IN THE SUPREME COURT OF BRITISH COLUMBIA

Citation: *Penticton (City of) v. AXA Pacific Insurance Company,* 2009 BCSC 1404

Date: 20091014
Docket: 37117
Registry: Kamloops

Between:

The Corporation of the City of Penticton

Plaintiff

And

AXA Pacific Insurance Company and Harcott Glanville Insurance Brokers Ltd.

Defendants

Before: The Honourable Madam Justice Ker

Reasons for Judgment

Counsel for Plaintiff:	D. K. Hori A. Hughes
Counsel for Defendant:	D. M. Twining
Place and Date of Hearing:	Kamloops, B.C. February 26, 2009
Place and Date of Judgment:	Kamloops, B.C. October 14, 2009

1. Introduction

[1] The plaintiff, the Corporation of the City of Penticton (the "City") has brought an application pursuant Rule 18A of the *Rules of Court* seeking an order declaring that the City is an insured under a policy of insurance issued by the defendant, AXA Pacific Insurance Company ("AXA Pacific"), and that AXA Pacific is liable under that policy of insurance to indemnify the City against all costs and expenses incurred by the City in defending four tort actions (the "MVA Claims") arising from a motor vehicle accident (the "MVA") which occurred in the City of Penticton on the 23rd day of October, 2001.

[2] The MVA occurred at an intersection under construction by Peters Bros. Construction Ltd. (the "Contractors"), an independent contractor the City hired in August 2001 to undertake repairs to certain roadways and subsurface areas in the City.

[3] A term of the contract between the City and the Contractors, required the Contractors to purchase a policy of liability insurance with the City named as an additional insured. A Certificate of Insurance dated August 30, 2001 was provided, adding the City as an additional insured to the Contractor's insurance policy. AXA Pacific was the insurer for the policy in issue.

[4] The issue that arises on this application is whether the City is entitled to contribution from AXA Pacific under the policy in issue for legal costs it incurred in defending the MVA Claims initiated as a result of the MVA. The City argues that AXA Pacific has a duty to defend the City based on its inclusion as an additional insured on the Contractor's insurance policy, as the MVA occurred as a result of the Contractors' negligence in removing a stop sign at the intersection and replacing it in the wrong location. The City argues that its liability "arises out of the operations of the insured" Contractor.

[5] AXA Pacific argues that when the true nature of the allegations as outlined in the pleadings are determined, liability does not arise out of the operations of the

Contractor but rather is the direct fault or negligence of the City in failing to replace the stop sign as stipulated in one portion of the contract it had with the Contractor, thereby breaching its statutory duty to have civic works relating to its roadways carried out in a safe and proper manner. Accordingly, argues AXA Pacific, there is no duty to defend owed to the City as an additional insured on the Contractor's insurance policy.

[6] AXA Pacific does acknowledge that the City is covered under the insurance policy but that its duty to defend only extends to the minor allegation of vicarious liability in two of the claims arising out of the motor vehicle accident actions. However, AXA Pacific goes on to argue that as the City did not defend the vicarious liability claim it is either not liable or only liable for a minimal contribution to the cost of defending the two vicarious liability allegations.

[7] The City is a municipality incorporated pursuant to the provisions of the *Local Government Act,* R.S.B.C. 1996, c. 323.

[8] AXA Pacific is an insurance company carrying on business in B.C.

2. The Evidentiary Record

[9] In order to determine the extent of an insurer's duty to defend, the analysis follows the "pleadings rule". Before determining whether AXA Pacific has a duty to defend the underlying action, it is first necessary to determine what materials can be properly considered on this application.

[10] In *Moneco Ltd. v. Commonwealth Insurance Co.*, 2001 SCC 49 Mr Justice Iacobucci expressed the "pleadings rule" at para. 28 in the following manner:

> 28. The starting premise for assessing whether an insurer's duty to defend has been triggered rests in the traditional "pleadings rule". Whether an insurer is bound to defend a particular claim has been conventionally addressed by relying on the allegations made in the pleadings filed against the insured, usually in the form of a statement of claim. If the pleadings allege facts which, if true, would require the insurer to indemnify the insured for the claim, then the insurer is obliged to provide a defence. This remains so even though the actual facts may differ from the allegations pleaded...

[11] In *Dave's K. & K. Sandblasting (1988) Ltd. v. Aviva Insurance Co. of Canada*, 2007 BCSC 791, Mr Justice Goepel reviewed the principles governing the scope of materials that are to be considered in assessing whether an insurer's duty to defend has been triggered in a particular proceeding, stating at paras. 9-12:

> 9 The starting premise for assessing whether the duty to defend has been triggered is the pleadings. If the pleadings allege facts, which if true would require an insurer to indemnify the insured for the claim, the insurer is obliged to provide a defence even if the actual facts differ from the allegations pleaded.
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> 10 One of the earliest articulation of the pleadings rules is found in Bacon (Guardian ad litem of) v. McBride (1984), 5 C.C.L.I. 146 (B.C.S.C.), where Wallace J. stated, at 151:
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> > The pleadings govern the duty to defend - not the insurer's view of the validity or nature of the claim or by the possible outcome of the litigation. If the claim alleges a state of facts which, if proven, would fall within coverage of the policy the insurer is obliged to defend the suit regardless of the truth or falsity of such allegations. If the allegations do not come within the policy coverage the insurer has no such obligation.
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> 11 Cases dealing with the duty to defend have not always distinguished between the statement of claim and other pleadings. Some cases have suggested that the court can also look at a statement of defence, particularly if it contains admissions, or other pleadings which could impact on coverage. In Unrau v. Canadian Northern Shield Insurance Co., 2004 BCCA 585, it was suggested in obiter that in some cases it might be helpful to analyze the defences when defining the nature of the claims. In Wi-Lan Inc. v. St. Paul's Guarantee Insurance Co., 2005 ABCA 352, the Alberta Court of Appeal held that it is wholly inappropriate to consider the statement of defence. I agree with that conclusion.
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> 12 The insurer's obligation to defend arises from the allegations in the statement of claim. Nothing filed by an insured in its statement of defence can create a duty to defend if that duty does not already exist. This conclusion is consistent with Non-Marine Underwriters, Lloyd's of London v. Scalera, [2000] 1 S.C.R. 551 where Iacobucci J. for the Court, said at paragraph 90:
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> > I therefore conclude that the respondent will only have to defend the appellant if the plaintiff's statement of claim (my emphasis) alleges a state of facts that, properly construed, would support an action that could potentially fall within coverage.

[12] In considering whether an insurer's duty to defend under a policy of insurance has been triggered, the court must look at the pleadings, that is, the statement of claim, and in this case the third party notices. The only extrinsic evidence a court may consider is that found in any documents explicitly referred to in the pleadings.

Such extrinsic evidence may be considered in determining the substance and true nature of the allegations, and, thus, to appreciate the nature and scope of an insurer's duty to defend: *Moneco Ltd*. at paras. 36-38; *Dave's K. & K. Sandblasting* at paras. 8-21; *Agresso Corp v. Temple Insurance Co*., 2007 BCSC 19 at para. 34.

[13] Thus, whether a claim falls within insurance coverage and triggers a duty to defend in an insurance policy is considered in relation to the substance and true nature of the allegations covered by the pleadings which set out the claim against the party seeking coverage. The allegations are compared to the insuring agreement and applicable exclusions of the policy.

[14] In this case the Contract Documents and the Insurance Policy are referred to in the pleadings and as such are also admissible and relevant to a consideration and determination of the substance and true nature of the pleadings.

3. Background Facts

a. The Motor Vehicle Accident

[15] One of the locations that the Contractor was responsible for under the Contract was the intersection of Okanagan Avenue and Camrose Street in Penticton. During the course of the Contractor's resurfacing work, a stop sign for northbound traffic on Camrose Street at the intersection with Okanagan Avenue, was removed by the Contractor or its employees and relocated to a nearby position where it was not readily visible to traffic travelling northbound on Camrose Street and approaching the intersection.

[16] On October 23, 2001, there was a motor vehicle accident at the intersection of Okanagan Avenue and Camrose Street when two vehicles collided in the intersection. Barry Matfield was travelling northbound on Camrose Street and failed to yield to the traffic travelling on Okanagan Avenue. As the Matfield vehicle drove through the intersection it collided with another vehicle operated by Dallas Jackson which was travelling eastbound on Okanagan Avenue. Alexis Carmela Brown was a passenger in the Jackson vehicle and was injured in the collision.

[17] The parties injured in the MVA initiated actions against a number of parties, including the Contractor, claiming that the MVA occurred because the stop sign at the intersection in issue had been removed and replaced in the wrong position. Only one action initially named the City as a party.

[18] The Contractor then issued third party notices against the City and claimed that the City had been negligent in failing to replace the stop signs contrary to its obligation under clause SS3.3 of the Contract Documents. As a consequence of this the plaintiffs in one underlying action filed amended statements of claim adding the City as a defendant and alleging negligence on the part of the City in removing the stop sign, failing to replace the stop sign, failing to warn that the stop sign had been removed, failing to supervise the Contractor's work as well as vicarious liability for the acts or omissions of the Contractors.

[19] The MVA Claims have all been settled. The City was not required to contribute to the settlement but incurred costs in relation to its defence of the claims. AXA Pacific has not paid any of these defence costs arguing that there was no duty to defend as the claims arose out of the City's own negligence. What remains outstanding is whether AXA Pacific, as insurer to the Contractor, had a duty to defend the City as an additional insured under the terms of the policy and certificate of insurance.

b. The Pleadings in the Underlying Actions

[20] As a result of the MVA, the above mentioned MVA Claims were initiated. The following summary of the relevant pleadings assists in determining whether AXA Pacific's duty to defend the City has been triggered:

1. *Matfield v Matfield and others*, Kelowna Registry No. S62505 (action by Barbara Edith Matfield, originally filed October 10, 2003). The amended amended statement of claim (amended in February 2005) added the City as a Defendant to that action after a third party notice, issued by the Contractors and filed on June 14, 2004, alleged the City was negligent and in breach of its contractual and statutory duties to replace the stop sign at the intersection. The amended amended statement of claim alleges the Contractor was negligent in removing

and relocating the stop sign and in a number of other particulars that relate to the construction of the intersection and the handling of the traffic stop sign. The amended amended statement of claim alleges the City was negligent in failing to supervise the construction work and in breach of its contractual duty to replace the stop sign at the intersection and its statutory duty to have the works safely undertaken in a manner to protect the public.

2. *Matfield v. Peter's Bros. Construction Ltd. and others,* Penticton Registry No. 24111 (action by Barry Ronald Matfield, originally filed September 15, 2003). The statement of claim did not include the City as a defendant. The City became involved in this action through the third party notice issued by the Contractor and filed on June 14, 2004, alleging the City was negligent and in breach of its contractual duty to replace the stop sign at the intersection and its statutory duty to have the works safely undertaken in a manner to protect the public.

3. *Brown v Matfield and others*, Penticton Registry No. 24618 (action by Alexis Carmela Brown originally filed January 22, 2004). The statement of claim named the City as a Defendant alleging it had been negligent in failing to have the works safely undertaken in a manner that would protect the public and in being vicariously liable for the acts and omissions of the Contractor and its employees. It also alleges the Contractor and its employees were negligent in removing and relocating the stop sign and in a number of other particulars that relate to the construction of the intersection and the handling of the traffic stop sign.

4. *I.C.B.C. v Peter's Bros. Construction Ltd and others*, Kelowna Registry No. S63074 (action by I.C.B.C. initiated on November 27, 2003). The statement of claim did not include the City as a defendant. The City became involved in this action through the third party notice issued by the Contractor and filed on June 14, 2004, alleging the City was negligent and in breach of its contractual and statutory duties in failing to replace the stop sign at the intersection.

[21] The City was named in each of these MVA Claims as either a defendant or a third party or both. In effect, there were six claims made against the City in the MVA Claims, two by plaintiffs (Barbara Matfield and Alexis Brown) and four by way of third party proceedings all initiated by the Contractor.

[22] The plaintiffs in each of the MVA Claims allege that the MVA occurred because the stop sign for northbound traffic on Camrose Street was removed and

then replaced in an inappropriate manner and location. The statements of claim in each of the MVA Claims allege, in particular, that the stop sign in issue had been removed and replaced by the Contractor, its agents, servants or employees.

[23] The specific allegations against the Contractor in the MVA Claims, as evidenced by the pleadings, include the following:

(a) failing to give adequate or any warning to traffic entering the intersection, that construction was under way in and around the intersection;
(b) removing the stop sign from its usual fixed setting;

(c) placing the stop sign in a location where it was not readily visible to northbound traffic approaching the intersection on Camrose Street, particularly during periods of darkness;

(d) failing to give any or any adequate warning that the stop sign had been moved to that location;

(e) failing to comply with building code, legislative, regulatory and contractual requirements regarding, inter alia, the following:

(i) notifying motorists of construction zones;

(ii) removal of stop signs;

(iii) moving stop sings to alternative locations;

(iv) taking reasonable care to ensure the safety of motorists and pedestrians passing through construction zones; and

(v) failing to comply with sections 137 and 138 of the Motor Vehicle Act, RSBC 1996, c. 318 and amendments thereto.

[24] The specific allegations against the City in the MVA Claims, as evidenced by all the pleadings, include the following:

(a) breaching its duty to have the works safely undertaken and in a manner to protect the public;

(b) not replacing the existing stop sign or erecting a new stop sign;

(c) failing to replace the existing stop sign in its usual and/or ordinary place;

(d) failing to warn that the stop sign has been relocated in other than its usual and ordinary place;

(e) failing to adequately supervise Peter's Bros. or its subcontractors in their contractual obligations;

(f) being vicariously liable for the negligent acts and omissions of the contractors, their agents, servants or employees.

[25] The Contractor, in all the third party pleadings initiated against the City, relied upon a clause in a section of the Contract Documents addressing existing traffic signs and the City's responsibility for the replacement of existing or installation of new traffic signs, to allege that any injuries, loss or damage suffered by the plaintiffs in the MVA Claims were due to the City's breach of contract with the Contractor and the breach of its statutory duty to protect the public by failing to have the works safely undertaken and the City's failure to warn the public that the stop sign had been relocated and in failing to replace the stop sign to its usual and ordinary location.

[26] Essentially, the plaintiffs in the MVA Claims allege negligence on the part of the Contractor and its agents and employees for the MVA because it removed and improperly relocated the stop sign. They allege negligence on the part of the City in failing to properly supervise the Contractor and in failing to discharge its statutory duty to ensure the safety of its roadway. In the third party notices, the Contractor alleges the City breached its contractual and statutory duties for failing to fulfil its responsibilities to replace and warn of the relocation of the stop sign and in failing to have the works safely undertaken in a manner to protect the public.

[27] In addition to considering the statements of claim and third party notice pleadings in the underlying actions, the Court can also review the terms of the Contract Documents and the Insurance Policy, those items having been specifically referred to in the pleadings.

c. The Terms of the Contract

[28] In August 2001 the City entered into a Capital Works Contract (the "Contract") with the Contractor for the improvement of specified roadways within the City boundaries.

[29] The Contract between the City and the Contractors was for the construction of underground utilities and road works and included the upgrading of sewers, water mains, and road services in the Penticton Industrial Development area, including the intersection of Okanagan Avenue and Camrose Street.

[30] The Contract itself set out the scope of the contractor's work and obligations and stated: "The *Contractor* will perform all *Work* and provide all labour, equipment and material and do all things strictly as required by the *Contract Documents*".

[31] The Contract Documents were defined as those documents listed in Schedule 1 of the Agreement and included a document entitled the Master Municipal Construction Documents (the "MMCD"), as well as documents the City formulated to amend the MMCD and were entitled the Supplemental General Conditions (the "SGC") and the Supplemental Construction Specifications (the "SS"). The relevant portions of the Contract Documents are outlined below.

[32] The MMCD contained the following provisions addressing the Contractor's control of the work project, indemnification and insurance:

> 4.1.1 The Contractor shall have complete control of the Work and shall effectively direct and supervise the Work so as to ensure conformance with the Contract Documents. Subject to the Owner's rights as specifically set out in the Contract Document to give directions regarding the Work, the Contractor shall be solely responsible for construction means, methods, techniques, sequences and procedures and for coordinating the various parts of the Work under the Contract.
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> . . . . . .
>
> 22.1.1 The Contractor shall indemnify and hold harmless the Owner and the Contract Administrator, their agents and employees from and against claims, demands, losses, costs, damages, actions, suits or proceedings by third parties that arise out of, or are attributable to, any act or omission or alleged act or omission of the Contractor, the Contractor's agents, employees or Subcontractors or suppliers in performance of the Contract.

. . . . . .

> 24.1.1 Contractor will at the Contractor's expense, carry with an insurance company or companies and under policies of insurance acceptable to and approved by the Owner the following insurance with limits not less than shown in the respective items:
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> b) Comprehensive General Bodily Injury and Property Damage Liability Insurance –
>
> Limits: Bodily Injury inclusive $5,000,000
>
> The insurance shall include Contractor's Contingent Liability and Contractual Liability of sufficient scope to include the liability assumed by the Contractor under the terms of this Contract, and Completed Operations Liability. The policy shall include the Owner, the Contract Administrator and all Subcontractors as additional insureds with a cross liability clause.

[33] The SGC component of the Contract Documents included requirements that the Contractor was responsible for traffic control including the following clause:

> **SGC 6.2** The Contractor shall be responsible for the supply, maintenance and removal of any and all construction zone traffic control which will, or may be required.

[34] The Instructions to Tender Documents were also incorporated into the Contract Documents and provided the following with respect to traffic safety:

> **4.10. Flag Persons/Traffic Safety:**
>
> 4.10.1 The Contractor prices shall include flag persons required and be responsible for retaining and directing safe public travelled lanes, signs, barricades and detours.
>
> - Prior to the start of works each day
> - During construction hours all day
> - End of each work day
> - After work hours and holidays

[35] Finally, the SS component of the Contract Documents, set out in Section 5 of the Contract Documents, included a provision addressing traffic signs that contained the following clause:

> **SS3. Existing Traffic Signs**
>
> .1 The Contractor shall be responsible for protecting and/or returning to City Yards, all existing street name or traffic signs. Damage to existing signs will result in replacement costs being invoiced to the contractor.

> .2 The Contractor shall notify the City, in writing, of any existing damage to these items prior to start of work.
>
> .3 The City will be responsible for the replacement of existing or the installation of all new street name, or traffic signs.

[36] Collectively the terms of the Contract Documents make it clear that the Contractor was responsible for the following: all aspects of the construction project including project safety of the construction areas, directing safe public travel in the construction area, supply and maintenance of all construction zone traffic control and day to day protection and maintenance of all existing traffic signs until the Contract was completed.

[37] The Contractor was also responsible for returning to the City Yards existing traffic signs and when that was done the City was responsible for the replacement of existing traffic signs or installation of new traffic signs.

d. The Terms of the Insurance Policy Adding the City as an Additional Insured

[38] Pursuant to the terms of the Contract, the Contractor instructed its insurance broker, Harcott Glanville Insurance Brokers, to take the necessary steps to add the City as an additional insured to its policy. The insurance brokers issued the Certificate of Insurance Policy #1172213 and AXA Pacific was the insurer. The Certificate of Insurance states:

> It is understood and agreed the policy/policies noted above shall contain amendments to reflect the following:
>
> 1. Any deductible or reimbursement clause contained in the policy shall not apply to the The Corporation of the City of Penticton, and shall be the sole responsibility of the Insured named above [the Contractor].
> 2. The Corporation of the City of Penticton is named as Additional Insured.

[39] The Certificate of Insurance and underlying Commercial Insurance Policy contains the following provision:

> The unqualified word "Insured" includes the Named Insured and any interest under the management control of the Named Insured, or for which the Named Insured is responsible for arranging insurance and also includes:
>
> c) each person, firm, corporation or government body for whom the Insured has contracted to provide insurance but only with respect to liability which arises out of the operations of the Insured, and only to the extent required by such contract. Notice of cancellation shall be provided to such persons, firms, corporations or government bodies in accordance with the certificates of insurance on file with the Insurer.
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> [Emphasis added]

4. Issues

[40] The central issue in this Rule 18A application is whether AXA Pacific has a duty to defend the City in the MVA Claims. More specifically the issues can be stated as:

1. Does AXA Pacific have a duty to defend the City in the underlying actions arising from the MVA of October 23, 2001?

2. Are the claims made against the City in the underlying action of a nature that they are liabilities attributable to the operations of the insured Contractor such that the City is covered as an additional insured pursuant to the certificate of insurance or are the claims against the City liabilities that are distinct and not attributable to the operations of the Contractor?

3. Is the City's statutory duty relating to public safety and the use of the City's roadways a non-delegable duty that gives rise to direct and independent fault on the part of the City?

a. The Plaintiff's Position

[41] The City says that the various statements of claim and third party notices that pertain to the MVA Claims from the MVA clearly demonstrate that the substance and true nature of the allegations in this matter are liabilities that arise out of the operations of the insured, the Contractor, for its failure to properly secure and maintain the safety of the construction area including the maintenance of proper traffic signage.

[42] The City argues that the totality of the pleadings and extrinsic evidence outlined above demonstrate that it is covered as an additional insured under the certificate of insurance for the liability arising out of the operations of the Contractor in removing and improperly relocating the traffic stop sign, failing to maintain safety of the roadway pursuant to the contract terms and in failing to notify the City of the movement of the traffic stop sign at the intersection of Okanagan Avenue and Camrose Street in Penticton, B.C. Consequently, argues the City, AXA Pacific has a duty to defend the City in relation to the MVA Claims that arose out of the negligence of the Contractor in its handling of construction site safety and traffic control of the intersection where the MVA occurred.

[43] The City also argues that given the inextricably intertwined nature of the claims as against the City for its alleged breach of contract and statutory duty to ensure the safety of the public when using its roadways, it would be difficult to apportion the costs of defending the breach of contract claim and the breach of statutory duty claim, therefore the duty to defend applies to all defence costs.

b. The Defendant's position

[44] AXA Pacific denies it is obliged to defend the City in any of the actions, with the exception of the two minor incidental claims dealing with the vicarious liability of the City in respect of the Contractor's negligence.

[45] In essence, AXA Pacific argues that since the pleadings in the MVA Claims all allege liability or fault on the City's part for its own negligence in its operations, including breaching its contractual duty to replace the existing traffic signs and breaching its statutory duty to have the works safely undertaken in a manner consistent with protecting the public and in failing to replace the stop sign to its usual or ordinary place or warning the public that the stop had been relocated, its duty to defend the City as an additional insured on the Contractors insurance policy does not arise. AXA Pacific thus argues that substantially all of the allegations in the various claims in which the City is either a defendant or a third party are grounded in the liability of the City for its direct fault through its own negligence in its operations

by failing to replace the stop sign (contrary to the requirements of the Contract Documents) or through breach of a non-delegable duty of ensuring the safety of the public on its streets.

[46] AXA Pacific has admitted that the City is insured under the insurance clause. However it says that when the substance and true nature of the allegations are determined, the pleadings rule establishes that the claims as against the City relate to its own direct fault or negligence, not the operations of the insured Contractor, in failing to fulfill its responsibility to replace existing traffic signs as clause SS3.3 of the Contract Documents above requires and in breaching its statutory duty to ensure the safety of the public on its streets and that the works were carried out properly. Accordingly, AXA Pacific argues it has no duty to defend the City under the terms of the policy as the City's liability arises out of its own actions, not the operations of the insured contractor.

5. Analysis

a. The duty to defend

[47] The parties do not differ on the principles that govern the duty to defend and have reviewed the principles in depth in their written submissions filed on this application.

[48] The law is clear that the duty to defend is governed by the pleadings. AXA Pacific will only have a duty to defend the City if the statements of claim in the underlying actions allege a state of facts that, properly construed, would support an action that could potentially fall within coverage: *Non-Marine Underwriters, Lloyd's of London v. Scalera*, 2000 SCC 24, [2000] 1 S.C.R. 551 at para. 90, *Nichols v. American Home Assurance Co.*, [1990] 1 S.C.R. 801 at 808; *Agresso Corp v. Temple Insurance Co.*, 2007 BCSC 19 at para. 31.

[49] The duty to defend is broader than the duty to indemnify "in the sense that the duty to defend arises where the claim alleges acts or omissions falling within the policy coverage, while the duty to indemnify arises only where such allegations are

proven at trial": *Reform Party of Canada v. Western Union Insurance Co*., 2001 BCCA 274, 87 B.C.L.R. (3d) 299 at para. 3, citing *Scalera* and *Nichols*; *Agresso Corp.* at para. 31 and footnote 1.

[50] The general rule regarding the scope of the pleadings was stated in *Bacon v. McBride* (1984), 51 B.C.L.R. 228 (S.C.) at 232:

> The pleadings govern the duty to defend – not the insurer's view of the validity or the nature of the claim or the possible outcome of the litigation. If the claim alleges a state of facts which, if proven, would fall within the coverage of the policy, the insurer is obliged to defend the suit regardless of the truth or falsity of such allegations. If the allegations do not come within the policy coverage, the insurer has no such obligation.
>
> [Emphasis added]

[51] The pleadings must be assessed to ascertain the substance and true nature of the claims, and the factual allegations must be considered in their entirety to determine whether they could possibly support the plaintiff's claims: *Monenco Ltd. v. Commonwealth Insurance Co*., 2001 SCC 49, [2001] 2 S.C.R. 699 at para. 35, *Agresso* at para. 33.

[52] In *Scalera*, Iacobucci J. developed a three-step process (at paras. 50-52)

> [50] First, a court should determine which of the plaintiff's legal allegations are properly pleaded. In doing so, courts are not bound by the legal labels chosen by the plaintiff. A plaintiff cannot change an intentional tort into a negligent one simply by choice of words, or vice versa. Therefore, when ascertaining the scope of the duty to defend, a court must look beyond the choice of labels, and examine the substance of the allegations contained in the pleadings. This does not involve deciding whether the claims have any merit; all a court must do is decide, based on the pleadings, the true nature of the claims.
>
> [51] At the second stage, having determined what claims are properly pleaded, the court should determine if any claims are entirely derivative in nature. The duty to defend will not be triggered simply because a claim can be cast in terms of both negligence and intentional tort. If the alleged negligence is based on the same harm as the intentional tort, it will not allow the insured to avoid the exclusion clause for intentionally caused injuries.
>
> [52] Finally, at the third stage the court must decide whether any of the properly pleaded, non-derivative claims could potentially trigger the insurer's duty to defend.

[53] The duty to defend principles outlined above must be considered within the overall context of the general principles of insurance contract interpretation. First, the general purpose of insurance is, as noted by Madam Justice Fisher in *Agresso* at para. 36, to provide "a mechanism for transferring fortuitous contingent risks":

> … insurance usually makes economic sense only where the losses covered are unforeseen or accidental. (Scalera at para. 68-69, citing C. Brown and J. Menezes, Insurance Law in Canada (2nd ed. 1991) at 125-126)

[54] Moreover, insurance contracts are essentially adhesionary, ambiguities are construed against the insurer; coverage provisions should be construed broadly and exclusion clauses narrowly: *Scalera* at para. 70, *Agresso* at para. 37.

[55] And finally, where the contract is unambiguous, a court should give effect to the clear language, reading the contract as a whole; where there is ambiguity, the court should give effect to the reasonable expectations of the parties: *Agresso* at para. 38. In this case the parties agree there are no ambiguities in the contract.

[56] The insurer's obligation to defend arises from the allegations in the statement of claim: *Dave's K. & K. Sandblasting (1988) Ltd.* at para. 11.

[57] The purpose of this application is not to determine the outcome of the underlying action. The only issue before the Court is whether or not the allegations in the statements of claim trigger coverage for the City and thus engage AXA Pacific's duty to defend.

[58] Considering all of these legal principles, I turn to the first issue that must be determined in assessing whether AXA Pacific's duty to defend the City is triggered in this case

b. What is the "substance and true nature of the claim" contained within the pleadings and relevant extrinsic evidence on the four MVA claims?

[59] Careful examination of the pleadings filed in the four MVA Claims, as reviewed above, reveals that the MVA giving rise to the MVA Claims was caused by the removal and relocation of the stop sign at the intersection where the MVA

occurred. The allegations with respect to the cause of the accident are identical in substance in each of the MVA Claims and in all the underlying actions the cause of the accident was the removal and relocation of the stop sign, an act alleged to have been done by the Contractor or its agents or employees.

[60] The City is named as a defendant in the actions initiated by Barbara Matfield and Alexis Brown and those two actions allege the City is liable in negligence, breach of contract or breach of statutory duty by:

> (a) breaching its duty to have the works safely undertaken and in a manner to protect the public;
>
> (b) not replacing the existing stop sign or erecting an new stop sign;
>
> (c) failing to replace the existing stop sign in its usual and/or ordinary place;
>
> (d) failing to warn that the stop sign has been relocated in other than its usual and ordinary place;
>
> (e) failing to adequately supervise Peter's Bros. or its subcontractors in their contractual obligations;
>
> (f) being vicariously liable for the negligent acts and omissions of the contractors, their agents, servants or employees.

[61] AXA Pacific argues that these allegations against the City, with the exception of (f), give rise to separate, distinct grounds of liability that are independent of the operations or conduct of the Contractor and thus do not fall within the coverage for liability arising out of the operations of the insured Contractor.

[62] Essentially AXA Pacific's argument of separate liability on the part of the City appears to simply analyze the allegations against the City as contained within the statements of claim and third party notices without considering the entirety of the underlying action as against the Contractor and the City. AXA Pacific also relies on the pleadings from the third party notices issued by the Contractor to suggest that the SS contract provisions in the Contract Documents relating to existing traffic signs have been breached by the City. But these arguments ignore the fact that the underlying action, the MVA Claims, all arise and revolve around work done by the Contractor at the intersection where the MVA occurred. The fact that the Contractor

endeavours to place the responsibility back on the City through its pleadings does not neutralize or eradicate the substance and true nature of the allegations in the underlying actions.

[63] AXA Pacific appears to be arguing that because ultimate responsibility in the Contractor's and its own view lies with City, that absolves AXA Pacific of its duty to defend the City. But as outlined above, that is inconsistent with principles of the duty to defend. The court is not to examine the underlying action from the perspective of the insurer's view of the validity of claim.

[64] In the Third Party Notice pleadings in all of the MVA Claims, the Contractor relies upon the terms of the Contract Documents contained in clause SS3.3 dealing with existing traffic signs. These specific terms are outlined above at para. 35 of these reasons.

[65] None of the allegations in the pleadings suggest that the City moved the stop sign or knew or ought to have known that the stop sign had been moved, that the Contractor returned the stop sign to the City yards, or that the Contractor notified the City that the stop sign had been relocated. Consequently, all of the allegations against the City in all of the pleadings flow from and arise out of the operations of the Contractor which, by the terms of the Contract Documents, was responsible for traffic control and safety around the construction area.

[66] Thus when the pleadings are assessed to ascertain the substance and true nature of all the claims, and the factual allegations are considered in their entirety, the claims against the City specifically all relate to its purported negligence in failing to have the works by the Contractor carried out in a safe manner and in failing to warn about the removal and improper replacement of the stop sign. But each and every claim in this regard, flows back to the movement of the stop sign and the conduct of the Contractor and its employees in removing and improperly relocating the stop sign and its failure to properly fulfill its obligations under the contract it had with the City. In other words the allegations are attributable to matters that "arise out of the operations of the insured", here the Contractor.

[67] To put it another way, and to adopt the neatly stated comments of Madam Justice Southin in the British Columbia Court of Appeal's decision upheld by the Supreme Court of Canada in its decision in *Monenco Ltd.* at para. 23, the claim in the underlying action is a claim "arising out of" the construction project and thus arising out of the works of the insured contractor. As Southin J.A. stated "[s]uffice it to say that if this project had not existed, there would have been no claim, ergo the claim arises out of it."

[68] In the case at bar, had the Contractor not been working on the construction contract at the particular intersection in issue and had it not removed and relocated the stop sign, there would have not have been any claims. Thus the liability arises out of the operations of the insured, the Contractor.

[69] All of these claims allege a state of facts which, if proven, result in allegations that arise out of the operations of the Contractor in initially removing and relocating the stop sign and failing to notify the City of the steps it had taken with respect to the stop sign and in failing to fulfill its obligations as to safety of its construction site and traffic flow in that area as stipulated in the Contract Documents.

c. Non-Delegable Duty and Apportionment

[70] AXA Pacific also argues that because the pleadings allege direct negligence and breach of contractual and statutory duties by the City in relation to its own operations in failing to have the works relating to construction activities on its roadway carried out in a safe manner, all of which relate to the failure to replace the stop sign in its usual place or at all and in failing to warn the public about the relocation, any breach of duty by the City relating to public safety and the use of the City's roadways is a non-delegable duty that gives rise to direct fault on the part of the City and cannot be characterized as vicarious liability arising through the operations of the Contractor.

[71] AXA Pacific relies upon a passage from *B.(M.) v British Columbia*, 2001 BCCA 227 where Madam Justice Prowse stated at para. 73:

> [73] ...it is important to bear in mind that the words "non-delegable duty" are somewhat misleading. To call a duty non-delegable does not mean that the duty cannot be delegated, but, rather, that ultimate responsibility for the performance of the duty cannot be delegated. Responsibility for the performance of the duty remains with the delegator who will be held liable in the event that the duty is not performed, or it is performed negligently or tortuously.

[72] AXA Pacific argues that this means that the City could not delegate its duty relating to its obligation to ensure public safety with respect to the use of the City's roadways. As the pleadings specifically aver to the City breaching its statutory duty to ensure public safety, this, submits AXA Pacific, gives rise to direct fault on the part of the City not vicarious liability arising out of the operations of the Contractor. Accordingly, the City's direct liability is not covered under the certificate of insurance issued for it being an additional insured on the Contractor's policy.

[73] While the City's duty to ensure public safety may well fall within the parameters of a non-delegable duty, the overall context of the allegations nonetheless and the true nature of the claims arise from actions taken and works done by the Contractor.

[74] It must be recalled that where a statement of claim alleges several causes of action or theories of recovery against an insured, one of which is within the coverage of the policy and another which is not, the insurer is bound to defend the insured regarding the cause of action which, if proved, would be within coverage: *Bacon v. McBride* at 233, *Hartup v. BCAA Insurance Corp.*, 2002 BCSC 972 at para. 21; *Agresso* at para. 35. Where apportionment of causes of action within and outside coverage can be conducted then the assessment should proceed in that fashion.

[75] AXA Pacific argues that there should be apportionment in this case and that any duty to defend the City relates only to the issue of vicarious liability for the Contractor's actions.

[76] In some circumstances though, it may well be difficult to separate out those portions of the allegations that arise solely from the operations and fault of the

insured, in this case the Contractor, as compared to the liabilities arising from independent operations and actions of the party arguing the insurer has a duty to defend it as well, in this case the City. In *Kelly Panteluk Construction v. AXA Pacific Insurance Co.*, 2005 SKQB 239 at para. 27, the court noted that there are at least three exceptions to the general rule regarding apportionment articulated in *Continental Insurance Co. V. Dia Met Minerals Ltd.* (1996), 77 B.C.A.C. 251: (i) where a claim alleges a single cause of action with different theories of liability; (ii) where an action raises mixed non-derivative claims that overlap to the degree it is impossible or impractical to apportion the cost of defending both; and (iii) where the insurer has failed to discharge its obligation to defend or to share in the cost of defending a claim covered by its policy of insurance.

[77] In *RioCan Real Estate Investment Trust v. Lombard Insurance Co.,* [2008] O.J. No. 1449 (S.C.J.) (QL), Hennessy J. of the Ontario Superior Court of Justice addressed the issue of the duty to defend where only some of the theories of liability claimed negligence on the part of a contractor in failing to perform obligations under a contract to remove snow and ice at two shopping mall properties. Two customers at the malls owned by RioCan were injured in separate incidents of falling on ice or snow in the mall parking lots. RioCan had a contract with another party to provide snowplowing and winter maintenance for the parking lots. RioCan was named as an additional insured on the contractor's insurance policy. Lombard Insurance refused to provide a defence to RioCan arguing that some of the claims asserted breaches of RioCan's statutory obligation as an occupier and that the contractor's insurance coverage did not extend to cover RioCan for its own negligent acts of breaches of the *Occupiers' Liability Act*, R.S.O. 1990, c. 0-2.

[78] Justice Hennessy found that Lombard Insurance had a duty to defend RioCan in the underlying actions. The fundamental issue raised in the actions and the true nature of the claim was found to be that the defendant was negligent in failing to maintain an ice-free parking lot and as a result the plaintiffs fell and sustained injuries. Issues of who was responsible if the snow and ice conditions were found to have caused the plaintiffs to fall were matters for the trial judge to determine. At the

hearing of the duty to defend application, it was impossible to determine where fault would lie for the plaintiffs' injuries.

[79] The Court concluded in *RioCan* at paras. 36-39 that where there is a duty on an insurer to defend some, or only one, of the claims against an insured and that claim embodies the true nature of the claim, a duty to defend the entire claim arises.

[80] A similar conclusion was reached by Mr Justice Beveridge [as he then was] in *SREIT (Park West Centre) Ltd. v. ING Insurance Co of Canada*, 2008 NSSC 183. As in *RioCan*, the owners of a shopping complex entered into a contract for snow clearing and to salt and sand the parking and sidewalk areas of the mall. A customer at the mall slipped and fell on a patch of transparent ice and suffered injuries. The insurer initially agreed to defend the owners of the shopping complex but then refused to participate when an amended statement of claim was filed that advanced multiple theories of liability that included operations outside the ambit of the contractor's snow removal responsibilities.

[81] Mr. Justice Beveridge reviewed the jurisprudence and noted that the mere existence of claims plainly outside the insurance coverage does not relieve the insurer of the obligation to defend and fund the defence of the whole claim where there are claims within coverage. The Court in *SREIT* concluded at ¶26-27 that the amended statement of claim contained allegations that were both within and some that were outside coverage, but the claims were so intertwined that there was no rational or practical basis for distinguishing costs related to the covered and arguably non-covered claims.

[82] In *Daher v Economical Mutual Insurance Co.*, [1996] O.J. No. 4394 (C.A.) (QL) the Ontario Court of Appeal upheld the ruling of a motions judge that the insurer was required to defend the parents of a student who was injured in a science experiment at school. The School Board had filed a third party claim against the student's parents alleging they were negligent in failing to properly instruct their son on the use of Draino and in giving him a can of Draino from their retail store. Draino had been used in the science experiment at the school. The parents brought a

motion to determine the issue of whether their insurer was required to defend the third party claim. In upholding the ruling of the motions judge, Mr. Justice Rosenberg wrote at para.14:

> [14] In a proper case it may be possible to apportion the defence costs where only certain claims fall within the terms of the policy. See Gosse v. Huemiller, [1988] O.J. No. 1595, [1988] I.L.R. (Ont. H.C.J.) and Continental Insurance Co. v. Dia Met Minerals Ltd. (1996), C.C.L.I. (2d) 72 (B.C.C.A.). This is not a case, however, of multiple causes of action where it is possible to divide the costs of defending the various causes of action. The third party claim alleges only one single cause of action with different theories of liability. The facts giving rise to the multiple theories of liability are so intertwined that I cannot see any principled basis upon which this court or an assessment officer could unravel them to apportion costs to one theory rather than another.

[83] The operations of the Contractor in this case included the resurfacing of the roadway at the intersection of Okanagan Avenue and Camrose Street in accordance with the provisions of the Contract. Thus the Contractor was responsible for all aspects of the works including traffic control, public safety and traffic sign preservation. The Contract Documents set out the duties of the Contractor and included responsibility for (i) retaining and directing safe public travelled lanes, signs, barricades and detours (as per the Instructions to Tender clause 4.10.1); (ii) the supply, maintenance and removal of any and all construction zone traffic control which will, or may be required (as per clause SGC 6.2); and, (iii) the protection of all existing street name and traffic signs (as per clause SS 3.1).

[84] Examination and comparison of all the allegations in the pleadings reveals that the underlying conduct or action giving rise to the MVA Claims was the removal and relocation of the stop sign at the relevant intersection and that the removal had been done by the Contractors and its employees or agents. There is only one single cause of action with different theories of liability advanced. The multiple theories of liability which include negligence, breach of contract and breach of statutory duty on the part of the City, as outlined in the pleadings, nonetheless are inextricably tied to and arise out of the conduct and operations of the Contractor. Thus each of these allegations could be attributable to, and have their genesis in, the failure of the

Contractor to perform its obligations under the contract as specified in the Contract Documents. Consequently, the facts giving rise to the multiple theories of liability, are so intertwined and tied to the conduct and operations of the Contractor that it is impossible, on any principled basis, to unravel them to apportion costs to one theory of liability or another.

[85] As in *RioCan, SREIT* and *Daher*, the totality of the pleadings in this case allege multiple theories of liability for the MVA. The substance and true nature of the claim, however, is that the MVA was caused by the removal and improper relocation of the stop sign. Who was responsible for the removal and replacement of the stop sign is not a subject for determination on this application, I need only consider whether or not it is possible that the allegations in the pleadings, that is the amended amended statement of claim of Barbara Matfield and the statement of claim of Alexis Brown as well as the third party notices could give rise to liability within the policy coverage.

[86] In this case the Contractor was responsible for all aspects of the construction project including project safety of the construction areas, directing safe public travel in the construction area, supply and maintenance of all construction zone traffic control and day to day protection and maintenance of all existing traffic signs until the Contract was completed. In these circumstances, it is my opinion that it is entirely possible that the allegations in the pleadings could give rise to liability within the policy coverage, that is the liability arose out of the operations of the Contractor, since it could be found that the Contractor failed to abide by its contractual obligation in performing the works and in its negligently removing and relocating the stop sign.

[87] Even if it could be said that the pleadings contain allegations that are both within and some are outside the coverage, the claims are, in my opinion, so intertwined that there is no rational or practical basis for distinguishing costs related to the covered and arguably non covered claims.

5. Conclusion

[88] When the substance and true nature of the allegations are discerned from the pleadings filed in the claims arising out of the underlying MVA Claims, it is readily apparent that the pleadings make allegations that could possibly give rise to liability within the insurance coverage. Thus the substance and true nature of the claims arise out of the operations of the insured, the Contractor, in performing the works under the contract it entered into as an independent contractor with the City. In this case AXA Pacific's duty to defend the City is triggered by the substance and true nature of the allegations contained in the pleadings.

[89] Accordingly, I make the following orders:

(a) The City is an insured under a policy of insurance issued by AXA Pacific under number 1172213;

(b) AXA Pacific is liable, under the aforesaid policy of insurance, to indemnify the City against all costs and expenses incurred by the City in defending the Actions referred to in the City's amended statement of claim arising from the motor vehicle accident which occurred on the 23rd day of October, 2001;

(c) AXA Pacific shall pay the defence costs and expenses to the City in an amount to be determined by a Master or Registrar of this Court; and

(d) The City is entitled to recover its costs of these proceedings against AXA Pacific.

"Ker, J."