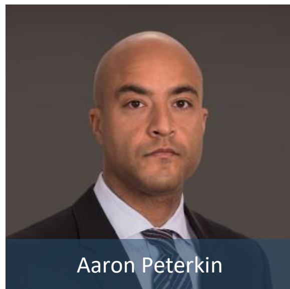
Heart Zap v. Lloyd's, (June 2019): Unpaid Merchandise Lost in Mail Scam Covered by All Risks Policy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Underwriters of "all risks" property policies take notice. Last month, Ontario's Superior Court of Justice decided in favour of coverage where the insured was defrauded of $37,000 of defibrillators devices, having mailed the merchandise, before receiving payment, to a "fake" purchaser (i.e. someone who never intended to pay). Respectfully, the decision is problematic.

The insuring intent of all risks policies is to indemnify against fortuitous property losses. In *Heart Zap v. Lloyd's Underwriters*, 2019 ONSC 3667, the loss in question arose by virtue of series of unquestionably intentional and non-negligent acts (i.e. the insured's unwitting but otherwise voluntary involvement in the fraudulent scam). Flynn J.'s reasoning expresses that an insured's lack of awareness or understanding of another's nefarious motives can provide the requisite element fortuity. Is gullibility in the course of a commercial transaction fortuitous? Apparently so. In the bigger picture, the Court's understandably sympathetic reasoning exposes property insurers to indemnify against an insured's poor or imprudent counterparty risk assessment. Respectfully, an "all risks" policy is not an "every conceivable risk" policy, nor should it be purposively interpreted as such.

Location of Loss by Mail Fraud

In Heart Zap, the policy provided coverage for property only while at locations specified in the declarations. The first issue considered was whether the loss occurred at the insured's address where defibrillators were mailed (i.e. covered property), or at the fraudster's address where they were received (i.e. not covered property). Deciding the loss occurred at an insured location, the Court explained:

> *"This was a loss by fraud. The property was lost … when it was shipped as a result of that fraud. … The location of a loss from fraud or theft is suffered not where the fraudsters are, it is the location from which the goods are taken."*

To the extent that this element of the decision expresses a definite rule, it is unobjectionable.

Is Voluntary Mailing a Fortuitous Loss? (Apparently, Yes)

The Underwriters argued that the loss of goods voluntarily handed over to a fraudster were not covered by the property policy. They reasoned that the insured's claim was really with respect to lost payment and not the lost property itself.

The Superior Court of Justice disagreed. Unfortunately, Flynn J. sidestepped any analysis of the policy's wording and intent (i.e. the requirement of fortuity) by addressing the Court's attention to the underlying contract of sale. The Court reasoned that, as an agreement for sale requires consensus ad idem between the buyer and seller, there can be no sale (and no consensual handing over of goods) when the rogue's intent was always to obtain the goods by fraudulent means. Flynn J. concluded:

> *" …. It was only in the belief that [the fraudster] had capacity to pay that [the insured] was willing to deal with them. As evidenced by the use of fake names and contact information, [the fraudster's] intent from the beginning was to obtain the [defibrillator] Units by fraud. Under the circumstances, there was no consensus ad idem and therefore no contract of sale was formed. As such, the Plaintiff did not voluntarily convey the [defibrillator] Units."*

In other words, because the insured had no knowledge that the fraudsters did not intend to pay, the mailing of the defibrillators was not a voluntary or intentional act. Stepping back from these specific facts and considering the implied general rule, Flynn J.'s reasoning is founded upon a curious premise.

Conditional Sale Exclusion

Observing that the merchandise was mailed before payment was received, the Underwriters lastly argued that coverage was withdrawn by a clause that excluded losses to property sold "under conditional sale, installment payment or other deferred payment plan, from the time of leaving the Insured's custody".

Rejecting the Underwriter's argument, the Court noted that a conditional sales contract is one in which the seller reserves title until the buyer pays for the goods. The matter before the Court was "a typical cash delivery contract" and there was no evidence of intent to withhold title. Again, the Court observed:

[The Underwriters'] argument presupposes that there was a contract of sale at all in this case. For the reasons I have set out above, there can be no sale, and therefore no conditional sale, where the vendor's consent to sell was obtained by fraud. As such, the exclusion of coverage for conditional sales does not apply.

Final Remarks

Very likely, the Underwriters did not expect they were insuring Heart Zap against the possibility that some of its customers might not intend or have the funds to pay for ordered goods. Respectfully, the result and the reasoning will pose challenges for property insurers. I expect that any rule of policy interpretation that might be drawn from the decision will be used by insureds to shoehorn business losses (that may have been avoided by more prudent conduct) into coverage. Without specific wording to that effect, this should not be an "all risks" property policy's purpose.

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