

COURTS IN CONFLICT OVER BUILDERS' INSURANCE COVERAGE

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A recent decision from the Ontario Court of Appeal is fuelling the ongoing debate on whether contractors can seek coverage under their commercial general liability (CGL) policies for claims that allege defects in work performed by a subcontractor. Few areas of insurance law have attracted as much legal commentary as the “your work” and “your product” exclusion clauses that are found in most CGL policies and this decision again considers those clauses.

Courts across Canada have interpreted these clauses in diverse ways, sometimes deciding for a contractor and at other times for an insurer. This has created uncertainty for both insurers and insured in terms of understanding the precise nature of the coverage. In the case of *Axa Insurance (Canada) v. Ani-Wall Concrete Forming Inc.*, which was decided in July 2008, the Ontario Court of Appeal resolved the question in favour of the contractor — Axa was required to defend legal proceedings that had been commenced against Ani-Wall concerning defective concrete foundations in a number of homes.

The facts behind the lawsuit were relatively straightforward. Ani-Wall was to supply concrete and construct the footings and foundation walls for a number of homes. Ani-Wall in turn retained the services of Dominion Concrete Group Ltd. to supply the necessary concrete which regrettably turned out to be defective. The footings and foundation walls that Ani-Wall constructed had to be removed and replaced at considerable expense. The builders of the homes commenced an action against Ani-Wall seeking reimbursement of those costs and Ani-Wall in turn tendered the claim to Axa, its commercial general liability carrier.

The Axa insurance policy carried by Ani-Wall covered claims for property damage — which was defined as “physical injury to tangible property” — but it excluded coverage for property damage to any part of Ani-Wall’s work that was damaged due to a defect in that work. This is the typical “your work” exclusion found in most CGL policies. However, the policy went on to state that the “your work” exclusion did not apply if a subcontractor performed the damaged work on the contractor’s behalf.

Axa sought a declaration from the court that the policy did not cover damage to the concrete footings and foundations because this was damage to Ani-Wall's own work. Ani-Wall responded that a subcontractor had supplied the defective concrete and so the policy applied. Axa was unsuccessful both at the trial level in the Ontario Superior Court of Justice and in the Court of Appeal. Axa conceded that this was a claim for property damage under the policy; the whole of the decision, therefore, focussed on the interpretation of the various exclusion clauses.

The Ontario Court of Appeal rejected the argument that Dominion, the concrete supplier, could not properly be characterized as a subcontractor of Ani-Wall. While choosing not to identify a rigid standard for what separates a subcontractor from a mere supplier, the Court was satisfied that Dominion had effectively assumed responsibility for a portion of the work, the supply of concrete, that Ani-Wall would otherwise have performed. The fact that the policy did not define the term "subcontractor" created a potential "trap for the unwary" in the Court's view.

While the Court had no hesitation in finding that the defective concrete foundations were an element of Ani-Wall's own work, and thus subject to the exclusion for coverage, it also had no hesitation in finding that Dominion was Ani-Wall's subcontractor: therefore the exception to the "own work" exclusion applied. Axa would be required to indemnify Ani-Wall for damages and, accordingly, had an obligation to defend Ani-Wall in the underlying action.

This decision followed a 2006 Ontario decision, *Bridgewood Building Corp v. Lombard General Insurance Company of Canada*, which also considered a case of defective concrete. There the court also found in favour of coverage for the general contractor where a subcontractor performed the damaged work. The same exception to the exclusion for damage to the contractor's own work was found in that policy as in the *Ani-Wall* decision.

Of note in both the *Ani-Wall* and *Bridgewood* decisions is the absence of any discussion of whether a claim for defectively constructed foundations met the definition of physical injury to tangible property, which is a prerequisite for applying coverage under the policy's property damage definition. In *Ani-Wall*, Axa conceded that the claim met this definition so there was no need for the Court to consider the point further.

Axa next argued that the policy contained a "rip and tear" exclusion which it said was intended to exclude claims for removing and replacing defective work. But the Court held that the exclusion clause was not sufficiently clear in its wording, even if the intent was discernible, to allow the insurer to rely upon it. This finding only serves to show how much of an uphill battle insurers have, at least in the Ontario courts, when they seek to limit the availability of coverage.

These Ontario judgments fit a pattern of running counter to British Columbia jurisprudence in analogous cases. To date, three British Columbia decisions have reached an opposite conclusion when interpreting very similar policy wordings. Those decisions followed an earlier British Columbia precedent handed down in *Privest Properties v. Foundation Company of Canada*; in that case, the B.C. Court of Appeal held that the cost of correcting defective workmanship did not meet the definition of physical injury to tangible property in the commercial general liability policy. B.C. courts considered the application of the subcontractor exception to the “your work” exclusion but there was no coverage granted in the first instance for the cost of correcting defective workmanship.

The B.C. courts likewise reasoned that an event of faulty workmanship was not an accidental occurrence and therefore not covered. They also do not look to the subcontractor exception to the exclusion clause to create coverage. In contrast, the Ontario courts have accepted the argument that the exclusion of faulty workmanship in the policy is redundant if defects in the work were never intended to be covered in the first instance.

An appeal to the British Columbia Court of Appeal is pending in one of those B.C. decisions, *Progressive Homes v. Lombard Insurance*. At the moment, however, the courts in British Columbia and Ontario appear to be divided on the issue of coverage for general contractors when they face claims arising out of defective work performed by subcontractors.