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## INNOCENT CO-INSUREDS MAY RECEIVE COVERAGE, DESPITE INTENTIONAL ACTS OF OTHER INSUREDS



Amendments to British Columbia's *Insurance Act* introduced in the Legislature last spring will, if passed, dramatically increase insurers' exposure in cases where claims might otherwise be denied on the basis of an intentional act exclusion.<sup>1</sup> The new legislation extends coverage to "innocent" co-insureds, notwithstanding the intentional, fraudulent, or even criminal actions of other co-insureds.

### OVERVIEW

Insurance is intended to cover losses occasioned by fortuitous perils. It typically doesn't cover intentional, harmful acts. For example, arson by an insured is not a fortuitous peril and is therefore excluded. Policies are specifically written to exclude coverage to insureds who deliberately damage their insured property. This approach is consistent with the underlying purposes of the insurance contract; it prevents wrongdoers from taking advantage of their own wrong, deters crime, and avoids fraud against insurers.

However, this exclusionary language can produce harsh and inequitable results for other parties covered under the same policy. It is arguably unfair to deny insurance protection to innocent insureds by imputing to them fraud committed by others. While insurance coverage might be "joint", should liability for the fraud or arson be several and separate? Co-insureds or unnamed insureds will ask why they should be penalized for others' wrongdoing. Should the "innocent" insured receive coverage?

This issue is most acute in fire insurance policies. Most standard homeowner policies extend coverage to family members or relatives resident on the premises. They also usually contain an exclusion which typically provides:

This policy does not insure: ... loss or damage caused by a criminal or wilful act or omission of the insured or any other persons whose property is insured hereunder. (emphasis added)

<sup>1</sup>Bill 40, containing the amendments, passed First Reading in the Legislature on April 30, 2008. However, it was not dealt with further during the brief Fall session in November. It is likely to resurface in the next session, and could be enacted during the spring of 2009.

Before 1989, the few Canadian decisions dealing directly with the issue of “innocent co-insureds” suggested that an innocent co-insured could not collect the proceeds of a fire insurance policy on jointly owned property intentionally destroyed by a co-insured. See for example the Supreme Court of Canada’s decision in *Scott v. Wawanesa Mutual Insurance*, in which parents whose 15-year-old son (who, as a resident, was also an insured) deliberately set their house on fire were denied coverage for the loss.

The issue of the innocent co-insured has also arisen in the commercial context. For example, if three dentists form a general partnership to purchase and insure a clinic and one of the partners burns it down, can the other partners recover? The Ontario Court of Appeal in *Higgins v. Orion Insurance* decided on similar facts that denying recovery to an innocent partner because of a co-partner’s guilt is unfair, punishing him or her vicariously for the co-partners’ crime. The ruling clarified that a Court must ascertain in each case whether the arsonist would benefit from the recovery and fashion its judgment accordingly. In *Higgins*, the Court allowed one partner to recover under the policy when it was clear that the other partner, who set the fire, would not in any way benefit financially from the arson.

## NEW BC INSURANCE ACT

British Columbia’s amended *Act* would reverse the ruling in *Scott*. Under the new legislation a “criminal or intentional act” exclusion would be effective *only* against the person who either caused the loss, abetted in causing the act causing the loss, or consented to the act causing the loss, knowing that the loss or damage would result:

### *Recovery by innocent persons*

28.5(1) ... [I]f a contract contains a term or condition excluding coverage for loss or damage to property caused by a criminal or intentional act or omission of an insured or any other person, the exclusion applies only to the claim of a person

- (a) whose act or omission caused the loss or damage,
- (b) who abetted or colluded in the act or omission,[or]
- (c) who
  - (i) consented to the act or omission, and
  - (ii) knew or ought to have known that the act or omission would cause the loss or damage...

Soon, insurers might have to grapple with the idea that all insureds except the arsonist or fraudster will be entitled to recover.

What would these innocent co-insureds be entitled to?

28.5(2) Nothing in subsection (1) allows a person whose property is insured under the contract to recover more than their *proportionate interest* in the lost or damaged property (emphasis added).

It is not clear what “proportionate interest” means. Will a spouse who owns a family home equally with an arsonist get 50% coverage? Will it matter if the property is owned as a joint tenancy as opposed to a tenancy in common? Would the two innocent dentists in the example above be entitled to 66% of the loss? These issues will have to be resolved by the insurance industry and through litigation as this new legislation is interpreted over the next few years. What is clear though is that the new amendments to the *Insurance Act* will, if passed, increase exposure for all insurers who provide coverage to British Columbian insureds.

If you have any questions regarding this legislation do not hesitate to contact us.

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