IADC COMMITTEE NEWSLETTER

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IN THIS ISSUE

This article is yet another example of the British Columbia Court of Appeal attempting to achieve clarity, predictability and intellectual honesty to the sometimes vexing world of insurance interpretation, exclusion clauses—pollution exclusion clauses in particular, and the law of costs in insurance disputes.

The Quixotic Quest for Ambiguity in Insurance Contracts: Revisiting the Pollution Exclusion Clause

ABOUT THE AUTHOR

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The first, and perhaps the last refuge, for those seeking enforcement of insurance contracts in the face of exclusion clauses is ambiguity. Granted, insurance contracts and the underlying facts can be a matter of some complexity. Yet, complexity alone does not necessarily lead to the conclusion of ambiguity giving rise to coverage where none should exist.

The British Columbia Court of Appeal has taken a leading role in Canada in resisting the siren call of ambiguity in the interpretation of insurance contracts in general. The Sirens, you may recall, were dangerous creatures who lured sailors with their enchanting music and singing voices to shipwreck on the rocky coast of their island. If justice requires certainty and predictability, then the attempt to create uncertainty and ambiguity where none properly exists is indeed a dangerous thing.

In *Riordan v. Lombard,* 2003 BCCA 267, the Court cited a line of authority against the strained search for ambiguity as follows:

> *The language of an insurance policy will be held ambiguous only if it is more reasonably subject to more than one interpretation. . .If an ambiguity exists, the court construes the language against the insurer. . .However, the courts must "fastidiously guard against the invitation to 'create ambiguities' where none exist."*

Notwithstanding such comments, and perhaps not surprisingly, counsel for insureds have continued to push the envelope in Alice in Wonderland semantic adventures seeking confusion and ambiguity where none should exist. The BC Court of Appeal has continued to take an intellectually honest and judicially prudent approach to such challenges.

Another recent example was *West Van Holdings Ltd. v. Economical Mutual Insurance Company*, 2017 BCSC 2397 and 2019 BCCA 110. The plaintiffs, West Van Lions Gate Cleaners Ltd. and West Van Holding Ltd. had owned business property in West Vancouver since 1976 and 1987 respectively, operating a dry-cleaning business and automotive repair business. They were insured under commercial general liability policies with Economical Mutual Insurance Company and Intact Insurance Company from roughly 1998 to 2012.

In 2014, adjacent landowners filed action against the plaintiffs herein, West Van Holdings Ltd and West Van Lions Gate Cleaners Ltd claiming that chemicals and petroleum products on the West Van lands had escaped and entered into the soils and groundwater of the adjacent landowners. The adjacent landowners sought an injunction, remediation, damages and costs. The actions were framed in negligence, nuisance, strict liability under *Rylands v. Fletcher* (1868) L.R. 3 H.L 330 (U.K.), and under the *Environmental Management Act*, SBC 2003, which deems the current owners of a contaminated site responsible for remediation subject to certain exceptions.

West Van filed a separate action against Economical and Intact seeking a duty to defend, indemnity and costs.

The plaintiffs argued that the underlying action sought compensatory damages arising out of property damage brought about by an occurrence during the relevant policy periods. Intact denied coverage relying on its "Environment Liability" exclusion and Economical denied coverage on its "Pollution Liability" exclusion, the terms of which were quite similar.

There is little dispute on the analytical framework that governs the duty to defend in Canada. The Chambers Judge cited Justice Fitzpatrick in *Co-operators General Insurance Company v. Kane*, 2017 BCSC 1720 who summarized the generally accepted principles as follows from para. 20:

> *Other general principles that apply in relation to the duty to defend and exclusion clauses are:*
>
> *a) an insurer is only required to defend a claim where the facts alleged in the pleadings, if proven, would require the insurer to indemnify the insured (i.e. the "pleadings rule"): Monenco Ltd. v. Commonwealth Insurance Co., 2001 SCC 49 at para. 28; Progressive Homes at para. 19; Lombard General Insurance Company of Canada v. 328354 B.C. Ltd., 2012 BCSC 431 at para. 21; Canadian Northern Shield Insurance Company v. Intact Insurance Company, 2015 BCSC 767 at para. 18;*
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> *b) all that is necessary, in order to trigger the duty to defend, is the mere possibility that a claim falls within coverage under the insurance policy based on a review of the pleadings: Monenco at paras. 29-30; Progressive Homes at para. 19; Lombard at para. 23; Johnson v. Aviva Insurance Company of Canada, 2014 ABQB 688 at paras. 33-35;*
>
> *c) where pleadings are not framed with sufficient precision to determine whether claims are covered by the policy, the duty to defend will be triggered where, on a reasonable reading of the pleadings, coverage can be inferred: Monenco at para. 31;*
>
> *d) "the widest latitude should be given to the allegations in the pleadings in determining whether they raise a claim within the policy": Scalera at para. 75, citing Nichols v. American Home Assurance Co., [1990] 1 S.C.R. 801. This is consistent with resolving any ambiguity in favour of the insured: Monenco at paras. 31-32; Lombard at para. 24; Johnson at para. 33.*

The plaintiffs properly argued that the threshold they had to meet was very low to trigger the duty to defend. They need only establish that there was a mere possibility that any claim made might succeed which might fall within coverage. They argued that

the "Environmental Liability" and "Pollution Liability" exclusions might capture some forms of liability, but not all. The potential for concurrent liability, contributory liability, and/or retroactive liability by virtue of statutorily-imposed responsibility for pre-existing third-party acts was not clearly excluded. They noted the distinctions in the wordings of certain exclusions, some of which contained wording such as "directly or indirectly" or "regardless of the cause of the loss or damage, other causes of the injury or damage or whether causes acted concurrently or in any sequence. . ." Such wording is sometimes referred to as "anti-concurrent causation" language.

The insurers argued that the plaintiff's arguments were semantic gymnastics, although in more wordy submissions. They relied on some quite persuasive authority that supported their position such as 699982 *Ontario Ltd. et al. v. Intact Insurance Company*, 2012 ONCA 268; *Dave's K & K Sandblasting (1988) Ltd. v. Aviva Insurance Company of Canada*, 2007 BCSC 791 and *Precision Plating Ltd. v. Axa Pacific Insurance Company*, 2015 BCCA 277. Unfortunately for the insurers, the judge held that all of these cases were distinguishable although the reasoning is somewhat difficult to follow. None of these cases involved acts or omissions by independent third parties where the insured was exposed to liability based on deemed responsibility under statute for contaminated sites. Some of the cases also contained "anti-concurrent causation" language.

The chambers judge concluded:

> *[212] In light of my determination that the exclusions do not "clearly and unambiguously" oust coverage for monetary relief arising out of pollutants that were used before West Van and Lions Gate owned and/or operated on the West Van lands, it is not necessary for me to address the plaintiffs' further arguments and I decline to do so.*
> *[213] As noted, "in order for an exclusion clause to oust the duty to defend, it must clearly and unambiguously apply to all of the claims made against the insured": Kane at para. 72, citing Progressive Homes, at paras. 54, 67. [Emphasis in the original.]*
> *[214] In other words, as long as there is a "mere possibility" that one of the claims is not "clearly and unambiguously" excluded, this is sufficient to trigger the duty to defend.*
> *[215] The defendants have not discharged their burden of showing that their "Environmental Liability" and "Pollution Liability" exclusions "clearly and unambiguously" apply to all of the claims made against the plaintiffs.*

Relying on the *Kane* decision, the judge also awarded legal costs of enforcing the duty on a full indemnity basis.

This case then proceeded to the Court of Appeal in November 2018 with a unanimous

reversal on April 5, 2019. Justice Goepel wrote for the Court. With reference to the costs awarded, Justice Goepel noted that there was no suggestion that the insurers breached any duty of good faith. There was no allegation of reprehensible conduct or anything that otherwise would be worthy of rebuke.

The insurers argued that the chambers judge erred in finding that the insureds were exposed to any claim arising from any pollutants that may have been used before they operated or used the lands in question. Even if such was the case, such claims were not covered as the policies only covered events that occurred during the term of the policies. The true nature of the claims was for the escape of pollutants and such was clearly excluded.

Justice Goepel agreed with the insurers. Each policy only covered property damage which occurred during their policy terms. In careful review of the underlying pleadings, Justice Goepel wrote as follows:

> *[48] The foundation of the submission is that West Van is exposed in the Underlying Action to a claim based on contamination caused by a predecessor third party. The difficulty with this submission is, however, that such a claim is not found in the NOCC. Paragraphs 7 and 8 of the NOCC reference West Van Holdings as owning the West Van Lands since October 1987 and Lions Gate operating a dry cleaning business on the West Van Lands since 1976. The NOCC makes no mention of a predecessor owner or operator.*
>
> *[49] Paragraph 9 of the NOCC states "that at all material times" dry cleaning chemicals and petroleum products have been used and allowed to escape, thereby damaging and contaminating the Lands. Reading the pleadings as a whole, "at all material times" must refer to the time that West Van has owned or operated on the West Van Lands. There is no suggestion in the NOCC that a third party predecessor owner or operator contaminated the Lands. Absent such an allegation, there is no possibility that West Van is exposed to liability because of the actions of a third party. To the extent that this was the foundation of the chambers judge's determination that there was a duty to defend, the decision, with respect, cannot stand.*
>
> *[50] Further, and in any event, even assuming that the pleadings could be read to contain such a claim, I find that such a claim does not fall within the grant of coverage. The exercise of interpretation should "avoid an unrealistic result or a result which would not be contemplated in the commercial atmosphere in which the insurance was contracted": Co-operators Life Insurance Co. v. Gibbens, 2009 SCC 59 at para. 20, citing Consolidated-Bathurst Export*

Ltd. v. Mutual Boiler and Machinery Insurance Co., [1980] 1 S.C.R 888 at 901 (per Estey J.).

[51] The CGL is an occurrence policy. The grant of coverage is for property damage which occurs during the policy period. The policy was not intended to provide coverage for events which took place long before it came into effect. It does not extend or cover property damage which arose at a prior point in time. Assuming without deciding that West Van could be liable under the EMA for such damage, it is not a risk that Intact and Economical insured under their policies. In the result, therefore, even assuming the NOCC could be read to include a claim based upon acts of a third party which took place prior to West Van commencing operations, such a claim is not covered under the policies and does not give rise to a duty to defend.

[52] The remaining claims under the EMA, in negligence, nuisance and Rylands v. Fletcher all allege property damage which occurred during the policy periods and fall within the initial grant of coverage. The issue is whether or not they are captured by the Exclusion Clauses.

[53] At the hearing of the appeal, counsel for West Van conceded that the remaining claims under the EMA and the claims in negligence, nuisance, and Rylands v. Fletcher, were all caught by the Exclusion Clauses. In correspondence written to the division following the hearing of the appeal, he resiled from that concession and advised that his position was that West Van was owed a defence against those claims under those of the appellant's policies which did not expressly exclude "migration of pollutants".

In conclusion, the Court held that it is clear that the claims in the underlying action fell outside the policy either because they do not come within the initial grant of coverage or are excluded by the Exclusion Clauses. The Exclusion Clauses were not ambiguous.

In dealing with the award of full indemnity for legal costs, the Court held that costs awards should be predictable and consistent. A trial judge cannot impose costs that are not authorized by the Rules of Court. Special costs, full indemnity, are usually only awarded when there is reprehensible conduct or conduct deserving of censure and rebuke, all of which was lacking here. Special costs are not a substitute for damages and they are not a remedy for breach of contract. Judges cannot fix costs arbitrarily or capriciously. The Court noted that the law of Ontario is somewhat different than BC and that those cases are not binding.

The Court also reviewed decisions from Newfoundland and lower court decisions in British Columbia where the courts had awarded full indemnity on duty to defend cases. The Court concluded:

[105] The special nature of insurance contracts however does not justify the creation of a different costs regime governing all insurance claimants. This question was canvassed at some length in a recent article in the Canadian Journal of Insurance Law: James Steele, "Deterrence not Damages: the Punitive Rationale for Solicitor-Client Costs" (2018) 36 Can J Ins L 1. As detailed by Mr. Steele, there is no principled reason why a different scale of costs should apply to insureds who successfully enforce a contractual obligation than any other litigant who is forced to bring an action in order to obtain relief. Many such plaintiffs are surely as sympathetic. Why, for example, should an insured receive a full or near indemnity while the plaintiff in a personal injury lawsuit finds the award eroded because he or she is only entitled to a partial indemnity.

[106] In this regard, it is also important to recall the caution in Marchen that costs are not a remedy for breach of contract.

[107] Party and party costs are designed to only partially indemnify a litigant. While party and party costs offer some compensation to the successful party, they avoid unduly discouraging the bringing of legitimate proceedings out of fear of the potential costs consequences. An insurer faced with a difficult question as to whether a duty to defend arises should be able to raise that defence without automatically incurring an exposure to special costs.

[108] The main purpose of special costs is to deter misconduct. If special costs are to be awarded regardless of conduct, there is no way to punish those unsuccessful parties who subject a successful party to an abusive proceeding. If a losing party faces full indemnity costs irrespective of their litigation conduct, the incentive for good conduct is correspondingly diminished.

[109] There is, in my respectful opinion, no principled reason to award costs in a duty to defend case in a manner different than other litigation. There already exist other suitable mechanisms to censure an insurer's wrongful conduct: Smithies Holdings at para. 134. If the insurer has breached its duty of good faith, or conducts itself in a manner that is worthy of rebuke, it will be sanctioned. If not, an insurer facing a duty to defend claim should be treated no differently than any other litigant who may breach a contract.

[110] With respect, the Supreme Court decisions in Paterson, Williams, Kane and Blue Mountain were all wrongly decided on the cost issue and should not be followed. They are not consistent with the Rules and the

> *principles that have long governed cost awards. I say nothing further about the decision in Tanious, which is presently on reserve in this Court.*

This decision will be of great value to the profession and the insurance industry generally in the interpretation of the true nature of the claims presented and the insurance policies in general. Arguments for ambiguity should be examined with care. Further, this case has ended a rogue line of cases in which full indemnity was awarded for duty to defend cases.

As it happens, Justice Goepel was one of my mentors when I was a young lawyer. One of his lessons was that a person should be careful to deny coverage if they must work at it too hard. It should not be a struggle. The corollary of this might be this: if one must struggle too hard to find ambiguity, you may wish to review your conclusions.

Addendum: Lead counsel for the plaintiffs was Neo Tuytel. I regret to advise that Mr. Tuytel died a some days ago, within a month of the Court of Appeal decision. He was a fierce and worthy advocate. He was a friend. May he rest in peace.

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