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INSURANCE POLICIES AREN'T SPECIAL! COSTS AND THE DUTY TO DEFEND IN BC

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In a recent British Columbia Court of Appeal decision, *West Van Holdings Ltd. v. Economical Mutual Insurance Company*, 2019 BCCA 110, the Court concluded insurance policies are not "special" contracts that justify successful litigants who seek coverage receiving special costs simply because an insurance policy includes a duty to defend claims that are covered by the policy. This precedent setting decision will impact the costs available in coverage disputes heard in this province and differs from appellate decisions in Ontario and Newfoundland.

The Facts

West Van Lions Gate Cleaners Ltd. began operating a dry-cleaning business in West Vancouver, BC in 1976 and West Van Holdings Ltd. had owned the property this business was operated on since 1987. In 2014 the owners of a neighbouring parcel of land sued these companies alleging contaminants used in the dry-cleaning business had polluted their lands (the "Claim").

Two insurance companies, who had provided CGL insurance to West Van Lions Gate Cleaners Ltd. and West Van Holdings Ltd. (the "Insureds") at various times between 1998 and 2012, refused to defend the Claim relying on the pollution exclusion clauses contained in their respective policies. The Insureds sued the insurers seeking a declaration they were obligated to defend the Claim.

No allegations of bad faith were made in relation to the coverage denials nor were any allegations made at trial that the insurers had behaved reprehensibly during the litigation.

The Trial Ruling

Following a summary trial, the trial judge determined the Insureds were entitled to a defence because the pollution exclusion clauses were ambiguous creating at least a "mere possibility" of coverage.

The trial judge then, relying on prior case law, awarded special costs to the Insureds. The prior cases had concluded insurance policies that include a duty to defend were unique contracts providing coverage for defence costs, therefore, an insured should be compensated for the costs incurred to obtain that defence

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even in the absence of reprehensible conduct in the litigation.

The Appeal Ruling

On appeal the Court, after a careful consideration of the pleading forming the basis of the Claim, the policies' terms and the law, concluded it was an error to find even a "mere possibility" of coverage.

Although this finding made it unnecessary to consider the award of special costs made at trial, the Court did so given the importance of this issue to other cases.

Analysis of the special costs issue began with a comparison of the law of costs in Ontario and BC. BC's Rules of Court provide for two categories of costs: party and party costs and special costs. Party and party costs are the default award and provide only partial indemnity based upon a tariff scale. Special costs provide greater indemnity but are usually awarded due to reprehensible conduct by a litigant. Ontario, in contrast, has three levels of costs: partial indemnity, substantial indemnity and full indemnity. The default, similar to the law of BC, is partial indemnity. Special costs in BC, if awarded, involve an assessment of what fees are "reasonably necessary" so a litigant is not necessarily fully indemnified by such an award. This can differentiate them in both name and substance from a "full indemnity" award.

Costs in BC, the Court concluded, must be awarded in accordance with the provincial Rules of Court which do not provide for "full indemnity" costs and preclude awarding special costs unless there is reprehensible conduct. A cost award that deviates from these rules may, however, be made based upon an agreement between the parties.

Turning to the agreements between the parties, the Court reviewed the policies' language. It was troubled by the special costs award being made when none of the policies addressed the Insureds' entitlement to costs in the event of a coverage dispute. Appellate courts in Ontario and Newfoundland have concluded that insurance policies containing a duty to defend, despite being silent on this issue, still form the basis for providing full indemnity cost awards as this duty creates an obligation to defend a claim at the insurer's expense instead of at the insured's. Lower courts in BC had, previously, adopted this reasoning although not consistently.

As there was no express term, the Court then assessed when contractual terms can be implied and concluded that an award for special costs was still not justified. Implying such a term would require: a particular custom; something incidental to a particular kind of contract; or a term necessary to provide business efficacy to the contract. None of these were found to apply in this case.

In the absence of allegations of bad behaviour or an express agreement, insurers should, the Court

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concluded, be treated the way any other litigant would when the appropriate level of costs to award a successful party is being determined in an action based on breach of a contract.

Practical Considerations for Insurers

In coverage disputes, insurers and insureds are now on an equal footing in BC when it comes to the potential cost consequences of success or failure. Both parties need to be wary that poor conduct during the litigation raises the risk of special costs and both are now likely to face only party and party costs if their legal argument regarding coverage is unsuccessful. Beware, however, that the law on this issue is not the same in every province!

This decision also, once again, highlights that, when it comes to coverage disputes, clear and unambiguous policy language is key. In this case the Court noted the "meticulous" drafting of the policies' terms and was not prepared to imply a term into them when they were silent on this issue. It also refused to stretch the language of the duty to defend provided in the policies to actions not specifically covered by the policies' wording.

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