

Can an insurer who has agreed to defend later deny an obligation to defend?

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The recent decision of Mr. Justice Keith A. Hoilett in *Economical Insurance Company of Canada v. Fleming*, [2008] I.L.R. I-4673, 57 C.C.L.I. (4th) 246, 89 O.R. (3d) 68 (Ont.S.C.J.) is one that all insurance defence counsel should read. The decision arises out of an application brought by Economical Insurance for an order declaring that it owed no duty to defend its insureds, Kenneth and Gabrielle Fleming, against a claim brought on behalf of a twelve year old plaintiff who sustained injuries while operating an all terrain vehicle (“ATV”) at the Fleming family cottage.

The Flemings were insured pursuant to a homeowner’s policy of insurance issued by Economical which contained the standard home owner’s policy exclusion for claims made against the insured “arising from the ownership, use, or operation of any motorized vehicle”. Economical argued that the young plaintiff’s claim was excluded from coverage by reason of her operation of the ATV, a motorized vehicle.

The statement of claim made allegations regarding the operation of the ATV and the Flemings failure to supervise the young accident victim. The Flemings argued that the allegations related to the “failure to supervise” were separate and distinct from the “use and operation” of the ATV and, as such, were not excluded under the policy. Justice Hoilett agreed and ordered Economical to defend the Flemings in the lawsuit, concluding that it was possible that the allegations of failure to supervise could give rise to liability which was distinct from the ownership, use and operation of the vehicle. This determination in itself could be the subject of future debate as there is jurisprudence which suggests that negligent supervision cannot exist independent of the use or operation of the vehicle and that accordingly the insurance policy does not have to respond. (See: *Unger (Litigation Guardian of) v. Unger*, [2003] 179 O.A.C. 108, 68 O.R. (3d) 257, 234 D.L.R. (4th) 119 (Ont. C.A.))

More relevant to this paper, Justice Hoilett provided a second reason for his decision that Economical Insurance was obliged to defend the Flemings. Within a month of service of the Statement of Claim, Economical wrote to the Flemings and advised that Economical would defend the action on their behalf. Five months later, Economical wrote again and reversed its position to the insureds, advising that “under no circumstance will Economical appoint defence counsel, or pay [...] for defence costs, arising from this claim”.

Counsel for the Flemings successfully argued that Economical had waived its right to rely on the “motorized vehicle” exclusion by reason of its original offer to provide a defence to the insureds. Justice Hoilett wrote: “...the facts in the present case strongly

support the respondents' contention that the applicant has waived its rights and may not now repudiate that position".

A 2004 Ontario decision of Madame Justice Bonnie L. Croll, *Bejinariu v. Primmum Insurance Co.*, [2004] I.L.R. I-4275, 8 C.C.L.I. (4th) 98 (Ont.S.C.J.) also examined the issues of waiver and estoppel following an insurer's initial acceptance and later denial of a duty to defend. At first glance, the *Bejinariu* case is at odds with Justice Hoilett's decision.

Bejinariu involved an application for the interpretation of an insurance policy to determine if the insurer was obliged to defend the insured, although the policy in question was a motor vehicle policy. In the *Bejinariu* case, the insurer initially retained counsel to defend the insured under the motor vehicle policy and a statement of defence was filed. The insurer later instructed defence counsel to remove itself from the record and, pursuant to the *Insurance Act*, add the insurer as a statutory third party. The insurer denied coverage based on the breach of a statutory condition – the plaintiffs in the two actions commenced had alleged that the defendant was racing at the time of the accident.

Although the *Bejinariu* and *Economical* decisions consider different insurance policies and statutory provisions, the clear distinguishing factor between the two was the manner in which the defences to the actions were handled by the respective insurers. The insurer in *Bejanariu* had taken the precaution of delivering a letter to the insured reserving the right to deny liability as well as having him execute a non-waiver agreement prior to delivery of a Statement of Defence. Accordingly, Justice Croll held that there had been no prejudice to the insured. She allowed counsel to be removed as counsel of record and permitted the insurer to be added as a statutory third party. The clear language of the reservation of rights letter delivered to the insured appears to be the factor that tipped the scales for Justice Croll and was the basis upon which Justice Hoilett distinguished the *Bejinariu* decision from the facts of the *Economical* case.

These decisions illustrate the fact sensitive nature of the waiver and estoppel argument in the context of the duty to defend under an insurance policy. If an insurer makes an unequivocal promise to defend the insured, it may be bound to make good on the promise. On the other hand, if the insurer makes a conditional promise to defend, or has taken other steps to limit its exposure then it may be in a position to revoke its offer should new facts come to light.