Litigation Strategy Series: Coverage Seminar

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Outline

Topics:

1. Insurance Coverage – 1st party insurance coverage vs. 3rd party liability coverage

2. Different types of liability coverage

3. Determining Coverage – duty to defend vs. duty to indemnify

4. Additional insureds

5. Coverage analysis – how to

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Insurance Coverage:
1st party insurance coverage vs. 3rd party liability coverage

- Insurance is, essentially, a contract for indemnity.
    - An agreement between insurer and insured that if the insured sustains a certain kind of loss under certain specified conditions, the insurer will pay a specific amount of money to the insured (or to specified third parties) in order to address that loss.
    - Important to remember that there is nothing magic about insurance – it is in essence just a contract (usually).
    - The actual wording of the contract (the insurance policy) will usually govern that relationship and the parties' respective obligations to each other.

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Insurance Coverage:
1st party insurance coverage vs. 3rd party liability coverage

- Two main types of insurance we are normally concerned with:
  - First party insurance coverage
  - Third party liability coverage

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First Party Coverage

- First Party insurance coverage is indemnity or benefits that must be paid to the insured to address a loss sustained directly by the insured.
  - Examples:
    - Property Insurance
    - Disability Insurance (STD/LTD)
    - Health Insurance
  - Each of these types of insurance requires the insurer to indemnify the insured for a loss or expense sustained directly by the insured

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First Party Coverage

- There are also forms of statutory first party insurance:
  - SABs
  - WSIB
  - These are special types of insurance because there does not necessarily need to be a specific contractual relationship between the claimant and the insurer (whether private or government). Rather, for these types of insurance, the insurer is required by legislation to pay claims made by individuals under certain specific conditions.
  - But these are still all forms of first party insurance, because they compensate the claimant for losses or expenses sustained by the claimant.

Third Party Liability Coverage

- By contrast, third party liability coverage insures against claims made against the insured by a third party.
  - Third party liability insurance typically must indemnify the insured for amounts the insured becomes legally obligated to pay to someone else, if certain specified conditions are met.
  - Third party liability insurance also often, but not always, provides coverage for other needs or expenses related to claims made against the insured, such as the expenses associated with the defence of a lawsuit and provision of that defence.

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Bundled Policies

- Many types of insurance policies bundle first party insurance with third party insurance.
    - For example, home insurance often contains a section providing coverage for damage to the insured's house, and a section providing general third party liability coverage.
    - Auto insurance usually provides coverage for the insured's vehicular negligence, and for damage to the insured's own vehicle.
    - Commercial insurance policies often bundle property insurance for the insured's own property with commercial general liability insurance.

Bundled Policies

- When dealing with a bundled policy that provides both first and third party coverage, it is important to ensure that you are reviewing the portion of the policy applicable to the type of claim at issue.

- If the claim at issue is a first party claim for the insured’s own loss, make sure you are looking at the first party coverage portions of the policy. If it is a claim for the insured’s liability for a third party’s loss, make sure you are looking at the third party liability portions of the policy.

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Different Types of Liability Coverage

- Home Insurance
  - Not a standard form policy, but home insurance policies tend to use the same or similar language for the liability section.
  - Generally insures the named insured(s), and any spouse or relatives of the named insured(s) while living in the same household as the named insured(s), for liabilities resulting either from their ownership or occupancy of the insured house, or from the insureds' actions anywhere in the world.
  - Usually does not cover claims made against an insured by another member of the household.
  - Usually does not cover claims arising from the ownership, use, or operation of an automobile.

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Different Types of Liability Coverage

- Automobile Insurance
  - Heavily regulated. Automobile insurance policies are standard form policies that are set by FSCO, that insurance industry regulator.
  - Most common form of auto insurance is the OAP 1 standard owner's policy.
  - Covers the named insured(s) in respect of their liability as owner of a specified vehicle (called the "described automobile"), including *HTA* vicarious liability, and in respect of liability arising from the use or operation of the described automobile, and the use or operation of other automobiles subject to certain terms.
  - Also covers anyone driving the described automobile with the named insured's consent.
  - Can be modified by attachment of endorsements, which are additional pages that can be attached to an insurance policy that modifies the language of the main policy. Endorsements form part of the policy language. Endorsements to auto policies are standard form and must be set or approved by FSCO.
  - Another common type of auto insurance is the SPF 6 non-owned auto policy. This policy is actually an endorsement that gets attached to a commercial general liability policy. It insures the insured (usually a business) against liability arising from the use or operation of a vehicle that the insured does <u>not</u> own.

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Different Types of Liability Coverage

- Commercial General Liability Insurance
  - CGL insurance is usually provides as part of a larger commercial insurance policy, but could be stand-alone insurance.
  - In any case, usually operates independently of other portions of a policy it may be bundled with.
  - CGL is not standard form, and the language can and often does differ from policy to policy.
  - However, CGLs tend to contain much of the same or similar language, so there is some consistency as to what CGLs cover and how the relatively standard provisions will be interpreted by the courts.
  - CGLs provide coverage for liabilities arising from a number of different types of risks faced by businesses. The coverages they provide vary, but the coverage we deal with most frequently is almost always present, which is coverage for liability arising from property damage or bodily injury.

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Different Types of Liability Coverage

- Commercial General Liability Insurance (continued)
  - The bodily injury and property damage coverage provided by CGLs are subject to a number of exclusions. They typically will not cover claims:
    - For injury or damage that was intended from the perspective of the insured (intentional acts);
    - Arising from or in connection with the use or operation of motor vehicles;
    - For the insured's contractual liabilities, except for liabilities the insured would have had irrespective of the contract (there are often other exceptions as well);
    - For property damage that is essentially just the insured's own shoddy work or defective product. CGL's are not intended to insure against the insured doing a poor job or creating a defective product, that then has to be repaired, replaced, or redone. However, CGL's will cover consequential damages to other property caused by the insured's shoddy work;
    - Arising from professional services rendered by the insured.

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Different Types of Liability Coverage

- Wrap-up Insurance
  - This is a species of CGL insurance.
  - Typically obtained for large construction projects, either by the owner or the general contractor.
  - Usually insures the owner, the GC, and essentially everyone else who worked on the project for loss or damage to or arising from the project for a limited period of time after the project is completed.
  - Idea is that for a specified time period after the completion of the project (usually two years), any issues that arise or occur with the building are dealt with by the wrap-up insurer, rather than by the individual trades and their insurers.

Different Types of Liability Coverage

- Professional Liability Insurance
  - Insures professionals for liability resulting from errors and omissions made in the course of professional duties.
  - Tend to operate differently than CGLs
    - Often "claims made" rather than "occurrence based," meaning the time period they insure applies to when a claim is made against the insured, rather than when the incident giving rise to the claim actually occurred.
  - Important to read these policies carefully to determine what they cover.

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Different Types of Liability Coverage

- Directors and Officers Liability Insurance
  - Insures directors and officers of a corporation against claims made against them in their capacity as directors and officers of the corporation.
  - May also insure the organization against certain types of claims, such as employment-related claims.

Determining Coverage: Duty to Defend vs. Duty to Indemnify

- An insurer's obligation to indemnify its insured only arises when the conditions for indemnity set out in the policy are met.
- For a liability insurance policy, those conditions are typically that the insured has become legally obligated to pay damages or compensation to a third party.
- In the context of a lawsuit, a defendant does not become legally obligated to pay damages to the plaintiff as soon as the action is commenced. The defendant only becomes legally obligated to pay damages upon settlement, or judgment against the defendant.
- So the duty to indemnify really only arises at the *end* of the case.

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Determining Coverage: Duty to Defend vs. Duty to Indemnify

- On the other hand, where the liability policy obligates the insurer to defend the insured in respect of a claim to which the insurance applies, that obligation arises much sooner.

- The insurer's duty to defend arises as soon as the insured is presented with a claim by a third party that could, if proven, potentially trigger indemnity coverage under the policy.

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Determining Coverage: Duty to Defend vs. Duty to Indemnify

- Accordingly, the insurer's duty to defend arises much sooner than the duty to indemnify, and is much broader.
  - The duty to defend arises at the beginning of a claim, whereas the duty to indemnify only arises at the end.
  - The duty to defend only requires that the claim, read broadly and generously, alleges facts that if ultimately proven true give rise to the mere possibility of indemnity coverage under the policy.
  - The duty to indemnify is usually determined on the basis of the actual facts as found at trial, or in a coverage proceeding following the determination of the underlying claim.

Determining Coverage: Duty to Defend vs. Duty to Indemnify

- The Pleadings Rule
  - From *Nichols v. American Home Assurance Co.*, [1990] 1 SCR 801
  - Usually, the insurer's duty to defend will be determined based only on the pleadings and the policy.
  - The court will review the pleadings and determine whether the allegations, if proven true, give rise to the mere possibility of indemnity coverage under the policy.
  - However, the court is not bound by the labels the claimant chose, and must consider the "true nature" of the claim against the insured. (*Non-Marine Underwriters, Lloyd's of London v. Scalera*, 2000 SCC 24)

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Determining Coverage: Duty to Defend vs. Duty to Indemnify

- The Pleadings Rule (continued)
  - On a duty to defend application, the court generally should not receive evidence about issues in the underlying dispute.
  - The idea is that the court should not make findings of fact in the coverage proceeding that should properly be made in the context of the underlying claim.
  - The pleadings rule is not absolute! There are exceptions.
  - The court may receive on a duty to defend application contracts and other documents referred to in the pleadings in the underlying action, and evidence of facts that are unrelated to the underlying dispute but which nevertheless may affect coverage. (*IT Haven Inc. v. Certain Underwriters at Lloyd's, London,* 2022 ONCA 71)

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Determining Coverage:
Duty to Defend vs. Duty to Indemnify

- Interpretive Aids
  - Insurance policies are generally considered to be contracts of adhesion. *Contra proferentem* applies strongly.
  - Courts will interpret coverage granting provisions broadly, and coverage limiting provisions narrowly.
  - Any ambiguity will be resolved in the insured's favour.
  - However, before resorting to these interpretive aids, there must a true ambiguity!
  - Just because a provision is hard to understand does not make it ambiguous. Ambiguity means that the provision is genuinely capable of more than one interpretation.

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Additional Insureds

- Liability policies generally cover the named insureds on the policy. These are the entities whose names are printed in the policy declarations as “the insureds”.
- However, many liability policies extend coverage to parties other than the named insureds. There are a number of different ways this is accomplished.

Additional Insureds

- Policy Definitions
  - Often, liability coverage is extended to parties other than the named insured through the use of defined terms in the policy.
  - Most policies have a "definitions" section, which contains a glossary of defined terms. Sometimes, those terms will include terms like "you" or "the insureds", and the definition of those terms will explicitly include entities other than the named insureds.
  - For example, a home insurance policy might define "the insureds" as the named insureds and their spouses and relatives who reside with them in the household. This makes any spouses or relatives of the named insureds additional insureds, as long as they reside in the same household as the named insureds.

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Additional Insureds

- “Who is Insured” Section (or similar)
    - Many policies have a section that contains specific provisions outlining conditions under which entities other than the named insureds will be afforded coverage as additional insureds under the policy.
    - E.g.: employees of the named insureds while in the course of their employment.

Additional Insureds

- Additional Insured Endorsement
    - Liability policies can be endorsed with an endorsement that adds other parties to the policy as additional insureds, often subject to specific terms (e.g. only for claims arising from the business operations of the named insureds).

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Additional Insureds

- Certificate of Insurance
  - These do not really create coverage for an additional insured.
  - These are issued by the insurance broker, rather than the insurer, and are merely evidence of an intention to add a particular party as an additional insured under the policy.
  - There should be a correlated additional insured endorsement or policy provision that actually extends coverage to the party listed in the certificate of insurance as an additional insured, and that terms of that endorsement or policy provision govern the additional insured's entitlement to coverage, not the certificate of insurance.
  - Not to be confused with a Certificate of Insurance in the auto insurance context – that is actually part of the policy (equivalent to the policy declarations for most other policy types).

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How to Conduct a Coverage Analysis

Read the pleadings, the background info, and the policy, and ask yourself:

- Is the party seeking coverage insured under the policy?
- Did the loss occur during the policy period?
- Does the claim fall within the grant of coverage?
- Are the damages claimed of a type that is actually covered by the policy?
- Is the loss within the geographic limits of coverage?

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How to Conduct a Coverage Analysis

- Is the loss excluded by a policy exclusion?
  - If so, does it meet the criteria for any exceptions to the exclusion?
- Has the insured breached any of the conditions of the policy?
  - E.g. late reporting of claim, failure to report a material change in risk.
  - Could the insured get relief from forfeiture?
- Could waiver or estoppel apply to bar the insurer from denying coverage?

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How to Conduct a Coverage Analysis

- Other insurance provisions: priority of coverage
  - If there is coverage under the policy, might the insured also be entitled to coverage for the same loss under another policy?
  - If so, how do the two policies contribute to the loss.

How to Conduct a Coverage Analysis

- Covered vs. uncovered claims and concurrent duties to defend.
  - In the context of determining an insurer's duty to defend, some of the allegations advanced against the insured may be covered, while others may not be.
  - In such circumstances, the insurer will generally be responsible for defending the insured in respect of the entire claim, unless there are specific, extricable defence expenditures that are clearly only related to uncovered claims (which is rare).
  - If two or more insurers have overlapping, concurrent duties to defend the same insured, courts will typically require the insurers to contribute equally to the cost of the defence, subject to a potential reallocation at the end of the case.

Thank you!!

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