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Partial Settlements and Other Litigation Agreements in Multi-Party Actions: The Peril of Non-Disclosure

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A recent decision of the Ontario Court of Appeal provides a stark reminder that when a partial settlement or other litigation agreement is reached in multi-party litigation, a critical step of disclosure must be considered. Missing this step can be fatal. *Handley Estate v. DTE Industries Limited*, 2018 ONCA 324 holds that failing to disclose to the court and the other parties a litigation agreement that alters the adversarial relationship between the contracting parties may jeopardize not only the litigation agreement, but a party's entire position in the lawsuit.

Background

The *Handley* case arose from the purchase and installation of a new outdoor oil tank at Helen Handley's residence. The tank leaked fuel oil into the surrounding soil. Ms. Handley's insurer, Aviva Insurance Company of Canada, commenced a subrogated claim in her name against the respective parties involved in the sale and installation of the tank, and the sale and delivery of the fuel oil. In effect, Aviva was the plaintiff.

Aviva had not named as defendants in the main action one of the oil tank vendors in the supply chain. By the time it decided to sue the omitted vendor, the limitation period for the main action had expired. Aviva then began to explore the possibility of a third party claim being initiated against the omitted vendor.

As the deadline for issuing a third party claim approached, Aviva and one of the defendants in the main action, H&M Combustion Services Ltd. ("H&M"), struck a litigation agreement that was not disclosed to the court or the other parties. Among the agreement's key terms were that: **(1)** H&M would defend the main action and commence the third party claim against the omitted vendor; **(2)** Aviva would contribute $5,000 to cover H&M's costs through the examinations for discovery; and **(3)** all communications between Aviva and H&M pertaining to the third party claim would be subject to common interest privilege.

Five years later, as the trial date was approaching, Aviva and H&M entered into a second litigation agreement that included the following terms: **(1)** H&M assigned to Aviva all its rights in the action, including the rights to receive all proceeds from the third party claim; **(2)** Aviva agreed to assume responsibility for defending H&M and prosecuting its third party claim and agreed to indemnify H&M for any costs or damages awarded against it; and **(3)** Aviva and H&M agreed to disclose the assignment to the other parties if required by law or reasonably necessary in the circumstances.

Piecemeal disclosure then began with Aviva disclosing part of the second litigation agreement to the other parties. Later, Aviva disclosed all of the agreement. This led to the other parties seeking a further Affidavit of Documents with a proper Schedule B describing all documents over which privilege was claimed. This process ultimately resulted in Aviva and H&M agreeing to waive any common interest privilege and producing the Schedule B documents which included both litigation agreements.

At that point, one of the other defendants and the third parties moved for an order staying the action on the basis that Aviva and H&M had failed to disclose immediately agreements that affected "the litigation landscape", contrary to the principles set down by the Court of Appeal in an earlier case, *Aecon Buildings v. Stephenson Engineering Limited*, 2010 ONCA 898.

The motion judge refused the request for a stay of the action. He distinguished *Aecon*, finding that it did not stand for the proposition that the claims against all parties to the litigation should "automatically" be stayed. Instead, he drew on the principle of proportionality and appeared to conclude that the moving party had suffered no prejudice from the delayed disclosure of the litigation agreements.

The Court of Appeal Decision

The Court of Appeal reversed the motion judge and stayed Aviva's action. The Court held that litigation agreements that alter the adversarial relationship divulged on the face of the pleadings must be disclosed to the other parties to the litigation *immediately*. Procedural fairness demands swift disclosure. This is because such agreements may have an impact on the strategy of the other parties to the litigation, such as a line of cross-examination to be pursued, evidence to be led, or responses to be made to steps taken by the parties to the litigation agreement. Most importantly, the court needs to be informed so that it can properly control its process in the interests of fairness and justice to all of the parties.

The obligation of immediate disclosure applies broadly. The Court of Appeal noted (at para. 39) that the obligation is not limited to traditional partial settlements such as pure *Mary Carter* or *Pierringer* agreements which, in broad strokes, involve arrangements between settling plaintiffs and defendants who cooperate in varying degrees, depending on the agreement, to facilitate redress being sought from non-settling defendants.

The Court of Appeal in *Handley* held (at para. 39): "The disclosure obligation extends to any agreement between or amongst parties to a lawsuit that has the effect of changing the adversarial position of the parties set out in their pleadings into a co-operative one". To maintain fairness, a court needs to "know the reality of the adversity between the parties" and whether an agreement changes "the dynamics of the litigation" or the "adversarial orientation" (citing *Moore v. Bertuzzi*, 2012 ONSC 3248, at paras. 75-79).

Implications

In dramatic fashion, *Handley* shows that the potential obligation to disclose a partial settlement, or any other litigation agreement, must be kept top of mind.

It is true that settlement privilege will apply to a partial settlement reached in a multi-party litigation case: *Sable Offshore Energy Inc. v. Ameron International Corp.*, 2013 SCC 37. It is also true that this privilege will generally protect the *amount* of the settlement from needing to be disclosed to the non-settling parties, at least until liability has been adjudicated when the settlement figure would ordinarily need to be disclosed in order to ensure that the plaintiff is not overcompensated: see *Laudon v. Roberts*, 2009 ONCA 383. But what *Handley* and the cases that precede it make clear is that settlement privilege will not protect from disclosure to the court and the non-settling parties the *fact* of a partial settlement and, inevitably, certain of its features, if former adversaries are now fellow travellers in the litigation.

The Court of Appeal in *Handley* could not be any clearer. A party's failure to disclose a litigation agreement that changes the "adversarial orientation" from what is reflected in the pleadings will be deemed an abuse of process. Absence of prejudice provides no refuge. Non-disclosure to the court and the other parties is a procedurally fatal error that will result in a stay of the non-disclosing party's claim.

If a party to a litigation agreement is uncertain whether the agreement attracts the mandatory disclosure obligation, that party should

move before the court for directions. The risk of non-disclosure is simply too great.

The information and comments herein are for the general information of the reader and are not intended as advice or opinion to be relied upon in relation to any particular circumstances. For particular application of the law to specific situations, the reader should seek professional advice.

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