# COURT OF APPEAL FOR ONTARIO

CITATION: Tedford v. TD Insurance Meloche Monnex, 2012 ONCA 429
DATE: 20120622
DOCKET: C54479

Lang, Epstein and Hoy JJ.A.

BETWEEN

Damon Tedford

Applicant (Respondent)

and

TD Insurance Meloche Monnex

Respondent (Appellant)

Marc D. Isaacs and Bonnie Huen, for the appellant

Danesh Rana, for the respondent

Heard: April 5, 2012

On appeal from the judgment of Justice Roydon J. Kealey of the Superior Court of Justice dated September 22, 2011, with reasons reported at 2011 ONSC 5500, [2011] I.L.R. I-5197.

Hoy J.A.:

**Overview**

[1] TD Insurance Meloche Monnex appeals the application judge's September 22, 2011 decision that it has a duty to defend the respondent, Damon Tedford, in an action alleging he made negligent misrepresentations in the Seller Property Information Statement completed in connection with the sale of his home. In that

action, the plaintiff purchaser pleaded that, as a result of the misrepresentations, she has incurred and will continue to incur repair costs, and has suffered anxiety, sleep disturbances, fatigue, stress, headaches and symptoms of depression (the "Health Consequences").

[2] At the time of the alleged misrepresentations, the respondent held a homeowner's insurance policy issued by the appellant, which provides coverage for damages the respondent is obligated to pay because of "Bodily Injury" or "Property Damage". The application judge concluded that the Health Consequences amounted to Bodily Injury, a duty to defend therefore arose, and that duty extended to the entire action. It is common ground that the damages the respondent may have to pay with respect to the repair costs do not constitute Property Damage under the policy. But for the alleged Bodily Injury, a duty to defend would not have arisen.

[3] The appellant advances two arguments on this appeal.

[4] First, it renews the argument made to the application judge that the true nature of the plaintiff's claim is one for economic loss arising out of a commercial transaction, the claim for Health Consequences is derivative of that claim and, as such, based on *Non-Marine Underwriters, Lloyd's of London v. Scalera*, 2000 SCC 24, [2000] 1 S.C.R. 551, should not be determinative of whether the appellant has a duty to defend.

[5] Second, it argues that, if it has a duty to defend, it should not be responsible for 100 per cent of the defence costs. Of the plaintiff's $185,000 damages claim, at least $150,000 relate to repair costs. The plaintiff seeks damages of approximately $25,000 for Health Consequences. Since the amount of damages related to Health Consequences is small in comparison to the claim for repair costs, the appellant argues it would be unreasonable for it to bear the cost of defending the entire claim.

[6] For the reasons that follow, I am not persuaded that the plaintiff's claim for Health Consequences is a "derivative claim" within the meaning of that term in *Scalera.* I do, however, conclude that, on the facts of this case, the appellant should not be responsible for 100% of the defence costs. To that extent, I would allow the appeal.

**The Policy**

[7] The homeowner's insurance policy issued by the appellant applies to accidents or occurrences that take place during the term of the policy.

[8] In "Coverage F", the appellant agrees:

> To pay on behalf of the Insured all sums which the latter shall become obligated to pay by reason of the liability imposed by law upon the Insured ... as damages ... because of Bodily Injury or Property Damage.

[9] "Bodily Injury" is defined as "physical injury, sickness or disease, including death resulting therefrom, sustained by any person."

[10] “Property Damage” is defined as “loss of or physical damage to or destruction of tangible property, including loss of use thereof resulting therefrom, and includes loss of use of tangible property which has not been physically damaged or destroyed provided such loss of use is caused by an accident.”

[11] In the policy, the appellant also agrees:

> With respect to such insurance as is afforded by this Policy under coverage F, the insurer shall
>
> > (1) defend any suit against an Insured alleging such Bodily Injury or Property Damage and seeking damages on account thereof, even if such suit is groundless, false or fraudulent; but the Insurer may make such investigation, negotiation and settlement of any claim or suit as it deems expedient;

[12] The policy contains various specific exclusions from coverage. None are argued to be relevant.

[13] The policy does not provide for allocation of defence costs where an insured is subject to both covered and uncovered claims and the same costs are incurred in the defence of both covered and uncovered claims.

**Legal principles governing an insurer’s duty to defend**

[14] The following principles emerge from the case law governing the duty to defend:

1. The insurer has a duty to defend if the pleadings filed against the insured allege facts which, if true, would require the insurer to indemnify the insured: *Monenco Limited v. Commonwealth Insurance Company*, 2001 SCC 49, [2001] 2 S.C.R. 699, at para. 28.

2. If there is any possibility that the claim falls within the liability coverage, the insurer must defend: *Nichols v. American Home Assurance Co.*, [1990] 1 S.C.R. 801, at p. 810.

3. The court must look beyond the labels used by the plaintiff to ascertain the "substance" and "true nature" of the claims. It must determine whether the factual allegations, if true, could possibly support the plaintiff's legal claims: Monenco, at paras. 34-35; Scalera, at para. 79.

4. The court should determine if any claims plead are entirely "derivative" in nature, within the meaning of that term as set out in Scalera. A derivative claim will not trigger a duty to defend.

5. If the pleadings are not sufficiently precise to determine whether the claims would be covered by the policy, "the insurer's obligation to defend will be triggered where, on a reasonable reading of the pleadings, a claim within coverage can be inferred": Monenco, at para. 31.

6. In determining whether the policy would cover the claim, the usual principles governing the construction of insurance contracts apply, namely: the contra proferentem rule and the principle that coverage clauses should be construed broadly and exclusion clauses narrowly: Monenco, at para. 31; Scalera, at para. 70. As well, the desirability, where the policy is ambiguous, of giving effect to the reasonable expectations of the parties: Scalera, at para. 71.

7. Extrinsic evidence that has been explicitly referred to in the pleadings may be considered to determine the substance and true nature of the allegations: Monenco, at para. 36; see 1540039 Ontario Limited v. Farmers' Mutual Insurance Company (Lindsay), 2012 ONCA 210.

**The derivative claim issue**

[15] The appellant argues that the claim for Health Consequences is derivative in the sense that it flows from the economic loss allegedly sustained by the plaintiff as a consequence of the alleged misrepresentations, and not from the misrepresentations themselves. The appellant bases this argument on *Scalera.*

[16] *Scalera*, however, is quite different from this case. In *Scalera*, the plaintiff brought a civil suit for sexual assault. She claimed sexual battery, negligence and breach of fiduciary duty. The defendant's homeowner's insurance policy excluded coverage for bodily injury "caused by any intentional or criminal act." The Supreme Court of Canada held that there was no duty to defend. Iacobucci J. described the negligence claim as merely derivative of the claim for sexual battery, and held that a derivative claim will not trigger a duty to defend.

[17] What Iacobucci J. meant by derivative is important. He explained, at para. 85, that when the court is faced with a situation where both an intentional tort, which is excluded from coverage, and a non-intentional tort, are pleaded:

> ... a court construing an insurer's duty to defend must decide whether the harm allegedly inflicted by the negligent conduct is derivative of that caused by the intentional conduct. In this context, a claim for negligence will not be derivative if the underlying elements of the negligence and of the intentional tort are sufficiently disparate to render the two claims unrelated. If both the negligence and intentional tort claims arise from the same actions and cause the same harm, the negligence claim is derivative, and it will be subsumed into the intentional tort for the purposes of the exclusion clause analysis. If, on the other hand, neither claim is derivative, the claim of negligence will survive and the duty to defend will apply ... *A claim should only be treated as "derivative", for the purposes of this analysis, if it is an ostensibly separate claim which nonetheless is clearly inseparable from a claim of intentional tort.* [Emphasis added.]

[18] In this case, only one cause of action – negligent misrepresentation – was advanced. The plaintiff does not allege that the respondent committed an intentional tort. The general damages for Health Consequences sought by the plaintiff represent a different category of damages resulting from the negligent misrepresentation, and not a derivative claim as contemplated by *Scalera.* I therefore see no error in the application judge's assessment of the true nature of the bodily injury portion of the action.

**The issue of apportionment of defence costs**

[19] Having regard to *Hanis v. Teevan*, 2008 ONCA 678, 92 O.R. (3d) 594, in my view, the application judge erred in requiring the appellant to defend the entire action without making provision for apportionment of the defence costs.

[20] In *Hanis*, at para. 2, Doherty J.A. addressed how the costs of defending a lawsuit should be apportioned between the insurer and the insured when some, but not all, of the claims made in the lawsuit are covered by the policy:

> Where there is an unqualified obligation to pay for the defence of claims covered by the policy, as in this case, the insurer is required to pay all *reasonable* costs associated with the defence of those claims even if those costs further the defence of uncovered claims. The insurer is not obligated to pay costs related solely to the defence of uncovered claims. [Emphasis added.]

[21] In *Hanis*, the insured had denied its duty to defend and the defendant retained its own counsel and proceeded to trial. The issue of the insurer's

obligation to defend, and the apportionment of costs, was determined following trial. In this case, the respondent seeks to have the appellant assume the conduct of the defence, and the covered claims represent a small portion of the total damages claimed. Considerations not addressed in *Hanis* arise.

[22] *Hanis* establishes that an insurer is responsible for all *reasonable* costs associated with the defence of a covered claim. As Doherty J.A. commented, at para. 23, the approach in *Hanis* is not unfair to the insurer: it does not result in an increase in the insurer's liability for defence costs.

[23] The respondent urged this court to follow *RioCan Real Estate Investment Trust v. Lombard General Insurance Co. of Canada* (2008), 91 O.R. (3d) 63 (S.C.), where the insurer was ordered to defend the entire action, although not all the claims were covered by the policy, and no order was made with respect to the allocation of costs. *RioCan* was decided before *Hanis* and is therefore not of assistance. Moreover, the facts in *RioCan* are different than those in this case. In *RioCan,* multiple theories of liability were advanced to support a claim for the same damages. The potential liability in respect of the covered claim was the same as that in respect of the uncovered claims.

[24] I would direct, unless the parties otherwise agree, that the appellant's counsel be instructed to defend both the covered and the uncovered claims, in a manner commensurate with the aggregate amount claimed, and that the

respndent bear the costs of the defence, to the extent they exceed the reasonable costs associated with the defence of the covered claims. In determining the reasonable costs associated with the defence of the covered claims, it is appropriate to consider the quantum of the covered claims. It would be unfair to the insurer to fix it with defence costs that are disproportionate to the extent of its potential liability for the covered claim.

[25] If the parties are unable to agree on an allocation of the costs, the appellant insurer shall be entitled to apply to the Superior Court of Justice for a determination of the allocation, in accordance with *Hanis*, after the matter is concluded or at such other time as the parties agree.

**Costs**

[26] The appellant was unsuccessful on the derivative claim issue and successful on the issue of allocation of costs. In these circumstances, I would award the appellant costs of the appeal, inclusive of disbursements and taxes, in the amount of $5,000. I would set aside the costs order of the application judge and substitute the amount of $2,500, inclusive of disbursements and applicable taxes, payable to the appellant.

Released: June 22, 2012
"SEL"

"Alexandra Hoy J.A."
"I agree S.E. Lang J.A."
"I agree G.J. Epstein J.A."