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Bars to Subrogation in the Landlord/Tenant and Strata Arenas

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A. Introduction

Subrogation is the right of an insurance company which has indemnified an insured for a loss suffered at the hands of a third party to recover costs or losses from the responsible third party. Through subrogation, rights of recovery against the third party from the person indemnified (the subrogor) transfer to the one that made the indemnity (the subrogee). The subrogee then stands in the shoes of the subrogor and exercises all of the rights of the subrogor when claiming against the party responsible for the loss.

B. Bars to subrogation

Principles of subrogation are found in the common law, but have been modified to some extent by statute and the wording of insurance policies. All of the provinces and territories of Canada have Insurance Acts that regulate insurers' rights of subrogation. For example, in B.C., the ***Insurance Act,*** RSBC 2012, c 1 [the "***Insurance Act***"] has removed the requirement set out in the common law that the insured be fully indemnified before the insurer gains a subrogated interest (***Insurance Act,*** s. 36(1)).

Regardless of the principles set out in the common law and statute, there may be situations where the insured has waived the right of subrogation against a potential defendant, preventing the insurer from recovering against that party. The insured may have done so without the insurer being a party to the waiver, or even being aware of the waiver until after the loss. Although not technically an express waiver of subrogation by the insured, a covenant to insure may also operate to exclude subrogated claims without the involvement of the insurer. There are two main contexts that will be addressed in this paper:

1. Landlord and tenant; and
2. Strata corporation and strata unit owner.

1. Landlord and tenant

The relationship between landlord and tenant is primarily determined by a lease agreement. In the event of damage to the leased premises caused by the negligence of either the landlord or the tenant, one would normally have the right to sue the other for the losses resulting from that negligence. However, the ability to sue is governed by the provisions of the lease which can take different forms.

The starting point on the question of whether a subrogated claim may be pursued in a landlord/tenant relationship is the Supreme Court of Canada's "trilogy" of cases: ***Agnew-Surpass Shoe Stores Ltd. v Cummer-Yonge Investments Ltd.***, [1976] 2 SCR 221 [***Agnew-Surpass***], ***Ross Southward Tire Ltd. v Pyrotech Products Ltd.,*** [1976] 2 SCR 35 [***Ross Southward***], and ***T. Eaton Co v Smith***, [1978] 2 SCR 749 [***T. Eaton***]. The trilogy recognized that certain provisions in commercial leases could give rise to the landlord being deemed to have waived the right of its insurer to bring a subrogated claim against the tenant. Each case in the trilogy involved landlord/tenant insurance arrangements and damage by fire caused by the negligence of the tenant, but each involved slightly different contractual provisions.

In ***Agnew-Surpass***, the issue was whether the tenant of a shopping centre was liable to the landlord for loss from a fire originating in the tenant's premises and caused by the tenant's negligence. The lease required the landlord to insure its shopping centre "against all risk of loss or damage caused by or resulting from fire" and required the tenant to take good and proper care of the leased premises, "except for reasonable wear and tear…and damage to the building caused by perils against which the lessor is obligated to insure hereunder".

The Majority decision of Pigeon J and minority decision of Laskin CJC both agreed that when all provisions of the lease were read together, the landlord's covenants to insure the building for loss by fire extended the benefit of that insurance to the tenant, such that the landlord's insurer had no right of subrogation against the tenant. The Court held that waiver of subrogation applied only to the extent that the landlord was obligated to obtain insurance under the covenant to insure.

In the second case, ***Ross Southward,*** the lease required the tenant to pay all "insurance rates". The landlord regularly charged the tenant for, *inter alia,* its share of the cost of fire insurance. The issue was whether the tenant's covenant to pay for insurance purchased by the landlord was enough to extinguish the landlord's right to maintain an action in negligence against the tenant.

Laskin CJC for the majority held that the provision respecting payment of insurance, in conjunction with the landlord presenting the bill to the tenant, passed the risk of loss by fire from the tenant to the landlord. The court held that the subrogated claim could not be maintained.

In the third case, ***T. Eaton***, two landlords covenanted to insure the leased premises against fire; the tenant on the other hand promised to repair on notice, damage by fire excepted.

The Court concluded that the landlord's covenant to insure their tenant's premises was regarded as a "supervening covenant" that prevailed even where the tenant's negligence had caused the loss. Writing for the majority, Laskin CJC characterized the issue in ***T. Eaton*** as:

> ... whether, in circumstances where, by the lease, the tenant is under an obligation to repair, and where its obligation to repair does not extend to repairing damage from accidental (as contrasted with negligent) fires, it is entitled, as between it and the landlord, to claim the benefit of a fire insurance policy (providing indemnity for loss arising from fires negligently caused), which the landlord had covenanted with the tenant to provide.
>
> ... This is not a case where one has to consider whether there is some provision exonerating one contracting party from liability to the other for the former's negligence. Rather is it a case where a supervening covenant has been given and taken to cover by an insurance policy the risk of loss from a fire caused by negligence. An insurer could not refuse to pay a claim for loss by fire merely because the fire arose from the insured's negligence. I can see no reason why its position can be any better against a tenant, whose negligence caused loss by fire, if the lease with the landlord makes it clear that a policy was to be taken out by the landlord to cover such fires, and a policy is written which does so. In short, the insurer can claim only by subrogation under the lease. [At 755-6; emphasis added.]

Chief Justice Laskin held that the covenants to insure in the leases had the effect of transferring the risk of loss by fire from the tenant to the landlords, and just as in ***Agnew-Surpass,*** the landlord's insurers were not permitted to maintain their subrogated claim.

A useful summary of the trilogy was provided in ***Madison Developments Ltd. v Plan Electric Co.*** (1997) 36 OR (3d) 80 (Ont. CA), where Carthy J.A. stated:

> …The law is now clear that in a landlord-tenant relationship, where the landlord covenants to obtain insurance against the damage to the premises by fire, the landlord cannot sue the tenant for a loss by fire caused by the tenant's negligence. A contractual undertaking by the one party to secure property

> insurance operates in effect as an assumption by that party of the risk of loss or damage caused by the peril to be insured against. This is so notwithstanding a covenant by the tenant to repair which, without the landlord's covenant to insure, would obligate the tenant to indemnify for such a loss. This is a matter of contractual law, not insurance law, but, of course, the insurer can be in no better position than the landlord on a subrogated claim. The rationale for this conclusion is that the covenant to insure is a contractual benefit accorded to the tenant, which, on its face, covers fires with or without negligence by any person. There would be no benefit to the tenant from the covenant if it did not apply to a fire caused by the tenant's negligence. [At 84; emphasis added.]

The trilogy was also applied by the B.C. Court of Appeal in ***North Newton Warehouses Ltd. v Alliance Woodcraft Manufacturing Inc.***, 2005 BCCA 309 [***North Newton***]. This case involved a fire in a leased premises caused by the negligence of the tenant. The landlord's insurer brought a subrogated claim against the tenant. The landlord had covenanted in the lease to take out and maintain insurance against "all risks" of loss or damage to the building and to repair the premises in the event of damage by "fire or other casualty not caused by the negligence of the Tenant"; the tenant had agreed to reimburse the landlord for its insurance premiums as a component of "additional rent". The Court of Appeal reversed the trial judge's decision and held that the requirement to pay premiums was sufficient to provide tort immunity for the tenant:

> Here the tenant Alliance has paid the landlord an amount for the insurance obtained by North Newton covering fire damage to the building. It seems to me that, as Laskin C.J.C. observed in the *Ross Southward* case at 39, a tenant who has paid for an expected advantage as between itself and its landlord should benefit from those payments, and loss issues thereafter are between the landlord and its insurer. In such circumstances, to allow the insurer of North Newton to pursue its subrogated action against Alliance would render nugatory benefits accruing to the tenant under the covenant of the landlord to insure. [At para. 42; emphasis added.]

and further:

> Ultimately, the policy rule underpinning the proposition that the insurer cannot pursue a tenant for damages in circumstances such as those present in the instant case is based on the proposition that it makes little business sense for a landlord to covenant to insure and for a tenant to pay the premiums if the tenant is not to derive some benefit from the insurance. One might properly say that there is something approaching a presumption in favour of a tenant benefiting from a landlord's covenant to insure. That is the legal principle that I take to be established from the trilogy of cases decided by the Supreme Court of Canada. [At para. 45; emphasis added.]

Mr. Justice Hall for the majority held that a subrogated claim brought by the insurer of a landlord against a tenant whose employees had negligently caused a fire was barred.

The decision in ***North Newton*** recognizes a presumption of public policy that, under a lease where the landlord gives a covenant to insure, and where the tenant agrees to pay for the cost of that insurance, the tenant will be entitled to the benefit of that insurance and thus a subrogated claim cannot be brought against the tenant.

The cases discussed above establish that a landlord's property insurer will not be permitted to pursue a subrogated claim against a tenant when the lease includes a landlord's covenant to insure. The vice versa is also true where it is the tenant, rather than the landlord, who has covenanted to insure (***Orange Julius Canada Ltd. v Surrey***, 2000 BCCA 467, at paras. 22 and 26). Even in the absence of an express covenant to insure, the courts have found in some circumstances, a parties' payment of insurance premiums can create an implied covenant to insure. What is clear is that the court will look at the intention of the parties to bear the risk of loss in determining whether there is a bar to subrogation.

2. Strata corporation and strata unit owner

In condominiums, loss in one unit can cause damage to the other units or common property (fire, smoke damage, water leaks, etc.). The insurer for the strata will usually be obliged to cover the cost of repairing damage to the common property and original fixtures. Occupants' insurers will typically cover contents, loss of rents or additional living expenses. An issue arises when the Strata' or owners' insurers bring subrogated claims against strata unit owners from within whose unit the cause of the loss originated.

Legislative framework under BC Strata Property Act

The ***Strata Property Act,*** SBC 1998, c 43 [***Strata Property Act***] modifies the common law principles of subrogation in the strata context. The ***Strata Property Act*** sets out that a strata unit owner owns his or her proportionate share of the strata's common property with the other owners as tenants in common (***Strata Property Act***, s. 66):

> Ownership of property
> 66 An owner owns the common property and common assets of the strata corporation as a tenant in common in a share equal to the unit entitlement of the owner's strata lot divided by the total unit entitlement of all the strata lots.

According to section 149 of ***Strata Property Act*** and section 9.1 of the ***Strata Property Regulation,*** BC Reg 43/2000 [***Strata Property Regulation***]**,** the strata corporation is required to maintain full replacement insurance on the strata's common property, common assets and certain fixtures:

> Property insurance required for strata corporation
> 149 (1) The strata corporation must obtain and maintain property insurance on
> (a) common property,
> (b) common assets,
> (c) buildings shown on the strata plan, and
> (d) fixtures built or installed on a strata lot, if the fixtures are built or installed by the owner developer as part of the original construction on the strata lot.
> (2) For the purposes of subsection (1) (d) and section 152 (b), "fixtures" has the meaning set out in the regulations.
> (3) Subsection (1) (d) does not apply to a bare land strata plan.
> (4) The property insurance must
> (a) be on the basis of full replacement value, and
> (b) insure against major perils, as set out in the regulations, and any other perils specified in the bylaws.

Definitions for section 149 of the Act
9.1 (1) For the purposes of sections 149 (1) (d) and 152 (b) of the Act, "fixtures" means items attached to a building, including floor and wall coverings and electrical and plumbing fixtures, but does not include, if they can be removed without damage to the building, refrigerators, stoves, dishwashers, microwaves, washers, dryers or other items.
(2) For the purposes of section 149 (4) (b) of the Act, "major perils" means the perils of fire, lightning, smoke, windstorm, hail, explosion, water escape, strikes, riots or civil commotion, impact by aircraft and vehicles, vandalism and malicious acts.

Section 155 of the ***Strata Property Act*** deems strata unit owners, tenants and others who "normally occupy" a unit as being named insureds on the strata corporation's policy "despite the terms of the insurance policy":

Named insureds
155 Despite the terms of the insurance policy, named insureds in a strata corporation's insurance policy include
(a) the strata corporation,
(b) the owners and tenants from time to time of the strata lots shown on the strata plan, and
(c) the persons who normally occupy the strata lots.

Section 158 of the ***Strata Property Act*** recognizes a strata corporation's right to sue a strata unit owner to recover an insurance deductible it has been paid in relation to a property damage claim provided that the owner was "responsible" for the loss:

Insurance deductible
158 (1) Subject to the regulations, the payment of an insurance deductible in respect of a claim on the strata corporation's insurance is a common expense to be contributed to by means of strata fees calculated in accordance with section 99 (2) or 100 (1).
(2) Subsection (1) does not limit the capacity of the strata corporation to sue an owner in order to recover the deductible portion of an insurance claim if the owner is responsible for the loss or damage that gave rise to the claim.
(3) Despite any other section of this Act or the regulations, strata corporation approval is not required for a special levy or for an expenditure from the contingency reserve fund to cover an insurance deductible required to be paid by the strata corporation to repair or replace damaged property, unless the strata corporation has decided not to repair or replace under section 159.

Sections 170 and 171 of the ***Strata Property Act*** allow a strata corporation to sue a strata unit owner for damage to common property:

Suits against owners
170 The strata corporation may sue an owner.

Strata corporation may sue as representative of all owners
171 (1) The strata corporation may sue as representative of all owners, except any who are being sued, about any matter affecting the strata corporation, including any of the following matters:

(a) the interpretation or application of this Act, the regulations, the bylaws or the rules;
(b) the common property or common assets;
(c) the use or enjoyment of a strata lot;
(d) money owing, including money owing as a fine, under this Act, the bylaws or the rules.

(2) Before the strata corporation sues under this section, the suit must be authorized by a resolution passed by a 3/4 vote at an annual or special general meeting.
(3) For the purposes of the 3/4 vote referred to in subsection (2), a person being sued is not an eligible voter.
(4) The authorization referred to in subsection (2) is not required for a proceeding under the *Small Claims Act* against an owner or other person to collect money owing to the strata corporation, including money owing as a fine, if the strata corporation has passed a bylaw dispensing with the need for authorization, and the terms and conditions of that bylaw are met.
(5) All owners, except any being sued, must contribute to the expense of suing under this section.
(6) A strata lot's share of the total contribution to the expense of suing is calculated in accordance with section 99 (2) or 100 (1) except that
(a) an owner who is being sued is not required to contribute, and
(b) the unit entitlement of a strata lot owned by an owner who is being sued is not used in the calculations.

Subrogation against strata unit owners

The ***Strata Property Act*** and the ***Strata Property Regulation*** impose a statutory covenant on strata corporations to obtain property insurance for the benefit of both itself and the strata unit owners. As a result, in most circumstances where the acts or omissions of a strata unit owner have caused damage to the common property, a subrogated claim cannot be brought by the strata corporation's insurer against the unit owner. A strata unit owner is typically entitled to the benefit of the strata corporation's insurance coverage on the common property, and therefore to allow a subrogated action against the strata unit owner would be akin to the strata corporation's insurer suing its own insured.

In ***Lalji-Samji v. Strata Plan VR-2135,*** [1992] BCJ No 176 (BCSC), the court held that the waiver of subrogation principle precluding subrogation against an owner for damage to common property extended to circumstances in which the strata corporation did not, but ought to have had insurance coverage in accordance with the legislation. The court concluded that if there had been proper insurance, the owner would have been an unnamed insured by virtue of the legislation and thus there could be no subrogated claim.

However, in ***Economical Mutual Insurance Co. v Aviva Insurance Co. of Canada,*** [2010] B.C.J. No. 1056, a social host liability case considering liability coverage under a strata's CGL, the Court held that when a strata corporation has not obtained insurance compliant with the ***Strata Property Act,*** the deeming provisions do not have the effect of creating coverage that would otherwise not exist. The coverage actually obtained by the strata corporation must be determined by reference to the terms of the contract of insurance. If the policy the strata corporation obtained is inadequate, or not in compliance with a requirement imposed by the ***Strata Property Act,*** that is an issue between the strata corporation and the owner. This case may support an argument which would allow for recovery against a "non-named" unit owner but significant obstacles, particularly the likely third party claim that could be made against the strata executive, would have to be overcome.

Subrogation against tenants of strata units

The caselaw is not yet clear on the issue of whether the prohibition of subrogation against strata unit owners also applies to claims against tenants of strata units. S 155 of the Strata Property Act deems tenants and persons who normally occupy strata lots to be insureds under strata corporations' property insurance policies, but tenants and occupants do not own common property and therefore arguably do not have insurable interests in that property. Determining whether a subrogation claim can be maintained against a tenant will also depend on the coverage extended to the tenant in the insurance policy.

Claims by a strata corporation to recover insurance deductible

Section 158 of the ***Strata Property Act*** specifically provides that a strata corporation can sue an owner to recover the deductible portion of an insurance claim if the strata unit owner is "responsible" for the loss or damage that gave rise to the claim.

In ***Strata Corp. LMS 2723 v Morrison,*** 2012 BCPC 300, the court addressed the issue of whether s. 158 of the ***Strata Property Act*** entitled a strata corporation to sue a strata owner to recover its insurance deductible for damage caused to common property where the damage was caused solely by the actions of the owner's tenant. In that case, an owner of a strata unit rented her suite to a tenant who caused a fire resulting in damage to her suite and the common property. The strata corporation recovered from its insurer for the damage to the common property, except to the extent of the $2,500 deductible. The Court concluded that "responsible for" as set out in the legislation was to be interpreted broadly based on the fact that although an owner may have no control over the tenant, the owner is responsible for what occurs in his or her unit independent of any negligence by the owner. The Court further held that it would be unfair to impose the burden of the deductible on all owners for what would ordinarily be borne by an owner of a particular unit if that owner owned the unit as a single family dwelling.

Whether a strata corporation can maintain an action to recover a deductible from a strata owner depends upon all the provisions of the applicable statute and the bylaws, rules, and regulations of the strata corporation.

C. Conclusion

Subrogation can be of very significant economic importance to property insurers, and it is important to be aware of the common bars to subrogation before incurring expense in commencing an action. Similarly, liability insurers have an interest in dismissing inappropriate recovery actions in their infancy. The above comments are not meant to be a comprehensive evaluation of the law, but should provide a starting point for the issues that can be fatal to subrogated claims in the landlord/tenant and strata contexts.