Assurances

Assurances

Insuring Conflicts on the Construction Site

Eric A. Dolden

Volume 59, numéro 3, 1991

URI : https://id.erudit.org/iderudit/1104851ar
DOI : https://doi.org/10.7202/1104851ar

Aller au sommaire du numéro

Éditeur(s)

HEC Montréal

ISSN

0004-6027 (imprimé)
2817-3465 (numérique)

Découvrir la revue

Citer ce document

Dolden, E. (1991). Insuring Conflicts on the Construction Site. *Assurances*, *59*(3), 377–402. https://doi.org/10.7202/1104851ar

Résumé de l'article

Le but de cet article est d'examiner les plus récents développements en matière d'assurance construction. Une couverture globale et adaptée aux besoins exige les efforts et la maîtrise de différentes disciplines, notamment dans les domaines juridique et technique. L'auteur tente de démontrer comment le milieu de l'assurance peut répondre aux problèmes les plus particularisés par une analyse exhaustive des principales clauses et conditions en vertu de l'assurance des biens et de l'assurance des responsabilités.

Insuring Conflicts on the Construction Site*

by

Eric A. Dolden..

Le but de cet article est d'examiner les plus récents développements en matière d'assurance construction. Une couverture globale et adaptée aux besoins exige les efforts et la maîtrise de différentes disciplines, notamment dans les domaines juridique et technique. L'auteur tente de démontrer comment le milieu de l'assurance peut répondre aux problèmes les plus particularisés par une analyse exhaustive des principales clauses et conditions en vertu de l'assurance des biens et de l'assurance des responsabilités.

~

PART ONE

Introduction

Ensuring adequate insurance coverage for a construction project is a complex task. The insurance industry has traditionally treated property, liability and errors and omissions. policies as responding to well defined and mutually exclusive risks which inherently assumed that a loss triggers only one policy coverage to the exclusion of ail other coverages. The reality of modern construction techniques does not dictate that result. Participants in the construction site are engaged in a diverse range of activities which can result in, on the one hand a loss of traditional insurance protection and, on the other hand claims for which more than one policy must respond.

The past decade has witnessed the emergence of contractors increasingly engaged in design fonctions traditionally handled exclusively by design professionals. This amalgam of fonctions has

---

•This article was prepared for an insurance seminar sponsored by the Insurance Insùtute of Briùsh Columbia on May 2, 1991, in Vancouver, B.C.

..Partner with the Vancouver law firm Freeman and Company.

raised difficult issues as to the nature and extent of the CGL's obligation to respond to claims resulting from a failure to properly provide professional services. Equally, the Broad Form Property Endorsement, intended by the industry to ameliorate the hardship resulting from construction losses not within the insured's control, is viewed by contractors as a type of first party property insurance that provides indemnity for the loss of the contractor's own work. The role of the CGL has been further constrained by industry wordings, including the CCDC Form 101, which, to a degree not evident in more traditional IBC wordings, indemnifies for contractual claims previously regarded as "business risks" outside the scope of liability insurance.

Within the realm of property policies the courts have been vigorous in the adoption of a "discoverability rule" in calculating the commencement of a statutory or contractual limitation period. That trend has meant that property policies issued for construction risks have the potential for "long tail" claims more customary to the liability policy.

The collective impact of these developments has had a discernible impact on the insurance industry's potential for claims on the construction site, including:

(a) greater potential for indemnity on lasses traditionally considered "business risks";

(b) an increased likelihood that two or more differing policies must respond to a loss;

(c) the increased likelihood that insurers will, through the contractual arrangements entered into by the construction site participants, seek to shift responsibility from one form of coverage to another in the event of loss.

The purpose of this paper is to examine recent judicial and industry developments, in both Canada and the United States, and in so doing, identify the most probable role each type of policy will play in the 1990s.

Property

A. The Scope of Statutory Condition #14 for Construction Losses and the Impact of the "Discoverability" Rule for Latent Defects

1. The Appropriate Limitation Period for Property Losses on the Construction Site

Within the insurance industry many have debated whether a Builders' All Risk policy is govemed by Part 6 *ofthelnsurance Act, R.SB.C.* The industry's concem focuses not on the broad application of Part 6, but rather, whether the statutory limitation period contained within Part 6 serves as a device of limitation that circumscribes the time within which a claim under a Builders' Ail Risk may be made.

Statutory Condition #14, unlike the more general limitation period contained in Section 24(1) of the *Insurance Act, R.S.B.C.* inherently restricts the time for the bringing of an action. Statutory Condition #14, unlike Section 24(1), is not dependent upon the fumishing of a proof of loss. It is instructive to examine the wording of the two provisions:

> Statutory Condition #14
>
> Every action or proceeding against the insurer for the recovery of any claim under or by virtue of this contract shall be absolutely barred unless commenced within one year next after toe loss or damage occurs.
>
> Section 24(1)
>
> Every action on a contract shall be commenced within one year after the furnishing of reasonably sufficient proof of loss or claim under the contract and not after.

The insurer's ability to rely upon Statutory Condition #14 in answer to first party property losses on the construction site can serve as a useful device in limiting the potentially "long tail" claims experience more typically associated with liability claims.

Part 6 of the British Columbia *Insurance Act, R.S.B.C.* is unique, being worded in a manner unlike its Ontario counterpart. In British Columbia, there are two relevant statutory provisions:

s. 1 *Pire insurance* means "insurance against loss of or damage to the property insured caused by fire, lightning, or explosion due to ignition."

Part 6 - Fire insurance

s. 213 This Part applies to insurers carrying on the business of fire insurance *and to contracts of/ire insurance,* whether or not a contract includes insurance against other risks as well as the risks included in the expression 'fire insurance' as defined by this Act, except:

(c) where the peril of fire is an *incidental peril* to the coverage provided;

[Emphasis added}

If the Builders' Ali Risk does not subordinate the peril of fire to an incidental risk the insurer can rely upon Statutory Condition #14.

Until January, 1991, there had existed a line of legal authorities within British Columbia which would suggest that the Builders' All Risk fell within Part 6 of the *Insurance Act,* and as a consequence the insurer could rely upon Statutory Condition #14.[1] These decisions tended to examine the range of perils being insured and then sought to determine whether the peril of fire was incidental to a perceived primary peril.

In recent decisions issued by the Court of Appeal of British Columbia, *Dressew Supply Ltd. v. Laurentian Pacifie Insurance Company* and *Elite Insurance Company*[2] and *Mindel/ v. Canadian Northern Shield Insurance Company*[3] the Court made clear this earlier approach was misconceived. In determining whether Statutory Condition #14 ought to apply to the policy the insurer must examine the whole of the descriptive package being provided in the policy to

---

[1] ***Briggs and Kolosoffv. B.C.A.A. Insurance Company*** (1989), 38 B.C.L.R. (2d) 303.

2(CA010268, January 22, 1991).

3(CA01186112, January 22, 1991).

determine whether each of the cc-extensive risks is incidental to the coverage provided in the contract as a whole.

In the case of a Builders' All Risk policy, in which fire is only one of the many defined risks, the exception to Part 6 will prevail (Section 213(c)) and as a consequence the policy is not subject to Statutory Condition #14. The insured's right to recover upon the policy will be limited only by Section 24(1) of the *Insurance Act, R.S.B.C.*

Contemplating that result, the CCDC Form 101 imposes, as a matter of contract, the limitation period contained in Statutory Condition #14. This is done by means of the following language:

> CONDITIONS
>
> The Statutory Conditions apply as Policy Conditions to the peril of fire and to ail other perils insured by this policy, except as modified or supplemented in this Policy or by riders or endorsements attached.
>
> STATUTORY CONDIDONS
>
> 14. Action
>
> Every action or proceeding against the Insurer for the recovery of any claim under or by virtue of this contract is absolutely barred unless commenced within one year next after the loss or damage occurs.

Many insurers question whether the language of Statutory Condition #14, imposed in an All Risk policy, is an effective limitation period as is the statutory provision. It will be effective only if the insurer can demonstrate that the insured in fact received a copy of the policy wording and had knowledge of the limitation clause. If the insurer cannot demonstrate that the policy wording, including the language of the limitation period, bas been delivered to the insured, then it is not open to the insurer to rely upon that condition. In those circumstances the insured would be limited only by the general limitation period contained in Section 24(1) of the *Insurance Act, R.S.B.C.*

The problem is vividly illustrated by the decision of the Manitoba Court of Appeal in *Canadian Imperia[Bank of Commerce*

v. Nickolievich and Canadian Home Insurance Company.[4] The insurer sought to rely upon a contractual limitation period to bar a daim following the loss of a residential home by wind storm. The insurer argued that by having incorporated, as a matter of policy wording, the statutory condition, the insured was still bound by the limitation period contained in Statutory Condition #14. The court concluded that the policy had not in fact been physically delivered to the insured and so the insurer could not take the position that it formed a term of the contract. The insured had neither agreed to the term nor been aware of its existence.

382

The comments of Sullivan, J.A., at page 400, are revealing:

> What happened is that [the insured], who was about to be married, applied to an insurance agent for insurance against "fire and miscellaneous perils." His application was made on 7 June. The loss occurred during a tomado on 7 July 1973. The premium was paid on 30 June 1973. The policy was delivered on 9 July 1973.
>
> [The insured] moved into his mobile home after his wedding in the confidence that the home was insured against fire and miscellaneous perils. The insurance agent assured him that was so. The insurance company has ratified the acts of the agent and does not dispute that insurance cover for wind storm ran from 7 June 1973.
>
> Under the special circumstances of this case, I am of the view that [the insured] cannot be held bound by a contractual condition to which he did not agree and of which he had neither knowledge nor means of knowledge. What the situation would have been had the policy been delivered before the loss, it is not necessary to consider in this case.5

2. The Operation of the Limitation Period for Latent Defects

The more fondamental issue is determining whether the statutory or contractual limitation period on a Builders' All Risk necessarily begins to operate from the date the loss arose. That is critical as many first party property losses which arise on the construction

4 (1977), 5 W.W.R. 397.

5 Supra at page 400.

site pursuant to an All Risk policy are not capable of being detected until months or even years following substantial completion of the project.

Assuming the insured leams that a latent defect has manifested into physical damage more than one year following substantial completion, can the insurer rely upon Statutory Condition #14 or its equivalent contractual wording and contend that the limitation period began to operate from the date that defective work was performed? That issue arose squarely for consideration in *Royal Insurance Company of Canada v. Callaghan Contracting Ltd.*[6] The case makes clear that the one-year limitation provided for in Statutory Condition #14, or its contractual equivalent, does not begin to operate until the insured has sufficient facts upon which he or she knew or ought to have known that there was a loss. That rule requires that the insured appreciate both (a) the nature of the claim, and (b) the amount of the claim.

The facts in *Callaghan Contracting Ltd. (supra)* are deserving of mention. The insured was hired by the Moncton Sewage Commission to install a sewer system. The insured's work was completed in September, 1984, at which time the system was sealed awaiting completion of the master system into which the insured's work would be connected. To seal the system the insured had placed a plywood cover over the manhole as a cap and had the manhole backfüled. The cap fractured between the date the insured completed its work and the date of its discovery causing a quantity of earth to enter the sewer pipes blocking the collector sewer system. Only in 1987, when the Sewage Commission leamed of the defects, was the insured notified and a claim made. The insurer resisted payment of the claim relying upon the language of Statutory Condition #14.

The insurer had issued an All Risk policy during the period of initial construction. Not unlike most Builders' All Risk policies the policy contained a limitation clause which was identical to Clause 14 of the CCDC Form 101:

> Every action or proceeding against the insurer for the recovery of any claim under or by virtue of this contract is absolutely

[6] 1989] I.L.R. 1-2491.

barred unless commenced within one year next after the loss or damage occurs.

The New Brunswick Court of Appeal concluded that the claim was not time-barred. In reaching that conclusion the Court outlined the separate but related changes occurring in other fields of the law that affected the operation of the limitation clause. These changes included:

1. the willingness of the Supreme Court of Canada to treat a cause of action in tort as arising when the material facts on which it is
384 based have been discovered or ought to have been discovered by the exercise of reasonable diligence;
2. the view of the Ontario Court of Appeal, in 1985, that this principle extended to a claim in contract;
3. the view of the Court that when an insurer utilizes the word *occurs* in a policy of insurance it means "not only must the damage have happened, but it must have been found";
4. the view of the Alberta Court of Appeal that when dealing with contracts of indemnity the limitation period does not begin to run until the discovery of the loss.

The insurer sought to have the decision of the Court of Appeal reviewed by the Supreme Court of Canada. Leave to appeal was denied on January 18, 1990. From the court's refusal to hear the case one might draw the inference that the country's highest court regarded the approach of the Court of Appeal as being correct.

The decision in *Callaghan Contracting (supra)* has profound implications for losses arising on the construction site. Typically, if the contractor's work manifests into a loss following occupation of newly constructed premises, the owner has tended to make claim on its commercial broad form policy. These policies frequently use an "AU Risk" wording. Most commercial insureds do not make claim on the course of construction coverage even though, based on the decision in *Callaghan Contracting (supra),* the time for making claim is in effect "suspended" until the owner appreciates both the fact of a claim and the amount of that claim.

The "discoverability rule" sanctioned in *Callaghan Contracting (supra)* was not intended to provide relief for insureds who, during

the currency of the one-year limitation period, appreciate the existence of a claim and remain willfully blind to both its reality and the corresponding need to submit a proof of loss. The Court's decision makes clear that if an insured ought reasonably to appreciate that there exists the basis for a claim then the "discoverability" rule does not arise. An example might include a contractor which, on the date of substantial completion, fails to appreciate that there has been a claim, but is apprised of facts three months following substantial completion that would reasonably lead it to believe that a claim has arisen. Should the contractor not give notice of a claim until 13 months following substantial completion the contractor should not be able to successfully invoke the "discoverability rule" to argue that the one-year limitation period commenced 13 months following substantial completion. In those circumstances the court should presumably conclude that knowledge of the claim, gained within the 12-month period, constituted actual knowledge such that the limitation period is treated as having arisen from the date the knowledge or basis for the knowledge was present.

Despite the common sense of that approach at least one decision, rendered in the aftermath of *Callaghan Contracting (supra),* suggests a contrary result. In *Gibraltar General Insurance Company v. L.E. Yingst Co. Ltd,* an unreported decision of the Saskatchewan Queen's Bench,[7] the Court held that the contractual limitation period of one year contained in a Builders' Ail Risk policy did not commence until the insured/owner obtained judgment against the general contractor. This conclusion was reached notwithstanding that the insured appreciated, within the 12 months following the loss, that in fact there existed a claim. The Court placed considerable emphasis on the fact that the "discoverability rule" presupposes that the insured has both knowledge of the nature of the claim and *the amount of the claim.* In effect, the trial judge was of the view that until the claim had been adjudged in the context of a tort lawsuit the 12-month limitation period provided for in the Builders' All Risk policy did not begin to operate.

In the writer's view this case was wrongly decided. The loss arose upon the date of its occurrence and not when liability in the related tort lawsuit was assessed. The insured clearly appreciated the

7[1991] I.L.R. 1-2687.

existence of a loss upon its occurrence. In no sense could it be said that the loss was not apparent. *Callaghan Contracting (supra)* was only intended to introduce an element of fairness in situations wherein the insured did not know, and had no reasonable basis for believing, that a loss had occurred. To that extent the decision in *L.E. Yingst Co. Ltd. (supra)* constitutes an unwarranted extension of the principle in *Callaghan Contracting (supra).*

B. Limits on Subrogation - Unnamed Insureds and Tradesmen that Contribute Labour and Materials to the Construction Site

386

Historical limitations on the doctrine of subrogation have had a significant impact on an insurer's ability to maintain subrogated proceedings following a loss on an All Risk policy. Those limitations result from two factors:

(i) common law ("judge-made") rules; and

(ii) customary language in All Risk policies.

The impact of these limitations is particularly pronounced in the construction setting when the parties have obtained Builders' All Risk coverage.

1. Limitations Imposed by Common Law

It has long been recognized that an insurer cannot, through subrogation, be indemnified by its insured. That principle has been extended to both the named insured and any unnamed insured. Typically, in a Builders' All Risk policy both the owner and the general contractor will be expressly included as insureds. So, for example, the All Risk insurer, having paid the loss, cannot, in the name of the owner, maintain subrogated proceedings against the general contractor alleging that the latter's fault caused the loss.[8] The unnamed insured is similarly protected if identified as being within a class of persons intended to be protected. An example would be a description of the *Named Insured* as "ABC Holdings Ltd., John

---

[8] *Lester Archibald Pu/Ling & Blasting Ltd. et al v. Commucial Union Assurance Co. Of Canada* (1987), C.C.L.1. 145.

Smith Contracting Ltd. and all-subcontractors carrying on work in respect of the project."

In *Commonwealth Construction Co. Ltd. v. lmperial* Oil *Ltd. et* a/9 the Supreme Court of Canada stated that unnamed insureds of this description are protected from subrogated proceedings. This results from the unique structure of a Builders' All Risk policy. By its very terms, the AU Risk policy contemplates that any person who supplies labour or material to the construction project has an insurable interest in the project to the extent of that tradesman's contribution.

Accepting this principle, an interesting question arises as to whether, in the context of an All Risk policy, the insurer can maintain subrogated proceedings against contractors, subcontractors, suppliers or tradesmen that are neither named as an insured nor incorporated by reference as an unnamed insured.

It is instructive to examine what the Builders' AU Risk insures. IBC Form 51208 (Builders' Risk Broad Form) states:

> Property Insured
>
> This poliey, except as herein provided, insures
>
> (a) buildings, structures, foundations, piers or other supports, *building materials and supplies*
>
> (l) owned by the Insured;
>
> (II) *owned by others,*
>
> provided that the value of such property is included in the amount insured;
>
> all to enter into and form part of the completed project including expendable materials and supplies not otherwise excluded, necessary to complete the project.
>
> *[Emphasis added]*

These words make it clear that persons who supply materials for the construction of the project are intended to have an insurable interest in the subject matter of the policy. In this respect All Risk

9(1977), 69 D.L.R. (3d) 559.

coverage is unique from other types of property insurance. The range of insureds extends not merely to those owning the land and building but also to other persans who contribute to its construction. All Risk policies give effect to that intent, firstly, by limiting the owner's subrogation rights against the class of person supplying materials and, secondly, by prohibiting subrogation of such claims as may exist between those who fall within the class of protected persans (an example being subrogated proceedings by the general contractor against the subcontractor).

388 As the Supreme Court of Canada stated in *Commonwealth Construction Ltd. (supra):*

> On any construction site, and especially when the building being erected is a complex chemical plant, there is ever present the possibility of damage by one tradesman to the property of another and to the construction as a whole. Should this possibility become reality, the question of negligence in the absence of complete property coverage would have to be debated in Court. By recognizing in ail tradesmen an insurable interest based on that very real possibility, which itself has its source in the contractual arrangements opening doors of the job site to the tradesmen, the Courts would apply to the construction field the principle expressed so long ago in the area of bailment. Thus all the parties whose joint efforts have one common goal, e.g., the completion of the construction, would be spared the necessity of fighting between themselves should an accident occur involving the possible responsibility of one of them. [10]

So, for example, in *Commonwealth Construction (supra)* the Court concluded that a subcontractor had an insurable interest in the project which extended to the entire works, and consequently, that the insurer had no right to subrogate against that subcontractor notwithstanding the latter's culpable behavior.

2. Limitations Imposed by Customary Terms

The insurance industry, by utilizing standard policy wordings, has effectively placed additional limits on subrogation. Customarily an All Risk policy will contain a waiver of subrogation which

10Supra at page 562.

extends beyond the parties to the insuring arrangements. IBC Form 51208 provides:

> The Insurer(s), upon making any payment or assuming liability therefor under this Policy, shail be subrogated to ail rights of recovery of the insured against others and may bring action in the name of the insured to enforce such rights, except that:
>
> (a) any release from liability entered into by the insured prior to loss shail not affect the right of the insured to recover;
>
> (b) *notwithstanding the provisions ofparagraph (a) hereofail rights of subrogation are hereby waived against any corporation,firm, individual, or other interest with respect to which insurance is provided by this Policy.*
>
> *[Emphasis added]*

To like effect at least one manuscript wording commonly used in Western Canada provides:

> Upon the payment of any claim under this Policy the insurers shail be subrogated to ail the rights and remedies of the insured arising out of such claim against any persan or corporation whatsoever... It is further understood and agreed that the insurers on paying a loss, hereby waive their right to a transfer of such rights:
>
> (a) Of any Insured(s) named herein against any other insured named herein by whose fault or negligence the loss or damage was caused;
>
> (b) *Of the Insured(s) against any Subcontractor (including their directors, officers, employees, servants or agents) engaged in performing the work herein, by whosefault or negligence the loss or damage was caused;"*
>
> *[Emphasis added]*

The waiver of subrogation provision, read with the provision which insures material supplied to the subject matter of the contract, has led the courts to conclude that this immunity from subrogation should be extended to anyone who supplies materials to the job site. This is so even if the parties to the All Risk policy had not actually intended to include these suppliers as unnamed insureds.

This is illustrated by the decision of the Alberta Court of Queen's Bench in *Timcon Construction Ltd. v. Riddle, McCann, Rattenbury Associates Ltd., Rattenbury and Halifax Insurance Company.*[11] The general contractor had been hired to construct a condominium project and obtained a Builders' All Risk policy. During construction a fire occurred and an action was commenced by the insurer, alleging that a subcontractor on the job was at fault in having caused the fire. The evidence was clear that it had not been the intent of either the owner or the contractor that the subcontractor constitute either a named or an unnamed insured under the policy.

390

Nonetheless, the insurer was barred from maintaining the action. Mr. Justice Foisey, after reviewing the nature of the coverage under a Builders' All Risk policy, including the waiver of subrogation clause, described some of the evidence at trial as follows:

> While it is always the fonction of the court to interpret contracts, it is nonetheless interesting to note that Rattenbury and Rambaut, both persans who have a great deal of experience in the insurance business and particularly in the builders' risk area, and Power, a highly qualified expert in the field of insurance, were collectively of the view that the builders' risk broad form contained in the policy covered all those connected with the project in question that were not named insureds and it was their view that the interpretation being placed on this form by the industry was of a like effect.12

His Lordship also cited supporting American authority, including *General Insurance Co. of America v. Stoddard Wendle Ford Motors,* which held:

> The courts have consistently held, in the builder's risk cases, that the lnsurance company - having paid a loss to one Insured cannot, as subrogee, recover from another of the parties for whose benefit the insurance was written even though his negligence may have occasioned the loss, there being no design or fraud on his part.13

---

11 (1981) A.L.R. 134.
12 S*upra* **at page** 139.
13 410 P2d 904 (1966).

3. The Scope of any Limitations Imposed by Customary Terms

To gain a "tort immunity" the nature of the activities undertaken by the wrongdoer must be integral to the construction of the project. If the nature of the service can be characterized as "collateral" to the mainstream of the construction process the wrongdoer does not attract the benefit of "tort immunity."

In *Canadian Pacifie Ltd.* v. *Base-Fort Security Services (B.C.) et al,* [14] a decision of the British Columbia Court of Appeal, issued January 3, 1991, a security firm had provided security guard services at the construction site. The issue was whether the security guard service could avail itself of the "tort immunity" principle.

In July, 1982, the named insured had obtained a Builders' All Risk policy that insured the work on the Rogers Pass project and, subsequently, let a contract for the construction of a camp necessary for the Rogers Pass project. Under that contract, the named insured was obligated to provide All Risk and CGL coverage insuring the interest of the named insured, the contractors and subcontractors. The named insured entered into a second contract with Base-Fort Security Services (hereinafter "Base-Fort") for the provision of security services to the Rogers camp.

In the Builders' All Risk policy *insured* was defined so as to include:

> Canadian Pacifie Limited and its wholly owned subsidiaries and/or controlled companies as may now or hereafter be constituted, architects and/or engineers and/or consultants and/or general contractors and/or subcontractors and their various tractes.

A loss arose and the named insured commenced legal action against Base-Fort. Base-Fort brought a preliminary application to determine whether it had the benefit of the "tort immunity" principle. In allowing the action to continue Mr. Justice Hollinrake made clear that the term *contractors* as used in the definition of *insured* was limited to those parties integral to the construction process itself and only to those who can be said to be within the "mainstream" of the

[14] 52 B.C.L.R. (2d) 393.

construction activities at the site. If the parties' activities merely ran "parallel" to but were not necessary to the construction process itself, that party is outside the scope of *contractors* as that expression is used in the definition of *insured.* Mr. Justice Hollinrak:e stated:

> I conclude that those persons whose contributions are an integral and necessary part of the construction process itself are within the definition of /*nsured* in the poliey and not those whose contributions are collateral to that process.... That appellant Base-Fort contracted with Canadian Pacifie "to provide security inspection as well as such other security services as Canadian Pacifie Limited from time to time requires...." *White it can be said that the services of Base-Fort under contract with the owner ran para/le/ to the project, those services cannot be said to be an integral and necessary part of the construction process itself. In my opinion those services were no more than collateral to the construction process, and that being so, Base-Fort was not an "insured" within the insuring agreement.* [15]
>
> *[Emphasis added]*

Notwithstanding this result, it is clear that the modem trend has been to limit the subrogation rights of the All Risk insurer and to extend an immunity to the class of persans who supply materials to the subject matter of the policy, whether or not the party procuring the policy intended to include them as unnamed insureds.

In summary, the courts have clearly signalled that a property insurer having issued an All Risk policy cannot maintain a subrogated claim against a sub-trade if the latter contributed materials or labour to the project and the policy contains a waiver of subrogation clause. The underlying theory is that the parties to the construction project, having expressly agreed that one of the parties must obtain a Builders' AU Risk, have also implicitly agreed that in the event of a loss all of the parties would look to the Builders' AU Risk as the sole remedy in the event of loss and would not, as between themselves, seek to shift that loss. The insurer is bound by this implied agree-

---

[15] *Supra* at page 400.

ment and is therefore unable to use subrogated proceedings to shift the loss to one or more of these parties.

Liabillty

C. The Contractor that Utilizes a Professional

The construction site is characterized by the risk of legal liability. Placing the owner, contractor, subcontractors, suppliers and consultants in close proximity to each other for a fixed period under pre-determined economic parameters is likely to result in loss or damage resulting in legal liability. For that reason the nature and scope of any liability coverage is of critical concern.

Legal liability for losses arising on the construction site falls within one of two distinct types of liability insurance - a Comprehensive General Liability policy (hereafter the "CGL") or, in the case of the engineer and architect, an Errors and Omissions policy (hereafter the "E & O"). The CGL is intended to indemnify should the operations or work of the contractor cause bodily injury or property damage to persons or property not associated with the construction project.

In contrast to the CGL, the E & 0 is restricted to a specific type of legal liability for a class of specific professionals. The E & 0 is triggered by the more exacting mechanism of a *daim* as opposed to an *occurrence.* The E & 0 indemnifies against the risk of legal liability in the delivery of professional services and extends beyond the professional's client to all persons who are darnaged by the design professional's fault. With an E & 0 policy there is no requirement of physical damage or bodily injury to trigger coverage, as exists with the CGL.

Despite these apparent distinctions it is unclear to many to what extent the CGL serves to provide a legal defence and indemnity to the insured in circumstances involving the insured's performance of professional services. That question frequently arises as the engineer or architect will, on many construction projects, be added as either a named or unnamed insured to the contractor's CGL.

Most design professionals assume that there exists little or no scope for indemnity in the context of a CGL policy by reason of the

"professional services" exclusion. For example, the 1982 CCDC Form 101 wording provides:

> This insurance does not apply to:
>
> (d) bodily injury to or property damage arising out of any professional services performed by or for the Named Insured, including:
>
> (i) the preparation or approval of maps, plans, opinions, reports, surveys, designs or specifications, or
>
> (ii) supervisory, inspection, architectural or engineering services.

394

Historically, even in the absence of any "professional liability exclusion," the CGL did not provide indemnity for loss or damage arising by reason of the provision of professional services. In *Foundation of Canada Engineering v. Canadian Indemnity* Co.,[16] a decision of the Supreme Court of Canada, an issue arose as to whether the general contractor's failure to properly supervise the project could allow for indemnity. The policy did not contain a "professional liability" exclusion. In a statement which has proved persuasive in subsequent decisions Mr. Justice de Grandpre stated:

> Without attempting to cast a mould meant to shape all future possibilities, it must be noted that historically a public liability policy is a contract insuring the general responsibility in tort of the insured to the world at large. It is sufficient here to recall that for many years policies of that type were limited to accidenta! events and clearly kept outside of the coverage all claims resulting from contractual arrangements. Admittedly, this concept has been broadened over the years as appears from toe insuring agreement in the case at bar which refers to occurrence as well as to accident and which refers also to liability assumed by contract as well as to liability imposed by law. *The question is: Does the insurance protection under examination here extend to the consequences of professional negligence... ? As already stated, the answer, in my view, must be in the negative.17*

16(1978] 1 S.C.R. 84.

17*Supra* at page 91.

[Emphasis added]

While the CGL does not require a professional services exclusion to bar that liability which should, in principle, be provided for by means of an E & 0, the issue is complicated by the courts' continued reluctance to treat many professional responsibilities as falling within the scope of the "professional services" exclusion. This willingness to narrow the operation of the exclusion has meant that the CGL does provide indemnity in a range of circumstances that would ordinarily be treated as falling within the purview of an E & 0 policy.

Prior to the advent of the standard IBC wordings it was not uncommon for there to exist some variation in the wording of the "professional liability" exclusion. In the interpretation of these early wordings insurers were unsuccessful in their reliance upon the exclusion unless there was proof both that the loss arose out of the provision of truly professional services and, secondly, that the services in question were undertaken by a professional purporting to act in that capacity. Representative of this approach is *Tested Truss Systems Inc. v. Canadian Indemnity Co.,* [18] a decision of the Alberta Supreme Court Appellate Division. The source for the general contractor's liability was the improper preparation of drawings for roof trusses. The policy simply purported to exclude coverage as follows:

> Coverage given by this policy does not apply to: ... The rendering of professional services or the omission thereof...

The trial judge, having reviewed that clause, stated:

> It is to be inferred from the agreed statement of facts and the arguments that the [insured] merely prepared and supplied design drawings for the roof of the building in question. It was apparently neither employed nor under any duty to supervise or be on the job. There was no evidence before me that it was either a professional architect or engineer. [19]

18(1974) 2 W.W.R. 288, affirming (1973) 4 W.W.R. 542.

19Supra at page 564.

Without a finding that professional services were being undertaken by either an architect or engineer the Court was not prepared to invoke the exclusion. The Appellate Division agreed.

Since the decision in *Tested Truss Systems Inc. (supra)* many insurers have adopted a "professional services" exclusion modelled upon the 1982 CCDC Form 101 wording which is intended to eliminate CGL coverage for the professional liability exposure of architects, engineers and surveyors. The Form 101 purports to achieve that result in several ways:

396

1. The exclusion applies to professional services "by or *for* the named insured";
2. The exclusion expressly excludes the liability stemming from the preparation of plans and surveys, as well as supervisory and inspection services;
3. The exclusion uses the very broad expression *any* professional services.

Notwithstanding this wide and embracing language it would seem, in light of the decision in *Chemetics International Ltd. v. Commercial Union Assurance Company of Canada,*[20] that unless the contractor is a professional and the loss arises while the contractor is employed in a professional capacity, indemnity is available under the CGL. Only if the insured represents itself as having a particular expertise, and if the third party hires and relies on the insured to use its expertise to perform a particular task, can the exclusion be successfully invoked. In *Chemetics International Ltd. v. Commercial Union Assurance Company of Canada* the insurer resisted indemnity on the basis of a "professional services" exclusion similar in its scope to the CCDC Form 101, which stated:

> This Policy shall not cover the liability for claims arising out of bodily injury, sickness or disease including death at any time resulting therefrom sustained by any person or persons, nor for damage to or destruction of, or loss of use of property caused directly or indirectly by:
>
> (i) defects in maps, plans, designs or specifications prepared, acquired or used by the Insured;

20(1984), *55* B.C.L.R. 60.

(il) errors or omissions in the rendering of professional services.[21]

The underlying tort liability was founded upon a jury verdict rendered in Virginia. The evidence in the Virginia tort action led to the conclusion that overfilling a water tower had caused a rupture of the roof. The insured's employee had failed to provide proper operating instructions, and in particular, a warning of the risk.

The Court of Appeal concluded that the provision of those instructions did not entail the rendering of professional services as those words are used in the "professional liability" exclusion. It was noteworthy, in the Court's view, that the policy expressly contemplated the very construction contract that was in issue and made clear that the insured would be providing design and engineering services.

In the Court's view the fact that the contractor's services were provided by an engineer was not determinative of the application of the exclusion. That position "mirrors" the approach taken in *Tested Truss Systems (supra).* The insured successfully argued that the professional services exclusion did not entail *all* services performed by a professional, but rather, only those services which *must* be undertaken by a professional. Since the faulty work was capable of being undertaken by an equipment operator or other nonprofessional, the Court was not prepared to treat that activity as amounting to a "professional service." The decision in *Chemetics International Ltd. (supra)* suggests, by necessary extension, that many activities inherent to a contractor's field review would be covered under the CGL.

What is clear from a review of recent decisions is the courts' willingness to recognize that, although the CGL was not intended to indemnify losses attributable to the provision of "professional services," such services are confined to the range of activities which only a consultant can provide during the design stage.

[21] Supra at page 61.

D. The Scope of the CGL if the Property Damage Arising from the Construction Loss Is Continuous and Progressive in Nature

While bodily injury liability admittedly constitutes a risk on the construction site, more typically a construction loss entails property damage and the consequent economic loss. Most CGL forms in use in Canada are written on an *occurrence basis* as opposed to an *accident basis.* Property damage need only be caused by an *occurrence* as opposed to an *accident.*

398

For the insured the advantage of an "occurrence based" policy is that coverage is dependent upon neither the time that notice of a claim is given nor when legal proceedings are commenced. This is so by reason of the definition of the word *occurrence.* The term is often defined as continuous and repeated exposure during the policy period that gives rise to an event that is both sudden and unexpected from the standpoint of the insured. In the IBC 2003 and CCDC Form 101 CGL *property damage* is defined to be that "... which *occurs* during the policy period..." Nowhere is there any definition of the word *occurs.* Only recently have the courts attempted to define when property damage "occurs."

The prevailing rule in cases involving property damage, a rule which is particularly true in the context of a construction loss, is that "property damage occurs" at the time the damage is disccovered, or when it has manifested itself. In recent years, however, some United States courts have examined cases involving "property damage" which is continuous or progressive in nature and results in physical damage years after the work has been completed. Uniformly the judicial response has been to impose responsibility upon:

(a) the insurer that provided coverage when the work was performed;

(b) the insurer who issued coverage following completion of the work and prior to the damage becoming manifest; and

(c) the insurer on risk when the damage became manifest.

This approach has brought with it a measure of uncertainty into the law. The result of this approach can be particularly significant in

construction activities which result in losses arising from unsafe materials. Examples include the "asbestos abatement" lawsuits in which building owners seek compensation from contractors for the removal and replacement of asbestos building materials.

While there exists a dearth of decided authority within Canada, what American authority there is suggests that two rules tend to govern in the context of construction claims:

1. **If** there exists a temporal lapse between the date the defective work was performed by the contractor and the date the harm manifested itself then only the CGL insurer providing indemnity during the policy period when the harm manifested itself is obligated to respond;

2. **If,** however, there is evidence that from the date the defective work was undertaken what occurred was a continuous and progressive pattern of physical damage then all of the CGL insurers that provided indemnity from the period during which the work was undertaken through the period during which the damage continued to manifest itself are obligated to indemnify; and that obligation is treated as being joint and several.

The operation of the first principle is most clearly illustrated by the decision in *Mil/ers Mutual Fire Insurance Co. of Texas v. Ed Bailey, Inc.*[22] of the Idaho Supreme Court. The insured installed polyurethane foam in a potato storage structure. The CGL lapsed and shortly thereafter a fire occurred in the newly constructed storage facility. Suit was brought against the insured. The Idaho Supreme Court concluded that the CGL insurer had no duty to defend.

Relying upon a definition of *occurrence* that entailed "an accident... which results in... property damage..." the Court held that an "accident" within the meaning of a policy insuring against liability, unless otherwise defined, does not occur until damages resulting from an insured act occur. Since the circumstances of the loss entailed a wrongful act which produced no discemible harm for a period of time following construction which then suddenly manifested itself in damage, the time of the accident is treated as being the time that the damage occurred.

22647 P.2d 1249.

The decision in *Ed Bailey (supra)* should be contrasted with the facts in *California Union Insurance Co. v. Landmark Insurance* Co.,[23] to illustrate the operation of the second principle. In *Landmark Insurance Company (supra)* the insured had constructed a swimming pool which was completed on June 18, 1979. The pipes to the swimming pool leaked and saturated the adjacent soil causing the embankment to collapse in the period from July, 1979 to November, 1980. Not until late 1980 was the cause determined. Landmark had issued a CGL which was in force from July 14, 1978 to July 14, 1980, following which Cal Union had afforded the coverage to the contractor.

400

The issues to be considered by the Califomia Court of Appeal were twofold: did this loss consist of one or two occurrences, and secondly, which CGL insurer should be obligated to indemnify for the damage that occurred after August, 1980.

The Court stated that the general rule is that the "occurrence" of an accident is the time when the complaining party is actually damaged, rather than when the wrongful act was committed. That is what occurred in *Ed Bailey Inc. (supra).* The Court of Appeal noted, however, that without exception previously decided cases in the United States involved delays of varying periods of time between the occurrence of the wrongful act and the actual loss. None involved a continuous active force at work between the parameters of those dates, nor did one involve a condition of progressively worsening damage to the property of another. The court, examining the circumstances of the loss, noted that:

> the leakage process was a continuous one and that for the entire period of time the damage was accumulating and becoming progressively more severe.[24]

In this latter situation the Court was constrained to hold that:

> in a "one occurrence" case involving continuous, progressive and deteriorating damage, the carrier in whose policy period the damage first becomes apparent remains on the risk until the damage is finally and totally complete, notwithstanding a policy provision which purports to limit the coverage solely to those

23145 Cal. Ap. 3d 463, 193 Cal. Rptr. 461 (1983).

24Supra **at page** 467.

> accidents/occurrences within the time parameters of the stated policy term.[25]

The second insurer, however, is not relieved of liability in cases involving continuing and progressive damage. Assuming evidence of continuing damage, apportionment between insurers is the rule and both insurers are jointly and severally liable for any amounts which the insurer is obligated to indemnify for.

The scope of this rule can be seen in other construction cases. In *Grou/ Construction Company Inc.* v. *Insurance Company of North America,*[26] a decision of the State of Washington Appeals Court, a general contractor had caused dry rot to develop around a residential home. In the tort litigation it was established that the deterioration of the structure resulted from improper backfilling practices. The dry rot was not discovered until a considerable time following substantial completion. Three separate CGL insurers had issued coverage to the contractor through the material period: one insurer during the period of construction, a second insurer when the dry rot was discovered, and a third insurer between those policy periods. All three insurers refused to defend. In concluding that in fact all three insurers were obligated to defend the Washington court stated:

> Here, the resulting damage was continuous; coverage was properly imposed under the language of [the second and third insurers' policies] even though the initial negligent act took place within the period of [the first insurer's] policy coverage.27

The court went on to add:

> [The insurers] assert that [the contractor] had the burden of proving the amount of damage that occurred within the time limits of each policy. We disagree. In a dispute between an insured who has sustained damages of a continuing nature, and the insurance carriers providing coverage, the burden of apportionment is on the carriers. The question turns upon whether the damage is joint and several. Here, the trial court properly

---

[25] *Supra* at page 469.

[26] 524 P2d 427 (1974).

[27] *Supra* at page 430.

found joint and several liability. The damage, though continuing over a period of time, constituted a single injury.[28]

What is clear from reviewing these decisions is that in the context of a construction loss the spectre of continuing damage, following substantial completion of the work, can cause numerous insurers to indemnify. That obligation is premised on the notion that an "occurrence" can take place over an extended period of rime and in a manner that supersedes stated policy period limitations.

[This article is to be continued in our next issue.}

28Supra at page 431.