

Historically, courts in Canada have been reluctant to award punitive or aggravated damages in commercial contexts, especially when the matter at issue is a breach of contract. “This rule,” writes Stephen Waddams, “is based on the assumption underlying much of contract law that a breach of contract, coupled with an offer to pay just compensation, does no harm to the plaintiff, is not morally wrong, and may be desirable on the grounds of efficiency.”¹ The Supreme Court of Canada recognized the rarity of punitive damages for breaches of contract in *Vorvis v. Insurance Corp. of British Columbia*, in which Justice McIntyre wrote, “In my view, while it may be very unusual to do so, punitive damages may be awarded in cases of breach of contract. It would seem to me, however, that it will be rare to find a contractual breach which would be appropriate for such an award.”²

Even when punitive or aggravated damages are awarded, until recently awards have been small.³ More significant punitive damages awards have been made in commercial contexts but only when there was a breach of a fiduciary duty.⁴

Over the last dozen years, circumstances have changed. Aggravated and punitive damages are more frequently awarded in commercial contexts, and the size of awards is escalating. These developments have been seen in a series of decisions of the Supreme Court of Canada, which chart the emergence of not only larger awards but also an increasing array of circumstances that give rise to claims for these more intangible damages. These landmark decisions of the Supreme Court of Canada are the focus of this article.

The starting point for a consideration of the availability of aggravated and punitive damages in commercial cases is the 1989 decision of the Supreme Court of Canada in *Vorvis*.

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¹ S.M. Waddams, *The Law of Damages*, looseleaf (Aurora: Canada Law Book, 2006) at 11.250.

² [1989] 1 S.C.R. 1085 at ¶ 26 [*Vorvis*].

³ See, for instance, *Adams v. Confederation Life Insurance Co.*, [1994] A.J. No. 308, in which the Court awarded punitive damages of \$7,500 where an insurer violated its duty of good faith to an insured. Indeed, the highest award in an “insurer bad faith” case prior to *Whiten v. Pilot Insurance Co.*, [2002] 1 S.C.R. 595 [*Whiten*] was \$50,000 (¶ 36).

⁴ See, for instance, *Re MacDonald Estate* (1994), 95 Man. R. (2d) 123 (C.A.), in which the Court awarded \$500,000 in punitive damages against a deceased’s former lawyer and business partner, who had been a co-executor of the deceased’s estate. The Manitoba Court of Appeal reduced this award to \$250,000.

More recent developments are illustrated by these Supreme Court of Canada cases:

- the 1995 decision in *Hill v. Church of Scientology of Toronto*⁵
- the 1997 decision in *Wallace v. United Grain Growers Ltd.*⁶
- the 2002 decision in *Whiten v. Pilot Insurance Co.*⁷
- the 2006 decision in *Fidler v. Sun Life Assurance Co. of Canada*⁸

Vorvis v. Insurance Corp. of British Columbia, 1989

The decision of the Supreme Court of Canada in *Vorvis* reflects, in the majority, the general proscription at that time against awards of punitive damages for breach of contract. It also foreshadows the bases upon which a broader view could be taken.

Vorvis was a wrongful dismissal case. An in-house lawyer was dismissed after 14 years of service in the defendant's legal department. The company initially purported to dismiss Mr. Vorvis for cause, but the trial judge dismissed that assertion, finding no cause for the dismissal. In addition to reasonable notice, the plaintiff had claimed aggravated and punitive damages for mental distress, among other damages. These damage claims were based upon what had happened to Mr. Vorvis before he was dismissed: his supervisor had become increasingly dissatisfied with his work and had instituted weekly "productivity meetings" that were found to have degenerated into a form of inquisition.⁹

At trial, damages for wrongful dismissal were awarded, but the claims for mental distress and aggravated or punitive damages were dismissed. The Court of Appeal upheld the denial of these additional damage claims. However, the dissenting judge in the Court of Appeal would have awarded the sum of \$5,000 for punitive damages as a result of the employer's pretermination conduct. At the Supreme Court of Canada, the Court also split, with a dissent that would also have approved an award of \$5,000 for punitive damages.

In considering these issues, the Supreme Court made a number of preliminary observations about the distinction between damages for mental distress, aggravated damages and punitive damages. Justice McIntyre, for the majority, noted that the damages for mental distress were "properly characterized as aggravated damages." In *Vorvis*, the damages were not claimed as a separate head, but it was argued that they were included in the general concept of punitive damages.¹⁰

Justice McIntyre observed that damages for mental distress would include damages properly classified as aggravated damages and punitive damages. These observations highlight one of the difficulties in considering damages in this area: often the same conduct gives rise to these various claims (that is, claims for damages for mental distress, aggravated damages and punitive damages). The main difference between these kinds of damages is that damages for mental distress and aggravated damages are compensatory, but punitive damages are not. Justice McIntyre stated as follows:

⁵ [1995] 2 S.C.R. 1130 [*Hill*].

⁶ [1997] 3 S.C.R. 701 [*Wallace*].

⁷ *Whiten*, *supra* note 3.

⁸ [2006] 2 S.C.R. 3 [*Fidler*].

⁹ *Vorvis*, *supra* note 2 at ¶ 33.

¹⁰ *Ibid.* at ¶ 5.

Punitive damages, as the name would indicate, are designed to punish. In this, they constitute an exception to the general common law rule that damages are designed to compensate the injured, not to punish the wrongdoer. Aggravated damages will frequently cover conduct which could also be the subject of punitive damages, but the role of aggravated damages remains compensatory.¹¹

In *Vorvis*, the majority of the Court held that aggravated and punitive damages may be awarded only when there is an independent actionable wrong. It was not sufficient that a course of conduct, not itself actionable, was related to an actionable course of conduct. That is, it was not sufficient that the pretermination misconduct of the supervisor also related to Mr. Vorvis's employment contract.¹² Hence, the claim for damages for mental distress (or aggravated damages) was dismissed by the majority.

In considering the claim for punitive damages, Justice McIntyre expanded on some of the problems that arise when the concept of punitive damages is raised in civil cases:

The award of punitive damages requires that:

... a civil court ... impose what is in effect a fine for conduct it finds worthy of punishment, and then remit the fine, not to the State Treasury, but to the individual plaintiff who will, by definition, be over-compensated. [citing *Waddams*]

This will be accomplished in the absence of the procedural protections for the defendant – always present in criminal trials where punishment is ordinarily awarded – and upon proof on a balance of probabilities instead of the criminal standard of proof beyond a reasonable doubt.¹³

Justice McIntyre noted that, nevertheless, it was settled law that in appropriate cases punitive damages may be awarded, but they should always receive the most careful consideration, and the discretion to award them should be most cautiously exercised.¹⁴

As with aggravated damages, Justice McIntyre concluded that punitive damages could be awarded only on the basis of an independent actionable wrong. He observed that it would be rare to find a contractual breach that would be appropriate for such an award.¹⁵ In contrast to tort claims, where the injured party is entitled to be made whole, remedies in contract are, as a matter of principle, those that the contracting parties bargained for.¹⁶

The majority decision in *Vorvis* also describes the conduct required to give rise to punitive damages in language more severe than we see the courts use today. The majority opinion refers to conduct requiring

¹¹ *Vorvis, ibid.* at ¶ 16.

¹² *Vorvis, ibid.* at ¶ 21.

¹³ *Vorvis, ibid.* at ¶ 24.

¹⁴ *Ibid.*

¹⁵ *Ibid.* at ¶ 25-26.

¹⁶ *Ibid.*

punitive sanctions with the following terms: malice, fraud, cruelty, abuse, insolent acts, high-handedness, maliciousness, contempt and “disregard for every principle of decency.”¹⁷

Justice Wilson, writing for the dissent,¹⁸ disagreed that there must be an independent actionable wrong. Justice Wilson advocated that the application of the rule in *Hadley v. Baxendale* regarding what damages were in the reasonable contemplation of the parties would properly extend to mental suffering.¹⁹

With respect to punitive damages, Justice Wilson noted the longstanding prohibition against such damages in breach of contract cases, based on the notion that the sole purpose of contract damage is to compensate the plaintiff.²⁰ However, she also noted that this once firm prohibition had “fallen by the wayside,” and there may be special cases, particularly shocking ones, where punitive damages may be awarded.²¹ Justice Wilson indicated that instead of requiring an independent actionable wrong, the Court should look for conduct that was shockingly harsh, vindictive, reprehensible or malicious; flagrant and deliberate misconduct “would also merit an award of punitive damages.”²² Justice Wilson would have found such conduct here, and would have upheld the decision of the dissenting judge in the Court of Appeal to award punitive damages of \$5,000.

This dissenting opinion is an early indication of a number of themes that have now become more established in cases such as *Wallace* and *Fidler*, discussed below, with one exception. On quantum, Justice Wilson observed that “when the purpose of the award was to reflect the Court’s awareness and condemnation of flagrant wrongdoing and indifference to the legal rights of other people, the award did not need to be excessive.”²³ As set out below, since *Vorvis* the courts have refused to interfere with very substantial awards of punitive damages, a trend marked by the next case.

Hill v. Church of Scientology, 1995

Though a defamation case rather than a breach of contract case, *Hill* is important for three reasons. First, the Supreme Court in *Hill* provides a test for the application of punitive and aggravated damages that has since been adopted in other, strictly commercial contexts. Second, the Court in *Hill* outlines when a reviewing court can interfere with an award of punitive damages made by a jury. Finally, and most conspicuously, *Hill* signals a break in the previously well established tradition of relatively small aggravated and punitive damages awards. As David Stockwood, QC, writes, “Any complacency about our conservative Canadian juries was shaken by the award of \$1.6 million (excluding interest) in the *Hill* case.”²⁴

After a jury trial, in addition to an award of \$300,000 for general damages for defamation, the Church of Scientology was found liable for aggravated damages of \$500,000 and punitive damages of

¹⁷ *Ibid.* at ¶ 27-28.

¹⁸ L’Heureux-Dubé J. concurring.

¹⁹ *Vorvis*, *supra* note 2 at ¶ 46-49; *Hadley v. Baxendale* (1854), 9 Ex. 341.

²⁰ *Vorvis*, *ibid.* at ¶ 50.

²¹ *Ibid.* at ¶ 54-55.

²² *Ibid.* at ¶ 60.

²³ *Ibid.* at ¶ 62.

²⁴ David Stockwood, QC, *The Sky’s the Limit ... or is it? Defamation damages after Hill and Botiuk* (1995) 14 Advocates’ Soc. J. No. 3, 14-20 at ¶ 4. Stockwood also notes that it is not possible to view *Hill* as a “one of a kind” judgment, as the Supreme Court in *Hill*’s companion case, *Botiuk v. Toronto Free Press*, [1995] 3 S.C.R. 3, “restored an award by Mr. Justice Carruthers which, with interest, exceeded \$1 million.” (Stockwood, ¶ 5)

\$800,000, that being the largest punitive damages award for defamation in Canadian history. These awards were upheld by the Ontario Court of Appeal and the Supreme Court of Canada.

Writing for a unanimous Court,²⁵ Justice Cory directly addressed the circumstances in which aggravated and punitive damages would be awarded for defamation. He wrote that aggravated damages would be found “in circumstances where the defendants’ conduct has been particularly high-handed, or oppressive, thereby increasing the plaintiff’s humiliation and anxiety.”²⁶ The Court ruled that the “entire conduct of the defendant prior to the publication of the libel and continuing through to the conclusion of the trial” is available to be assessed by the judge or jury in determining the quantum of aggravated damages.²⁷ The Court found that for an award of aggravated damages in defamation there must be a finding of “actual malice” that “increased the injury to the plaintiff, either by spreading further a field the damage to the reputation of the plaintiff, or by increasing the mental distress and humiliation of the plaintiff.”²⁸ The Court ruled that in this case there was “ample evidence” upon which the jury could find aggravated damages, and it upheld the \$500,000 award against the Church of Scientology.

In the assessment of the punitive damages awarded against the Church of Scientology, Justice Cory noted first that punitive damages should be awarded only in those circumstances where the defamation “is so malicious, oppressive and high-handed that it offends the Court’s sense of decency.”²⁹ This test has since been applied in commercial contexts, most notably in *Whiten* and *Fidler*, discussed below. Justice Cory then asserted that in gauging the reasonableness of the quantum of punitive damages, the Court should look carefully at the amount that had already been assessed against the defendant in general damages and aggravated damages; punitive damages should be awarded only if these amounts are not sufficient to punish the defendant properly. The Court cited the decision of the Ontario Court of Appeal in *Walker v. CFTO Ltd.*,³⁰ finding that a court is entitled to intervene in reducing a damages award only when “the verdict is so exorbitant or so grossly out of proportion ... as to shock the Court’s conscience and sense of justice,”³¹ a test also since applied in the *Whiten* case.

In *Hill*, the Court’s finding that the \$800,000 punitive damages award should be upheld was described as highly fact specific; the Court focused on the extraordinarily malicious conduct of the church (which it called “insidious, pernicious and persistent”)³² during the events at issue, which confirmed that “no amount of general or aggravated damages would have deterred Scientology,” making this an appropriate circumstance for a very large award of punitive damages.³³ Notwithstanding the Court’s comments on the fact-specific nature of the award, amounts awarded for aggravated and punitive damages began to rise substantially after *Hill*.

Wallace v. United Grain Growers Ltd., 1997

The availability of aggravated and punitive damages in commercial cases next came before the Supreme Court of Canada in *Wallace*, another wrongful dismissal case.

²⁵ L’Heureux-Dubé J.’s separate opinion concurred with the majority on the issues relevant to this article.

²⁶ *Hill*, *supra* note 5 at ¶ 188.

²⁷ *Ibid.* at ¶ 189.

²⁸ *Ibid.* at ¶ 190.

²⁹ *Ibid.* at ¶ 197.

³⁰ 59 O.R. (2d) 104.

³¹ *Hill*, *supra* note 5 at ¶ 159.

³² *Ibid.* at ¶ 202.

³³ *Ibid.*

Jack Wallace, a salesman, was hired away from a secure position at one employer on assurances that if he joined another company, Public Press (which was owned by the defendant, United Grain Growers), he could work there until his retirement. In addition, assurances were made to him regarding fair treatment and remuneration. He performed extremely well at Public Press, but was summarily dismissed 14 years after being hired. Public Press asserted that Mr. Wallace was unable to perform his work properly, and that it had properly terminated him for cause, an allegation that was maintained until the eve of trial over two years later. The termination of Mr. Wallace's employment created "emotional difficulties for Wallace and he was forced to seek psychiatric help."³⁴

The Supreme Court's most significant determination in *Wallace* was that damages flowing from the nature of the termination of an employee are compensable by means of an extended notice period. Justice Iacobucci wrote as follows, for a six-justice majority:³⁵

[W]here an employee can establish that an employer engaged in bad faith conduct or unfair dealing in the course of dismissal, injuries such as humiliation, embarrassment and damage to one's self-worth and self-esteem might all be worthy of compensation depending upon the circumstances of the case. In these situations, compensation does not flow from the fact of the dismissal itself, but rather from the manner in which the dismissal was effected by the employer.³⁶

Justice Iacobucci made a practical compromise here.³⁷ The judgment in *Wallace* does not assert that damages for mental distress are compensable in breach of contract. However, Justice Iacobucci allowed damages for this kind of mental distress, in the form of an extended notice period, where the dismissal violates a duty of "bad faith and fair dealing," thereby leaving the door open to employees to gain compensation for bad faith conduct by employers that causes harm. Justice Iacobucci justified this analysis by asserting that employment contracts are unique in that they control a relationship in which one party is particularly vulnerable.³⁸ Not all commentators have considered this to be a principled compromise; as some have pointed out, the notice period is the time that is needed to find replacement employment, and has nothing to do with the manner of dismissal.

In shedding light on what this "obligation of good faith and fair dealing" requires, Justice Iacobucci asserted that "employers ought to be candid, reasonable, honest and forthright with their employees and should refrain from engaging in conduct that is unfair or is in bad faith by being, for example, untruthful, misleading or unduly insensitive."³⁹ The Court emphasized that it was not compensating Mr. Wallace for the act of the termination itself, from which might arise mental distress that is not compensable at law, but rather for the manner in which the dismissal occurred.

The majority of the Court analogized the application of these kinds of damages to compensatory damages that are available in defamation, for "any kind of high-handed, oppressive, insulting or

³⁴ *Wallace*, *supra* note 6 at ¶ 7.

³⁵ La Forest, L'Heureux-Dubé and McLachlin JJ., dissenting.

³⁶ *Wallace*, *supra* note 6 at ¶ 103.

³⁷ See Lee Stuesser, "Wrongful Dismissal – Playing Hardball: *Wallace v. United Grain Growers*," (1998) 25 Man. L.J. 547 at ¶ 53–¶ 68.

³⁸ *Wallace*, *supra* note 6 at ¶ 90.

³⁹ *Wallace*, *supra* note 6 at ¶ 98.

contumelious behaviour by the defendant which increases the mental pain and suffering caused by the defamation.”⁴⁰ In that regard, Justice Iacobucci stated as follows:

In my view, there is no valid reason why the scope of compensable injuries in defamation situations should not be equally recognized in the context of wrongful dismissal for employment. The law should be mindful of the acute vulnerability of terminated employees and ensure their protection by encouraging proper conduct in preventing all injurious losses which might flow from acts of bad faith or unfair dealing on dismissal, both tangible and intangible. I note that there may be those who would say that this approach imposes an onerous obligation on employers. I would respond simply by saying that I fail to see how it can be onerous to treat people fairly, reasonably, and decently at a time of trauma and despair. In my view, the reasonable person would expect such treatment. So should the law.⁴¹

The majority found that the inducement of Mr. Wallace to leave his previous employment on a promise of a secure job was a factor that could be used to determine the length of the notice period, along with the “appellant’s advanced age, his 14-year tenure as the company’s top salesman and his limited prospects for re-employment.”⁴² Adding to these factors were the indicators of the employer’s bad faith conduct: the “abrupt manner in which Wallace was dismissed” as well as the “unfounded allegations of cause [that were] maintained until the day the trial began.”⁴³ On these grounds, the Court upheld the trial court’s finding of a 24-month notice period.

Despite its finding with respect to the duty of good faith and fair dealing, as noted above, the majority also found that an award of compensation for mental distress must be founded on an independently actionable wrong. Finding that the actions of United Grain Growers did not constitute a separate actionable wrong in this case, the majority denied any award of damages under this head. The majority further found that there was no implied duty of good faith present in the contract upon which Mr. Wallace could ground an action in breach of contract. The Supreme Court also refused to create a tort that would imply an obligation of good faith and fair dealing with regard to dismissals. Finally, the majority found that the actions taken by United Grain Growers were not sufficiently “harsh, vindictive and malicious” as to require the imposition of punitive damages.⁴⁴

Justice McLachlin, writing for the dissent,⁴⁵ saw the majority as departing from the Court’s decision in *Vorvis*. Justice McLachlin, citing *Vorvis*, concluded that only if the employer dismisses an employee in a manner that negatively affects the employee’s chances of finding alternative employment should a Court increase the reasonable notice period. Otherwise, the reasonable notice assessment should not be increased to compensate for employer misconduct in a manner of dismissal. The dissent held that the compensation for such injuries must be founded on an independent cause of action.⁴⁶ However, the dissent also found that the independent cause of action need not be a tort; it could be a breach of an implied contractual term to act in good faith.

⁴⁰ *Ibid.* at ¶ 105.

⁴¹ *Ibid.* at ¶ 107.

⁴² *Ibid.* at ¶ 82.

⁴³ *Ibid.* at ¶ 108.

⁴⁴ *Ibid.* at ¶ 79.

⁴⁵ As she then was (La Forest, L’Heureux-Dubé concurring).

⁴⁶ *Wallace*, *supra* note 6 at ¶ 130.

Hence, the dissent would have compensated Mr. Wallace for the breach of the term not by an increased notice period but by damages for mental distress. Accordingly, the dissent would have upheld the trial judge's award of \$15,000, representing compensation for those additional damages.⁴⁷

Thus, although different principles were adopted, all of the Court justices agreed that Mr. Wallace ought to be compensated in some fashion for mental distress because of the manner of termination of his employment. Although both the majority and the dissent purported to follow *Vorvis*, *Wallace* nonetheless represented a marked change in the approach to damages in this type of commercial contract case. Essentially, in any case where there is any complaint about the manner in which the dismissal was handled, a plaintiff may allege bad faith in the manner of the dismissal and ask for additional "Wallace damages." Instead of being the exception, what previously would have been called aggravated damages has become regularly available without the demonstration of an independent actionable wrong. This is illustrated by a later Supreme Court of Canada decision in the same area, *McKinley v. BC Tel.*⁴⁸ In this wrongful dismissal case, the plaintiff received "Wallace damages" even though there appeared to be little or no evidence of improper conduct in the termination itself.⁴⁹

Whiten v. Pilot Insurance Co., 2002

Whiten was the next landmark case. The appellant's house, in which she lived with her husband and children, was destroyed by a fire. Ms. Whiten's insurance company, Pilot, made some very small payments but then engaged in a protracted legal battle with her, alleging that she had committed arson. It was later found that there was no basis for this allegation. The allegation of arson had been rejected by all the initial experts who had evaluated the fire; despite this, the insurer sustained an allegation of arson against Ms. Whiten throughout the course of an eight-week trial. The jury awarded the appellant \$318,252 in compensatory damages and \$1 million in punitive damages. The Ontario Court of Appeal upheld the finding of the jury on compensatory damages but reduced the award of punitive damages to \$100,000.

At the Supreme Court of Canada, Justice Binnie wrote for the majority.⁵⁰ His reasons can be understood as an attempt to chart the limits of punitive damages awards, while at the same time allowing a claim that, on the extraordinary facts of the case, was "not so disproportionate as to exceed the bounds of rationality."⁵¹ Rudy Buller writes:

Certainly Binnie J. did not intend to open the floodgates. Indeed, in the very first sentence of his majority opinion, he recognized: "This case raises once again the spectre of uncontrolled and uncontrollable awards of punitive damages in civil actions". Much of Binnie J.'s analysis was designed to provide some measure of control on the award and quantum of punitive damages.⁵²

Following the Court's ruling in *Vorvis*, Justice Binnie found in *Whiten* that to ground an award of punitive damages, there must be an independent actionable wrong separate from the breach of the

⁴⁷ *Ibid.* at ¶ 148.

⁴⁸ 2001 SCC 38.

⁴⁹ Since this was a jury trial, less information is available, but from the case reports, the circumstances of the termination itself do not appear to be severe. There was subsequent conduct of the defendant, in the course of the litigation, that may have founded a claim for aggravated damages, but there was no independent actionable wrong.

⁵⁰ McLachlin C.J., L'Heureux-Dubé, Gonthier, Major and Arbour JJ. concurring.

⁵¹ *Whiten*, *supra* note 3 at ¶ 128.

⁵² *Rudy v. Buller, Whiten v. Pilot: Controlling Jury Awards of Punitive Damages, Case Comment* (2003) 36 U.B.C.L. Rev. 357 at ¶ 4.

contract itself. Pilot conceded that in insurance contracts the insurer is required to meet a duty of good faith and fair dealing. Justice Binnie found that a breach of this duty of good faith and fair dealing constituted the independent actionable wrong required for punitive damages.⁵³

In assessing the quantum of the jury's award, Justice Binnie embarked on two separate analyses. First, he assessed the rationality of the jury's award of punitive damages, as rationality was described by Justice Cory in *Hill*: "The appellate review should be based upon the Court's estimation as to whether the punitive damages serve a rational purpose. In other words, was the misconduct of the defendant so outrageous that punitive damages were rationally required to act as deterrence?"⁵⁴

Justice Binnie determined that the jury's response was indeed rational, and that the jury had been clearly "incensed at the idea that the respondent would get away with paying no more than it ought to have paid after its initial investigation in 1994 (plus costs)."⁵⁵ Justice Binnie found that the "award answered a perceived need for retribution, denunciation and deterrence," which are the hallmarks of punitive damages awards.⁵⁶

Justice Binnie then evaluated the proportionality of the award, assessing such factors as whether the award was proportionate to the blameworthiness of the defendant, among other elements.⁵⁷ Justice Binnie identified some of the factors that would influence the Court's assessment of blameworthiness, as follows:

- (1) whether the misconduct was planned and deliberate;
- (2) the intent and motive of the defendant;
- (3) whether the defendant persisted in outrageous conduct over a lengthy period of time;
- (4) whether the defendant concealed or attempted to cover up its misconduct;
- (5) the defendant's awareness that what he or she was doing was wrong;
- (6) whether the defendant profited from its misconduct;
- (7) whether the interest violated by the misconduct was known to be deeply personal to the plaintiff ... or a thing that was irreplaceable.⁵⁸

According to Justice Binnie's analysis, an award of punitive damages must also be proportionate to the vulnerability of the plaintiff. In most commercial contexts, the Court observed, there would not be the kind of vulnerability evident in the relationship between Ms. Whiten and Pilot Insurance. More usually, both parties will have "enter[ed] the marketplace knowing it is fuelled by the aggressive pursuit of self-interest."⁵⁹ This factor "militates against the award of punitive damages in most commercial situations."⁶⁰

⁵³ *Whiten, supra* note 3 at ¶ 128.

⁵⁴ *Ibid.* at ¶ 100.

⁵⁵ *Ibid.* at ¶ 103.

⁵⁶ *Ibid.*

⁵⁷ *Ibid.* at ¶ 112-113.

⁵⁸ *Ibid.* at ¶ 113, citations omitted.

⁵⁹ *Ibid.* at ¶ 115.

Significantly, Justice Binnie noted that the nature of the contract as a “peace of mind” contract (where the object of the contract is to secure the “peace of mind” of a party), in combination with the vulnerability of the insured, was a consideration that was properly acted on by the jury members in their deliberations with respect to punitive damages:

The obligation of good faith dealing means that the appellant’s peace of mind should have been Pilot’s objective, and her vulnerability ought not to have been aggravated as a negotiating tactic. It is this relationship of reliance and vulnerability that was outrageously exploited by Pilot in this case. The jury, it appears, decided a powerful message of retribution, deterrence and denunciation had to be sent to the respondent and they sent it.⁶¹

Justice Binnie did not elaborate further on his assertion with respect to the importance of the status of the insurance contract as a “peace of mind” contract; this would await the Court’s decision in *Fidler v. Sun Life Assurance Co. of Canada*, discussed below.

In his dissent in *Whiten*, Justice LeBel noted that the fundamental principle of tort law is compensation, not punishment. Though he accepted the role of punitive damages in Canadian tort law, Justice LeBel would have held that the award of \$1 million in punitive damages served no rational purpose because it failed to directly address any public interest that was compromised by Pilot’s actions:

The award fails the rationality test because its sole purpose remains to punish adequately bad faith and unfair dealing by employees of Pilot and its counsel. It does not address any widespread practice in the insurance industry. It does not pretend to effect a disgorgement of unfairly acquired profit. The punishment far exceeds whatever property or economic losses may have been caused by the nonperformance of the contract. In such cases, the criterion of proportionality requires that the use of punitive damages remain carefully controlled and that punitive damages should not significantly exceed the amount of damages to property, or economic interests, including aggravated damages, if any are claimed.⁶²

Justice LeBel would have upheld the decision of the Court of Appeal to reduce the jury’s punitive damages award to \$100,000.

Fidler v. Sun Life Assurance Co. of Canada, 2006

In *Fidler*, the Supreme Court of Canada took another step toward a more expanded approach to mental distress damages in commercial cases.

Ms. Fidler began receiving long-term disability (LTD) benefits after she lost her ability to work as a bank receptionist and was diagnosed with chronic fatigue syndrome and fibromyalgia. The insurer initiated surveillance, which suggested that Ms. Fidler was more active than had been reflected in the forms she had completed to indicate her capabilities. The trial judge noted that the “video depicted Ms. Fidler carrying out a number of what can be described as errands or personal business activities.”⁶³ The

⁶⁰ *Ibid.*

⁶¹ *Ibid.* at ¶ 129.

⁶² *Ibid.* at ¶ 162.

⁶³ *Fidler*, *supra* note 8 at ¶ 12.

insurer terminated benefits. Just prior to trial, approximately five years after the benefits had been terminated, the insurer offered to reinstate the benefits and pay all outstanding amounts. The trial proceeded in respect of aggravated and punitive damages.

In contrast to *Wallace* and *Whiten*, at the *Fidler* trial there was no medical evidence of mental distress caused by the termination of LTD benefits. Nor were any financial problems demonstrated. On the contrary, the plaintiff had gone on international trips and purchased major assets (including a Harley-Davidson motorcycle, a Sea-Doo personal watercraft and a motorboat) after her benefits were terminated.⁶⁴ The plaintiff's evidence of inconvenience, frustration and disappointment caused by the termination of insurance benefits was of a general nature, and a significant part of the pretrial delay was caused by unmeritorious positions taken by the plaintiff in the litigation.

The trial judge awarded \$20,000 in aggravated damages but did not award punitive damages. In denying punitive damages, the trial judge found that Sun Life's conduct "could not be characterized as an act of bad faith" given that Ms. Fidler's injury could not be "demonstrated by indicators such as x-ray or MRI."⁶⁵ In addition, the degree of misconduct on the part of Sun Life with respect to Ms. Fidler did not rise to the level demonstrated by the insurer in cases like *Whiten*; the trial judge was not satisfied "that this is one of those exceptional cases where punitive damages should be awarded."⁶⁶

The Court of Appeal upheld the trial judge's award of aggravated damages but also found \$100,000 in punitive damages.

The Supreme Court upheld the award of aggravated damages and overturned the Court of Appeal's award of punitive damages, restoring the decision of the trial judge. Chief Justice McLachlin and Justice Abella, writing for the Court, found that in "peace of mind" contracts, damages for mental distress will flow directly from the breach of the contract, when such damages can be proven. For this principle the Court relied on the concept of foreseeability as set out in *Hadley v. Baxendale*,⁶⁷ writing that "as long as the promise in relation to state of mind is a part of the bargain in the reasonable contemplation of the parties, mental distress damages arising from its breach are recoverable."⁶⁸

The Court set out a two-part test for the determination of whether mental distress damages will flow directly from the breach of a contract:

1. Is the object of the contract to secure a psychological benefit that brings mental distress within the reasonable contemplation of the parties?
2. Is the degree of mental suffering caused by the breach of a degree sufficient to warrant compensation?⁶⁹

The Court answered both parts of this test in the affirmative (finding that an unwarranted delay in receiving the promised insurance protection can be "extremely stressful"⁷⁰) and upheld the award of \$20,000 as damages for mental distress (rather than aggravated damages).

⁶⁴ Plaintiff's trial testimony, AR Vol. 2, pp. 169, 178, 186-7, Vol. 3, pp. 346, 353.

⁶⁵ *Fidler*, *supra* note 9 at ¶ 38.

⁶⁶ *Ibid.* at ¶ 39-40.

⁶⁷ *Supra* note 19.

⁶⁸ *Fidler*, *supra* note 8 at ¶ 48.

⁶⁹ *Ibid.* at ¶ 47.

The Court observed that in “normal commercial contracts, the likelihood of a breach of contract causing mental distress is not ordinarily within the reasonable contemplation of the parties.”⁷¹ The Court further noted that the degree of mental distress experienced by parties to commercial contracts is “minimal,”⁷² not usually rising beyond “incidental frustration,”⁷³ and as such is generally not compensable.

However, this circumstance changes when the “parties enter into a contract, an object of which is to secure a particular psychological benefit.”⁷⁴ The Court held that these “peace of mind” contracts should not therefore be viewed as “exceptions to the general rule of the non-availability of damages for mental distress in contract law” but rather as simple applications of the rule in *Hadley v. Baxendale*. In these contracts mental distress is reasonably foreseeable as a consequence of breach, and should therefore be compensable based on the “reasonable contemplation or foreseeability principle that applies generally to determine the availability of damages for breach of contract.”⁷⁵

By way of clarification, the Court noted that these mental distress damages might be characterized as “aggravated damages” but they should be carefully distinguished from “true aggravated damages.”⁷⁶ “True aggravated damages,” in the Court’s analysis, arise from an independent cause of action, “usually in tort-like defamation, oppression or fraud.”⁷⁷ Though they are compensatory, like all aggravated damages, they are described as being completely different from mental distress damages that flow directly from the breach of the contract and are based instead in the foreseeability principle articulated in *Hadley v. Baxendale*.

Thus, the Supreme Court awarded damages for mental distress in the absence of a finding of bad faith, and by doing so departed from its approach taken in prior cases and broadened the availability of such damages in commercial cases.

The Supreme Court in *Fidler* did not uphold the Court of Appeal’s finding of punitive damages against the insurer. The Court followed its decision in *Whiten*, where it found that an independent actionable wrong is required for a finding of punitive damages, which in the case of insurance contracts can mean a breach of the insurer’s “independent contractual obligation to deal with the respondent in good faith.”⁷⁸ In addition to this independent wrong, the Court ruled that it must also find “malicious, oppressive or high-handed” conduct that “offends the Court’s sense of decency.”⁷⁹

The Court found that although the conduct of the insurer was inappropriate, it did not meet the standard required to find punitive damages; the insurer did not act in bad faith with respect to Ms. Fidler, and as such there was no independent actionable wrong that would warrant the award of punitive damages. In making this determination, the Court noted that Ms. Fidler’s illness was difficult to prove,

⁷⁰ *Ibid.* at ¶ 58.

⁷¹ *Ibid.* at ¶ 45.

⁷² *Ibid.*

⁷³ *Ibid.* at ¶ 46.

⁷⁴ *Ibid.* at ¶ 45.

⁷⁵ *Ibid.* at ¶ 49.

⁷⁶ *Ibid.* at ¶ 52.

⁷⁷ *Ibid.*

⁷⁸ *Ibid.* at ¶ 63.

⁷⁹ *Ibid.* at ¶ 62.

and that Sun Life's surveillance of her "seemed to demonstrate an ability to engage in some activities."⁸⁰ These factors weighed against a finding of bad faith.

Most significantly, the Court noted that "an insurer will not necessarily be in breach of the duty of good faith by incorrectly denying a claim that is eventually conceded, or judicially determined, to be legitimate."⁸¹ This theoretically leaves open the right to be wrong; that is, a contracting party ought not be exposed to non-compensatory damages simply because the party turned out to have breached a contract.

The Court did not address a potentially significant concern about the impact of its approach on settlements. Often, breach of contract cases settle not because one party or the other concedes its position but because it is more efficient to settle than to try the case. There is always a risk of an adverse outcome at trial, which is factored into a settlement position. Settlements also factor in trial dynamics, which may have to do more with sympathy factors than with the merits. If, by agreeing to restore benefits in a settlement, a party will increase its exposure to aggravated or punitive damages, the party will be less willing to settle. This is becoming a more significant issue as plaintiffs increasingly press for additional amounts for claims for aggravated and punitive damages, before settling those claims. These developments seem contrary to the efficient administration of justice in commercial cases.

The Slippery Slope

The Court's approach in *Fidler* raises important questions with respect to the award of mental distress damages for breach of contract. As noted above, the Court in *Fidler* found that it is not only the breach of "peace of mind" contracts that can give rise to damages in mental distress. Basing its reasoning on the House of Lords' decision in *Farley v. Skinner*,⁸² the Court found that the psychological element of the contract in question need not be the "dominant" or "essential" element of the contract in order for its breach to earn the plaintiff damages in mental distress.

Immediately problematic in this reasoning is that *all* contracts involve, to one degree or another, an element of peace of mind. Indeed, a fundamental reason for entering into any kind of contract for the future delivery of any good or service is that the promise entered into provides the parties with mutual assurance—"peace of mind"—that the promises made will be carried out. If the type of contracts for which mental distress damages will be awarded is expanded, the natural question becomes: Where does it stop? Won't the breach of any contract potentially lead to damages for mental distress?

This problem was alluded to in the oral arguments made before the Court. Plaintiff's counsel advanced the position that there are two kinds of contracts whose breach can bring damages for mental distress: first, there are "peace of mind" contracts, and second, there are contracts where it is reasonably foreseeable that the breach of the contract will cause mental distress. The breach of both kinds of contracts, plaintiff's counsel argued, should give rise to a claim for damages for mental distress. In the course of this argument, a justice of the Court asked:

Just before you go further, do you have cases on this recovery for mental distress as a failure to provide services or goods? Because I see a whole range of potential problems, [such as] a contract for a new dishwasher and they bring it in two weeks late and in the meantime I have not only physical distress because I have to wash dishes but I have mental distress and that kind of thing. I'm not trying to trivialize it, but [I] just [want] to

⁸⁰ *Ibid.* at ¶ 69.

⁸¹ *Ibid.* at ¶ 71.

⁸² [2001] 4 All E.R. 801.

illustrate that there have to be some lines and I wonder where the cases have put those lines.⁸³

In response to this question, plaintiff's counsel argued that the disability insurance contract at issue was a classic "peace of mind" contract and its breach should therefore award the plaintiff damages for mental distress. But another justice pressed even on the concept of "peace of mind" contracts:

I have some difficulty really trying to understand why we concentrate ... on peace of mind as a phenomenon. You enter into a contract for peace of mind because you enter into it on the expectation that the contract will be performed. So, in a sense, all contracts are peace of mind contracts. So I'm not sure it helps us. I know that disability insurance policies have been carved out this way but I don't know that as analysis it's all that helpful.⁸⁴

The Court's concern with the drawing of lines, as evidenced by its questions, is reflected to some degree in the *Fidler* judgment itself, where the Court attempts to put limits around the award of mental distress damages by finding that "[i]n normal commercial contracts, the likelihood of a breach of contract causing mental distress is not ordinarily within the reasonable contemplation of the parties. It is not unusual that a breach of contract will leave the wronged party feeling frustrated or angry. The law does not award damages for such incidental frustration."⁸⁵

Despite these questions raised at the hearing, the approach in *Fidler* allows for mental distress to be compensable in the absence of an independent actionable wrong.

It is not only the *Fidler* case that raises questions of whether we are heading down a slippery slope. Each of the four recent cases discussed above, whether by allowing for a very large quantum of punitive damages (as in *Hill* and *Whiten*) or by expanding the means by which damages can be awarded (as in *Wallace* and *Fidler*), allows plaintiffs to recover larger awards than had previously been considered appropriate in commercial contexts. In each of these cases we have moved further along a continuum toward the more frequent awarding of aggravated and punitive damages, or damages for mental distress, in commercial contexts, and awards are now sizable.

Another significant concern is the possibility for overlapping awards. Conceptually, there are now series of notionally different kinds of damages that are all founded on what amounts to the same conduct: extended notice periods for wrongful dismissal, breach of contract damages for mental distress, aggravated and punitive damages. However appropriate in theory, these potential damage claims all arise from the same course of conduct and give rise to a significant risk of overcompensation. This is obviously unfair to defendants, who may be called upon to pay three times for a single course of conduct. Plaintiffs stand to be grossly overcompensated for a single breach of a contract. Courts must, therefore, exercise great care in determining the appropriate remedies in commercial matters, and it is not surprising that juries may overcompensate based on a perception that each head of damage is different.

The imposition of punishment in the civil courts is also replete with problems. Stephen Waddams has raised concerns that are echoed by Justice McIntyre in *Vorvis* and by other jurists and scholars:

⁸³ DVD of oral argument.

⁸⁴ *Ibid.*

⁸⁵ *Fidler*, *supra* note 8 at ¶ 45.

The theoretical justification for an award of exemplary damages has long been debated, for it appears anomalous for a civil court to impose what is in effect a fine for conduct it finds to be worthy of punishment, and then to remit the fine, not to the State Treasury, but to the individual plaintiff who will, by definition, be over-compensated ...

Even if it is conceded that one of the effects of the civil law is deterrence, this concession does not necessarily justify exemplary damages. The award of compensatory damages has, in itself, a deterrent effect, and one can support this effect, without supporting an award expressly made for deterrent purposes ... The main argument against exemplary damages is that punishment and the avoidance of private vengeance is the function of the criminal law. If the conduct in question falls outside the scope of the criminal law, that is because Parliament has chosen not to make it punishable ...⁸⁶

It is important that courts reflect on the important reservations that have been raised from many corners regarding punitive damages as an appropriate remedy in commercial contexts. The large punitive damages awards in *Hill* and *Whiten* were upheld despite these serious concerns.

Some of the cautionary messages articulated by the Court in *Vorvis*, by Justice LeBel in his dissent in *Whiten* and by scholars such as Waddams need to re-emerge and begin again to play a more important role in the consideration of these issues. It must be remembered that punitive damages in the commercial context ought to be highly unusual, in that they are meant to punish, whereas the main purpose of remedies in contract law has historically been to compensate plaintiffs for the losses they incurred as a result of breaches. **T**

⁸⁶ Waddams, *supra* note 1 at 11.20-11.40.