

The Insurer's Duty to Defend

By Geneviève Cotnam

Stein Monast, L.L.P.

genevieve.cotnam@steinmonast.ca

www.steinmonast.ca

The issue of the insurer's obligation to defend has raised numerous debates in the jurisprudence over the past few years.

Recently, the Court of Appeal of Quebec in *Groupe DMR Inc. v. Kansa General International Insurance Company Ltd*, AZ-50488250 revisited this question. Since this problem is part of the day-to-day business of insurers, it seems timely to seize the opportunity and reiterate the principles that apply.

First, it is important to recall that the obligation to defend is separate from the obligation to indemnify. As such, the obligation to defend can exist even if, ultimately, no indemnity is payable by the insurer. It is useful to clarify that in Québec, the Civil Code holds that the defence costs are payable by the insurer, in addition to the amount of the coverage (s. 2503 C.C.Q.).

The solution lies in an attentive analysis of the motion to institute proceedings and supporting evidence. For the purposes of this analysis, the insurer must undertake to prove the allegations and interpret them in the broadest way possible.

As the Court of Appeal emphasizes, four situations are liable to arise under this analysis:

1. On the face of it, the claim may appear entirely covered by the insurance policy. In this case, the insurer must assume its insured's defence.
2. The situation is equally simple when the claim is clearly not covered either in light of the alleged offence or the damages claimed. In certain cases, the loss may be specifically excluded by the insurance policy. In this case, the insurer is justified in refusing to assume its insured's defence.
3. In many cases, it is impossible to determine whether the claim is covered or not, as both possibilities are plausible, according to the evidence administered. The insurer must therefore assume its insured's defence, because at this stage the single possibility that the claim may be covered is sufficient to trigger the obligation to defend.
4. Only a portion of the claim is covered while the other portion is clearly not. This case will be used as an example when exemplary damages are claimed.

This last case raises practical difficulties for the insurer. In effect, in principle, the insurer is only obligated to defend the claims covered, and the insured must deal with its own interests for the balance. However, there should only be one lawyer *ad litem* per party. In the *Kansa case*, the Court considers the following avenues: if the insurer agrees to defend the claim, even if it is only partly covered, it could then require the defence costs to be shared between the insurer and the insured since only one lawyer will act on the basis of two separate mandates. This type of situation is liable to create significant difficulties for the lawyer, who may find himself in a conflict of interest between these two mandates. Conversely, the insured could choose to retain the services of his own lawyer at his own expense. In this last case, having two lawyers on the file should not create an additional burden on the other side. It would therefore be important to manage the file attentively.

An insurer who refuses to defend exposes itself to a type of "Wellington Motion" aimed at forcing it to intervene in the file and assume the defence for the covered portion. Otherwise, it could be called in warranty by the insured who assumed his defence alone. The insured would then claim reimbursement of the defence costs and eventually the indemnity to which he considered himself entitled. The court would then have the thankless task of determining how the defence costs should be shared between the insurer and the insured. In this respect, some confusion remains. Some argue that the defence costs should be shared *pro rata* based on the effort required to ensure the defence of the covered portion of the claim. In other cases, the Courts settle for a mathematical calculation like the one used in the *Kansa* decision where the Court determined that the covered portion of the conviction represented 28% of the total damages granted and therefore set the percentage of defence costs to be assumed by the insurer at 28%.

If the rules for analyzing the coverage and the obligation to defend are now clearer, this is not the case regarding the role of the lawyer and the sharing of defence costs.