SUPREME COURT OF CANADA DECISION IN PROGRISSIVE: Potentially Reopens Door for Insurance Coverage for General Contractors

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Canada's highest Court has overturned the 2009 decision of the BC Court of Appeal in the Progressive case, potentially re-opening the door for insurance coverage for general contractors being sued in leaky condo cases (*Progressive Homes Ltd. v. Lombard General Insurance Company of Canada*, [2010] SCC 33).

What does this mean for strata corporations suffering leaky condo syndrome? In essence, it means that insurance companies that provided a commercial general liability insurance policy to builders and general contractors of leaky buildings will be back at the bargaining table – it is business as usual.

This is significant since the allocated apportionment of blameworthiness for general contractors could be as much as 25% of the remediation costs based on the reasoning of Mr. Justice Grist in *Strata Plan NW3341 v. Canlan Ice Sports Corp.* [2001] B.C.J. No. 2661 (BCSC) (the "*Delta*" case). This equated to about $800,000.00 out of a damage award of over $3,200,000.00 in *Delta*. The Court held that fault was to be apportioned on a several basis among the major players in the leaky condo project as follows:

Owner/Developer 30%
General Contractor 25%
Designer 25%
Municipality 20%

There are two major matters that must be considered when embarking on a law suit in leaky condo cases – liability and recoverability. Whether a defendant is legally responsible to pay is addressed primarily by the expert witness evidence (usually an engineer or architect). If a defendant is liable, then the next major hurdle is where the money will come from to satisfy a judgment.

If the builder constructed the project using a shell company (e.g. a corporation without assets), then the builder could be judgment-proof. In this event, a judgment would be a hollow victory, since there is no ability to collect. The Progressive decision is significant since insurance companies that provided coverage during construction (which might have taken place in the late 1980's or 1990's) could, in appropriate circumstances, be required to indemnify for resultant damage. Legal advice should be sought on these important matters.

Prior to this SCC decision, insurers were taking the position, based on the BC Court of Appeal decision in *Progressive* and earlier rulings of the BC Supreme Court, that they had no duty to defend because the insurance policy was not triggered (*Progressive Homes Ltd. v. Lombard General Insurance Company of Canada*, [2009] BCCA 129; *Swagger Construction Ltd. v. ING Insurance Company of Canada*, [2005] BCSC 1269 and *GCAN Insurance Company v. Concord Pacific Group Inc.*, [2007] BCSC 241).

As a result of these earlier decisions, the general contractor was without insurance coverage when being sued in leaky condo cases. Without insurance, general contractors were basically "off the hook" – unless, of course, they had attachable assets.

It is submitted that the SCC decision has re-opened the door for insurance coverage for general contractors. Insurers are required to defend a claim if there is a "mere possibility" that the claim against the insured falls within the insurance policy. In order to determine if the claim falls within the policy, it is necessary to look to the substance of the claim against the general contractor and examine the clauses in the insurance policy itself.

The Progressive Decision: The Background

Progressive Homes Ltd. ("Progressive") was the general contractor hired to build several housing complexes for the BC Housing Management Commission ("BC Housing"). BC Housing alleged that four buildings suffered building

envelope failures due to water penetration, and eventually four lawsuits were initiated against Progressive alleging breach of contract and negligence.

Throughout the construction, Progressive had been insured by Lombard General Insurance Company of Canada ("Lombard") through a series of commercial general liability insurance policies ("CGL policies"). As the insurer, Lombard initially defended Progressive, but then withdrew, arguing that the claims of BC Housing were not covered under the insurance policies. Lombard argued that the damages in question were the consequences of poor workmanship, and the policies were not issued to indemnify Progressive for failing to meet its contractual obligations. It argued the policies covered damage to property caused by an accident or occurrence, and this did not include the defective building envelope. Progressive turned to the Court.

Both the BC Supreme Court and the majority of the BC Court of Appeal held that the claims against Progressive did not fall within the coverage granted by the CGL policies, and therefore, Lombard did not have a duty to defend Progressive. Madam Justice Huddart of the BC Court of Appeal provided a dissenting opinion, indicating that the insurer did have a duty to defend, and that evidence would be necessary to determine if the claims fell within the coverage of the policies.

The Supreme Court of Canada ("SCC") overturned the decision of the majority of the BC Court of Appeal. The SCC held that based on the claims made in the lawsuits against Progressive and the wording of the insurance policies in question, Lombard does have a duty to defend Progressive.

The Progressive Decision: Key Points

As noted above, the SCC made it clear that two basic questions will have to be answered to determine whether the insurance policy covers the damage in question:

1. The true nature or substance of the claim; and,

2. The interpretation of the policy in question.

The SCC concluded that the interpretation of the policy focuses on the language of the policy. The rules for interpreting insurance policies are clear: the coverage provisions should be construed broadly, while exclusion provisions should be construed narrowly. Furthermore, these clauses must be read together and understood as a whole.

Most CGL policies follow a particular format: they set out the coverage, then list exclusions and then set out exceptions. Exclusions do not create coverage – they preclude coverage when the claim is otherwise included. Exceptions bring an otherwise excluded claim back within coverage. The Court held that the policy should be interpreted in that order: coverage, exclusions and then exceptions (Para's 26-28).

The Court noted that the onus is on the insured (Progressive) to show that the claims fall within the initial grant of coverage (Para.29). If the insured shows that the claim falls within the initial grant of coverage, the onus shifts to the insurer (Lombard), to show that coverage is precluded by an exclusion clause (Para. 51).

The CGL policies in the *Progressive* case were occurrence policies: they covered "property damage" caused by "occurrences" or "accidents" (Para. 29). The SCC held that the onus was on Progressive to show that the damage in question – the failure of the building envelope due to water infiltration – constituted "property damage" under the policy; it also had to show that the property damage was caused by an "accident" or "occurrence".

There were five CGL policies in place from the time of construction until the time the lawsuits were brought against Progressive. There were three versions, and the relevant portions are reproduced in Table 1, below. Despite the change in the wording of some clauses, the SCC found that the essence of the policies was the same: Progressive was covered (subject to specific exclusions) for property damage caused by an accident (Para. 8).

Property Damage

The SCC held that the water ingress and infiltration alleged in the Claim against Progressive caused "property damage" as defined in the policy. The Court set out the definition of "property damage" in the first policy as follows (Para. 30):

> "Property damage" means
>
> > (1) physical injury to or destruction of tangible property which occurs during the policy period, including the loss of use thereof at any time resulting therefrom, or
> >
> > (2) loss of use of tangible property which has not been physically injured or destroyed provided such loss of use is caused by an accident occurring during the policy period.

The Court then set out the definition in the subsequent policies, where references to destruction were removed:

> "Property damage" means:
>
> > a. Physical injury to tangible property, including all resulting loss of use of that property; or
> >
> > b. Loss of use of tangible property that is not physically injured.

The main argument of the insurer was that "property damage" does not result from damage to one part of a building arising from another part of the same building. It argued that damage to a part of the same building is pure economic loss, and that the policies covered property damage to third-party property (Para. 31). This argument stems from the rejection of the "complex structure" theory in the Supreme Court of Canada case of *Winnipeg Condominium Corporation No. 36 v. Bird Construction Co*., [1995] 1 SCR 85, where the Court held that the structural elements of a building formed an indivisible unit.

Lombard in this case argued that as a result of this general principle in tort law, the property damage could not mean damage caused by other parts of the same building, and that property damage would be limited to third-party property, not damage to the insured's own work (Para. 34).

The SCC disagreed with this interpretation of "property damage". The Court held that the focus is on the language of the policy at issue – not general principles of tort law. There was no restriction to third-party property in the definition of "property damage", and the plain language of the definition included damage to any tangible property (Para. 35-36).

The SCC added that this interpretation was consistent with reading the policy as a whole, including looking to the "work performed" exclusion of the policy (Para. 37). This exclusion is common in CGL policies, which precludes coverage for damage to the insured's own work once it is completed. The Court also noted that excluding "defects" from the definition of property damage would also be inconsistent with the exclusion clauses excluding coverage for defects (Para. 40).

On the issue of "property damage", the SCC concluded as follows:

> [41] Do the pleadings allege "property damage"? In my view, they do. The pleadings describe water leaking in through windows and walls and allege "deterioration of the building components resulting from water ingress and infiltration". The pleadings also describe defective property, which may also be "property damage": e.g., improperly built walls, inadequate ventilation system, poorly installed windows. Whether specific property actually falls within the definition of "property damage" is a matter to be determined on the evidence at trial. This meets the low threshold of showing that the pleadings reveal a possibility of property damage for the purpose of deciding whether Lombard owes a duty to defend.

Accident

The SCC then went on to determine whether Progressive could show that the property damage was caused by an "accident" or "occurrence".

The first policy defined "accident" as follows:

> "Accident" includes continuous or repeated exposure to conditions which result in property damage neither expected nor intended from the standpoint of the Insured.

The Court noted that the definition for "occurrence" in the subsequent policies was essentially the same (See Table 1).

Progressive argued that the plain meaning of "accident" included the negligent act that caused the damage.

Lombard argued that faulty workmanship is not an accident, and that including faulty workmanship in a policy would offend the assumption that the insurance is designed to cover "fortuitous contingent risk". Lombard further argued that including faulty or defective workmanship would convert CGL policies into performance bonds (Para. 45).

The Court did not accept Lombard's positions on these points. To paraphrase, the Court stated the following on these arguments (Para's 46 – 49):

> (a) the question of whether "accident" could include faulty workmanship was a case-specific determination, dependant upon the allegations in the pleadings and the definition of "accident" in the policy;
>
> (b) the law did not support the proposition that faulty workmanship could never be an accident – it was dependant on the specific language of the policy;
>
> (c) including faulty workmanship in the interpretation did not offend the assumption that insurance provides for "fortuitous contingent risk", because fortuity is built into the definition of "accident"; and,
>
> (d) including faulty workmanship did not convert the CGL policies into performance bonds, which ensure work is brought to completion – the CGL policies in this case only cover damage to the insured's own work "once completed".

The SCC concluded that the plain meaning of "accident" included "continuous or repeated exposure to conditions", the property damage was not expected or intended, and the negligence alleged suggested the damage was "fortuitous".

The SCC found that there was a possibility of coverage on the facts of this case, and as such, Lombard had a duty to defend Progressive. Having found that coverage was possibly available, the onus shifted to Lombard, the insurer, to show that coverage was precluded by an exception clause.

Work Performed Exclusion

As noted above, exclusion provisions are narrowly interpreted. In this regard, the SCC stated that the exclusion had to "clearly and unambiguously exclude coverage" (Para. 51).

The main exclusion clause referred to in this case was the "work performed" exclusion. In general, this exclusion precludes coverage for damage to the insured's own work once it is completed. There were three versions of this exception clause in the policies covering Progressive (See Table 1). In the first and second versions of the policy, there was no express exception for work performed by subcontractors, but the subcontractor exception was added in the fourth version (Para's 52-53).

The SCC held that Lombard did not discharge its burden of showing that the "work performed" exclusion operated to "clearly and unambiguously exclude coverage" (Para 54).

In arriving at this conclusion, the Court examined how the wording of the exclusion clause evolved in the three versions of the policy. With respect to the first version, the Court stated as follows:

> [55] In the first version of the policy the original "work performed" exclusion was modified by what was called a General Liability Broad Form Extension Endorsement, which Progressive purchased in addition to the basic CGL policy. The original "work performed" exclusion read:
>
> > This insurance does not apply to:
> > . . .
> > (i) property damage to work performed by or on behalf of the Named Insured arising out of the work or

> any portion thereof, or out of materials, parts or equipment furnished in connection therewith; [Emphasis added.]

Clause (i) was replaced by clause (Z) in the Broad Form Extension Endorsement, which read:

> (Z) 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. [Emphasis added.]

The Court held that as a result of clause (Z), only work performed by Progressive was excluded. In other words, it did not exclude damage caused by subcontractors – which was the purpose for the upgrade to the Broad Form Extension (Para. 57).

In the second version of the policy, the exclusion read as follows:

> J. '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.

The Court stated that although there was no subcontractor exception in the second version of the policy, the clause only excluded coverage for repairing defective components – not resulting damage. As such, the Court found that there is a possibility of coverage under this second version. The evidence at trial would determine which "particular parts", if any, of the work caused the damage (Para. 65).

In the third version, the "work performed" exclusion read as follows:

> j. "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.

The Court held that the exclusion portion of this clause is identical to the exclusion portion of the second version, and therefore, only excludes coverage for defective property, not resulting damage. This clause also has an express subcontractor exception, which expands coverage once again – allowing coverage of defective work of subcontractors.

Conclusion

The SCC concluded that Lombard, the insurer, had a duty to defend Progressive in the four lawsuits:

> [72] … Under the first version of the CGL policy, there is a possibility of coverage for damage to work completed by a subcontractor and for damage resulting from work performed by a subcontractor. Under the second version of the policy, there is a possibility of coverage for damage resulting from the particular part of the insured's work that was defective. Under the third version of the policy, there is a possibility of coverage both for resulting damage and for any damage to work completed by a subcontractor.

The SCC makes it clear that whether the insurer will have a duty to defend will depend on the circumstances of each case. It will be necessary to review the pleadings, to determine the substance of the claims against the insured, and to review the specific clauses of the insurance policy or policies in issue.

It is submitted that the SCC decision in Progressive will certainly be welcome news to those affected by the leaky condo crisis. Lawyers issuing claims will generally use similar language to that used in Progressive, and the CGL policies in existence during the relevant time-periods will also be substantially similar to those at issue in Progressive.

TABLE 1 - KEY CLAUSES DEFINED

CLAUSE	
Property Damage	*First policy* Property damage means (1) physical injury to or destruction of tangible property which occurs during the policy period, including the loss of use thereof at any time resulting therefrom, or (2) loss of use of tangible property which has not been physically injured or destroyed provided such loss of use is caused by an accident occurring during the policy period. *Second to fourth policies* Property damage means: (a) physical injury to tangible property including all resulting loss of use of that property; or (b) loss of use of tangible property that is not physically injured.
Accident or Occurrence	*First policy* Accident includes continuous or repeated exposure to conditions which result in property damage neither expected nor intended from the standpoint of the insured. *Second to fourth policies* Occurrence means an accident, including continuous or repeated exposure to substantially the same general harmful conditions.
Work performed or your work exclusion	*First policy exclusion* This insurance does not apply to… (i) property damage to work performed by or on behalf of the Named Insured arising out of the work or any portion thereof, or out of materials, parts or equipment furnished in connection therewith. *Upgrade-1998 (replaced (i) with (z)* (z) With respect to the completed operations hazard to property damage to work performed by the Named Insured arising out of the work of any portion thereof, or out of materials, parts or equipment furnished in connection therewith. *Second and Third Policy exclusion* 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. *Fourth policy exclusion* Property damage to that particular part of “your work” arising out of it or any part of it and included in the products-completed operation hazard. This exclusion does not apply if the damaged work or the work of which the damage arises was performed on your behalf by a subcontractor.
Completed Operations Hazard	Completed operations hazard incudes … property damage arising out of operations, but only if the … property damage occurs after such operations have been completed or abandoned and occurs away from the premises owned by or rented to the Named Insured. Operations include materials, parts or equipment furnished in connection therewith. Operations shall be deemed completed at the earliest of the following times ….