**Supreme Court Clarifies When Insurance Must Respond to Defend Construction Deficiency Claims**

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In *Progressive Homes Ltd. v. Lombard General Insurance Co.*, 2010, S.C.C. 33, the Supreme Court of Canada recently ruled on an insurer's duty to defend a general contractor in the context of a construction deficiency claim. These cases often involve the decay of, or damage to, interior building component parts after the failure of an exterior cladding system, or portions of it. The S.C.C. ruling settled differences among provincial appellate decisions when considering the coverage of such claims under a Comprehensive General Liability (“CGL”) insurance policy. The *Progressive Homes* decision provided some guidance on the interpretation of policy definitions of “property damage”, “accident”, “occurrence”, and the “work performed” exclusion.

The *Progressive Homes* case endorsed a uniformed approach to these interpretive issues. The British Columbia courts, and the British Columbia Court of Appeal in particular, in cases which preceeded *Progressive Homes*, had approached the interpretation of the policies in question that led to coverage denial under the particular CGL policies in question. And often in leaky condominium building envelope cases

In *Progressive Homes*, the Supreme Court of Canada overruled the B.C. Court of Appeal, and the lower court which had decided that no coverage extended to the contractor for the claims it was being sued for in a number of lawsuits. The defence costs alone were going to be significant.

The main argument in the *Progressive Homes* case was that “property damage” does not result from damage to one part of the building arising from another part of the same building. According to the argument, damage to other parts of the same building is pure economic loss, not “property damage”. What follows from this argument is that “property damage” is limited to damaged third party property. This argument builds on a distinction between property damage and pure economic loss, which argument is drawn in part from the Supreme Court of Canada’s prior decision in *Winnipeg Condominium Corporation v. Bird Construction* [1995] 1 S.C.R. 85. In the *Winnipeg Condo* case, subsequent owners claimed negligence by the original general contractor, subcontractor and architect after a storey high section of exterior cladding fell from the side of the building to the ground below. The S.C.C. in *Winnipeg Condo* found that the loss was not “property damage” but a recoverable form of economic loss. In short, the insurer argued that “property damage” does not include damage to the insured’s own work, and the context matters, the work should be looked at as whole when a building is the context for the claim.

In answer, the S.C.C. said an insurer’s duty to defend only requires the possibility of coverage. Whether any specific property fell within the definition of “property damage” or not would be a
matter to be determined on the evidence at trial. For purposes of the application and the trigger of the insurer’s duty to defend, it was a low threshold of showing the pleadings reveal a possibility of “property damage” for the purpose of deciding that question.

The alleged “property damage” at the root of this case requires an application of sometimes confusing concepts of an exclusion to coverage, and exceptions to exclusions to coverage. The common exclusion to coverage is a “work performed”, or “own work” exclusion. A common exception to such an exclusion is a “subcontractor exception”. Exclusions do not create coverage and neither do exceptions to exclusions. Exceptions bring an otherwise excluded claim back within coverage where the claim fell within the initial grant of coverage in the first place.

The central exclusion in the appeal was whether the “work performed” exclusion applied. To make matters more complicated, there were three version of the “work performed” exclusion at play in the appeal since there were successive insurance policies that applied to the period of alleged damage, which spanned a number of years.

The Court persuasively traced changes in insurance policy language in their various forms and found (1) on a plain reading damage was excluded only where it was caused by Progressive Homes to its own completed work but not property damage caused to, or by, a subcontractor’s work (2) the pleadings indicated the involvement of subcontractors which was itself sufficient to trigger to duty to defend (as it might at trial materialize that the damage was caused to a subcontractor work or a subcontractor’s work itself caused the damage) and (3) coverage for repairing defective components might be excluded on one version of the policy at play, but resulting damage would not be excluded.

It must be remembered that these issues were only determined at the pleading stage, which is to say very early in the lawsuit. Triggering a duty to defend requires the insurer to pay the investigation and litigation costs (i.e. defence costs) but not necessarily provide an indemnity. Depending on what was ultimately proved at trial as the Supreme Court of Canada itself noted “if as Lombard alleges the buildings are wholly defective, then the exclusion will apply and Lombard will not have to indemnify Progressive” under one of the versions of the policy.

At the early stages of a construction deficiency claim, an insurer will be properly required to defend those claims which possibly result in coverage. These claims are often historical claims brought years later, and are not inexpensive claims to defend.