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DETERMINING COVERAGE UNDER A LIABILITY POLICY

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Over the past decade, the Supreme Court of Canada has issued three landmark cases that provide guidance in determining when a duty to defend is triggered in an insurance policy.

In the first decision, *Non-Marine Underwriters, Lloyd's of London v. Scalera*¹, a case litigated by Dolden Wallace Folick LLP, the Court articulated a three-step process to determine whether allegations as pleaded fall within the grant of coverage triggering a duty to defend. This three-step process, known as the "derivative rule" requires an analysis that looks beyond the legal labels attached to the allegations in the pleadings to determine the true substance of the allegations. By applying this three-part test, it can be determined whether the allegations have been crafted to merely manipulate coverage by attempting to convert an uncovered claim into a covered claim.

After *Scalera*, the Court next clarified when it is appropriate for courts to examine extrinsic evidence when seeking to determine the true meaning of the pleadings: *Monenco v. Commonwealth Insurance Company*.²

Finally, in *Derksen v. 539938 Ontario Ltd.*³ the Court clarified the duty to defend when the Statement of Claim alleges two or more consecutive or concurrent causes of a loss, and outlined the method for determining coverage when one of two losses was covered and one was excluded.

The first section of this paper will discuss *Scalera*, *Monenco*, and *Derksen*, focussing on their impact in the context of determining coverage under a liability policy. The latter part of the paper will focus on the consequences of late reporting to the liability insurer of a claim by an insured and the unique "Canadian" application of "relief from forfeiture".

I. PLEADINGS AND THE DUTY TO DEFEND

Historically, Canadian judges have only examined the Statement of Claim to determine whether a liability insurer has a "duty to defend". Essentially, it is a search to determine whether the pleadings, by their very nature, could give rise to a potential liability which is within the coverage granted by the liability insurer. In undertaking

¹ [2000] 1 S.C.R. 551 ("*Scalera*").

² 2001 SCC 49 ("*Monenco*").

³ [2002] S.C.J. No. 27 (Q.L.) ("*Derksen*").

this analysis, the Court will not consider whether the allegations are in fact true. There is no “search for truth” at the “duty to defend” stage of a lawsuit. The mere possibility of a state of facts and law that could result in indemnity will result in a “duty to defend”. The liability insurer is left to re-evaluate coverage when the case settles or proceeds to trial to determine whether in fact the liability is within coverage.

However, two recent Supreme Court of Canada rulings have addressed the effect of third party pleadings on an insurer’s duty to defend its insured. *Scalera* dealt with the application of an “intentional harm” exclusion found in a homeowner’s policy in relation to a claim founded in sexual assault. *Monenco* dealt with the application of a “turnkey” exclusion in a CGL policy in relation to a claim for professional negligence against an engineering firm. Both cases narrow the axiom that an insurer’s duty to defend is determined by the pleadings.

A. SCALERA

Scalera involved sexual assault allegations by an adolescent female against five B.C. Transit bus drivers, including Vincent Scalera, who was insured by Lloyd’s under a homeowner’s insurance policy. The female plaintiff alleged that Scalera:

- a) committed various sexual acts;
- b) misrepresented the sexual acts as being healthy and normal;
- c) breached the duty of care he owed her as a passenger on his bus;
and
- d) breached the fiduciary duty he owed.

The policy excluded coverage for bodily injury caused by “any intentional or criminal act or failure to act”.

Lloyd’s sought a declaration that it not be required to defend the plaintiff’s claim on the basis that the claims against the insured were excluded as intentional acts.

In her Statement of Claim the 22-year old female plaintiff alleged that she was subjected to sexual assaults by the insured when she was between 14 to 18 years old. The plaintiff also alleged that Scalera’s acts were negligent and a breach of fiduciary duty. The Supreme Court of Canada concluded that the insurer had no duty to defend Scalera because the plaintiff’s claim made no allegation that could potentially give rise to

indemnity under the policy. An insurer only has a duty to defend when a lawsuit against the insured raises a claim that could potentially fall within coverage. The insurer's duty to defend is related to its duty to indemnify, so if an insurance policy excludes liability arising from intentionally-caused injuries, there will be no duty to defend actions based on such injuries.

The Court then went on to formulate a three-step process to determine whether a claim could trigger indemnity. First, a court should determine which of the plaintiff's legal allegations are properly pleaded. Courts are not bound by the legal labels chosen by the plaintiff because a plaintiff cannot change an intentional tort into a negligent one simply by choice of words. When ascertaining the scope of the duty to defend a court must look beyond the choice of labels and examine *the substance and true nature* of the allegations. The policy reason for such an approach is that an insurer should not be at the mercy of a third party when determining its duty to defend.⁴

The second step in the process is to determine if any claims are entirely derivative in nature. A duty to defend will not be triggered simply because a claim can be cast in terms of both negligence and intentional tort. If both the negligence and intentional tort arise from the same actions and cause the same harm, the negligence claim is derivative and it will be subsumed into the intentional tort for the purposes of the exclusion clause. A claim for negligence will not be derivative if the underlying elements of the negligence and intentional tort are sufficiently different to render the two claims unrelated.

Finally, the court must decide whether any of the properly pleaded, non-derivative claims could potentially trigger the insurer's duty to defend.

In *Scalera*, the Court concluded that the alleged misrepresentations and breaches of duty were designed to seduce the plaintiff and convince her to engage in sexual activity with the plaintiff. The Court thus concluded, as a matter of insurance law, that the negligence and fiduciary duty claims were excluded from coverage as being derivative of the intentional sexual assault claims.

⁴ *Monenco*, *supra* note 2.

1. Derivative Claims Across Canada

This portion of the paper will review subsequent court decisions that have addressed and, in many instances, expanded the range of claims that are derivative of excluded claims and therefore not covered by a liability policy.

a. Assault and Battery

It is understandable that cases involving assault and battery, also known as trespass to person, would be among the first claims alleged to be derivative. Below we discuss three cases that indicate a varied willingness to cast claims of negligence as derivative of assault.

i. Joachin

In *Joachin v. Abel*,⁵ the plaintiffs brought three actions against the insured all claiming damages arising from a single incident. One plaintiff alleged that the insured operated his motor vehicle in a malicious, reckless and dangerous manner by deliberately “ramming” into the plaintiff, a pedestrian, intending to cause him harm. An alternative pleading of negligent operation of his motor vehicle was also made against the insured. It is notable that the first plaintiff alleged that the insured had been charged, but not yet convicted, with attempted murder. In the second action, none of the deliberate, malicious or intentional language was used in pleading and the action was framed as being one that “resulted solely from the negligence of the [insured]”. The pleadings in the third action mirrored those of the second action.

The automobile insurer refused to defend on the basis that all claims against the insured were derivative of the illegal use of the automobile and excluded by the “illegal use” provisions of the “Ontario Automobile Policy (OAP 1) Owners’ Policy” as well as the “criminal or unlawful act exclusion” in the Ontario *Insurance Act*.

In spite of the particulars of negligence alleged, including improper lookout, improper vehicle maintenance and improper control, the Court concluded that:

“the *substance* of the allegations of wrongdoing relate to deliberate wrongdoing or conduct that, in the circumstances, leaves no room for allegations of negligence or non-deliberate conduct. The alleged negligence is based on the same conduct and harm as the intentional wrongdoing. I can find no non-derivative claims or allegations that could trigger the insurer’s duty to defend.” (Emphasis added)

⁵ (2001) 27 C.C.L.I. (3d) 50 (Ont. S.C.).

The Court in *Joachin* did not specifically state its rationale for precluding the insurer from its duty to defend in the two actions that did not allege deliberate wrongdoing. We must presume that it did so in order to avoid an obvious absurdity.

ii. Morrison

In 2004 the New Brunswick Court of Appeal in *Morrison v. Co-Operators General Insurance Co.*⁶ had occasion to determine a case that potentially contained the manipulative pleadings described in *Scalera*. *Morrison* involved a series of amended Statements of Claim. The initial claim alleged that the defendant insured, “in an effort to prevent the Plaintiffs from leaving his property, violently struck the [plaintiffs’] vehicle with [his] vehicle with such a force that the [plaintiffs’] vehicle was flipped on its side causing injuries to the Plaintiffs”. The Claim went on to allege that the insured, subsequent to the collision, exited his vehicle and assaulted the plaintiffs with an aluminum baseball bat.

Following the original Statement of Claim the plaintiffs exercised their right to amend without leave and removed all allegations of deliberate conduct in respect of the collision from the Claim alleging that the collision was simply a result of the insured’s negligence. The insurer refused to defend on the basis that all of the insured’s acts violated criminal or other law and were thus excluded from coverage pursuant to the public policy rule in the New Brunswick *Insurance Act*.

In determining the matter the Court upheld the motion Court’s decision and obliged the insurer to defend on the basis that:

- a) the last filed Statement of Claim was the relevant one for the analysis;
- b) the insurer’s contention that the pleadings were manipulative was simply conjecture (the amendment, for example, could be explained on the basis that the original claim was simply misdrafted) ;
- c) no extrinsic evidence as to manipulation, even if admissible, was tendered by the insurer; and

⁶ (2004) 12 C.C.L.I. (4th) 171 (N.B.C.A.) (“Morrison”).

- d) the allegations in the last Claim support the view that the negligence claim was not derivative of the assault claim because it was not based on the same act or conduct.

The Court also took the further step of stating that an allegation of deliberately causing the collision, combined with an alternative pleading of negligently causing the collision, may still attract a duty to defend:

“Having said all this, I am not convinced that, in a case such as this, a plaintiff could not claim that [the defendant] intentionally caused the collision in an attempt to stop the Dedam vehicle from leaving his property, or, in the alternative, that he caused the injuries by driving his vehicle in a negligent manner. *It is arguable, in my view, that the two torts involve different acts or conduct based upon [the defendant’s] state of mind, one being an intentional tort and the other a non-intentional tort.*” (Emphasis added)

It should also be noted that the Court in *Morrison* quoted extensively from the Ontario Court of Appeal decision in *Cooper v. Farmers’ Mutual Insurance Co.*⁷ on the issue of admissibility of extrinsic evidence in showing manipulative pleadings. In *Cooper* the Court refused to allow the introduction of pleadings in an action founded on the same events discontinued by the plaintiff. The admissibility of such pleadings, for which clearly there was no duty to defend, would have shown that the current action contained manipulative pleadings. The Court in *Morrison* however did not go so far as to discuss the appropriateness of admitting extrinsic evidence to resolve allegations of manipulation.

iii. Unrau

The case of *Unrau v. Canadian Northern Shield*,⁸ the British Columbia Court of Appeal considered whether an insurer, in the context of a homeowners’ liability policy, had a duty to defend a lawsuit entailing allegations that the insureds prevented the plaintiff’s friends from assisting him and rescuing him from a beating being administered by others. The policy excluded coverage for “*bodily injury or property damage caused by the intentional or criminal acts or the failure to act, by or at the direction of any person insured by this policy*”.

The allegations in the Second Amended Statement of Claim stated that the plaintiff was injured as a result of the intentional assault by the Defendants Jewell and Lord and also the following wrongs by the Unraus:

⁷ (2002), 59 O.R. (3d) 417 (C.A.).

⁸ (2004), 15 C.C.L.I. (4th) 189 (B.C.C.A.).

- a) negligent participation in formulating a plan to confront the plaintiff;
- b) negligently inciting a mob to assault the plaintiff and failing to take any steps to prevent the assault;
- c) careless participation in a group activity with a reasonable foreseeability of harm to the plaintiff; and
- d) negligently failing to contact the police.

The Unraus were also defendants to a third party notice which alleged that they were aware of Jewell's propensity to violence and, amongst other things, failed to warn the plaintiff of these tendencies.

At issue was whether any of the negligence allegations, properly construed, sound in intentional tort. Counsel for the insureds submitted that the failure to take any steps to prevent the assault or to intervene were true pleas in negligence. Counsel for the insurer posed the question "*If you take away the intentional tort, is there any basis for negligence?*" The Court concluded that there was not, and accordingly, that the claims did not fall within coverage. It went on to say:

"What are outlined in the alleged facts and claims are the intentional acts of the Unraus to participate in a mob activity and a deliberate decision not to act. In the latter category are assertions that the appellants should have called the police or other persons. The plaintiff pleaded that there was a duty of care owed by the appellants "to take reasonable steps to prevent assault." In response the respondent cites what was said by Mr. Justice Sopinka (in his dissent) in *Hall v. Hebert*, [1993] 2 S.C.R. 159:

The good Samaritan deserves the world's accolades because he had no legal duty to act and would not have been civilly liable if he, too, had crossed over to the other side as did the Levite and the priest.

One way that the plaintiff might establish that the Unraus owed a duty of care to him is by proving that they participated in placing him in a position of danger. That is, that they, in the words of the pleadings, "incited the mob and encouraged the assault." However, if this is established it does not sound in negligence, but rather in an intentional or criminal act. If it was found that there was a negligent component to the failure to act, the negligence claim, per *Scalera*, would be "derivative" and it will be subsumed into the intentional tort."

The decision in *Unrau* highlights that seemingly viable pleadings of negligence may be subsumed in an intentional tort excluded from coverage.

b. Parental Supervision

However, in two cases courts have determined that allegations of negligent parental supervision are *not* derivative of otherwise excluded claims. The findings of the Court in each case were based on the fact that the alleged offending acts of the parents did not arise from the actions excluded under the policies, even though the same harm arose.

i. Godonoaga

In *Godonoaga (Litigation Guardian of) v. Khatambaksh (Guardian of)*⁹ the Ontario Court of Appeal dealt with a case involving allegations that the defendant insured children assaulted the plaintiff child and that the defendant children's mother sent at least one of the children to commit the assault. In addition to the allegations of intentional harm the plaintiff alleged that the mother and father were negligent for:

- a) failing to instill in their children reasonably acceptable values;
- b) failing to properly supervise their children; and
- c) allowing their emotionally and psychologically disturbed children into the community.

The Court found that the claims of negligence against the parents were not derivative of the excluded claims of intentional harm. The Court stated:

"The action by [the plaintiff's mother] against the Khatambaksh parents in negligence is derivative in the sense that she does not have a cause of action in circumstances where her son would not have one. However, it does not follow that the Khatambaksh parents would not have a defence to the action against them simply because their sons may not have one. In this case, the sons could readily be held liable for assault and the action in negligence against their parents dismissed. In this sense the liability of the parents is not derivative of the claims against their sons and can not constitute a reason for denying them coverage and a defence."

*ii. Fitzgerald*¹⁰

In this case the insured parents applied for an order compelling their homeowner insurer to defend them in an action for bodily injury allegedly caused by their twelve-year old son's negligent operation of an ATV. The insurer took the position that all

⁹ (2000), 20 C.C.L.I. (3d) 262 (Ont. C.A.).

¹⁰ *Fitzgerald v. Co-operators Insurance Co.* (2003), 50 C.C.L.I. (3d) 307 (N.S.S.C.).

claims in the lawsuit were derivative of an excluded claim, namely the “ownership, use or operation of any motorized vehicle.” In addition to alleging that the plaintiff’s injuries resulted from the child’s negligent *use* of the motorized vehicle the plaintiff alleged that the insured parents were negligent in their supervision of their child and maintenance of the ATV’s brakes. The latter allegation was deemed to be a “use or operation” of the motor vehicle.

The Court concluded that the parents were entitled to a defence stating:

“In my opinion, neither the claim of negligent operation nor the claim of negligent supervision is derivative under the other in the sense of *Scalera*. While both “cause the same harm” they do not arise from the same actions. The claim against the boy arises from his “lookout”, “control” and “regard to the presence of other motorists”. The charge of negligent supervision broadens the claim from the events that day on Quarry Road to the entire history of the boy and his family. Further, a finding of negligent operation on the part of the boy is not prerequisite to a finding of negligent supervision on the part of the parents. In the former, the plaintiffs must establish that the boy is capable of being found negligent and, if he is, that he did not exercise the carefulness expected of a twelve year old having like intelligence and experience... Negligent supervision aims at the behaviour of children, even children so young etc. as to be incapable of negligence. Behaviour which is not negligent for the child may still be behaviour which a parent has a duty to control.”

c. Malicious Prosecution

In 2002 the Ontario Supreme Court was asked to determine the issue of coverage under a standard tenant’s insurance policy for a lawsuit alleging malicious prosecution.

In *Lee v. Townsend*,¹¹ the plaintiff Mr. Lee had been acquitted on assault charges brought on the complaint of the defendant, Ms. Townsend. The Statement of Claim alleged that the insured defendant knew or should have known that her untrue allegations against the plaintiff would result in criminal or other charges being laid against the plaintiff by the police. The Claim went on to allege that the plaintiff’s damage and losses were caused by Townsend’s negligence, including her failure to disclose to the police and the her history of “prior emotional and psychiatric problems.” The insurer declined to defend on the basis of the “intentional act” exclusion, on the premise that malicious prosecution is an intentional tort. The insured attempted to trigger coverage by arguing that the “intent” component required for malicious prosecution could include reckless indifference – a mental state with a negligence basis.

¹¹ (2002), 43 C.C.L.I.(3d) 261 (Ont. S.C.).

The Court refused to follow the insured's argument which it described as ingenious. The Court held that even if any of the allegations of negligence could constitute the high level of negligence involved in reckless indifference, which was not pleaded, such conduct was still derivative of the intentional tort of malicious prosecution and subject to the exclusion clause. Neither bare negligence nor its highest form of recklessness could survive apart from the intentional tort.

d. Conspiracy and Deceit

A civil conspiracy entails a confederacy of two or more entities having the common purpose of defrauding or causing economic harm to another. A claim in deceit entails a fraudulent or deceptive misrepresentation used to induce a course of conduct detrimental to the recipient of the misrepresentation. The Ontario Court of Appeal recently canvassed both causes of action in the insurance coverage context.

In *Temple Insurance Co. v. Sirman Associates Ltd.*¹² the Court upheld the trial judge's decision to preclude a defence under an "Errors and Omissions Liability Policy" for the insured, a firm of environmental consultants, who had been sued by the Ontario Realty Corporation in relation to the insured's consulting and remediation work on thirty-five properties. At the heart of the action were allegations of deceit, secret commissions, bid-rigging, fraud and conspiracy. Breach of contract and negligence were also alleged against the insured. The insured's policy excluded coverage for "claims arising out of deliberate, dishonest, criminal or fraudulent acts committed by the insured".

The trial judge found the negligence claims to be derivative of the intentional torts:

"It would seem to me that every allegation of negligence to the foregoing 6 properties would be truly derivative of the intentional conduct excluded by the dishonesty exclusion. ... The true nature of the claims are not negligence in a non-derivative form, notwithstanding some general language of negligence is found."

The Court of Appeal agreed:

"The plaintiff's claims of negligence, as pleaded in the main action, arise from precisely the same allegations giving rise to the claims of fraud, conspiracy and dishonesty. Indeed, the plaintiff's pleadings repeat the same factual allegations in support of both claims of fraud and alternative claims of negligence."

¹² (2003), 4 C.C.L.I. 162 (Ont. C.A.).

e. Trespass to Land

Trespass to land provides a remedy for the direct, intentional or negligent physical interference with land in the possession of another. It is actionable without proof of damage. It is to be distinguished from trespass to person which is akin to assault and battery.

In *F.(R.D.) (Litigation Guardian of) v. Co-Operators General Insurance Co.*,¹³ the insured was a schoolboy who allegedly started a fire on school property that spread and resulted in extensive damage. The Statement of Claim alleged both negligence and trespass to property. The school boy was insured under his parents' homeowner's policy. The insurer denied a duty to defend on the basis of the policy's "intentional act" exclusion. The intentions relied upon were a deemed intention arising from the tort of trespass, and the intentional act of lighting the fire.

The insured did not dispute that the fire had been set deliberately, but instead argued that there was a distinction between intending to set the fire and intending to damage the school. Furthermore, the insured argued that only the latter would trigger the exclusion; if the resulting damage was unforeseen, the damage was at most negligent, not intentional.

The Court distinguished *Scalera* on the basis that that case, involving sexual abuse, necessarily entailed intent to injure if consent was absent. The intent to injure could not be deemed in this case, and the Court reviewed numerous fire cases in which insureds were afforded coverage on the basis that an intent to start fires did not equate with an intent to damage property. After referring to the allegation that the fire started was "small and local" the Court concluded that:

"Even though the fire was intentionally started, the damages to the school may very well have been unforeseen physical consequences; that is, they were not substantially certain. The claim in negligence is properly pleaded. So too is trespass to property. They are alternate claims. The negligence claim is not derivative of the claim in trespass. The claims as pleaded raise, at a minimum, a possibility that a claim within the policy will succeed. Therefore, Co-Operators has a duty to defend".

The judgment in *F.(R.D.)* is very thorough and well-reasoned and stands for the proposition that alternative pleadings of intentional torts and negligence can stand together in certain circumstances.

¹³ 2004 MBCA 156.

f. Summary

In the six years since *Scalera* the Canadian legal landscape has changed significantly through the affirmation that covered claims deriving from excluded claims will not beget coverage. Below we set out the guiding principles on which a Court will decide if a claim is derivative. Thereafter we highlight some practical considerations for insurance personnel that may be useful in dealing with the changing legal landscape surrounding derivative claims.

(i) The Essence of a Derivative Claim

Close examination of the varying decisions makes clear that in some cases otherwise “covered pleas” will be excluded from coverage and yet in other cases those same pleas will attract coverage. In attempting to rationale the differing outcomes the Courts have developed a “bright line” test in applying the “derivative plea” doctrine. If the factual underpinnings of the cause of action practically dictate that the ensuing cause of action is within the ambit of an exclusion clause any suggestion that this cause of action falls within coverage is likely to fail. That is so even if the “label” afforded to the cause of action might suggest, by its very name, attract coverage. However, if the factual underpinnings to the cause of action are capable of giving rise to a cause of action that is otherwise within coverage and that cause of action could be pleaded separate and independent of a cause of action that is otherwise outside of coverage, the Courts will compel the liability insurer to afford a defence.

It is perhaps useful to illustrate the application of these principles using case examples. If, for example, a claimant alleges that an act of rape constitutes “negligence” the Courts will not compel a liability insurer to defend the action notwithstanding the Statement of Claim uses the label “negligence”. That arises because Judges recognize that the act of rape, by its very nature, is “intentional” and thus outside of coverage. In contrast, if a motorist strikes a pedestrian on the side of the road and the pedestrian sues the driver contending that either the driving behaviour was done with an intent to harm, or, at the very least, arose through carelessness, then the driver is likely to be afforded a defence. That is because Judges equally recognize that poor driving behaviour can arise either from an accident, or, with an intent to harm. It is not inconceivable that the driver’s conduct arises from mere carelessness as opposed to the intention to harm.

In practical terms this means that the “derivative doctrine” is likely to have its greatest application in cases where the “gist” of the lawsuit primarily entails conduct which, by its very nature, falls within an exclusion and the so-called “covered claims” do not sensibly arise out of the complained of conduct.

(ii) Practical Considerations for Insurers

- 1) *Joaquin* and *Cooper* demonstrate that pleadings in other actions may be relevant in determining if claims are derivative. Prior to finalizing a position, take steps to determine whether pleadings in other actions exist that may be relevant to the analysis. Conducting a court registry search for other actions, either active or discontinued, should be considered;
- 2) Closely examine preceding or related pleadings to determine whether the preceding admissions give rise to the spectre of manipulative pleadings;
- 3) The result in *Morrison* was a product of continuing amendment and refinement of pleadings by the plaintiff. The amendments may have been made for the purpose of attracting a “deep pocket” to the claim. In order to prevent this type of tactic liability insurers should commence proceedings to determine coverage early in the litigation;
- 4) The “intentional act” exclusion has been the focus of much of the litigation involving derivative claims but attention should also be paid to other exclusions such as “use or operation of a motor vehicle” in homeowner’s policies and “dishonesty” and “damage to tangible property exclusions” in E&O policies;
- 5) In addition to policy wordings, consider the impact of legislation on coverage. Section 28 of the *Insurance Act*, R.S.B.C. 1996, c. 226 provides that a violation of criminal or other law with the intent to cause loss renders a claim for indemnity unenforceable;
- 6) In cases involving assault of any kind, pleadings should refer to the status of criminal proceedings, if any exist;
- 7) Understand the nature of the wrong alleged in the underlying action. Intentional torts such as malicious prosecution, trespass to person or land, false imprisonment, intentional infliction of mental suffering and breach of privacy may allow for a denial of coverage though framed as negligent acts. The same can be said of unlawful possession of property claims such as conversion and detinue.
- 8) Be extremely careful of “artful” pleadings such as those contained in *Unrau*. Seemingly negligent pleadings may not be viable “but for” an excluded act, thereby rendering them derivative.

Canadian insurers can expect plaintiffs, in attempting to trigger “deep pockets”, to frame claims based on typically excluded acts as negligent acts without reference to the excluded acts. Accordingly, insurers must be both creative and vigilant in order to expose such tactics as manipulative.

B. MONENCO

In 2001 the Supreme Court of Canada provided some clarification in *Monenco* on the issue of the extent to which, if at all, a court could examine extrinsic evidence when seeking to illuminate the substance or true meaning of pleadings. expanded the range of documents that a Judge can examine in determining whether there exists a “duty to defend”. In *Monenco Ltd. v. Commonwealth Insurance Company* [2001] 2 S.C.R. 699, the Court said that a Judge can examine any uncontroverted contractual document, relevant to coverage, that is expressly referred to in the Statement of Claim.

In this case Monenco, the insured, sought a declaration that it was entitled to a defence under the comprehensive general liability policy issued by the insurer. The insurer claimed it was exonerated from its duty to defend under the turnkey exclusion and/or the professional services exclusion contained in the policy.

Between 1978 and 1987 Monenco, through its subsidiary, participated as engineers in a joint venture expansion project of a tar sands plant in Alberta owned and operated by Suncor Inc. Pursuant to the joint venture Monenco was responsible “for the management, engineering, procurement and construction of an expansion of the synthetic crude production capacity of Suncor’s then existing plant and facilities.” Part of the services included the design and construction of the power and electrical system for the plant. For this, the insured purchased and used electrical cables jacketed in polyvinyl chloride (PVC).

In October 1987 a substantial portion of the plant was destroyed by fire. Suncor alleged that a significant factor in the destruction of their facility was the travel of fire along the PVC cables and that the insured was negligent in specifying those cables, constructing the plant with the cables and further, failing to warn Suncor of the dangers associated with the cables.

Both of the Courts below and the Supreme Court of Canada concluded that a “turnkey exclusion” was applicable to exempt the insurer from its defence obligation. It was worded:

IT IS HEREBY UNDERSTOOD AND AGREED that:

The Insurer is not liable under this policy for claims arising out of projects for which the professional Architectural and/or Engineering services are performed by the Insured and the actual construction, installation, erection, fabrication assembly or manufacture thereof is performed by the Insured, or any legal entity wholly or partly owned by the Insured, or any individual or firm acting in the capacity or a subcontractor of the Insured.

The Supreme Court of Canada adopted the procedure of the British Columbia Court of Appeal for determining whether the claims against the insured were covered under the CGL policy. At the appellate level the Court considered what extrinsic evidence could be examined to determine whether Suncor's claims "arose out of" a project of the sort described in the turnkey exclusion. The Court decided that since Suncor had pleaded the contract with the insured it was "sufficiently incorporated by reference" into the pleadings. Moreover, the Court found that since Suncor had pleaded the existence of the joint venture the joint venture agreement could be analysed as well. After reviewing the two contracts the Court concluded that the insured was obliged to design and construct a "turnkey project" and as such, what it undertook was within the precise words of the turnkey exclusion.

In upholding the Court of Appeal's acceptance of limited extrinsic evidence the Supreme Court stated that such a procedure was "consistent with the reasoning in *Scalera*" insofar as the review "illuminates the substance of the pleadings".

A recent application of the principle in *Monenco* was applied to the issue of "undisclosed" partnerships and joint ventures in *Kingsway General Insurance Co. v. Lougheed Enterprises Ltd.*,¹⁴ a case argued by Dolden Wallace Folick LLP. In *Kingsway* three companies, each with differing shareholders, agreed to build a three storey condominium building in Richmond, B.C., in 1983. The three companies agreed to enter into a general partnership for the specific purpose of constructing the residential building in question. The partnership agreement did not contemplate any "joint activity" other than the proposed development. Each of three corporate partners undertook other development projects to their own account.

All three partners contributed money and labour in differing degrees and the partnership agreement provided for the division of profits based on their relative contributions. The building was constituted as a strata corporation.

Commencing in July, 1997 Kingsway General Insurance Company (hereafter "the Liability Insurer") only insured two of the three corporate partners; primarily because

¹⁴ 13 C.C.L.I. (4th) 173 (B.C.C.A.). ("*Kingsway*").

they had common directors and officers and purchased insurance together using the same insurance broker. However, the development of the project entailed a third corporate partner, which made no monetary contribution to the project's development, but which acted as the "Managing Partner" for supervising the trades doing the work. The third corporate partner was unrelated to the other two corporate partners, at a shareholder level, and used a differing insurance broker to purchase its insurance.

Within several years of project completion, the residential units were sold and the partners disbanded the partnership having presumably withdrawn their profits.

So, while the Liability Insurer covered the first two corporate partners as "Named Insureds" on the same policy, it did not cover as a "Named Insured" or as an "additional insured" the third corporate partner.

Then two unfortunate events arose. On July 11, 1998, a year after the Liability Insurer came on risk, a fire occurred in the building destroying much of the structure. The fire started from a balcony barbecue, but spread dramatically since the building did not have proper firewalls and fire separations, as required by the in force B.C. Building Code.

To compound matters, a second fire occurred on October 9, 2000 in another part of the building. Again, like the first fire, the fire spread was extraordinary, in view of the lack of proper fire protection as required by the relevant B.C. Building Code.

The two corporate partners requested that the Liability Insurer defend them in the lawsuits that had ensued by 2003. The Liability Insurer responded "no" relying upon the explicit policy language that contemplates an absence of coverage for a partnership or joint venture that is not explicitly enumerated on the declaration page, or by means of a specific endorsement, the Liability Insurer said in effect "*.. while we would cover you for your own activities as a developer, when you are sued solely by reason of your participation in a joint venture or partnership which you did not disclose to us, we do not have to cover that*". Kingsway filed a legal proceeding in the Supreme Court of British Columbia to determine whether its coverage position was indeed correct. The Court disagreed with Kingsway and concluded that there was coverage for the "undisclosed" partnership.

On appeal, the Court applied the *Monenco* principle to the issue of "undisclosed" partnerships and joint ventures. Practically this meant that in this case the Court could examine not only the Statement of Claim, but also the partnership agreement to determine the identity of the partners, the role each played and (indirectly) whether the nature of the partnership posed an "enhanced hazard" for which the underwriter would be unaware. After considering the allegations in the Statement of Claim and

reviewing the partnership agreement, the Court agreed with Kingsway and concluded that there was no coverage for the "undisclosed partnerships and joint ventures.

C. DERKSEN

1. The Impact of the *Derksen* Decision: Concurrent Causes of Loss Language

a. Introduction

In the broadest terms, this section outlines wording revisions that increase the operation of certain exclusions in situations where two or more consecutive or concurrent perils give rise to a liability exposure. The practical effect of these changes is to move the defence obligation from the liability insurer onto the shoulders of either an automobile liability policy, or, other more specialized forms of coverage such as marine liability, or aviation liability policies.

Historically, when faced with a claim for coverage under a liability policy, Canadian liability insurers looked to determine if there was a single, dominant, or "proximate" cause of the loss. If so, and that cause of the loss was an included peril of coverage, then coverage was granted. If that cause of the loss was an excluded peril, then coverage was not available.

However, the term "proximate cause" is a negligence law concept, and its application in an insurance policy analysis can be problematic. In the past decade there has been a shift away from the "proximate cause" approach to a more expansive approach to ascertain if a peril fits within the outer parameters of coverage. This issue was ultimately considered in 2001 by the Supreme Court of Canada in the *Derksen* case. The Supreme Court of Canada not only assumed the role of deciding if there could be more than one cause of a loss, but also outlined the method for determining the applicability of coverage when one of the losses was covered and one was excluded.

The liability insurance industry has typically taken the stance that exclusions are premised upon either the existence of another policy of insurance, or, because the loss was not fortuitous. However, our Courts are finding there can be many losses arising from a "mix" of perils, some of which are covered, others are not and the issue has become "*does the insured have coverage when one of the perils is excluded and yet another peril that contributed to the loss is covered under the policy?*"

Trial Courts have responded to the decision in *Derksen, supra* in unpredictable ways. Given the varied response, the IBC elected to include “anti-concurrent causation language” in the New IBC CGL Form Automobile Exclusion, and in other exclusions as well. The question becomes how will the Courts now respond to this new “anti-*Derksen*” language? What “post-*Derksen*” results will now be eliminated?

b. The Law Before *Derksen*

Thirty years ago Canadian Courts would have likely adopted the English Court of Appeal’s practice that where two causes of a loss existed, one within coverage and one not, the Court would search to “...determine which cause is the ‘effective or dominant cause’.”¹⁵ Fifteen years ago the Supreme Court of Canada stated that “...it should not debate on which of various causes of a loss were proximate....scepticism is advised when addressing this metaphysical topic...”.¹⁶ Then, ten years ago, the B.C. Court of Appeal spoke on this issue. It clarified that a very common cause of loss in B.C., namely water damage due to seepage and leakage, may in fact have a concurrent or second cause, namely a burst water pipe (one typically covered, the other typically excluded).¹⁷ By this time, the judicial door was opened to a series of otherwise excluded claims against Canadian liability insurers, which caused great debate as to what constituted “concurrent causes of loss.”

In the same time period the Supreme Court of Canada gave a broad interpretation to the words “ownership, use or operation” of a vehicle. In the case of *Amos v. I.C.B.C.*,¹⁸ the Court concluded an injury arose out of the ownership, use or operation of a vehicle, after an individual had been attacked and shot through the window of his car by persons apparently attempting to gain entry to the car. The Court found the incident resulted from an “ordinary and well-known activity” to which motor vehicles are put and found a sufficient connection between the injuries and the use of the vehicle. In doing so, the Supreme Court considered the causation issue and noted that the words “arising out of” were viewed in certain cases as words of a much broader significance than “caused by”. It was decided that negligence or fault in the use or operation of the vehicle did not need to be the cause of the injury.

All of these rulings would ultimately play a role in the decision in *Derksen, supra*.

¹⁵ *Wayne’s Tank & Pump Co. v. Employer’s Liability Assurance Corp* [1974] Q.B. 57.

¹⁶ *CCR Fishing Ltd. v. British Reserve Ins. Co* [1990] 1 R.C.S. 814.

¹⁷ *Pavlovic v. Economical Mutual Insurance Company* 99 B.C.L.R. (2d) 298 (B.C.C.A.).

¹⁸ 1995 Carswell BC 1142 (S.C.C.) [hereinafter “*Amos*”].

c. The *Derksen* Decision

In 2001 the Supreme Court of Canada considered the coverage issues that arose out of an accident in which one child was killed and three were injured. A steel base plate (part of a road sign assembly), which had been put on the defendant's truck by the defendant driver as part of the clean up at a work site, flew off the truck through the windshield of an oncoming school bus.

The Plaintiffs alleged negligence both at the work site and in the operation of the truck. The Ontario Trial Judge decided that the accident resulted from concurrent causes, negligent clean up and negligent operation of the truck, and that both the liability policy and the auto policies provided coverage. This finding was upheld by the Supreme Court of Canada. This conclusion was reached notwithstanding the standard exclusion in the liability policy of the "use or operation of an automobile".

The Supreme Court of Canada made the following broad findings

- (a) *Derksen, supra*, was based on a series of events that were separate causes contributing to the same loss, as opposed to a series of events that were the same cause of the loss;
- (b) Insurers may suggest there was an independent and intervening act (more proximate cause) that broke the chain of causation, but this is not correct. The operation of an intervening force will not ordinarily absolve a defendant of further responsibility if it can be considered a normal incident of the risk created by the harm;
- (c) Where there are concurrent causes there is no presumption that all coverages are ousted if one of the concurrent causes is an excluded peril. This is a matter of interpretation and must be expressly stated in the insurance policy;
- (d) As insurers have language available to them that would remove all ambiguity from the meaning of an exclusion clause in the event of concurrent causes, there was no reason to decide in favour of the insurer;
- (e) The broad interpretation of the phrase "arises out of the use or operation of an automobile" did not apply. The broad meaning of the phrase "arises out of" applies in the context of a claim for coverage. In *Derksen*, the phrase "arises out of" was in the context

of an exclusion clause (in the CGL policy) which is given a narrow interpretation.

- (f) There was nothing in the CGL policy to indicate there was no coverage for an insured risk if an expressly excluded risk was an additional cause of the injury. Therefore the exclusion clause was ambiguous with respect to losses from concurrent causes; and
- (g) Each insurer was liable for coverage for only that portion of the loss attributable to their insured's risk.

d. The Application of *Derksen* in Motor Vehicle Cases

Despite what is described as a continuing shift toward a more expansive definition of the phrase "arising out of the use or operation of a motor vehicle" since the decision in *Amos, supra*, the ruling in *Derksen, supra*, has allowed Courts to look to other conduct which might have otherwise been included under an auto insurer's coverage. The following are some examples:

- (a) Oil Leaked from a fuel truck and caused pollution to lands

Although a fuel leak is considered to be an "ordinary and well-known activity" to which vehicles are put, and was connected to the operation of the fuel truck, this was also a failure to inspect the fuel lines which was deemed to be covered under the CGL policy. Both the auto and CGL policies applied.¹⁹

- (b) Motor vehicle accident caused during a sales demonstration of vehicle

The insured caused the accident while demonstrating an amphibious vehicle. There was an exclusion for the use and operation of a motor vehicle. The Court found a concurrent cause of the loss - the insured's allegedly defective salesmanship - which was covered under the policy.²⁰

¹⁹ *Harvey's Oil Ltd. v. Lombard General Insurance Co. of Canada*, 231 Nfld & P.E.I.R. 281.

²⁰ *Neary v. Wawanesa Mutual Insurance Co* 216 N.S.R. (2d) 219.

(c) Dog in back of open truck bites person

The allegation that the Defendant dog owner failed to keep his dog contained in the vehicle constituted a causal connection to the loss and therefore was a “use and operation”. The failure to control the dog also called for coverage under the dog owner’s liability policy. Both the general liability insurer and the auto insurer were required to provide a defence and indemnity for the Defendant.²¹

Auto insurers and insureds will continue to rely on *Derksen* to try and stretch the web of coverage wide enough to find a second cause of a loss to obtain additional coverage. Fortunately for Canadian liability insurers, the Ontario Court of Appeal has offered some guidance on how to deal with pleadings that attempt to obtain dual coverage. In the Ontario Court of Appeal decision in *Unger (Litigation Guardian of) v. Unger*²² an employee, while driving his work vehicle, injured the Plaintiff. The Plaintiff sued both the employee and the employer. The Ontario Court of Appeal determined that an allegation against the employer for negligent hiring, training or supervision of the employee may be germane to whether the defendant was negligent in the use or operation of a vehicle, but not a “stand alone ground for recovery”. The Court stated that “[T]he allegations, even if proved, without also proving negligent use of a motor vehicle would not allow the insured to succeed.”

II. BREACH OF A CONDITION

An insured may be in breach of a condition of his policy either pre or post loss. An example of an insured breaching a condition pre loss is the insured's failure to comply with the condition that the insured insure all of its aircraft through the same aviation insurer.²³ If an insured fails to comply with the notice provisions of his or her policy, he may have breached a condition post-loss. If there has been a breach of a condition by the insured that occurs either pre or post-loss the Canadian courts will, in some cases, determine whether "relief from forfeiture" applies so that the insured is excused from the consequences of his breach. In this section, cases dealing with breaches of conditions by the insured pre and post-loss will be discussed as well as the principle of "relief from forfeiture".

²¹ *Taylor v. Maris* 201 B.C.A.C. 314 (B.C.C.A.).

²² [2003] O.J. No. 4587 (Ont. C.A.).[“*Unger*”].

²³ See *Webber v. Canadian Aviation Insurance Managers Ltd.* 42 C.C.L.I. (3d) 124 (BCSC) (“*Webber*”).

A. POST-LOSS BREACHES

In a liability policy an insured is required to notify the insurer as soon as practicable after the "occurrence" has occurred. If an insured delays in reporting the claims to his or her insurer and the insurer then denies coverage on the basis of "late reporting", a Court in determining coverage will first look at how late the insured was in providing notice to the insurer. The Court will then determine if the late notice prejudiced the insurer in its investigation and whether pursuant to section 10 of the *Insurance Act*, R.S.B.C. 1996, c. 226 the insured is entitled to relief from forfeiture.

The leading "late notice" case is *Marcoux v. Halifax Fire Insurance Co.*²⁴ In *Marcoux* the insured's truck driver struck a pedestrian. Following the accident the driver offered to take the pedestrian to the hospital, but the pedestrian declined. The driver relayed the incident to his employer and that in his view the pedestrian was not injured. No notice of the accident was given to the insurer until two months later when the pedestrian commenced an action against the driver. The insurer declined to defend and indemnify the insured on the basis of "late notice".

The SCC upheld the insurer's denial of coverage and in determining this issue stated:

The policy of insurance is a contract between the parties. The respondent undertook to indemnify the appellant; but on a condition, that is, that it be given prompt notice of the accident. One readily understands the reason justifying this clause of the contract. It is for the purpose of permitting the insurance company to make an investigation immediately, to check the facts, to seek the names of witnesses who later on may not be discoverable, and thus not to be at the mercy of the claimant. This is a protection justly claimed in the contract, and of which the insured cannot deprive his insurer with impunity....

It is not the assured who is to determine the gravity of the injuries and decide whether or not the insurance company should make an investigation. His obligation is to give notice, the company will take measures it deems necessary. The appellant perhaps acted in good faith, but the events demonstrated he was wrong, that he was ill-informed, as the evidence has revealed that as a result of this accident, Roger had three ribs fractured and suffered other bodily injuries. It is the appellant who must suffer the consequences and not the respondent.

The notice was a condition precedent to any recourse the appellant could exercise against the respondent, and as he did not give it, his claim must be dismissed.²⁵

²⁴ [1948] 4 D.L.R. 143 (S.C.C.) ("*Marcoux*").

²⁵ *Supra* note 24 at 146.

In *Sumitomo Canada Ltd. v. Canadian Indemnity Company*²⁶ the Plaintiff sued the insured's insurer to recover on a judgment it had obtained. Canadian Indemnity refused to indemnify the Plaintiff because its insured had failed to report the claim. The insured had two policies of insurance and had reported the claim to its broker after it had been served with a Writ of Summons and Statement of Claim. The broker notified one insurer but did not notify Canadian Indemnity. Approximately 22 months after the damage occurred Canadian Indemnity was notified. The Court, citing a Supreme Court of Canada decision, *Marcoux v. Halifax Fire Ins. Co.*²⁷ stated that Rand J. was prepared to assume that the language of the condition in the policy requiring notice:

...must be interpreted not absolutely but in the background of the ordinary and reasonable understanding of such a requirement on the part of persons who enter into such contractual relations...

The Court in *Sumitomo Canada Ltd.* stated:

Applying the test of Rand J., that the condition should be applied, not absolutely, but in the background of the ordinary and reasonable understanding of such a requirement, I cannot find that Sea Import acted improperly. It received a writ, it notified its broker and it had competent, experienced legal advice. To apply the condition here would be to apply it absolutely. The authority I have cited suggests that I should not do that.

I wish to add that I do not think the defendant has been prejudiced in any meaningful way by the failure of Sea Import to give notice when the writ was served. By that time the coils had been shipped to California, many months earlier, and Sea Import had retained the most competent expert witnesses who were available.

Despite the fact that the insurer received notice 22 months after the "occurrence", the Court concluded from the evidence that the insurer had not been prejudiced given that the insured had obtained competent legal advice and had retained excellent experts who assisted in defending this matter. As a result, the insured had to indemnify the insured.

In *Thomas v. Hickey*²⁸ the insured notified the insurer 20 months after the motor-vehicle accident had occurred and the Court concluded that notwithstanding the late reporting, the insurer had a duty to defend the underlying litigation. This decision is contrasted with *Marcoux* discussed above wherein the Court concluded that late notice of 2 months resulted in the insurer having no duty to indemnify the insured. There is no hard and fast rule as to the length of the delay in reporting a claim by an insured before the Court

²⁶ [1981] 5 W.W.R. 508 (B.C.S.C.) ("*Sumitomo*").

²⁷ [1948] S.C.R. 278.

²⁸ (1995), 22 O.R. (3d) 331 (Gen. Div.).

will conclude that the insurer has no duty to defend and indemnify the insured in the underlying litigation. The key is whether the insurer is in fact prejudiced by the delay.

Even if the Court concludes that the insured was late in reporting its claim to the insurer, the Plaintiff may argue that he should be relieved from forfeiture pursuant to the *Insurance Act*. Relief from forfeiture is an equitable remedy available to a party that allows it to maintain the benefits of a contract in instances where it has failed to strictly comply with its own obligations thereunder. Courts may be convinced that it would be unjust to relieve an insurer from liability on the basis of the insured's "imperfect" compliance with the insurance contract. In such cases the Court may excuse the breach through either of two statutory provisions.

Section 10 of the *Insurance Act* says:²⁹

If there has been imperfect compliance with a statutory condition as to the proof of loss to be given by the insured *or other matter or thing required to be done or omitted by the insured with respect to the loss...*the court may, on terms it deems just, relieve against the forfeiture... (Emphasis added)

Similarly, the *Law and Equity Act*,³⁰ contains a general provision which permits the Court to relieve against the requirement for strict compliance with contractual terms if to enforce the terms would cause unfair hardship. Section 4 of the Act says:

If a plaintiff or petitioner claims to be entitled...to relief on an equitable ground against a deed, instrument or contract, or against any right, title or claim asserted by a defendant or respondent in a cause or matter, ... the court,...must give the plaintiff or petitioner the relief that ought to have been given by the court in a suit or proceeding in equity for the same or similar purpose properly commenced before April 29, 1879.

An example of the Court granting relief from forfeiture occurred in *312630 British Columbia Ltd. v. Alta Surety Co.*³¹ In that case, an aggregate supplier sought payment from a surety under two Labour and Material Payment Bonds. A clause in the bonds required that notice of a claim be given within 120 days, however, the insured had been late in affording written notice.

The case is instructive in that it is one of the few decided cases in which the doctrine of relief from forfeiture was used to reduce the insured's claim by a monetary amount that was caused or attributable to the breach of condition; in this case late notice. The Court permitted the insured to recover \$100,000 of the \$170,000 claimed on the bonds on the

²⁹ R.S.B.C. 1996 c. 226

³⁰ R.S.B.C. 1996 c. 253

³¹ [1995] B.C.J. No. 1600 (B.C.C.A.)

premise that any amounts in excess of \$100,000 arose from the bonding company's inability to properly manage the risk had notice in writing been provided on a timely basis. In reducing the insured's recovery in a monetary manner the Court addressed various factors to be considered in deciding whether to grant relief from forfeiture including the degree and type of prejudice to the surety, the insured's knowledge and awareness of the contractual requirement, the experience and knowledge of the insured and the insured's degree of delay in affording written notice. The Court stated:

I agree that those are all relevant factors in relation to the discretion *but by far the most important factor is the factor of whether the surety has suffered prejudice. ...In my opinion, the question is whether the surety has suffered actual prejudice.* (Emphasis added)

This decision illustrates how the Court will use the doctrine of relief from forfeiture to provide a solution when there has been a breach of condition while ensuring that the insurer does not pay a monetary sum in excess of what would otherwise have been paid had there been no breach of a condition.

Section 10 of the *Insurance Act* applies to breaches of conditions that occur post loss. In determining whether the equitable relief from forfeiture is available in particular cases, the Courts have concluded that it is not available in situations where the insured has failed to pay an insurance premium as the effect of a breach of this nature brings the contract to an end. There being no contract, there are no rights to be forfeited so there can be no forfeiture and therefore nothing to relieve against. In another case, the Court refused to grant equitable relief from forfeiture when the insured failed to maintain registration of a vehicle.

In these cases the Courts will not use the relief provision to create obligations where they do not already exist or where they have expired. Further, Courts will not grant equitable relief from forfeiture, in cases where the insured has attempted to commit a fraud against the insurer by inflating his claim. When considering whether equitable relief will be granted the Plaintiff must come to the Court with "clean hands".

B. PRE-LOSS BREACHES

In *Webber v. Canadian Aviation Insurance Managers Ltd.*³² the Court refused to grant equitable relief from forfeiture when the Plaintiff failed to comply with the requirements for coverage under his aircraft insurance policy. The Plaintiff had insured three aircraft under his aircraft insurance policy. The Plaintiff applied for coverage for a

³² 42 CCLI (3d) 124 (BCSC).

fourth aircraft that he owned with his son. Coverage for this aircraft was denied. The Plaintiff's insurance broker obtained coverage for this aircraft through a different insurer. The Plaintiff bought a fifth aircraft and obtained coverage for it. The day after coverage was obtained this aircraft was involved in a collision.

The Plaintiff sought coverage under the "New Acquired Aircraft" provision. Coverage was only triggered if all of the Plaintiff's aircraft was insured with the defendant insurer. The insurer denied coverage. The Plaintiff commenced a declaratory action for coverage. In determining that there was no coverage, the Court then went on to consider whether equitable relief ought to be granted:

An examination of the conduct of the parties discloses that CAIM acted promptly in dealing with the Plaintiffs' application for insurance coverage for LWQ, notifying the insurance brokers within days of receiving the application (first by telephone and then in writing) that the application had been denied.

As far as the conduct of the Plaintiffs is concerned, their insurance brokers were aware that coverage had been denied within days of the application having been made. The fact that the insurance brokers do not appear to have informed the Plaintiffs of this occurrence is an issue between them and the Plaintiffs. It was not a matter over which CAIM had any involvement or control.

Moreover, although the insurance brokers did not apparently notify the Plaintiffs of the denial of coverage, the Plaintiffs, on the other hand, do not appear to have made any inquiries as to the status of the LWQ application.

With respect to the gravity of the breach, the breach was a serious one in this case. In particular, *there was non-compliance with a fundamental requirement of coverage* under the Newly Acquired Additional Aircraft provision of their policy.

Upon considering the conduct of the parties and the gravity of the breach, I conclude that it would be unjust to grant relief from forfeiture in this case. Given that conclusion, I decline to exercise my discretion under s. 24 of the Law and Equity Act. This application is dismissed.

In summary, in considering whether relief from forfeiture will be granted the factors the Court will take into consideration in determining whether it should grant relief are:

- (a) the conduct of the insureds;
- (b) the gravity of the breach; and

- (c) the disparity between the value of the property forfeited and the damage caused by the breach.

If the Court does grant relief from forfeiture, the insured's breach is excused resulting in the insurer having to defend and indemnify the insured.