The Liability of Lessors and the Insurance Implications of Bill 35

The British Columbia Legislature recently took steps to cap the liability exposure of auto dealers and auto leasing companies. Included in Bill 35, the *Miscellaneous Statutes Amendment Act (No. 2) 2007* are provisions amending both the *Insurance (Vehicle) Act* and the *Motor Vehicle Act*. These amendments were introduced in the Spring 2007 Legislative Session and, absent any amendments, are expected to come into force in the near future.

The amendments are intended to address concerns that sellers under conditional sales agreements and lessors are owners of vehicles, and therefore exposed to unlimited liability. This follows on the British Columbia Court of Appeal's decision in *Yeung* v. *Au*, which found that section 86(3) of the *Motor Vehicle Act* did not exclude sellers under option to purchase agreements. The Supreme Court of Canada, in a judgment handed down October 11, 2007 agreed with the Court of Appeals decision. What these decisions mean in practice is that plaintiffs with significant damage awards, unable to fully recover against a negligent driver, will pursue the sellers and lessors of the vehicles since the sellers and lessors are often corporations with significant assets. During second reading of Bill 35, the Minister noted that limiting liability would help keep businesses like car rental companies in the province, thereby supporting major industries like tourism.

The Present Regime

Drivers of vehicles are liable for the loss or damage that they cause. In most jurisdictions legislation also imposes vicarious liability on owners. The key provision in British Columbia is section 86 of the *Motor Vehicle Act*. Section 86 now reads as follows:

> 86 (1) In an action to recover loss or damage sustained by a person by reason of a motor vehicle on a highway, every person driving or operating the motor vehicle who is living with and as a member of the family of the owner of the motor vehicle, and every person driving or operating the motor vehicle who acquired possession of it with the consent, express or implied, of the owner of the motor vehicle, is deemed to be the agent or servant of that owner and employed as such, and is deemed to be driving and operating the motor vehicle in the course of his or her employment.
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> (2) Nothing in this section relieves a person deemed to be the agent or servant of the owner and to be driving or operating the motor vehicle in the course of his or her employment from the liability for such loss or damage.
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> (3) If a motor vehicle has been sold, and is in possession of the purchaser under a contract of conditional sale by which the title to the motor vehicle remains in the seller until the purchaser becomes the owner on full compliance with the contract, the purchaser is deemed an owner within the meaning of this section, but the seller or the seller's assignee is not deemed to be an owner within the meaning of this section.

Note that 86(1) imposes vicarious liability for the acts of persons living with, and as a member of, the family of the owner and on persons driving with the owner's consent. Section 86(2) imposes liability on employers for the negligence of employees.

"Owner" is broadly defined in section 1 of the *Motor Vehicle Act* as follows:

> "Owner" includes a person in possession of a motor vehicle under a contract by which he or she may become its owner on full compliance with the contract.

This definition is not limited in any way. Thus, lessors of vehicles are considered owners and therefore subject to liability. The only qualification on this approach is what is set out in section 86(3) of the *Motor Vehicle Act*. This provision excuses sellers who enter into a conditional sales agreement with a purchaser. Initially, it was understood that "conditional sale" was to be interpreted broadly so as to include situations where the seller became, or had the option of becoming, the owner of the vehicle. This was the approach of the Court of Appeal in *Schoenbach* v. *Truong* [1996] B.C.J. No. 927 (BCCA). This expansive definition was derived from the *Sale of Goods on Condition Act*, which was repealed in 1990. In *Yeung* v. *Au*, 2006 BCCA 217, a five-judge panel of the Court of Appeal held that the reasoning in *Schoenbach* was not correct and narrowed the definition to the common law definition of conditional sale, which did not include the option of becoming the owner of the goods. Thus, many conditional sale agreements in the marketplace became subject to section 86(1) of the *Motor Vehicle Act*.

The result of all this is that sellers under conditional sales agreements and lessors of vehicles are subject to vicarious liability. What this means in practice is that, if there is a large claim that exceeds whatever insurance has been put on the vehicle, usually by the person in possession of the vehicle, the injured party may then turn to the assets of the person in possession (usually someone with no significant assets) as well as the assets of the lessor or seller (usually a company with significant assets).

Lessors and sellers have tried to push the liability down by requiring persons in possession of vehicles to name them as additional insureds under the applicable motor vehicle insurance policies. However, these policies only protect the lessors and sellers up to the limits of the policies.

The New Regime

What Bill 35 will do is amend section 86 of the *Motor Vehicle Act* so that it reads as follows:

> 86 (1) In the case of a motor vehicle that is in the possession of its owner, in an action to recover for loss or damage to persons or property arising out of the use or operation of the motor vehicle on a highway, a person driving or operating the motor vehicle who
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> (a) is living with, and as a member of the family of, the owner, or
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> (b) acquired possession of the motor vehicle with the consent, express or implied, of the owner,
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> is deemed to be the agent or servant of, and employed as such by, that owner and to be driving or operating the motor vehicle in the course of his or her employment with that owner.
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> (1.1) In the case of a motor vehicle that is in the possession of its lessee, in an action to recover for loss or damage to persons or property arising out of the use

or operation of the motor vehicle on a highway, a person driving or operating the motor vehicle who

(a) is living with, and as a member of the family of, the lessee, or

(b) acquired possession of the motor vehicle with the consent, express or implied, of the lessee,

is deemed to be the agent or servant of, and employed as such by, that lessee and to be driving or operating the motor vehicle in the course of his or her employment with that lessee.

(1.2) In the case of a motor vehicle that is in the possession of its lessee, in an action to recover for loss or damage to persons or property arising out of the use or operation of the motor vehicle on a highway, a person driving or operating the motor vehicle who acquired possession of the motor vehicle with the consent, express or implied, of its lessor is deemed to be the agent or servant of, and employed as such by, that lessor and to be driving or operating the motor vehicle in the course of his or her employment with that lessor.

(1.3) The liability under subsection (1.2) of a lessor is subject to the applicable limit established under section 82.1 of the *Insurance (Vehicle) Act*.

(2) Nothing in this section relieves a person deemed to be the agent or servant of the owner or lessee and to be driving or operating the motor vehicle in the course of his or her employment from the liability for such loss or damage.

(3) In this section:

"lessee" means a person who leases or rents a motor vehicle from a lessor for any period of time;

"lessor" means the following:

(a) subject to paragraph (b), a person who, under an agreement in writing and in the ordinary course of the person's business, leases or rents a motor vehicle to another person for any period of time;

(b) if the lessor referred to in paragraph (a) has assigned the agreement, the assignee;

"owner"

(a) includes a purchaser of a motor vehicle who is in possession of the motor vehicle under a contract of conditional sale by which title to the motor vehicle remains in the seller, or the seller's assignee, until the purchaser takes title on full compliance with the contract,

(b) if a purchaser of a motor vehicle is in possession of the motor vehicle, does not include the seller of that motor vehicle under a contract of conditional sale described in paragraph (a) or the assignee of that seller, and

(c) does not include a lessee of a motor vehicle who is in possession of the motor vehicle under an agreement in writing with the owner, whether or not the lessee may become its owner in compliance with the agreement.

The definitions in what will be section 86(3) are most important. Note that "owner" is defined so it excludes the seller of a motor vehicle where the motor vehicle remains in the possession of the purchaser under the contract of conditional sale until such time as the purchaser takes title in full compliance with the contract. Thus, sellers under conditional sales agreements are excused from liability as owners. There is also a limit put on what lessors are liable for, pursuant to sections 86(1.1) and (1.2). These provisions essentially make lessees vicariously liable for persons living with them as members of the family and persons who acquire possession of the motor vehicle with their consent. Section 86(1.3) then limits the liability of lessors to that established under the *Insurance (Vehicle) Act*.

At the same time as the amendments to section 86 were introduced, the *Insurance (Vehicle) Act* was also amended so as to add section 82.1, which provides as follows:

> 82.1 (1) In an action to recover for loss or damage to persons or property arising out of the use or operation of a leased motor vehicle on a highway in British Columbia, the maximum amount for which the lessor of the motor vehicle is liable, in that lessor's capacity as lessor of the motor vehicle, in respect of any one incident is the amount determined under subsection (2).
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> (2) The maximum amount for the purposes of subsection (1) is the greatest of the following amounts:
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> (a) $1 000 000;
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> (b) the amount established, or determined in the manner prescribed, by regulation;
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> (c) the amount of third party liability insurance coverage required by law to be carried in respect of the motor vehicle.
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> (3) Subsection (1) does not apply
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> (a) in respect of amounts payable by a lessor other than by reason of vicarious liability imposed under section 86 of the *Motor Vehicle Act*, or
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> (b) to prescribed lessors or motor vehicles, or prescribed classes of lessors or motor vehicles.
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> (4) This section applies only in relation to loss or damage sustained on or after the date this section comes into force.

What all this means is that lessors are only vicariously liable for $1 million. Lessees are otherwise responsible for damages which may be caused while the vehicle is in their possession. As noted above, sellers under conditional sales agreements are excused entirely.

Note that section 82.1(1) applies to actions for loss or damage to persons or property. This provision should be read with sections 68 and 178 of the *Insurance (Vehicle) Regulation*, which give claims arising out of injury or death priority to the extent of 90% of the available amount. Ontario's legislation, discussed below, applies the limitation on the liability of lessors only to claims arising from bodily injury and death.

The Insurance Issues

This does not seem to change the insurance ramifications, except that lessees and purchasers under conditional sales agreements are well-advised to obtain coverage up to a significant limit and not expect the assets of the lessor or selling company to in any way respond to a catastrophic loss.

Lessors will continue to require that they be named as additional insureds under the motor vehicle insurance put in place by lessees. Likewise, sellers under conditional sales agreements will also continue to demand that they be named in the purchasers' motor vehicle policies as additional insureds, although liability does not flow to such sellers. Keep in mind that lessors and sellers will want protection under the applicable collision and comprehensive coverage, as well as the liability coverage.

The odd part is that, if the lessor is named as an additional insured under the lessee's insurance policy and the lessee only obtains $1 million coverage, the $1 million coverage, once exhausted, will be all that there is to respond to the loss. The lessor will not otherwise be responsible. The lessee's own assets will then become exposed. In other words, the $1 million limit which lessors may take advantage of is not in addition to or intended to supplement whatever insurance coverage is obtained by a lessee.

This outcome appears to have been contemplated by the Minister when the Bill was debated. The Minister explained that the outcome with a leased vehicle should be no different that if the vehicle were owned outright and, in both instances, injured parties have recourse to the uninsured motorist protection plan.

This situation is not that different from what prevails in Ontario, although the Ontario legislation is somewhat more straightforward, where section 267.12 of the *Insurance Act* provides as follows:

> **267.12** (1) Despite any other provision in this Part, except subsections (4) and (5), in an action in Ontario for loss or damage from bodily injury or death arising directly or indirectly from the use or operation of a motor vehicle that is leased, the maximum amount for which the lessor or lessors of the motor vehicle are liable in respect of the same incident in their capacity as lessors of the motor vehicle is the amount determined under subsection (3) less any amounts,
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> (a) that are recovered for loss or damage from bodily injury or death under the third party liability provisions of contracts evidenced by motor vehicle liability policies issued to persons other than a lessor;
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> (b) that are in respect of the use or operation of the motor vehicle; and
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> (c) that are in respect of the same incident. 2005, c. 31, Sched. 12, s. 4.
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> (2) For the purposes of subsection (1), the amounts referred to in clauses (1) (a), (b) and (c) include only amounts recovered under the coverages referred to in subsections 239 (1) and (3) and section 241 and exclude,

(a) any sum referred to in subsection 265 (1);

(b) any amount payable as damages by the Motor Vehicle Accident Claims Fund under the *Motor Vehicle Accident Claims Act*; and

(c) any other amounts determined in the manner prescribed by the regulations. 2005, c. 31, Sched. 12, s. 4.

Maximum amount

(3) The maximum amount for the purposes of subsection (1) is the greatest of,

(a) $1,000,000;

(b) the amount of third party liability insurance required by law to be carried in respect of the motor vehicle; and

(c) the amount determined in the manner prescribed by the regulations, if regulations are made prescribing the manner for determining an amount for the purposes of this clause. 2005, c. 31, Sched. 12, s. 4.

Exceptions

(4) Subsection (1) does not apply,

(a) in such circumstances as may be prescribed by the regulations or to such persons, classes of persons, motor vehicles or classes of motor vehicles as may be prescribed in the regulations, subject to such terms, conditions, provisions, exclusions and limits as may be prescribed by the regulations;

(b) in respect of amounts payable by a lessor other than by reason of the vicarious liability imposed under section 192 of the *Highway Traffic Act*; or

(c) in respect of a motor vehicle used as a taxicab, livery vehicle or limousine for hire. 2005, c. 31, Sched. 12, s. 4.

Application of subs. (1)

(5) Subsection (1) applies only to proceedings for loss or damage from bodily injury or death arising from the use or operation of a motor vehicle on or after the day this section comes into force. 2005, c. 31, Sched. 12, s. 4.

Definitions

(6) In this section,

"lessor" means, in respect of a motor vehicle, a person who is leasing or renting the motor vehicle to another person for any period of time, and "leased" has a corresponding meaning; ("bailleur")

"motor vehicle" has the same meaning as in subsection 1 (1) of the *Highway Traffic Act*. ("véhicule automobile") 2005, c. 31, Sched. 12, s. 4.

What this means is that the $1 million liability of the lessor is less any amounts available under motor vehicle policies that are available to cover the loss.

The Ontario legislation is not without its problems, however. Because the usual practice requires lessees to name lessors as additional insureds in the lessee's policies, such policies are not, under section 267.12(1)(a), "policies issued to persons other than a lessor". Thus, the amount available under these policies cannot be subtracted and lessors must still contribute $1 million. Steps have been taken to amend the policies so that such policies are deemed not to have been issued to the lessor. The British Columbia legislation does not create such an issue.

The parties that will now have difficulty are severely injured plaintiffs who were at one time able to go after significant assets of a lessor or a seller under a conditional sales agreement. Those assets will no longer be there to be realized upon. Instead, it will be the assets of the party in possession, usually owners without any significant assets of their own.

Short term rentals present interesting issues. Most British Columbians renting vehicles will have the basic $200,000 liability coverage under an owner's certificate plus optional insurance, usually up to $1 million or more. Where an accident occurs this insurance would not respond on behalf of the lessor, because the lessor is not named as an additional insured. However, lessors usually require that short term lessees purchase additional liability insurance naming the lessor as an additional insured. Note that a British Columbia driver covered only under a driver's certificate, and not an owner's certificate, will have only $200,000 liability coverage in which case lessors are well advised to have the driver purchase additional insurance in conjunction with the rental. Otherwise, the lessor's own policy must respond up to the $1 million limit.

Umbrella insurance obtained by lessors may also require consideration since these policies may name drivers of the leased vehicles as additional insureds. Where this occurs, lessors may have their own liability limited, but find that drivers are turning to the lessors' policies for coverage.

Potential Conflicts in the Insurance Context

Lessors, as well as sellers under conditional sales agreements, require an indemnity in their contracts with lessees and purchasers. Thus, if lessors or sellers pay out pursuant to a loss, the lessors or sellers may bring a claim against the lessees and purchasers.

Potential conflicts are a concern for insurers under the existing regime where the claim by an injured third party has the potential to exceed the policy limits. Thus, separate defences may be owed to a lessor and lessee, for example, given the potential claim over by the lessor.

Under the new regime this potential conflict disappears so long as the lessee or purchaser has obtained at least $1 million liability coverage. Sellers under conditional sales agreements are not owners. Lessors' liability is capped at the $1 million available under the applicable policy and there will be no claim back against the lessee.

Conclusion

The new regime will limit the liability of lessors, as well as the liability of sellers under conditional sales agreements. This will be a benefit to the leasing industry in British Columbia and industries such as tourism.

However, lessees in particular are well advised to obtain sufficient third party liability insurance to cover them in the event of a catastrophic loss. Injured third parties will no longer be able to look to the assets of leasing companies for recovery and will be forced to recover what they can from the assets of the lessee. Insurers, so long as there is at least $1 million coverage, need not be concerned about conflicts between named insureds (lessees) and additional (lessors), but may need to educate their insureds about the consequences of catastrophic losses.

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CWA32757.1