NORTON ROSE FULBRIGHT

Legal update

Can a breach of a performance guarantee be subject to insurance under Quebec law? The Superior Court takes a stand

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Insurance

On May 17, 2018, Justice Danye Daigle of the Superior Court of Québec dismissed a Wellington motion filed by LeProhon Inc. against its insurer, Federated Insurance Company of Canada (Insurer). The Superior Court of Québec's decision in *9071-3975 Québec inc. v. Leprohon inc.*[1] gives guidance on whether coverage under a commercial general liability policy (CGL Policy) and a professional liability/errors and omissions policy (E&O Policy) applies when the essence of the claim arises from a breach of the insured's obligations under a letter of performance guarantee.

Nature of the underlying claim and denial of coverage

The plaintiff 9071-3975 Québec Inc. (Lucyporc) operates in the pork processing industry. After LeProhon performed work on behalf of Lucyporc, the latter filed an action against LeProhon mainly alleging a breach of the obligations set forth in a letter of performance guarantee attached to the agreement entered into between LeProhon and Lucyporc.

After receiving a notice of the action, the Insurer refused to take up LeProhon's defence pursuant to the issued insurance policies. The Insurer determined that the grounds of Lucyporc's claim, which was based on LeProhon's failure to satisfy the performance guarantee, did not trigger application of the insurance policies' coverage.

Coverage not applicable

After going over the general principles that apply in the context of Wellington motions, the Court reviewed the insurance policies that the Insurer issued to LeProhon to determine whether the coverage could apply.

The E&O Policy

The Court concluded that Lucyporc's claim was explicitly subject to the exclusions set forth in the E&O Policy, more specifically the "manufacturer's express warranty" exclusion, because it referred to delays, refusals to complete work and the breach of the performance guarantee.

CGL Policy

The CGL Policy specifically provided that property damage should result from an occurrence in order for insurance coverage to be triggered. The CGL Policy defined *occurrence* in the usual manner, which is "[translation] an accident, including continuous or repeated exposure to substantially the same risks."[2]

Relying on the Supreme Court of Canada's teachings on the notions of "occurrence" and "accident" in *Progressive Homes*, the Court determined that the breach of a performance guarantee does not constitute an accident or repeated exposure to certain conditions, this despite giving a broad and liberal interpretation to the CGL Policy. Consequently, the Court ruled that the insurance coverage under the CGL Policy was not triggered by the claim.

Conclusion

In sum, this decision emphasizes that insureds can't offer co-contractors a performance guarantee in the belief that they can fall back on their insurance coverage in the event of a breach. The courts must examine the reasons for which insureds breach their obligations under a contract to determine if the loss is attributable to an insured risk, otherwise insurers would be bound by every single one of their insureds' undertakings. As the Court so carefully summarized, "[translation] this would distort both the nature and the objectives of insurance contracts."[3]

This decision has not been appealed.

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Footnotes

1. 2018 QCCS 3434.
2. *Ibid*, para. 48.
3. *Ibid*, para. 60.

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