Federal Court of Appeal

Cour d'appel fédérale

Date: 20120730

Docket: A-141-11

Citation: 2012 FCA 215

CORAM: **LÉTOURNEAU J.A.**
PELLETIER J.A.
MAINVILLE J.A.

BETWEEN:

FEUILTAULT SOLUTION SYSTEMS INC.

Appellant

and

ZURICH CANADA

Respondent

Heard at Montreal, Quebec, on January 17, 2012.

Judgment delivered at Ottawa, Ontario, on July 30, 2012.

REASONS FOR JUDGMENT BY: PELLETIER J.A.

CONCURRED IN BY: LÉTOURNEAU J.A.
MAINVILLE J.A.

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REASONS FOR JUDGMENT

PELLETIER J.A.

INTRODUCTION

[1] This is an appeal from the decision of the Federal Court, reported as *Feuiltault Solution Systems Inc. v. Zurich Canada*, 2011 FC 260, [2011] F.C.J. No. 309 (Reasons), dismissing Feuiltault Solutions Systems Inc.'s (Feuiltault) claim against its insurer under an all-risks marine insurance policy. The issues raised by the appeal are who bears the onus of showing fortuity/lack of fortuity, and whether the policy exclusion with respect to packing applied to the loss.

FACTS

[2] Feuiltault is a manufacturer of specialized book binding machines known as pocket feeders. It sold forty of these machines to a customer in Germany. The goods were loaded into three separate containers. Feuiltault's employees used pieces of pressure treated wood to immobilize the machines within the containers. The Court accepted that the machines were in good condition when they left Feuiltault's yard. The containers were trucked from Feuiltault's yard to the Port of Montreal where they were loaded onto a ship for the transatlantic voyage.

[3] The containers were off-loaded at the North Sea Terminal, Bremerhaven, Germany, after an uneventful ocean voyage, and were then trucked to the customer's premises. When the containers were opened, all of the machines were rusted to the point that they were eventually declared a total loss.

[4] The consignee, Feuiltault's customer, refused to accept the goods. Various investigations were undertaken in order to determine the cause of the rusting. Feuiltault made a claim under its marine insurance policy. When Feuiltault's insurer, Zurich Canada (Zurich) refused to pay, Feuiltault sued pursuant to the Ocean Marine Certificate issued by Zurich, which incorporated the Institute Cargo Clauses (A). These clauses constitute an industry standard insurance policy, which are given contractual effect as a result of being incorporated by reference in a certificate of insurance, as they were here.

[5] Clause 1 provides that the insurance "covers all risks of loss or damage to the subject-matter insured" except as provided in the exclusions. Zurich denied coverage on the basis of the exclusion found at Clause 4.3 which, in its material parts, provides:

> 4. In no case shall this insurance cover
> …
> 4.3 loss, damage or expense caused by insufficiency or unsuitability of packing or preparation of the subject matter insured …

[6] The insurer did not plead lack of fortuity and did not rely on the exclusion of loss caused by inherent vice: Appeal Book, Vol. 1, p.55-57.

THE FEDERAL COURT'S DECISION

[7] After reviewing the evidence of the various expert witnesses, the Federal Court came to a conclusion as to the proximate cause of the loss. The Federal Court accepted the conclusions of Zurich's expert, Captain Fernandes. These conclusions were summarized by the Federal Court as follows:

> He [Captain Fernandes] concludes that it is reasonable to attribute the corrosion damage to heavy condensation within the containers during transit and that the most likely source of the heavy condensation is the high moisture content in the heat pressure treated lumber. Cpt. Fernandes concludes that the machinery was insufficiently packed (unwrapped steel machines in a container full of wood that has not been kiln dried and no use of desiccants) and that the wood used as dunnage was clearly unsuitable because of its high moisture content.
>
> Reasons, at para. 50.

[8] The Federal Court then began its review of the relevant law by referring to the famous passage from *British and Foreign Marine Co. v. Gaunt*, [1921] 2 AC 41 [*Gaunt*], with respect to all-risks insurance policies:

> There are, of course, limits to "all risks". They are risks and risks insured against. Accordingly the expression does not cover inherent vice or mere wear and tear or British capture. It covers a risk, not a certainty; it is something, which happens to the subject-matter from without, not the natural behaviour of that subject-matter, being what it is, in the circumstances under which it is carried.

[9] The Federal Court took from this passage that, in order to succeed, the insured needs to establish on a balance of probabilities that the loss was due to a fortuity, that is, an external, accidental cause: see Reasons, at para. 60.

[10] The Federal Court then reviewed some of the jurisprudence where the issue of lack of fortuity has been considered. The Court referred to *Global Process Systems Inc. v. Syarikat Takaful Malaysia Berhad*, [2011] UKSC 5 [*Global Process Systems*], *T. M. Noten B.V. v. Harding*, [1990] 2 Lloyd's Rep 238 (C.A.) [*Noten*], and *Nelson Marketing International Inc. v. Royal and Sun Alliance Insurance Co. of Canada*, 2006 BCCA 327, [2006] B.C.J. No. 1454 [*Nelson Marketing*].

[11] The Federal Court also considered whether, on the facts of this case, it could be inferred that the loss was due to a fortuitous event or an accident in the course of the voyage. It found that although an inference could be drawn that a fortuitous event had occurred if other shipments had been made under closely comparable circumstances without being damaged, that was not the case here. The presence of pressure treated wood in the containers was a departure from past practice and, as a result, the Court could not infer that the loss was due to a fortuity.

[12] The Federal Court considered that this case was analogous to the *Noten* and *Nelson Marketing* cases, cited above. The Court noted that, as in those cases, there was in this case no evidence of any unusual or untoward weather, or of any unusual features of the containers

themselves. Nor was there evidence of any ingress of water or humid air in the course of the voyage. It is implicit in the Court's reasoning that the absence of these factors pointed, as it did in *Noten* and *Nelson Marketing*, to the absence of a fortuitous cause of loss.

[13] The Federal Court also rejected Feuiltault's theory that the loss was caused by the presence of an aggressive chemical agent accidentally introduced into the container in the course of the voyage. The presence of such an agent would have satisfied the requirement of a fortuitous cause of loss.

[14] In the end result, the Court concluded that there was no coverage for the claim because Feuiltault, the insured, had not shown that the loss was caused by a fortuity.

[15] The Federal Court went on to consider the exclusion pleaded by Zurich, namely "insufficiency or unsuitability of packing". The Court referred to the decision of the Supreme Court of Canada in *Canadian National Railway Co. v. Royal and Sun Alliance Insurance Co.*, 2008 SCC 66, [2008] 3 S.C.R. 453 [*CNR*], a case which dealt with an exclusion for "faulty and improper design" in a builder's risk policy. The Court was of the view that the standard applied by the Supreme Court to determine if the design in that case was "faulty or improper" should also be used to determine if the packing or preparation of the cargo was insufficient. The standard applied by the Supreme Court was that of the "ordinary reasonably cautious and prudent person": see Reasons, at para. 67.

[16] The Federal Court concluded, after considering all of the evidence, that the packing and preparation of the cargo were insufficient. The Court also found that the pressure treated wood used to brace the machines in the containers was unsuitable considering the absence of wrapping

to protect them from rusting. The Court found that, had the machinery been wrapped with a protective covering, as it was in a later shipment, the loss would not have occurred.

[17] As a result, the Federal Court dismissed Feuiltault's claim against Zurich.

STANDARD OF REVIEW

[18] This is an appeal of a decision of a judgment rendered after a trial. As such, the standard of review set out in *Housen v. Nikolaisen*, 2002 SCC 33, [2002] 2 S.C.R. 235, at paras. 8, 10, and 37, applies: palpable and overriding error with respect to questions of fact and questions of mixed fact and law (save in the case of an extricable legal error), and correctness with respect to questions of law.

ANALYSIS

[19] The first issue to be considered is whether the Federal Court erred in concluding that Feuiltault had the onus of showing that the loss was caused by a fortuity. In my view, the proposition that an insured under an all-risks policy must prove that the loss occurred as a result of a fortuity is of limited application and is subject to the caveat that, where the insurer has contractually excluded non-fortuitous losses, the onus of proving lack of fortuity with respect to those losses falls on the insurer.

[20] Ever since *Gaunt* was decided, it has been the law that "all-risks" policies cover only losses caused by fortuity or casualty, that is, "something which happens to the subject-matter from without, not the natural behaviour of that subject-matter, being what it is, in the circumstances under which it is carried": see *Gaunt*, cited above, at 455. In his speech, Lord Sumner expanded upon this notion:

> There are risks and risks insured against. Accordingly the expression does not cover inherent vice or mere wear and tear or British capture. It covers a risk, not a certainty; it is something which happens to the subject-matter from without, not the natural behaviour of that subject-matter, being what it is, in the circumstances in which it is carried. Nor is it a loss which the assured brings about by his own act, for then he has not merely exposed the goods to the chance of injury, he has injured them himself.
>
> *Gaunt*, cited above, at 455.

[21] The roots of the issue with respect to fortuity raised by this appeal lies in the passage that immediately follows the one quoted above:

> Finally, the description "all risks" does not alter the general law; only risks are covered which it is lawful to cover, and the onus of proof remains where it would have been on a policy against ordinary sea perils. I think, however, that the quasi-universality of the description does affect the onus of proof in one way. The claimant insured against and averring a loss by fire must prove loss by fire, which involves proving that it is not something else. When he avers loss by some risk coming within "all risks", as used in this policy, he need only give evidence reasonably showing that the loss was due to a casualty, not to a certainty, or to inherent vice or to wear and tear.
>
> *Gaunt*, cited above, at 455.

[22] Two propositions emerge from these passages. The first is that the insured has the onus of showing that the loss was due to a fortuity or a casualty. The second is that inherent vice is not a fortuity. These two propositions must be considered together with another legal proposition,

namely that the insurer has the burden of proving the exclusions upon which he relies when denying coverage:

> A long standing line of authorities require an insurer, seeking solace in an exclusion from otherwise unlimited liability, to show that the exclusion applies.
>
> *Continental Insurance Co. v. Dalton Cartage Co.*, [1982] 1 S.C.R. 164 [*Dalton Cartage Co.*].

[23] *Dalton Cartage Co.* is not a marine insurance case. However, the same rule applies in marine insurance cases: see *Global Process Systems*, cited above, at para. 20.

[24] The question of onus becomes important where the insurer excludes non-fortuitous losses, such as losses caused by inherent vice. The definition of inherent vice was settled in *Soya GmbH Mainz KG v. White*, [1983] 1 Lloyd's Rep 122 (H.L.) [*Soya*], where Lord Diplock, at page 126, wrote:

> This phrase (generally shortened to "inherent vice") where it is used in s. 55(2) refers to a peril by which a loss is proximately caused; it is not descriptive of the loss itself. It means the risk of deterioration of the goods shipped as a result of their natural behaviour in the ordinary course of the contemplated voyage without the intervention of any fortuitous external accident or casualty.

This definition was confirmed by the Supreme Court of the United Kingdom in *Global Process Systems*, cited above, at paras. 45, 81, and 129-133.

[25] In light of this definition, it is manifest that there is a conflict between the following propositions:

a) an insured under an all-risks policy must show, if only by inference, that the loss was caused by a fortuity; and

b) the insurer must prove the application of the exclusion, including non-fortuitous losses, on which it relies to deny coverage.

An insured who cannot show that the loss was caused by a fortuity will have, in effect, shown that the loss was caused by inherent vice, since, by definition, inherent vice is the deterioration of the cargo without the intervention of any fortuitous external accident or casualty. This reverses the onus with respect to proof of the cause of loss, since requiring the insured to show that the loss was due to a fortuity imposes on the latter the onus of *disproving* inherent vice.

[26] In my view, the jurisprudence with respect to the burden on the insured to prove a fortuity as a condition of recovery under an all-risks policy must therefore be read carefully. It is trite law that insurance policies must be read as a whole so as to give effect to all terms of the contract: see *BG Checo International Ltd. v. British Columbia Hydro and Power Authority*, [1993] 1 S.C.R. 12, [1993] S.C.J. No. 1 at para. 9 [*BG Checo*]. In practice, this means that the scope of coverage is determined by the interplay between the insuring agreement and the exclusions. Where the question of coverage falls to be decided solely on the scope of the insuring agreement, in the absence of exclusions, *Gaunt* is authority for the proposition that the insured must show his loss is fortuitous. But where the question of coverage depends upon both the insuring agreement and the exclusions, then *Gaunt* and the jurisprudence that follows it must be read subject to the following caveat: where the insurer has specifically excluded non-fortuitous losses, especially inherent vice, then it must be taken to have accepted the burden of proving lack of fortuity.

[27] This is also consistent with the rule that all terms of the policy must be given meaning: see *BG Checo*, cited above, at para. 9. Requiring the insured to prove that the loss was due to a fortuity effectively renders the exclusion of non-fortuitous losses superfluous. If the insured can prove that the loss was caused by a fortuity, the exclusions cannot apply. If the insured cannot

prove that the loss was cause by a fortuity, his claims fails and the issue of the exclusions for non-fortuitous losses will never arise. The only way to give both the insuring agreement and the exclusions their proper scope is to hold that the insured under an all-risks policy needs only show that the cargo was in good condition when the insurance attached and that the goods were damaged while the insurance was in force. It is for the insurer who wishes to deny coverage to prove that the exclusion with respect to inherent vice or other non-fortuitous loss applies.

[28] *Nelson Marketing*, cited above, which the Federal Court relied on in coming to its conclusion, illustrates the anomaly that results from an unqualified application of the principle set out in *Gaunt*. In *Nelson Marketing*, the insured cargo was laminated flooring, manufactured in Malaysia and shipped from there to North America. Upon arrival, the flooring was found to be cracked, delaminated and water-stained.

[29] The insurance policy was the same as the one in issue in this case, an all-risks policy that excludes, among other perils, loss caused by or resulting from inherent vice, or from the nature of the subject-matter insured. The insurer denied the insured's claim under the policy. The insured sued and lost at trial. The insured appealed.

[30] In considering the matter, the British Columbia Court of Appeal made the following observations:

> Thus, to succeed on a claim under an "all risks" cargo policy, the Insured must establish, by direct evidence or by an inference to be drawn from the available evidence, that an external fortuitous occurrence caused the deterioration of the cargo as distinct from the cargo having simply succumbed to the ordinary incidents of the voyage because of the cargo's inherent nature or susceptibility.
>
> *Nelson Marketing*, cited above, at para. 13.

The Court then framed the issue before it as follows:

> The issue is only whether what did cause the loss was fortuitous and not attributable to the inherent nature of the flooring. The nature of the flooring was to absorb and release moisture. The amount of moisture absorbed and released (and the damage that could result) varied with the environmental conditions of temperature and humidity to which the flooring was exposed. For the cause of the loss to have been fortuitous, the flooring, which had absorbed some moisture before shipment, must have been exposed to conditions other than what could be said to have been ordinary in the holds of feeder vessels on each of the three carriages from the Malaysian ports to Singapore. *The Insured bore the burden of establishing that the conditions in the holds of the three vessels was substantially different than was to be expected as part of the ordinary incidents of the carriage.* The question now is only whether there was evidence that would support a finding that the environmental conditions were substantially out of the ordinary.

Nelson Marketing, cited above, at para. 23 (my emphasis).

[31] In the end, the Court found that the insured had not shown that the environmental conditions were out of the ordinary, with the result that, having failed to establish that the loss was due to a fortuitous condition, the insured was denied coverage under the policy.

[32] The significance of the environmental conditions was that, if they were proven by the insured to be out of the ordinary, they would have represented a fortuity that brought the loss within the terms of coverage. But as I noted above, proof of such a fortuity necessarily renders the exclusion for inherent vice superfluous and the insurer is thereby relieved of the burden of proving that the exclusion applies. The Court would have come to the same result had it considered that the loss was, *prima facie*, within the terms of coverage and then applied the exclusion for inherent vice.

[33] I am therefore of the view that, in order to give full effect to the terms of the policy in this case, it is necessary to treat the exclusions for non-fortuitous losses (inherent vice, wear and tear,

deliberate acts of the insured) as an undertaking by the insurer to assume the burden of proving that the loss was not fortuitous, thereby relieving the insured of the obligation to do so. In my view, this is an incremental advance, based on the terms of the policy, on the principle set out in *Arnould's Law of Marine Insurance and Average*, 17th ed. (London: Sweet & Maxwell, 2008), at p. 1058, "[i]f the goods are shipped sound and arrive damaged, and the damage is of such a kind as to raise a presumption of some external cause, there is [under an "All risks" policy] *prima facie* evidence of loss by an insured peril, and the burden is on the underwriter to prove that the loss in fact occurred in some way for which he is not liable." See also *Canadian National Railway Co. v. Royal and Sun Alliance Insurance Co. of Canada*, [2008] 3 S.C.R. 453, 2008 SCC 66 at paras. 5, 31 and 34.

[34] As a result, I find that the Federal Court erred in law in imposing on the insured the burden of proving that the loss was caused by a fortuity. In doing so, it failed to give effect to the contract between Feuiltault and Zurich.

[35] Since the insurer did not plead that the loss was caused by a non-fortuitous loss, the only remaining issue is whether the exclusion for insufficiency of packing relieves Zurich of liability under the policy. For ease of reference, I reproduce the exclusion again:

> 4.3 Loss, damage or expense caused by insufficiency or unsuitability of packing or preparation of the subject matter insured.(for the purpose of this Clause 4.3 "packing" shall be deemed to include stowage in a container or lift van but only when such stowage is carried out prior to attachment of this insurance by the Assured or their servants).
>
> Appeal Book, Vol. 1, p. 31.

[36] While the jurisprudence on this exclusion is sparse indeed, it has been held to apply to "those steps which are necessary to prepare the cargo for the loading process, not the very acts which result in the cargo being stowed on board": see *Helicopter Resources Pty Ltd v. Sun Alliance Australia Ltd (The Icebird)*, (1991) 312 LMLN (Supreme Court of Victoria), at 31. I understand this to mean that the exclusion applies to the steps taken by the insured to protect the cargo from the ordinary incidents of carriage, including stowing cargo in a container and taking steps to immobilize it in the container. By necessary implication, I also understand this exclusion to refer to the suitability of the materials used by the insured for those purposes. The application of this clause to circumstances where the conditions encountered in the course of the voyage depart from "the ordinary incidents of carriage" does not need to be answered here as it does not arise on these facts.

[37] In order for the exclusion to apply, the packing must occur prior to the attachment of the insurance. Clause 8.1 deals with the attachment of the insurance:

> 8.1 This insurance attaches from the time the goods leave the warehouse or place of storage at the place named herein for the commencement of the transit, continues during the ordinary course of transit …
>
> Appeal Book, Vol. 1, p. 35.

[38] It is not contentious that the containers were packed on the insured's premises prior to being picked up for transportation to the Port of Montreal and onwards.

[39] The exclusion requires that the loss or damage be caused by the insufficiency or unsuitability of packing. In this case, the Federal Court accepted that the corrosion of the cargo was caused by condensation in the container due to the high moisture content of the pressure treated wood used to secure the machinery in the container. Since the wood was a packing

material, I agree with the Federal Court's conclusion that the packing was unsuitable. It follows from this that the unsuitability of the packing was the cause of the loss. The Federal Court also found that the packing was insufficient. It appears that the insufficiency consisted in the absence of protective wrapping which could have prevented the loss. While the absence of the protective wrapping, in an of itself, did not cause the loss, in the circumstances of this case, it did contribute to the loss so as to satisfy the requirements of the exclusion.

[40] This conclusion is consistent with the general purpose of marine insurance, which is to indemnify against the risks incident to a maritime voyage, and not to guarantee the skill and workmanship of the insured in preparing the cargo for such a voyage.

CONCLUSION

[41] For these reasons, I would dismiss the appeal with costs.

"J.D. Denis Pelletier"
J.A.

“I agree
Gilles Létourneau J.A.”

“I agree
Robert M. Mainville J.A.”

Federal Court of Appeal  Cour d'appel fédérale

FEDERAL COURT OF APPEAL

NAMES OF COUNSEL AND SOLICITORS OF RECORD

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