

CONSTRUCTION DEFECTS: PROPERTY DAMAGE? ACCIDENT?

The Supreme Court rules

Stein Monast LLP¹ | www.steinmonast.ca



Geneviève Cotnam
Partner | 418 640-4447



Maud Rivard
Associate | 418 640-4423

Summary

In *Progressive Homes Ltd v. Lombard General Insurance Co. of Canada*, a decision rendered last September 23rd, the Supreme Court looked at an insurer's duty to defend its client, a general contractor that had built four buildings and was being sued by the owner for construction defects.

Facts

The owner of the buildings was alleging construction defects in the building shell, which supposedly caused major damage due to water infiltration. In particular, the owner mentioned rot, infestation and general deterioration of the buildings.

Progressive, whose liability insurer, Lombard, had denied it coverage on the ground that this was not a claim for property damage due to an occurrence or an accident under the terms of the policy, had applied to the courts for a declaration that its insurer owed it a duty to defend. The lower courts of British Columbia held that the insurer did not have a duty to defend its insured. The Supreme Court overturned those judgments.

The Supreme Court's decision

The Supreme Court interpreted the policy wording narrowly and applied the basic principle that the unambiguous language of a policy must be interpreted by giving effect to its clear language, reading the contract as a whole. The Court examined the allegations in the suit against Progressive to determine whether it was covered by Lombard's policies, bearing in mind that one must look at the true nature of the claim, not the labels selected by the plaintiff, and that the duty to defend will arise from the mere possibility that the claim falls within the policy, regardless of whether the insured is really liable, or whether the insurer is really obligated to indemnify.

According to the Court, the plain meaning of property damage includes damage to any tangible property, thus rejecting Lombard's argument that the damage has to be caused to third-party property. To the Court, "defective" property, and even a defect, can constitute property damage depending on the circumstances. In this case, the Court found that the allegations referred to property damage, for they describe the deterioration of the building's components, which was caused by water leaking through the windows and walls. The Court also considered the fact that the pleadings described the defective property, namely improperly built walls, an inadequate ventilation system, poorly installed windows, etc., which can also constitute property damage.

The Supreme Court found that, under the circumstances of this case, the alleged construction deficiencies constituted an accident under the wording of the policy. It was a fortuitous event, being unlooked for, unexpected and unintended by the insured, and it resulted from continuous or repeated exposure to conditions. The Court bore in mind that a liability insurance policy applies when the performance bond no longer applies. It offers protection once the work is completed.

Finally, the Court considered the exclusion clause for "work performed," the wording of which varied between the three different versions of the policy that Lombard successively issued, namely:

1) *With respect to the completed operations hazard to property damage to work performed by the Named Insured arising out of the work or any portion thereof, or out of materials, parts or equipment furnished in connection therewith.*

2) *"Property damage" to "that particular part of your work" arising out of it or any part of it and included in the "products – completed operations hazard."*

"Your work" means:

- a. *Work or operations performed by you or on your behalf; and*
- b. *Materials, parts or equipment furnished in connection with such work or operations.*

3) *"Property damage" to that particular part of "your work" arising out of it or any part of it and included in the "products-completed operations hazard".*

This exclusion does not apply if the damaged work or the work out of which the damage arises was performed on your behalf by a subcontractor.

It should be specified that the pleadings indicated the involvement of subcontractors in the defective construction work. After studying the wording of the various clauses and recalling that historically the broad form extension endorsement was intended to offer protection for work done by subcontractors, the Court found that when before a clause that is limited to work done by the insured, the fact that the pleadings indicate the involvement of subcontractors is sufficient to trigger the duty to defend. If, at trial, it materializes that the damage was due to work done by a subcontractor or was caused by the work of a subcontractor, the claim will fall within the scope of coverage. As for the other exclusions, the Court, narrowly interpreting the wording of the policies in question, found that the various versions of the exclusion did not apply and that Lombard owed Progressive a duty to defend.

Conclusion

In Quebec, in addition to exclusions for defects which are usually found in policies, Article 2465 of the Civil Code of Québec, which applies to both property and liability insurance, stipulates that:

2465. The insurer is not liable to indemnify for injury resulting from natural loss, diminution or losses sustained by the property arising from an inherent defect in or the nature of the property.

It will therefore be interesting to see how Quebec's courts will apply the principles laid down by the Supreme Court in this case.

¹ This article does not constitute a legal opinion and is not binding on the authors.