Cooper et al. v. Farmer's Mutual Insurance Company [Indexed as: Cooper v. Farmer's Mutual Insurance Co.]

59 O.R. (3d) 417

[2002] O.J. No. 1949

Docket No. C37051

Court of Appeal for Ontario,

Abella, Charron and Cronk JJ.A.

May 17, 2002

Insurance -- Insurer's duty to defend -- Horse trainer sustaining injuries when she fell from horse at horse farm operated by insured -- Trainer suing insured in negligence -- Trainer originally alleging that she was employee of insured but discontinuing action and delivering second statement of claim deleting references to employment relationship -- Insurance policy excluding coverage for bodily injury sustained by employees in course of their employment -- Insured seeking declaration that insurer has duty to defend them under policy -- Motions judge did not err in declining to consider extrinsic evidence which insurer claimed proved that trainer's pleadings were manipulated to ensure that insurance coverage was triggered -- Facts asserted by trainer in second statement of claim should be taken as pleaded for purpose of insurance coverage application -- Insurer has duty to defend claim.

The respondents operated a horse farm. A horse trainer, B, sustained injuries when she fell from a horse at the farm. B sued the respondents in negligence. She alleged in her original statement of claim that she was an employee of the respondents at the time of the accident and that she was engaged in the duties of her employment when she was injured. She later discontinued her first action and delivered a second statement of claim deleting all references to an employment relationship. The respondents were insured by the appellant under a farm liability insurance policy. Coverage under the policy was excluded for bodily injury sustained by an employee while in the course of his or her employment or a person entitled to benefits under workers' compensation law. The appellant refused to defend the respondents under the policy on the basis that B's claim fell within the exclusion as she was an employee of the respondents. The respondents brought an application for a declaration that the appellant had a duty to defend them under the policy. The appellant filed copies of statements made by the respondents to the appellant's insurance adjuster and other documents which the appellant claimed proved that B's pleadings were manipulated to ensure that the respondent's insurance coverage was triggered, and that B's claims fell within the coverage exclusion. The appli-

cations judge declined to consider that material. She allowed the respondents' application. The appellant appealed.

Held, the appeal should be dismissed.

The applications judge was correct in declining to consider the extrinsic evidence filed by the appellant for the purpose of determining whether the appellant had a duty to defend B's action. The issue of whether an insurer has a duty to defend should be determined by examination of the pleadings (including any document incorporated by reference in the pleadings) and the terms of the insurance policy. The court must take the factual allegations as pleaded. A judge hearing an insurance coverage application is precluded from fact-finding on matters at issue in the underlying tort litigation. The extrinsic evidence relied upon by the appellant concerned the issue of whether B was an employee of the respondents. This was a matter which was, or might be, relevant in the underlying tort action brought by B because if B was in fact an employee, her claim might be statute-barred under workers' compensation legislation. Accordingly, if the applications judge had considered this evidence in determining the coverage a pplication, she would have engaged in a prohibited form of fact-finding. While consideration of extrinsic evidence may be appropriate in a proper case to determine the true nature of a claim, it was neither appropriate nor necessary in this case to assess B's claim.

The mere possibility that a claim within the policy may succeed is sufficient to engage an insurer's contractual duty to defend. The policy in this case obliged the appellant to defend any civil action brought against the insured on account of any insured loss "even if such suit is groundless, false or fraudulent". B's current pleadings brought her claim within the policy. The appellant had a duty to defend the claim.

Nichols v. American Home Assurance Co., [1990] 1 S.C.R. 801, 72 O.R. (2d) 799n, 39 O.A.C. 63, 68 D.L.R. (4th) 321, 107 N.R. 321, [1990] I.L.R. 1-2583, apld

Monenco Ltd. v. Commonwealth Insurance Co., [2001] 2 S.C.R. 699, 97 B.C.L.R. (3d) 191, 204 D.L.R. (4th) 14, 274 N.R. 84, [2002] 2 W.W.R. 438, 2001 I.L.R. 1-3993, distd

Other cases referred to

Cummings v. Budget Car Rentals Toronto Limited, [1996] O.J. No. 2179 (C.A.); Jon Picken Ltd. v. Guardian Insurance Co. of Canada, [1993] I.L.R. 1-2973 (Ont. C.A.); Longarini v. Zuliani (1994), 17 O.R. (3d) 527, 113 D.L.R. (4th) 633, 23 C.C.L.I. (2d) 306 (C.A.); Non-Marine Underwriters, Lloyd's of London v. Scalera, [2000] 1 S.C.R. 551, 185 D.L.R. (4th) 1, 253 N.R. 1, [2000] I.L.R. 1-3810 (sub nom. Lloyd's of London v. Scalera); Trafalgar Insurance Co. of Canada v. Imperial Oil Ltd. (2001), 57 O.R. (3d) 425 (C.A.); Web Offset Publications Ltd. v. Vickery (1999), 43 O.R. (3d) 802n (C.A.) [Leave to appeal to S.C.C. refused (2000), 256 N.R. 200n]

Statutes referred to

Family Law Act, R.S.O. 1990, c. F.3, s. 61

Rules and regulations referred to

Rules of Civil Procedure, R.R.O. 1990, Reg. 194

APPEAL from a judgment of E. Macdonald J. (2001), 32 C.C.L.I. (3d) 284 allowing an application for a declaration that an insurer had a duty to defend a claim against the applicants.

Martin P. Forget, for appellant.
Thomas J. Donnelly, for respondents.

The judgment of the court was delivered by

[1] **CRONKJ.A.**: -- This appeal concerns an insurer's duty to defend an insured in connection with claims for damages for personal injuries where it is alleged by the insurer that the third party tort claims against the insured were wrongly manipulated so as to trigger the insured's insurance cover. At the conclusion of the hearing, this court dismissed the appeal for reasons to follow. These are those reasons.

The Facts

[2] The respondents operate a horse farm at Pefferlaw, Ontario. Karen Boyd ("Boyd"), a horse trainer, sustained injuries when she fell from a horse at the respondents' farm. Boyd sued the respondents in negligence, claiming compensatory damages for her injuries. She alleged in her original statement of claim that she was an employee of the respondents at the time of the accident, and that she was engaged in the duties of her employment when she was injured.

[3] Following delivery of the statement of claim, counsel for the respondents informed Boyd's counsel of her view that Boyd's action was barred by workers' compensation legislation if, as alleged, Boyd was an employee of the respondents at the time of the accident. Boyd then discontinued her first action and delivered a second statement of claim. In her second pleading, Boyd deleted all references to an employment relationship with the respondents and asserted that she had been "hired or retained" by the respondents "from time to time" to train their horses and that she was engaged in the training of one of their horses when the accident occurred through the negligence of the respondents. Subsequently, Boyd delivered a third statement of claim, which is essentially identical to her second pleading save for the addition of a claim for damages for her mother under the Family Law Act, R.S.O. 1990, c. F.3, s. 61.

[4] At the time of the accident, the respondents were insured by the appellant under a farm liability insurance policy. Under the insuring agreement in the policy, the appellant agreed to pay, within the policy limit, all compensatory sums which the respondents would become legally obligated to pay as damages for bodily injury caused by accident or occurrence. Coverage under the policy is excluded, however, for bodily injury sustained by: a) any employee while in the course of his or her employment, b) a person entitled to benefits under workers' compensation law, and c) a person defined as an "insured" under the policy.

[5] The appellant refused to defend the respondents under the policy on the basis that Boyd was an employee of the respondents and that, as such, her claim fell within the above-noted exclusions in the policy. In explaining its refusal to the insured, the appellant referred to statements made by the respondents and to documentation submitted in respect of the claim. The appellant also relied on the initial statement of claim in which Boyd stated that she was employed by the respondents, and

contended that the subsequent pleadings, in omitting any reference to employment, had been deliberately, and improperly, designed to trigger the insurance coverage.

[6] The respondents brought an application under the Rules of Civil Procedure, R.R.O. 1990, Reg. 194 for a declaration that the appellant has a duty to defend them under the policy. On the application, the appellant maintained its previous position and, in further support of its contention that the respondents' second and third pleadings were manipulated, sought to rely on various correspondence between counsel for the respondents and counsel for Boyd, and between counsel for the respondents and the appellant or its adjuster. The appellant argued that, in the circumstances, it was necessary for the applications judge to consider that extrinsic evidence to ascertain the true nature of the claim.

[7] By judgment dated August 30, 2001, Justice E. Macdonald allowed the respondents' application and awarded them their costs. The appellant appeals that decision. It alleges that the applications judge erred by: a) declining to consider extrinsic evidence for the purpose of determining whether the appellant has a duty to defend Boyd's actions in the circumstances, b) finding that a duty to defend applies, and c) declining to refer the coverage issue for the trial of an issue.

Analysis

(1) Consideration of extrinsic evidence

[8] The appellant included in its materials filed on the coverage application, copies of statements made by the respondents to the appellant's insurance adjuster and other documents which the appellant claims prove that Boyd's pleadings were manipulated to ensure that the respondents' insurance coverage was triggered, and that Boyd's claims fall within the coverage exclusions under the policy. The appellant asserts that the applications judge should have considered these materials in determining whether the appellant has a duty to defend the respondents in Boyd's actions. In my view, for the reasons that follow, the applications judge was correct in declining to do so.

[9] The issue of whether an insurer has a duty to defend in connection with a claim traditionally has been determined by examination of the pleadings in an action (including any documents incorporated by reference into the pleadings) and the terms of the relevant insurance policy. Absent merely speculative allegations by a claimant, the underlying facts concerning the claim, the policy or the potential outcome of the litigation generally are not to be considered. (Nichols v. American Home Assurance Co., [1990] 1 S.C.R. 801, 68 D.L.R. (4th) 321; Longarini v. Zuliani (1994), 17 O.R. (3d) 527, 23 C.C.L.I. (2d) 306 (C.A.); Jon Picken Ltd. v. Guardian Insurance Co. of Canada, [1993] I.L.R. 1-2973, 17 C.C.L.I. (2d) 167 (Ont. C.A.); Web Offset Publications Ltd. v. Vickery (1999), 43 O.R. (3d) 802n (C.A.), leave to appeal to the Supreme Court of Canada refused (2000), 256 N.R. 200n; Cummings v. Budget Car Rentals Toronto Ltd., [1996] O.J. No. 2179 (C.A.); and Trafalgar Insurance Co. of Canada v. Imperial Oil Ltd. (2001), 57 O.R. (3d) 425 (C.A.)).

[10] The appellant argues that the decision of the Supreme Court of Canada in Monenco Ltd. v. Commonwealth Insurance Co., [2001] 2 S.C.R. 699, 204 D.L.R. (4th) 14 recognizes that extrinsic evidence may be considered by the court for the purpose of discerning the true substance of a claimant's allegations. It relies, in particular, on the following passage by Iacobucci J., writing for the court (at pp. 716-18 S.C.R., pp. 26-27 D.L.R.):

> [I]t follows that the proper basis for determining whether a duty to defend exists in any given situation requires an assessment of the pleadings to ascertain the "substance" and

> "true nature" of the claims. More specifically, the factual allegations set out therein must be considered in their entirety to determine whether they could possibly support the plaintiff's legal claims.
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> [O]ne important question arising in this appeal has been left open by the jurisprudence to date. That is, whether, in seeking to determine the "substance" and "true nature" of a claim, a court is entitled to go beyond the pleadings and consider extrinsic evidence. Without wishing to decide the extent to which extrinsic evidence can be considered, I am of the view that extrinsic evidence that has been explicitly referred to within the pleadings may be considered to determine the substance and true nature of the allegations, and thus, to appreciate the nature and scope of an insurer's duty to defend . . . .

(Emphasis added)

[11] On proper review, Monenco does not support the appellant's argument. Iacobucci J.'s comments in Monenco, above-referenced, endorse consideration of extrinsic evidence that has been explicitly cited by the parties in their pleadings. This court's subsequent decision in Trafalgar is to the same effect. Under Ontario's Rules of Civil Procedure, documents referred to in a party's pleadings are deemed to be part of the pleading. Thus, consideration of such materials does not deviate from the proposition that a pleadings review, and an examination of the relevant insurance policy, are the cornerstones for determining whether an insurer's duty to defend arises. Justice Iacobucci further reasoned in Monenco (at pp. 717-18 S.C.R., pp. 27-28 D.L.R.):

> [W]e cannot advocate an approach that will cause the duty to defend application to become "a trial within a trial". In that connection, a court considering such an application may not look to "premature" evidence, that is, evidence which, if considered, would require findings to be made before trial that would affect the underlying litigation.
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> In endorsing [the review of extrinsic evidence in the Monenco case], I must emphasize that it was not considered for the purpose of examining the contentious points in issue in the underlying litigation between Suncor and the appellants . . . A review of the extrinsic evidence simply illuminates the substance of the pleadings and as such, is consistent with the reasoning in [Non-Marine Underwriters, Lloyd's of London v. Scalera (2000), 185 D.L.R. (4th) 1 (S.C.C.)].

[12] Finally, in Monenco, the documents at issue had been referred to in the parties' pleadings. In this case, the documents which the appellant sought to have reviewed by the applications judge did not form part of the pleadings.

[13] As confirmed in Non-Marine Underwriters, Lloyd's of London v. Scalera, [2000] 1 S.C.R. 551, 185 D.L.R. (4th) 1, if a claim alleges a state of facts which, if proven, would fall within the coverage of the policy, the insurer's obligation to defend applies regardless of the truth or falsity of the allegations in the claim (at pp. 595-99 S.C.R., pp. 34-36 D.L.R., per Iacobucci J.). The courts must take the factual allegations as pleaded. Moreover, a judge hearing an insurance coverage application is precluded from fact-finding on matters at issue in the underlying tort litigation (Monenco and Trafalgar). As observed by Iacobucci J. in Monenco, a coverage application is not to be converted into "a trial within a trial" (at p. 717 S.C.R., p. 27 D.L.R.).

[14] I am satisfied that the applications judge properly considered and applied these principles. In particular, the extrinsic evidence relied upon by the appellant, which it urged the applications judge to consider, concerned the issue of whether Boyd was an employee of the respondents. This is a matter which may well be directly relevant to the underlying tort actions brought by Boyd because if Boyd, in fact, was an employee at the time of the accident, her claims may be statute-barred under applicable workers' compensation legislation. Accordingly, if the applications judge had considered this evidence in determining the coverage application, she would have engaged in a prohibited form of fact-finding. While consideration of extrinsic evidence may be appropriate in a proper case to determine the true nature of a claim, it was neither appropriate nor necessary in this case to assess Boyd's claims.

(2) The duty to defend and the trial of an issue

[15] In Nichols it was held that the mere possibility that a claim within the policy may succeed is sufficient to engage an insurer's contractual duty to defend. The policy here obliges the appellant to defend, at its cost, any civil action brought against the insured on account of any insured loss "even if such suit is groundless, false or fraudulent". Boyd's current pleadings bring her claims within the policy. It is possible that she may succeed based on the facts now alleged by her.

[16] For the purpose of the respondents' coverage application, the facts asserted by Boyd in her second and third statements of claim must be taken as pleaded. The claims advanced by Boyd are for compensatory damages arising from bodily injuries allegedly occasioned by the negligence of the respondents. I conclude that they fall within the coverage to which the appellant committed under the insuring agreement in the policy. In addition, if, as alleged, Boyd was an independent contractor at the time of the accident and not an employee of the respondents, the coverage exclusions under the policy do not apply. I agree, therefore, with the applications judge's conclusion that there is nothing in Boyd's current pleadings "which justifies a declaration that the claim[s] falls outside of coverage" (at para. 22).

[17] The facts asserted in Boyd's second and third statements of claim and the clear wording of the policy establish that the appellant's contractual duty to defend arises in this case. No trial of an issue is required for this determination. In my view, the applications judge correctly stated (at para 30):

> [T]he claim alleges a state of facts which, if proven, would fall within coverage of the policy with the result that the insurer is obliged to defend the suit regardless of the truth or falsity of such allegations. [Citations omitted]

Conclusion

[18] It is for these reasons, that we dismissed the appeal. The respondents are entitled to their costs of the appeal on a partial indemnity basis. The respondents have filed a bill of costs with the court. In order to comply with the rule that now requires this court to fix costs, the appellant shall file its written submissions concerning costs within ten days from the release of this court's decision and the respondents may reply thereto in writing within five days thereafter.

Appeal dismissed.