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Court of Appeal Provides a Further Look at the Additional Insured

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Disputes over additional insured status are legendary and frequent. Every insurer faces demands for a defence from additional insureds. Brokers are requested to issue certificates of insurance on a daily basis, identifying people or companies as additional insureds. Assigning insurance obligations is an essential feature of most contractual relationships. There is no avoiding the issue of the duty to defend an additional insured. Yet the outcomes of legal disputes about the issue have been unpredictable in the past and only recently has a trend towards more predictability emerged. On December 22, 2015, the Ontario Court of Appeal released its latest decision on the topic. While still not yet solving all of the problems in the area, it continues the trend towards a framework for insurers to resolve these disputes without unnecessary litigation.

In *Carneiro v. Durham (Regional Municipality),* 2015 ONCA 909, the liability issue related to a fatal car accident, allegedly caused by icy road conditions. The deceased's family members sued the Regional Municipality of Durham for its liability as the owner of the roads. The co-defendant was Miller Maintenance Limited hired by Durham as its road maintenance contractor.

The Court of Appeal characterized the allegations against Durham and Miller as "a laundry list of identical particulars of negligence". The allegations included the failure to keep the road free from ice and snow, inadequate design of the road, and failure to close the road during a snowstorm. The plaintiffs did not distinguish between the defendants. Durham and Miller appointed separate defence counsel and maintained crossclaims against the other, alleging the other was solely responsible.

As expected, the road maintenance contract required Miller to obtain general liability insurance and to ensure that Durham was named as an additional insured on Miller's insurance from Zurich. When Durham requested Zurich to defend it in the action, Zurich refused. Zurich argued the allegations against Durham were unrelated to Miller's work and therefore fell outside its coverage as an additional insured. Durham commenced a third party claim against Zurich

seeking a declaration that Zurich must defend and indemnify Durham. Durham brought a motion seeking a determination of the issue.

The motions judge refused to order Zurich to defend Durham. He found that the duty to defend existed only with respect to "claims insured for Miller". The judge accepted the argument that Durham was required to defend itself against allegations unrelated to the contractor's negligence. The judge further reasoned that Durham's liability exposure arising from the contractor's negligence was adequately protected by the contractor's own defence.

Durham appealed and won. The Court of Appeal commenced its analysis by reminding the parties that the duty to defend an additional insured is governed by the allegations in the pleadings and the terms of the insurance contract. The Court observed that the Zurich policy "contained an unqualified promise to defend the [additional] insured for actions covered by the policy." The pleadings rule dictates that the mere possibility some allegations in an action will fall within coverage engages the obligation to defend the action. The true nature of the pleading was that the deceased's car slid on an icy roadway. The common allegation that Durham and Miller failed to keep the roadway clear related directly to the obligations under the maintenance contract. Accordingly, because the statement of claim alleged facts that, if true, were within the coverage, Zurich's obligation to defend Durham was triggered.

The Court's use of the word "unqualified" should not be interpreted as suggesting the duty to defend is unlimited, but only that the insurance policy did not provide for a mechanism to deal with situations where an action contains both covered and non-covered allegations. The Court observed that there is no obligation to pay costs related solely to the defence of uncovered claims. Further, it acknowledged that the obligation is to pay only the reasonable costs associated with the defence of the covered claims. In accordance with the Court's decision in *Hanis v. University of Western Ontario*, 2008 ONCA 678, where there are allegations both inside and outside of coverage (so-called "mixed" claims), any reasonable costs associated with the defence of the covered claims are payable, even if they happen to benefit the uncovered allegations. In this way, the defence obligation is "unqualified".

In the face of "mixed" claims, the defence obligation is not unrestricted. This means the insurer may seek an apportionment and reimbursement of defence costs incurred solely with respect to uncovered claims. What is emerging in the *Carneiro* decision and the Court's prior decision in *Tedford v. TD Insurance*, 2012 ONCA 429 is the preference that any reallocation be by agreement of the parties or by application to the Superior Court "at the end of the proceedings." Prior case law seeking to have a Court make an interim allocation of costs for an additional insured appears to be falling out of favour. The duty to defend the action against an additional insured may now require the insurer to pay 100% of the defence costs on an interim basis. But the additional insured may be required to reimburse the insurer at a later date.

The focus must now shift to how *Carneiro* will impact cases involving a legitimate argument that an additional insured has independent negligence for an accident. Postponing the allocation discussion may have unintended consequences. No doubt there remains many issues to be

resolved with respect to coverage for the additional insured. The industry may well revisit the manner in which it endorses policies for additional insureds.