A RE-EXAMINATION OF THE TEST OF MATERIALITY IN QUEBEC INSURANCE LAW

In the absence of fraud, a misrepresentation or concealment on the part of an insured will be a cause of nullity in favour of the insurer only under certain conditions. The insurers are bound to establish the non-disclosure, the fact that the applicant had knowledge of the true situation, and the fact that they (the insurers) did not have this knowledge. In addition, they must show that the evasions were *material* to the risk. The great problem confronting the courts in the majority of insurance cases today is the determination of what constitutes *material* facts .

The first of the statutory conditions in the Quebec Insurance Act (applicable to policies of fire insurance) imposes a sanction of nullity where the insured: "misrepresents or omits to communicate any circumstance which is material to be made known to the company, in order to enable it to judge of the risk it undertakes."[1]

Beyond thus noting that materiality is a subjective concept, to be assessed from the insurer's point of view, no attempt at definition is made by the statute.

In the Quebec Civil Code, the general article relating to representation declares that the material facts — that is, those which must be disclosed on pain of nullity — are those which show, "the nature and extent of the risk, and which may prevent the undertaking of it, or affect the rate of premium."[2]

Article 2487 of the Code supplies the teeth to the foregoing provision, providing a sanction of nullity for misrepresentation or concealment of facts, "of a nature to diminish the appreciation of the risk or change the object of it." And, in Article 2489, "material concealment" is assimilated to "substantial concealment".

Until 1953, these articles were interpreted as restating the test of materiality as laid down in the English Common Law, namely: "A representation is material which would influence the judgement of a prudent insurer in fixing the premium or determining whether he will take the risk."[3]

The question was examined in our Supreme Court as recently as 1941. As the case arose in Quebec, the court had to decide whether the provisions of Article 2487 had been infringed. Kerwin J. states the law as follows:

> . . . were the inaccuracies of a nature to diminish the appreciation of the risk or change the object of it? The criterion, I apprehend, that is to be followed is the same as that set forth by the Privy Council, in *Mutual Life Insurance Co. vs. Ontario Metal Products Co.*,[4] i.e. whether if the matters concealed or misrepresented had been truly disclosed they would, on a fair consideration of the evidence have in-

[1](1941) R.S.Q., cap. 299, sec. 240(1).

[2]Article 2485.

[3]*Marine Insurance Act* (1906) 6 Edw. 7, cap. 41, sec. 20(2).

[4][1925] A.C. 344.

fluenced a reasonable insurer to decline the risk or to have stipulated for a higher premium.[5]

In 1953, in *Alliance Insurance Co. of Philadelphia et al.* v. *Laurentian Colonies and Hotels Limited,*[6] the Quebec Court of Appeal changed direction as regards the interpretation of Articles 2485-2489, and abandoned the subjective test of materiality. Briefly, the facts in the case were as follows:

A company known as the Laurentian Colonies and Hotels Limited had been organized by one Audet with a view to the erection of a resort hotel at Ste. Marguerite Station in the Laurentian mountains. Pending the completion of the construction, a total of $359,125. of insurance was acquired through the agency of a firm of insurance brokers. Less than a month later, the property was almost completely destroyed by fire. Thirty of the thirty-one companies who were on the risk disputed their liability, on five general grounds.

Firstly, it was established that Audet had been convicted of the criminal offense of living off the fruits of prostitution, and had duly served a penal sentence of five years. Secondly, other insurers had refused to cover the risk on "moral grounds", and some other insurance that was held had been cancelled. Thirdly, the property was overburdened with heavy mortgages. Fourthly, the financial status of the company was precarious. And, these four situations were not disclosed to the insurers. The fifth ground was the fact that the buildings were not sprinklered, although it had been represented that an adequate sprinkler system would be installed.

The trial judge found, as a matter of fact, that there had been a clear intention to equip the hotel with a sprinkler system, as an engineer had been consulted and estimates had been submitted. Thus the representation had been substantially complied with. He found that the non-disclosures were not material under the circumstances of the case; and the test he applied was the subjective one of the probable effect of the truth on the minds of the underwriters.

In the Court of Queen's Bench, the principal decision was delivered by Mr. Justice Stuart McDougall, and was concurred in by Barclay, Gagné, and Hyde JJ. On the question of materiality, the learned judge reasoned as follows:

> There is a vast difference between material facts which relate to the risk and of which the insurer is entitled to be informed, and information which he desires in order to decide whether or not to cover the risk and issue a policy. This reasoning leads to a consideration of certain differences between our law and the common law. The *Marine Insurance Act,* which defines materiality, is accepted as governing in all forms of insurance under the common law system.
> A comparison of [the language of this Act] with the language of Article 2485 shows that the scope of materiality under the common law is wider than under our law. A 'fact which shows the nature and extent of the risk, and which may prevent the undertaking of it, or affect the rate of premium' covers a much narrower field than a 'circumstance which would influence the judgement of a prudent insurer in

[5] *Gauvremont* v. *Prudential Insurance Co. of America* [1941] S.C.R. 139, at p. 160.
[6] [1953] Q.B. 241.

> [fixing the premium or] determining whether he will take the risk'. This view of the difference in meaning is reinforced by the language of Article 2487, under which the only misrepresentation or concealment which may be a cause of nullity is of 'facts of a nature to diminish the appreciation of the risk or change the object of it'. Under the common law the field of what are known as moral hazards would therefore be much larger than under our law.[7]

This analysis of Article 2485 by McDougall J. is perfect from a grammatical point of view. According to the plain meaning of the English words, the insurer wishing to establish materiality must prove two things. He must prove in the first place that the fact "shows the nature and extent of the risk". Secondly, he must prove either that it might have prevented the undertaking, or that it might have affected the rate of premium. The first proof is objective and narrow; the second proof is subjective and wide. Since the insurer is compelled to make both proofs, the net result is that, in our law, materiality is a narrower concept than in the English law. And, in this view, the test of materiality is — at least partially — an objective one.

Leaving aside the moot question as to whether this view ought to be the law, it is the purpose of this article to examine the provisions of the Civil Code, in order to determine whether this actually is the law of Quebec. For, it will be noted that the French version of Article 2485 provides that: "L'assuré est tenu de déclarer pleinement et franchement tout fait qui peut indiquer la nature et l'étendue du risque, empêcher de l'assumer, *ou* influer sur le taux de la prime."

In the French version, the duty of disclosure is phrased in the alternative, with the result that a material fact is one which does any of three things: it shows the nature and extent of the risk; or it prevents the undertaking; or it affects the rate of premium. In this case, our law is in harmony with the Common Law instead of being narrower, and the prevailing test of materiality is applicable in Quebec as well.

Which version is to prevail? There exists, within the Civil Code itself, an article whose purpose is the resolution of just such a difficulty, and which provides that: "If in any article of this Code founded on the laws existing at the time of the promulgation, there be a difference between the English and French texts, that version shall prevail which is most consistent with the provisions of the existing laws on which the article is founded; and if there be any such difference in an article changing the existing laws, that version shall prevail which is most consistent with the intention of the article, and the ordinary rules of legal interpretation shall apply in determining such intention."[8]

Our Codifiers note that Articles 2485-2489 are of general application, and contain rules common to the law of insurance in all countries.[9] Moreover,

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[7] *Ibid.*, at pp. 253-255.

[8] **Article 2615.** And cf. *City of Montreal* v. *Watt and Scott* [1922] 2 A.C. 555, for interpretation of what is meant by "a difference".

[9] Report of the Commissioners to Codify the Laws of Lower Canada in Civil Matters, Seventh Report, p. 242.

there is nothing to indicate that it was their intention to change the law on this subject. It is evident, therefore, that Aricle 2485 is founded "on the laws existing at the time of the promulgation". It follows that the version which shall prevail is that one "which is most consistent with the provisions of the existing laws on which the article is founded".

To determine the law upon which Article 2485 is founded, we return to the Codifiers' Reports to examine the sources referred to by them under this article. Beneath the article which later became Article 2485, a reference is made to the French author, Pardessus, and to the references following the next two articles. In all, six references are made to ancient and modern French sources, three to American sources, and one to an English source.[10] In addition, the Codifiers referred to a pre-codification decision of our courts.

Pardessus notes that: "Le contrat doit énoncer, avec exactitude, en quoi consiste la chose assurée, et tout ce qu'il importe à l'assureur de bien connaître, pour apprécier l'étendue des risques auxquels il s'expose."[11] That is, a material fact, according to Pardessus, is one which it is of consequence for the insurer to know in order for him to estimate the extent of the risks he is assuming.

The Codifiers refer to Pothier, but, beyond noting that "la prime est l'estimation des risques",[12] the learned author makes no declaration on the subject of materiality. The other French sources referred to are Alauzet,[13] Dalloz,[14] Boudousquié,[15] and Article 348 of the French *Code de Commerce.* These sources say substantially the same thing as does Pardessus. Boudousquié, for example, states as follows: "Ainsi, tout ce qui peut servir à l'appréciation des risques doit être mis, par l'assuré, à la connaissance de l'assureur; lui laisser ignorer une seule des circonstances qui peuvent influer sur son opinion, et par suite sur son volonté, c'est l'autoriser à dire qu'on a mis à sa charge des chances qu'il n'aurait pas voulu garantir, ou qu'il n'aurait garanties qu'à des conditions différentes s'il les avait connues."[16]

The English source referred to is Arnould, a noted authority on English insurance law. His answer as to what constitutes material facts is that: "every representation is to be deemed material which there is just reason to believe determined the underwriter to insure, or influenced his estimate of the premium.

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[10]A further reference is made to Bell, *Commentaries on the Laws of Scotland.* This source, however, makes no mention of materiality, and must have been referred to for other purposes.

[11]J. M. Pardessus, *Cours de Droit Commercial,* 5th. ed., Vol. 2, No. 593.

[12]M. Pothier, *Traité des Contrats d'Assurances,* 1781, ch. 3, sec. 3.

[13]I. Alauzet, *Traité Général des Assurances,* 1844, esp. Vol. 1, No. 202, and Vol. 2, at p. 414.

[14]Dalloz, *Dictionnaire Pratique:* esp. Assurances Terrestres, No. 85.

[15]P. A. Boudousquié, *Traité de l'Assurance Contre l'Incendie,* 1829.

[16]*Ibid.,* at p. 140.

The test of materiality is the probable influence of the statement made, on the mind of the underwriter."[17]

Marshall, an American authority referred to, puts the matter as follows: "A representation is said to be material, when it communicates any fact or circumstance, the belief of which may be reasonably supposed to influence the judgement of the underwriters, in undertaking the risk, or calculating the premium."[18]

The other two American sources referred to are Phillips,[19] and Kent.[20] They agree substantially with what was said by Marshall. Kent, for example, says at one point, that the insured is obliged "to communicate every species of intelligence which he possesses, which may affect the mind of the insurer either as to the point whether he will insure at all, or as to the rate of premium."[21]

The pre-codification case referred to is that of *Casey* v. *Goldsmid et al.*[22] In it, the defense to an action on a policy of fire insurance was concealment of material facts. The Superior Court dismissed the action, but the Court of Queen's Bench allowed the appeal on the ground that the concealment was not fraudulent. The Court of Appeal did not deal with the question of materiality at all, holding that proof of fraud was required to annul an insurance contract for concealment. The presence of Article 2487 in the present Code indicates the rejection of this view by the Codifiers.

The decision in first instance, which therefore is the one our Codifiers adopted, contains the following statement: "By material facts, in this respect, are meant all those which if communicated to the insurer, would induce him, either to refuse the insurance altogether, or not to accept it unless at a higher rate of premium."[23]

This survey of the sources which gave birth to Article 2485 indicates clearly that, at the time of the codification, the laws of England, France, and the United States were in harmony on the subject of materiality. In substance, all the sources referred to assessed materiality from the subjective point of view of the insurer.

The writer must conclude therefore, with all due respect for the analysis made by McDougall J., that the subjective test of materiality as laid down in the English *Marine Insurance Act* is in harmony with the rules of the Quebec Civil Code. The excursion into the sources referred to by our Codifiers, necessitated by the difference between the English and French

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[17]Joseph Arnould, *A Treatise on the Law of Marine Insurance*, 2nd. ed., Vol. 1, No. 194.

[18]Samuel Marshall, *A Treatise on the Law of Insurance*, 3rd. ed., No. 452.

[19]Willard Phillips, *A Treatise on the Law of Insurance*, 4th. ed.; esp. Vol. 1, No. 88.

[20]James Kent, *Commentaries on American Laws*, 1832.

[21]*Ibid.*, Vol. 3, No. 285.

[22](1852), 2 L.C.R. 200, and (1854), 4 L.C.R. 107.

[23](1852), 2 L.C.R. 200, per Meredith J.

texts of Article 2485, clearly establishes the French version of that article, and the subjective test of materiality.

Finally, it will be noted that the learned judge reinforced his interpretation by referring to Article 2487. With respect, the writer contends that it is possible to interpret this article so as to support the present analysis of Article 2485. The article referred to provides that concealment of a fact, "of a nature to diminish the appreciation of the risk" is a cause of nullity. The writer submits that the ordinary meaning of the word "appreciation" is a subjective one, referring in this instance to the estimation of the risk in the mind of the insurer.[24]

STANLEY TAVISS*

[24]For support of this contention, see G. Wasserman, "Materiality of Facts Relating to the Risk in Fire Insurance" (1954), 14 Revue du Barreau 397, at pp. 405-407.

Third Year Student.