not know that Mr. Grewal would continue to do HotWorks at the mill prior to the loss.

61. As to the requirement of Endorsement #31 that any HotWorks be carried out by a "qualified third party contractor", Mr. Grewal's qualifications are not relevant. The third party contractor was Shellborn, which had been in business for many years preceding its contract with the Claimant, and which employed a number of welders, some of whom are licensed, and others not. In alleging that Mr. Grewal was not qualified (whether he was or not), the Defendant cannot show a breach of Endorsement #31, because Mr. Grewal was not the third party contractor.

62. There is nothing in the material before me to show that Shellborn was not a qualified third party contractor. There is nothing before me as to the meaning of the word "qualified" in this context. What qualified means, and whether Shellborn meets that definition, are matters upon which evidence may be adduced.

63. Moreover, Endorsement #31 does not require that the "third party contractor" employ only licensed or ticketed welders to perform HotWorks at the mill. It requires only that "the third party welder must adhere to the conditions of endorsement 7."

64. Paragraph 55 of the Defence repeats paragraph 30, and says that the Claimant knew that Mr. Grewal was "not a qualified welder". In its submission it says that the Claimant has not shown that the Defendant knew or agreed to Mr. Grewal continuing as the welder in the mill.

65. The essence of the Defendant's complaint concerning the breach of Endorsement #31 is that Mr. Grewal continued to do welding work at the mill. But that is not what Endorsement #31 precludes. If the Defendant did not want Mr. Grewal, or any other of the Claimant's employees, to go to work for the third party contractor, it should have stipulated for wording to that effect.

66. I would therefore summarily dismiss as irrelevant the allegation in paragraph 30(a) that Mr. Grewal was untrained, unqualified and unlicensed.

67. I would also summarily dismiss the allegations in paragraphs 55 and 56 that Mr. Grewal was unqualified and that the Claimant knew or ought to have known of that.

68. In its submission, the Claimant makes an extensive argument that the Defendant is estopped from raising, or has waived, the right to deny coverage under Endorsement #31, on the basis that Mr. Grewal did not have a welding ticket, was not formally trained, or was otherwise

precluded from conducting HotWorks at the mill, because the Defendant knew of all those matters in advance. (See the Claimant's submission at paras. 77-79.)

69. In its response, the Defendant submits that it did not know or agree to the Claimant's continuing use of Mr. Grewal as welder. (See the Defendant's submission at paras. 78-81.)

70. However, the issues of waiver and estoppel are not before me on the Claimant's application to strike pleadings or summarily dismiss defences.

71. Waiver and estoppel are only raised by the Claimant in its reply (at paras. 12 and 16-18). The Defence has made no application to strike those pleadings, nor any others.

72. I therefore decline to address the issue of whether the Defendant waived, or is estopped from, denying coverage under Endorsement #31 on the basis that Mr. Grewal was not licensed, trained or qualified, and that the Defendant knew of those matters when the Policy was renewed.

73. The second requirement of Endorsement #31 is that the third party contractor carry liability insurance of $5,000,000.00. It is not in dispute that at the time of this loss, Shellborn did have such liability coverage in place.

74. The third requirement of Endorsement #31 is that the "third party welder" must "adhere to the requirements of the HotWorks Warranty-Endorsement #7". This Endorsement requires completion of a "HotWorks Permit" by an authorized person before any HotWorks activities are undertaken; the appointment of a "fire watch" to be named in the permit; and the maintenance of a fire watch in compliance with the Provincial Fire Code.

75. Whether the Claimant was in breach of any of the requirements of Endorsement #7 raises questions of fact that the Claimant does not seek to resolve on this application.

76. It remains open to the defence to allege that Mr. Grewal, as the third party welder, failed to adhere to the requirements of Endorsement #7, as alleged in paragraph 53(c) and paragraphs 57-59.

77. Other questions raised concerning Endorsement #7 in conjunction with Endorsement #31, are whether evidence as to the parties' subjective intentions is admissible in the interpretation of those provisions; whether Endorsements #7 and #31 (as well as Endorsement #6) are conditions

precedent to coverage; and whether the wording of Endorsements #7 and #31 require the Defendant to prove that any breach of same caused the October 2014 fire loss. I turn to those matters now.

VII. THE PARTIES' SUBJECTIVE INTENTIONS CONCERNING ENDORSEMENT #7 AND ENDORSEMENT #31

78. Paragraph 10 of the Defendant's Statement of Defence pleads:

> *10. Endorsement #7 is the Policy's Hot Work Activities warranty. Its purpose is to reduce the risk of a fire by ensuring that Hot Works are carried out only by "people trained in use of equipment, hazards and precautions to prevent fires" when Hot Works Activities are undertaken.* (emphasis added)

79. Paragraph 52 of the Statement of Defence pleads:

> *52. The Defendant repeats and relies on paragraphs 25-28 of the Statement of Defence and submits that Endorsement #31 was added to the Policy to manage the risk posed by having unqualified welders carry out Hot Work Activities..* (emphasis added)

80. In its Reply, the Claimant says that evidence as to the purpose or subjective intention behind the endorsements is irrelevant to interpreting the words used in the Policy.

81. The Defendant amplified the suggested relevance of its subjective intentions in its June 17, 2016 Reply to the Claimant's application, at paragraphs 12(n), 15, and 40-42.

82. In its submission of June 30, 2016, the Defendant says (at paras. 164-172) the evidence it will seek to adduce is evidence of the parties' common understanding as to the purpose of Endorsements #7 and #31, and not simply its own subjective intention. It says evidence of the circumstances surrounding negotiations for the Settlement Agreement, and the inclusion of Endorsement #31 in the Policy, can assist in interpreting the words such as "qualified third party contractor" and "third party welder".

83. As discussed earlier under Part 5 (concerning the Defence paragraphs 66-69) evidence of the Defendant's subjective intention is generally not admissible.

84. I take it as settled law that evidence of a party's subjective intention is only admissible if there is ambiguity in the language of the contract:

> *The contractual intent of the parties is to be determined by reference to the words they used in drafting the document, possibly read in light of the surrounding circumstances which were prevalent at the time. Evidence of one party's subjective intention has no independent place in this determination.*
>
> *Eli Lilly v. Novopharm,* 1988 CanLII 791 (SCC)

85. However, as indicated in Part 6 above, it is not clear what the words "qualified third party contractor" mean, nor whether Shellborn satisfies that criteria. Similarly, the meaning of the words "third party welder" in Endorsement #31 must be read and understood in the context of the endorsement as a whole. To the extent that extrinsic evidence of the surrounding circumstances may shed light on those matters, it may be admissible in the Arbitration.

86. But evidence as to the intent or purpose of either party for the choice of language used in the Policy cannot be admitted. Paragraphs 10 and 52 of the Defence as pleaded are essentially statements of the Defendant's purpose or intent.

87. I would order that paragraphs 10 and 52 of the Statement of Defence be struck out.

VIII. WHETHER ENDORSEMENTS #6, #7 AND #31 ARE "CONDITIONS PRECEDENT" TO COVERAGE (See the Claimant's submissions at paragraph 98-103 and the Defendant's submission at 82-102)

88. The Claimant applies to strike, or summarily dismiss, the defences under Endorsements #7 and #31, as contained in paragraphs 17, 26, 43, 54-63, and 71-74 of the Statement of Defence.

89. As to Endorsements #7 and #31, the Claimant's Reply (see paragraphs 3, 6, 7, 10 and 11), says that the last sentences of both Endorsement #7 and Endorsement #31 qualify their preceding language, which might otherwise be construed as "conditions precedent".

90. The last two sentences of Endorsement #7 read:

> ***It is a Condition Precedent to the liability of the insurers that these procedures are in place and enforced at all times. Should a loss arise due to the failure of the insured to abide by this warranty, then any claim resulting from the loss will be void.***

91. The last two sentences of Endorsement #31 read:

> *It is a Condition Precedent to the liability of the insurers that these procedures are in place and enforced at all times. Should a loss arise due to the failure of the insured to abide by this warranty, then any claim resulting from the loss will be void.*

92. As to Endorsement #6, the Protective Safeguard Endorsement, it says in its opening words:

> *FAILURE TO COMPLY WITH THE PROTECTIVE SAFEGUARD CLAUSES SHALL SUSPEND THIS INSURANCE.*
>
> ...
>
> *... it is a condition of this policy that the Insured shall exercise due diligence...*

93. Heading A, Automatic Sprinkler System, of Endorsement #6 says: "...it is a condition of this policy that the insured shall have ..."

94. I will address Endorsement #6 first. By paragraph 17 of the Statement of Defence, the Defendants purport to quote Endorsement #6 as reading "... it is a condition precedent of this policy ..." (emphasis added).

95. As noted above, Endorsement #6 does not say that its provisions are a condition "precedent", but simply that its terms are a "condition" of the Policy.

96. Paragraph 17 of the Statement of Defence is a misquote of the Endorsement, and should be struck out. Whether the Claimant complied with the provisions of Endorsement #6 raises questions of fact that cannot be determined on this application. Whether the Claimant's non-compliance with Endorsement #6, if proven, "suspends" the insurance, as stated in the opening words of the endorsement, and what that wording means, are questions to be resolved if it should be shown that the Claimant was in fact non-compliant with Endorsement #6.

97. With respect to Endorsements #7 and #31, the Defendant says they are true conditions precedent, and it does not have to prove a causal connection between the breach of same and the loss as claimed by the Claimant.

98. Alternatively, the Defendant says it is entitled to void the Policy if the Claimant's breach of the provisions "materially increased" the risk of the loss suffered and it argues that any ambiguity is to be construed against the Claimant (para. 90).

99. With respect to the final two sentences of both Endorsements #7 and #31, the Defendant says they do not alter the result. In context, they simply mean that if the Claimant fails to

comply with their terms then any claim from the resulting loss is void (Defence submission para. 103).

100. Alternatively, the Defendant says the two endorsements are "promissory warranties" and that if a breach of their terms materially increased the risk, the Defence was justified in voiding the claim or Policy, whether the breach actually caused the loss or not.

101. The Defendant says its defences premised upon breaches of Endorsements #7 and #31 should not be struck out, or summarily dismissed, because whether there was a breach of their terms requires factual and opinion evidence.

102. Endorsements #7 and #31 are not, in my opinion, on their plain wording, true conditions precedent. The last sentence of both endorsements transforms each into cause-based exclusion clauses. The words: "...should a loss arise due to the failure of the Insured ... then any claim resulting ...", in both endorsements clearly show an intention that non-compliance with their provisions will only void claims if that non-compliance caused the loss in question.

103. If these provisions were true conditions precedent, non-compliance would result in any claim being void, regardless of whether it caused the loss or not. That is clearly not the intention expressed in the wording of these two endorsements.

104. In further answer to the Defendants' allegations that Endorsement #7 and #31 are conditions precedent, the Claimant by its Reply in paragraphs 6, 7, 10, and 11 says the Defendant has admitted that a breach of such endorsement must be causative of the loss, before the Defendant can deny liability; and has thereby waived, or is estopped, from relying on them absent proof of causation. These pleas appear to be well founded, but given my conclusion based on the plain language used, it is unnecessary to decide the questions of waiver or estoppel.

105. I conclude that none of Endorsements #6, #7, and #31 are conditions precedent, and order that such defence as pleaded in paragraphs 17, 26, 43, 54-63, and 71-74 of the Statement of Defence be summarily dismissed.

IX. DOES LLOYD'S HAVE TO PROVE THAT BREACH OF ENDORSEMENTS #7 AND #31 CAUSED THE FIRE LOSS OF OCTOBER 2014?

106. The Claimant applies to strike out paragraphs 48, 49, 55-64, and 77 of the Statement of Defence on the grounds set out in its Reply at paragraphs 13, 36-40, and 42.

107. The impugned paragraphs of the Defence allege that Claimant's failure to meet the requirements of the endorsements "enhance", "materially enhanced", "materially increased" the risk of, or "contributed to" the October 2014 fire. The Claimant says that the defences as pleaded do not allege any causal connection between the Claimant's alleged breaches of the endorsements and the loss, and the Claimant says such breaches as are alleged cannot be proven to have caused the fire (Claimant submissions paras. 125-128).

108. In its Reply to the Claimant's application, the Defendant says that the issue of causation cannot be properly addressed at this time. As noted above, it says it will lead factual and opinion evidence to show that it was the Claimant's acts or omissions that caused the fire; and that its conduct constituted the breaches of Endorsements #6, #7, and #31 on which it relies.

109. As indicated under Part VI above, whether the Claimant was in breach of any of the requirements of Endorsement #7 are questions of fact, as are the alleged breaches of Endorsements #6 and #31. Similarly, whether any such breaches in fact "caused" the loss, are also questions of fact.

110. At paragraph 130 of its Submission, the Claimant agrees that such factual questions of breach or causation cannot be decided summarily. But it says the Defence does not plead any causal connection between the loss and any alleged lack of welding qualifications by either Shellborn or Mr. Grewal (Claimant's submission at para. 126(a)), and the Claimant says that as Shellborn was the "third party contractor", only its qualifications and not Mr. Grewal's are relevant for purposes of compliance with Endorsement #31.

111. I respectfully agree.

112. As noted above, whether Mr. Grewal had a welding ticket or certificate, or other qualification, is irrelevant to the question of whether the Claimant was in breach of the requirements in Endorsement #31 for a "qualified third party contractor".

113. Other factual issues relevant to Endorsements #7 and #31, such as the time of Mr. Grewal's welding operations, and the time of their conclusion; the presence or absence of a fire watch, and whether absence of a fire watch caused the fire are questions of fact which should be addressed by evidence.

114. I conclude that Endorsements #7 and #31 require proof of causation between any alleged breach of their provisions, and the loss of October 2014, which is the subject of this claim. The defences pleaded in paragraphs 48, 49, 55-64 and 77 that non-compliance with the terms of Endorsement #7 and #31 "enhance", "materially enhanced", "materially increased" the risk of, or "contributed to" the subject fire are struck out.

115. What the defence must prove in order to successfully defend this claim is that the Claimant's breach of any provision of Endorsement #7 or #31 caused the loss.

X. MATERIAL CHANGE IN RISK UNDER STATUTORY CONDITION #4 (ENDORSEMENT #3)

116. At paragraphs 70-78 of its Statement of Defence, the Defendant pleads that in addition to constituting a breach of Endorsement #6 (the Protective Safeguard Endorsement), the disabling of the sprinkler system as a result of the front end loader accident on the day of the fire, and the impairment of the automatic fire alarm due to two faulty pressure switches which had not been replaced, those circumstances also constituted a material change in the risk, requiring the Claimant to give prompt notice to its insurer or agent.

117. The Claimant applies to strike out the defence pleaded under Endorsement #3, Statutory Condition #4, on the basis that:

1) there is no independent defence of material change in risk under Condition 4, absent a breach of Endorsement #6 (see para. 26 of the Claimant's Reply);

2) Endorsement #6 requires an "automatic fire alarm" and not an "automatic sprinkler alarm"; and the former does not include the latter;

3) the fact that the automatic fire alarm was not in complete working order, if proven, is not a material change to the risk unless in addition there is proof that the Claimant had knowledge of, and failed to give immediate notice of, the

alleged impairment; the defence as pleaded in paragraph 76 is therefore derivative, and dependent upon proof of both the Claimant's knowledge and its failure to give immediate notice, as alleged in paragraphs 72-75 of the Defence;

4) it is the specific provisions of Endorsement #6 which govern the Claimant's obligation to disclose any impairment in the automatic fire alarm system, and not the more general provisions of Endorsement #3, Statutory Condition #4.

118. The Defendant's response to the application to strike the defence under Endorsement #3, Statutory Condition #4, is that it imposes a separate and distinct obligation on the Claimant from that imposed by Endorsement #6, even if the two provisions are somewhat overlapping.

119. The extent, if any, to which either Statutory Condition #4 or Endorsement #6 may afford the Defendant a defence, depends upon findings of fact which cannot properly be made at this time. I would refuse the Claimant's application to strike out the defence under Statutory Condition #4 at this time, leaving it open to the parties to address the matter further in the arbitration proceedings.

XI. CAN THE DEFENDANT RELY ON THE SETTLEMENT AGREEMENT OF APRIL 14 TO AVOID COVERAGE?

120. Clause 5 of the Settlement Agreement contained this:

> *5. **The Policy**. ... The Policy will include an additional endorsement, the precise wording of which is to be agreed, which will require future hot works on the Property to be conducted by an appropriately qualified external contractor carrying liability insurance of at least Cnd $5,000,000.00 (the "Hot Works Endorsement"). The Insured will agree to and consents to the addition of the Hot Works Endorsement to the Policy.*

121. The Defendant pleads this provision at paragraph 25 of its Defence, and alleges that the Claimant was in breach of its provisions at paragraphs 66-69 of the Defence.

122. In applying to strike these defences, the Claimant says the Settlement Agreement was a "mere agreement to agree", which has been superseded by the inclusion of Endorsement #31 in the reinstated Policy.

123. I agree. The terms of Clause 5 were satisfied by the amended Policy, and no further obligation on the Claimant arises under Clause 5. I would order that paragraphs 66-69 be amended to remove any allegations based on Clause 5 of the Settlement Agreement.

XII. SUMMARY

124. To summarize my conclusions on the Claimant's applications to strike or summarily dismiss:

1) The defence of "dishonest contractual performance" as pleaded in paragraphs 66-69 of the Defence is struck out;

2) The defence that Mr. Grewal was untrained, unlicensed, or unqualified as pleaded in paragraph 30(a) of the Defence is struck out;

3) The defence that Mr. Grewal was unqualified, and that the Claimant ought to have known that, as pleaded in paragraphs 55-56 of the Defence is struck out;

4) Allegations of subjective intent as pleaded in paragraphs 10 and 52 of the Defence are struck out;

5) Allegations that Endorsements #6, #7, and #31 are conditions precedent, as pleaded in paragraphs 17, 26, 43, 54-63, and 71-74 of the Defence, are summarily dismissed;

6) The defences as pleaded in paragraphs 48, 49, 55-64, and 77 that non-compliance with the terms of Endorsements #7 and #31 "enhance", "materially enhance", "materially increase" the risk of, "or contributed to" the subject fire are struck out. Causation must be proven;

7) A decision on whether Statutory Condition #4 provides the Defendant with a separate defence from Endorsement #6 is deferred for the time being;

8) The defence that the Claimant was in breach of Clause 5 of the Settlement Agreement as pleaded in paragraphs 66-69 of the Defence is struck out.

125. The parties are at liberty to amend their pleadings accordingly.

126. What remains in issue, is the meaning of the word "qualified" in Endorsement #31, as it modifies "third party contractor", and whether Shellborn satisfies that criteria.

127. As well, there remain issues of whether the Claimant was in breach of any of the requirements of Endorsements #6, #7, and #31 and if so, whether such breach can be shown to have caused the loss for which the Claimant claims.

128. The burden of proving both breach and causation rests upon the defence.

Part B

DEFENDANT'S APPLICATIONS

129. The Defendant has brought three applications for determination prior to the hearing of this Arbitration.

I. ADMISSIBILITY OF RECORDINGS AND TRANSCRIPTS

130. The first application is for a ruling that recordings and interview transcripts of eight potential witnesses be found to be admissible. Transcripts of the recorded interviews of these eight people are exhibited to the Affidavit of Garry Daniels, the Defendant's adjuster. (The Defendant's application misstates the date of the Jason Fogal interview which appears to have taken place on December 3, 2014, and not on December 23, 2014 as set out in the application.)

131. The second part of the Defendant's first application is for a ruling that the evidence of "key witnesses" be adduced *viva voce* at the Arbitration Hearing, and subject to cross-examination.

132. As to the first part, the Defendant says that the recordings and transcripts have been sufficiently authenticated by Mr. Daniels' Affidavit and that they are admissible as real evidence.

133. As to the second part of this application, although the Defendant does not identify who the "key witnesses" may be, it appears they would be witnesses who could testify as to the circumstances leading up to the addition of Endorsement #31 to the Policy, and the "factual matrix" known to the parties at the time Endorsement #31 was negotiated.

134. The Claimant opposes both aspects of the Defendant's first application.

135. As to the admissibility of the recordings and transcript, the Claimant relies on BCICAC Rule 19 which provides for the "just, speedy and economical determination of the proceeding on its merits"; and Rule 26 which provides that, subject to direction from the Arbitration Communal, evidence of every witness shall be presented in written form, and received as direct evidence, and that those witnesses may be required to attend for cross-examination.

136. The Claimant says further that a ruling on the admission of this voluminous evidence should not be made until the issues for determination have been finalized. It questions the reliability of the interview transcripts, because the interviews were conducted without counsel, were not under oath, and many were translated by a person whose credentials as translator are unknown.

137. As to the Defendant's application concerning "key witnesses", the Claimant says questions concerning credibility are simply speculation at this point, that oral evidence will add significant costs to the Arbitration, and that a general ruling as to unidentified "key witnesses" is premature and unjustified.

138. As to the first part of this Application, I have read the eight transcripts exhibited to Mr. Daniels' Affidavit. I decline to order that the recordings and transcripts of the eight persons interviewed by Mr. Daniels be admitted. In my view, to grant this application would result in a most inefficient and unsatisfactory means of adducing evidence.

139. To the extent that the evidence of any of these persons may be relevant, and necessary to decide the issues which remain open as a result of my rulings on the Claimant's applications, that evidence should be presented as a clear and concise written statement from each witness. Such statements may be received as the direct evidence of that witness, in accordance with Rule 26. If a party considers it necessary, it may apply to cross examine the witness upon his written statement. It may be that parts of the interview transcripts or recordings referred to earlier, may be used for the purposes of such cross examination.

140. If a written statement is not presented as direct evidence of a witness, and a party opposing wishes to adduce the evidence of that person, it would be open to that party to call that person as a witness adverse in interest, and to cross examine him.

141. As to the second part of the Defendant's first application concerning the *viva voce* evidence of "key witnesses", I am again of the view that the least expensive and most expeditious way to adduce evidence is by means of written statements. As to evidence of the "factual matrix", known to the parties when Endorsement #31 was negotiated, my earlier rulings on the Claimant's applications will render such evidence irrelevant. The meaning of that endorsement is, in my view, plain and obvious on its face. What remains open for decision on

that, and the other Endorsements, is whether as a matter of fact the Claimant is in breach of any of their requirements, and if so, whether any such breach caused the loss.

142. I therefore dismiss both aspects of the Defendant's first application.

II. PRODUCTION OF SOLICITOR'S FILE

143. The Defendant's second application is for an order that the Claimant produce the entire unredacted file of its solicitor, Ian McKinnon, and that any claim for solicitor/client privilege over that file be set aside for the purposes of this arbitration.

144. The communications in issue are those between the Claimant and Mr. McKinnon in the period between March 24 and April 11, 2014, leading up to the Settlement Agreement on the latter date, and the drafting of Endorsement #31, which was added to the Policy as a result of that Agreement.

145. The Defendant says that by its pleadings the Claimant has placed its "state of mind" in issue. It says the Claimant received legal advice which helped form its state of mind, as a result of which privilege is deemed to be waived. It also says that the Claimant has further waived privilege by producing some of its communications with the solicitor. And finally, it says that privilege cannot attach to these communications, because they relate to unlawful conduct on the Claimant's part, namely breach of the terms of the Policy.

146. The Claimant opposes the Application for further production of privileged communications with its solicitor. It agrees that its state of mind is in issue in relation to Clause 5 of the Settlement Agreement, and the drafting of Endorsement #31, and says that it has already provided a limited waiver of privilege relating to communications on those matters.

147. There is nothing before me to support the Defendant's assertion that the Claimant has improperly selected ("cherry picked") those parts of the solicitor's file to be produced. In my view, solicitor/client communications that do not relate to Clause 5 of the Settlement Agreement, or Endorsement #31, continue to be protected by solicitor/client privilege. That privilege has not been waived, and the Defendant's application provides no basis for concluding otherwise.

148. I dismiss the Defendant's application for production of the solicitor's unredacted file, on the basis that it continues to be protected by solicitor/client privilege, except for those parts already produced.

III. PRODUCTION OF DOCUMENTS

149. The Defendant's third application is for an order compelling the Claimant to produce documents grouped under 11 headings. The first group comprised documents concerning the cost of or estimates for, repair or replacement of the mill. The second and third groups comprise correspondence or agreements with lenders concerning repair costs, or financing the repair, or the business. The remaining eight groups all appear to relate to documents that would be relevant to various heads of claim for business interruption losses.

150. The Claimant opposes the application for further production of documents on the basis that not all documents sought have been shown by the Defendant to be relevant and material.

151. In my opinion, whether any or all of the documents sought are relevant and material to the Claimant's claim, their production at this time is premature, and may well lead to unnecessary expense and delay. The matters that must be addressed in order to determine whether the Defendant is liable to provide indemnity under the Policy, are dealt with in the first part of this award, which addresses the Claimant's various claims for relief.

152. Once those issues have been addressed, and the basis for liability under the Policy, if any, established, one will be better able to decide what documents going to proof of damages must be produced. Requiring production of the documents sought, prior to a determination of liability, may well result in substantial unnecessary expense.

153. I would dismiss the Defendant's application to produce documents at this time, leaving open the possibility of a renewed application following a decision on liability.

INTERIM AWARD OF THE ARBITRATOR,
AT VANCOUVER, B.C., AUGUST 10, 2016

L.G. Finch, Q.C.