2010 CarswellOnt 8113, 2010 ONSC 5911, [2010] I.L.R. I-5064

2010 CarswellOnt 8113, 2010 ONSC 5911, [2010] I.L.R. I-5064

PCL Constructors Canada Inc. v. **Encon** Group

PCL Constructors Canada Inc. (Applicant) and The **Encon** Group, **Encon** Insurance Managers Inc., Temple Insurance Company (Respondents)

Ontario Superior Court of Justice

Darla A. Wilson J.

Heard: July 20, 2010
Judgment: October 27, 2010
Docket: CV-10-402403

Counsel: Jamieson Halfnight for Applicant

Morris A. Chochla for Respondents

Subject: Insurance; Civil Practice and Procedure

Insurance --- Actions on policies — Commencement of proceedings — Obligations of insurer — To defend — Allegation in pleadings

Insured was general contractor for construction of 34-storey high-rise residential condominium in Toronto — Insurer was sued by condominium corporation for damages for alleged defects and deficiencies in construction of project — After being served with claim, insured sent it to insurer — Response was denial of duty to defend on basis that there was no coverage for claims asserted — Insured retained counsel who served statement of defence and crossclaim — Insured subsequently retained coverage counsel who sent letter to insurer requesting it reconsider its position with respect to duty to defend pursuant to policy — After receiving no response to letter, insured brought application for declaration that insurer was obligated to provide defence to insured — Insured paid costs of its own defence, but sought reimbursement of this amount as well as order that insurer pay costs of defence going forward — Application granted in part — Duty to defend was engaged — Reasonable reading of claim supported claim for damages that fell within provisions of policy — There was no restriction contained in policy to types of property damage and words must be given their plain meaning — Pleadings contained allegation of property damage — Statement of claim plead that as result of defective workmanship, water penetrated through suites and other areas causing various damages — Insured was acting as general contractor for project and claims against it as contained in amended statement of claim appeared to be based on allegation that building was not watertight and windows were not installed properly and water was allowed to leak into building.

Insurance --- Actions on policies — Commencement of proceedings — Obligations of insurer — To defend — Interpretation of policy

Insured was general contractor for construction of 34-storey high-rise residential condominium in Toronto — Insurer was sued by condominium corporation for damages for alleged defects and deficiencies in construction of project — After being served with claim, insured sent it to insurer — Response was denial of duty to defend on basis that there was no coverage for claims asserted — Insured retained counsel who served statement of defence and crossclaim — Insured subsequently retained coverage counsel who sent letter to insurer requesting it reconsider its position with respect to duty to defend pursuant to policy — After receiving no response to letter, insured brought application for declaration that insurer was obligated to provide defence to insured — Insured paid costs of its own defence, but sought reimbursement of this amount as well as order that insurer pay costs of defence going forward — Application granted in part — Duty to defend was engaged — Insurer did not discharge onus of demonstrating that exclusion excluded coverage such that there was no possibility that insurer would have to indemnify insured on claim as it was currently pleaded — Exclusion excluded from coverage work done by insured which was defective — It was unclear from statement of claim and expert reports specifically what deficient work was or who performed it — Reasonable reading of language of exclusion indicated that insured would not be indemnified for fixing particular part of work on project that it performed which was defective.

Insurance --- Actions on policies — Practice and procedure — Miscellaneous issues

Choice of counsel — Insured was general contractor for construction of 34-storey high-rise residential condominium in Toronto — Insurer was sued by condominium corporation for damages for alleged defects and deficiencies in construction of project — After being served with claim, insured sent it to insurer — Response was denial of duty to defend on basis that there was no coverage for claims asserted — Insured retained counsel who served statement of defence and crossclaim — Insured subsequently retained coverage counsel who sent letter to insurer requesting it reconsider its position with respect to duty to defend pursuant to policy — After receiving no response to letter, insured brought application for declaration that insurer was obligated to provide defence to insured — Insured sought to select own counsel — Application granted in part — There was no real conflict of interest to justify order that insurer not be permitted to control defence and appoint counsel of its choosing — Mere fact that insurer denied duty to defend did not demonstrate that there existed conflict of interest or that there was real concern that insurer might appoint counsel that would attempt to move claims out of coverage.

Insurance --- Actions on policies — Practice and procedure — Costs — Insurer declining to defend

Obligation to pay costs.

Cases considered by *Darla A. Wilson J.*:

Bridgewood Building Corp. (Riverfield) v. Lombard General Insurance Co. of Canada (2006), [2006] I.L.R. I-4498, 2006 CarswellOnt 2017, 79 O.R. (3d) 494, 35 C.C.L.I. (4th) 163, 16 B.L.R. (4th) 1, 51 C.L.R. (3d) 1, 211 O.A.C. 4, 266 D.L.R. (4th) 182 (Ont. C.A.) — followed

Derksen v. 539938 Ontario Ltd. (2001), 15 M.V.R. (4th) 1, 205 D.L.R. (4th) 1, 2001 SCC 72, 2001 CarswellOnt 3605, 2001 CarswellOnt 3606, [2002] I.L.R. I-4029, 277 N.R. 82, 33 C.C.L.I. (3d) 1, [2001] 3 S.C.R. 398, 153 O.A.C. 310 (S.C.C.) — referred to

Hanis v. University of Western Ontario (2008), 69 C.C.E.L. (3d) 86, *(*sub nom. *Hanis v. Teevan)* 92 O.R. (3d) 594, *(*sub nom. *Guardian Insurance Company of Canada v. University of Western Ontario)* [2008] I.L.R. I-4748, 241 O.A.C. 303, 2008 ONCA 678, 2008 CarswellOnt 5867, 67 C.C.L.I. (4th) 196 (Ont. C.A.) — followed

Nichols v. American Home Assurance Co. (1990), [1990] I.L.R. 1-2583, 45 C.C.L.I. 153, 39 O.A.C. 63, 107 N.R. 321, 68 D.L.R. (4th) 321, [1990] 1 S.C.R. 801, 1990 CarswellOnt 619, 72 O.R. (2d) 799 (note), [1990] R.R.A. 516, 1990 CarswellOnt 994 (S.C.C.) — referred to

***PCL** Constructors Canada Inc. v. Lumbermens Casualty Co.* (2009), 2009 CarswellOnt 3695, 76 C.C.L.I. (4th) 259, *(*sub nom. ***PCL** Constructors Canada Inc. v. Lumbermens Casualty Company Kemper Canada)* [2009] I.L.R. I-4860, 81 C.L.R. (3d) 186 (Ont. S.C.J.) — followed

Progressive Homes Ltd. v. Lombard General Insurance Co. of Canada (2010), 92 C.L.R. (3d) 1, [2010] 10 W.W.R. 573, 2010 SCC 33, 2010 CarswellBC 2501, 2010 CarswellBC 2502, 9 B.C.L.R. (5th) 1 (S.C.C.) — considered

R.W. Hope Ltd. v. Dominion of Canada General Insurance Co. (2001), 2001 CarswellOnt 4440, 34 C.C.L.I. (3d) 192, *(*sub nom. *Trafalgar Insurance Co. of Canada v. Imperial Oil Ltd.)* 57 O.R. (3d) 425, *(*sub nom. *Trafalgar Insurance Co. of Canada v. Imperial Oil Ltd.)* [2002] I.L.R. I-4064, 154 O.A.C. 7 (Ont. C.A.) — referred to

APPLICATION by insured for declaration that insurer had duty to defend and other relief.

***Darla A. Wilson J.*:**

1 This is an application brought for a declaration that Temple Insurance Company ("Temple") is obligated to provide a defence to **PCL** Constructors Canada Inc. ("**PCL**") in an action commenced in Ontario Superior Court action number 06-CV-317325PD1("the action") pursuant to a specific project wrap-up liability policy number WUT40802 ("the policy"). A further order is sought requiring Temple to provide a defence to **PCL** and to reimburse **PCL** for the expenses incurred in defending the action.

2 At the outset of the motion, counsel advised that on consent the application was to be dismissed against the **Encon** Defendants.

Background

3 **PCL** is a company which is involved in the management of construction in commercial buildings. In this case, **PCL** was the general contractor for the construction of a 34 storey high-rise residential condominium located at 81 Navy Wharf Court in Toronto. It is not disputed that **PCL** purchased Specific Project Wrap-Up Policy No. WUT40802 which covered the period September 1, 2000 through December 31, 2003 or the date of acceptance by the project owner, whichever date was earlier. Coverage was extended for another 24 months — the "completed operations" period — during which there was no exclusion for property damage to the building itself.

4 In 2006, **PCL** was sued (along with other parties) by Toronto Standard Condominium Corporation No. 1537 ("the condo corporation") for damages for alleged defects and deficiencies in the construction of the project. The Statement of Claim was amended in December of 2009.

5 After being served with the claim, **PCL** sent it to the insurer. The response was a denial of a duty to defend on the basis that there was no coverage for the claims asserted. The claims analyst cited exclusions 2(ii)(d) and 2(v) of the policy and wrote:

> The above noted policy provisions exclude any and all risks that an Insured may be called upon to rectify any deficiencies in the work performed under contract as opposed to the costs of rectifying the damages caused to other parties. As there is no coverage for this claim under the terms of the policy, you are not entitled to indemnification under the terms of the policy and accordingly, we must advise you that there is no duty to defend nor to indemnify you should the court ultimately rule against you. ...

6 **PCL** then retained counsel who served a Statement of Defence and Crossclaim. **PCL** subsequently retained coverage counsel who sent a letter to the insurer requesting it reconsider its position with respect to the duty to defend pursuant to the policy. After receiving no response to the letter from coverage counsel, this application was brought.

7 **PCL** has paid the costs of its own defence. As of the end of April 2010, the costs of the defence was $105,821.61 and **PCL** seeks reimbursement of this amount as well as an order that Temple pay the costs of the defence on a move forward basis.

The Policy

8 The exclusions relied on by Temple are 2(ii)(d) and (v), which I reproduce here for ease of reference:

Exclusions

9 *This policy does not apply to any liability: 2. Under Coverage B for: Injury to, or destruction of, or loss of use of (ii)(d)that particular part of any property, not on premises owned by or rented to the Insured: (i) upon which operations are being performed by or on behalf of the insured at the time of the injury thereto or destruction thereof, arising out of such operation; or (ii) out of which any injury or destruction arises; or (iii) the restoration, repair or replacement of which has been made or is necessary by reason of faulty workmanship thereon by or on behalf of the Insured;...(v) that particular part of any work performed by or on behalf of the insured, if such work is deemed unsafe, inadequate, faulty or unsatisfactory because of any known or suspected defect or deficiency therein. Any expense incurred by the insured for the inspection, withdrawal, repair or replacement of* such work, or loss of use of such work or is not reimbursable by this policy and is not a subject of cover hereunder... *[emphasis mine]*.

Positions of the Parties

The Applicant

10 The Applicant argues that the policy clearly covers property damage and Temple owes **PCL** a duty to defend the action. The Statement of Claim contains allegations of consequential property damage to the building and other property arising from the alleged construction defects and the policy provides coverage for these claims. The claims all deal with the position of **PCL** as general contractor for the project and it is alleged that the construction work was done in a substandard fashion, particularly with respect to waterproofing. It is alleged that damage occurred from water penetration which was ongoing since the time the building was constructed. It is the position of the applicant that it is clear that at least *some* of the claims pleaded fall within coverage and therefore, the duty to defend is triggered.

11 It is submitted that even if the claim advanced is ambiguous, if the claim can be interpreted to bring it within coverage under the policy, the insurer must provide a defence. Of significance is the fact that the exclusion for property damage to the building was removed for the completed operations period.

12 The applicant argues that Temple must reimburse **PCL** for the legal expenses paid to date. Further, it is argued that **PCL** ought to be able to select its own counsel whose future accounts will be paid by Temple because of the failure of Temple to recognize its duty to defend. There is a concern that Temple would be in a conflict of interest given its past conduct.

The Respondent

13 Temple submits there is no duty to defend **PCL** as none of the alleged claims, even on a reasonable reading of the amended pleadings, fall within coverage. The Wrap-Up policy is intended to cover an insured's tortuous liability to

other parties, not to cover the cost of repairing the insured's own defective work. There would have to be damage to property *other* than the project of **PCL** that required repair for the policy to respond as there has been no "occurrence" which would be covered under the policy. The claims contained in the Statement of Claim are for economic loss, not property damage, and there is no coverage provided under the policy and no duty to defend.

14 Even if the Court were to find that some of the claims being asserted are covered under the policy, Temple argues that these claims would be excluded under Exclusion 2(ii)(d) or 2(v). The respondents argue that Exclusion 2(ii)(d) [the exclusion for injury to or destruction of or loss of use of *that particular part* of any property upon which operations are being performed by or on behalf of the insured at the time of the injury... or out of which any injury or destruction arises; or the restoration, repair or replacement of which had been made necessary by reason of faulty workmanship by or on behalf of the insured] or (v) [the exclusion for injury to or destruction of or loss of use of *that particular part* of any work performed by or on behalf of the insured if such work is deemed unsafe, inadequate, faulty or unsatisfactory because of any defect or deficiency] excludes coverage. This Wrap-Up policy is intended to cover **PCL's** tortuous liability to third parties and not its own defective work. **PCL** was the general contractor for this project and as such, the completed condominium project is the "work" of **PCL** and building damage caused by poor workmanship or defective materials is not covered by the policy.

15 Finally, and alternatively, if coverage is found and the exclusions are not found to apply, the Respondent argues that defence costs should be apportioned between Temple and **PCL**.

Analysis

Is there a duty to defend?

16 The duty to defend is a broad one, and is triggered if the statement of claim alleges claims that *potentially* could fall within the coverage afforded by the policy: *Nichols v. American Home Assurance Co.*, [1990] 1 S.C.R. 801 (S.C.C.). It is often the case that pleadings are vague and lack specificity. However, the duty to defend as articulated by the Supreme Court of Canada, "is triggered not by actual acts or omissions, but by allegations, applying even if any of the allegations of the suit *are groundless, false or fraudulent.": Nichols v. American Home, supra.*

17 The wording of the Statement of Claim is not determinative on whether the duty to defend arises. "What is determinative is the true nature or the substance of the claim.": *Progressive Homes Ltd. v. Lombard General Insurance Co. of Canada*, 2010 SCC 33 (S.C.C.).

18 In my view, the court must take a reasonable reading of the statement of claim, consider the real nature of the allegations and determine whether there are any claims for which the insurer could be called upon to provide indemnification. As noted by Osborne, J.A. (as he then was) "the threshold established by *Nichols* is rather low. The duty to defend arises where there is a "mere possibility" that the claim made against the insured is covered by the policy.": *R.W. Hope Ltd. v. Dominion of Canada General Insurance Co.* (2001), 57 O.R. (3d) 425 (Ont. C.A.).

19 In the case at hand, paragraph 17 of the amended statement of claim sets out many alleged "defects, damage and deficiencies" which create a "dangerous building" and which, it is further alleged, "will lead to failures of the components of the condominium complex and cause physical harm and property damage."

20 The statement of claim makes reference to expert reports from an engineering company, Halsall Associates Limited, and an architectural firm, Best Consultants. These reports detail the nature of the defects which, it is pleaded, cause "danger and damage to people and property."

21 The policy provides coverage to **PCL** for damages arising out of the insured's operations in connection with the project because of property damage which is defined in the policy as "physical injury to or destruction of tangible

property caused by an *occurrence* (as defined herein) which means an accident, including continuous or repeated exposure to conditions, which result in bodily injury or property damage."

22 While I appreciate that the wrap-up policy is intended to cover an insured's tortuous liability to others and is not intended to cover the insured's own defective workmanship, the policy provides coverage for damage to tangible property caused by an occurrence. There is no restriction contained in the policy to the types of property damage and in my view, the words must be given their plain meaning.

23 It is clear that the pleadings contain allegations of property damage. The statement of claim and the expert reports referred to in the claim include claims for damage to people and property arising out of water leaking through the windows, water leaking in the parking garage, smoke and odour damage into condominium suites, and moisture damage inside the suites, to cite a few examples. The expert reports expand on the nature of the deficiencies causing damages.

24 The statement of claim pleads that as a result of defective workmanship water has penetrated through to the suites and other areas causing various damages. In my view, a plain reading of the allegations against **PCL** contained in the statement of claim makes it clear that at least some of the claims can be interpreted in a manner to bring them within coverage under the policy. **PCL** was acting as a general contractor for the project and the claims against it as contained in the amended statement of claim appear to be based on the allegation that the building was not watertight and that in particular, the windows were not installed properly and water was allowed to leak into the building. It is alleged that in some instances, water ponded while in others, the water penetrated over a period of years, with resultant damage.

25 Whether the property damaged falls under the definition of "property damage" is something that will be determined based on the evidence called at trial. However, "this meets the low threshold of showing that the pleadings reveal a possibility of property damage for the purpose of deciding whether [the insurer] owes a duty to defend.": *Progressive Homes Ltd.*, *supra*. A reasonable reading of the claim, in my view, supports a claim for damages that falls within the provisions of the policy and thus, the duty to defend is engaged. .

26 This is consistent with the "interpretative aid approach" taken by the Court of Appeal in *Bridgewood Building Corp. (Riverfield) v. Lombard General Insurance Co. of Canada* (2006), 79 O.R. (3d) 494 (Ont. C.A.). By this, I mean that that the Courts must look not at general principles of insurance in order to determine the proper meaning of the contract, or consider the general nature of the policy, but rather, must look at the language used in the policy. The general principles of contract interpretation are "interpretative aids" that can be used by the court but they are not determinative. As Justice Moldaver noted in *Bridgewood*, *supra*:

> ... it is not now, nor, to my knowledge, has it ever been the position of this court that, standing alone, the "general principle" precludes coverage of an insured's own defective work or product regardless of provisions in the policy that evidence a contrary intent. Rather, it constitutes an interpretative aid that can be helpful, though not decisive, when interpreting particular provisions of a CGL policy in an effort to determine the scope and extent of the risks that the insurer has agreed to cover...

I agree with this view.

Is there an exclusion that applies?

27 The duty to defend is, of course, subject to Temple demonstrating that there is an applicable exclusion which operates to completely exclude coverage, clearly and unambiguously. I accept the submission of counsel for the respondent that the exclusions in the policy are to ensure that there is no coverage for the insured's own defective work because to do so would be to render the policy a performance bond.

28 The Supreme Court of Canada has stated: Whether an exclusion clause applies in a particular case of concurrent causes is a matter of interpretation. This interpretation must be in accordance with the general principles of interpretation of insurance policies. These policies include, but are not limited to: 1) The *contra proferentem* rule; 2) The principle that coverage provisions should be construed broadly and exclusion clauses narrowly; and 3) The desirability, at least where the policy is ambiguous, of giving effect to the reasonable expectations of the parties: *Derksen v. 539938 Ontario Ltd.*, [2001] 3 S.C.R. 398 (S.C.C.).

29 Counsel for the insurer submits that the "your work" exclusion contained in 2(v) of the policy precludes coverage. It is argued that in the case at hand, **PCL** was the general contractor and its "work" is the entire project so any damage caused by faulty workmanship or the use of defective materials is not covered under the policy. I do not accept this interpretation of exclusion 2(v).

30 In considering the meaning of the exclusions, it is necessary to look at the plain meaning of the words. As I read the exclusion, it excludes from coverage work done by **PCL** which is defective — that particular part of any work performed by or on behalf of the insured. In order to successfully rely on an exclusion, the insured must demonstrate that an exclusion applies to oust coverage. In my view, **PCL** is excluded from recovering for fixing *the particular part* of *its* work on the condominium project that contains the deficient work. This makes sense, because to permit this would be to enable **PCL** to recover indemnity for correcting its own deficient work.

31 The work performed exclusion must be interpreted narrowly and if there is any ambiguity, it must be resolved against the insurer. One of the difficulties at this juncture is that the pleadings are vague and the exact damages being claimed are unclear. It is impossible to know with any specificity what the damages are and their source.

32 It is unclear from reviewing the statement of claim and the expert reports specifically what the deficient work is or who performed it. It is far from clear the source of the damages but it cannot be said that the damages only emanate from the building envelope, which is the insured's "own work". I do not accept the argument of counsel for the insurer that *all* of the claims alleged are to the building itself and consequently are captured by Exclusion 2(v) of the policy.

33 Rather, in my view, a reasonable reading of the language of the exclusion indicates that **PCL** will not be indemnified for fixing "that particular part" of the work on the project that it performed which is defective. The words "that particular part" were inserted in the exclusion for a reason; otherwise they would be superfluous.

34 Rather, a reasonable reading of the Statement of Claim indicates that damage is being claimed for damage to property owned by others. It is at least arguable that claims are being advanced by owners of the condominium units for damage to their property from leakage, which would not be subject to an exclusion and would attract coverage under the policy. Similarly, the claim may be read as alleging there is damage to other parts of the building, such as the interior, which would not be work done by **PCL**.

35 As noted by Justice Rothstein in the *Progressive Homes Ltd. case, supra:*

> It will have to be determined at trial which "particular parts" of the work caused the damage. Repairs to those defective parts will be excluded from coverage under this version, regardless of whether they were the result of Progressive's own work or the work of subcontractors... However, the pleadings allege that there was resulting damage: deterioration of the building components resulting from water ingress and infiltration. This is sufficient to trigger the duty to defend...

36 In my opinion, Temple has not discharged the onus of demonstrating that the "your work" exclusion clearly excludes coverage such that there is no possibility that the insurer would have to indemnify the insured on the claim as it is currently pleaded.

The Costs of the Defence

37 At the present time, in my opinion, it is impossible to separate the costs of the defence for claims that would be covered from those for which there would be no coverage. I agree that at some point, it may be possible to separate out the costs that relate exclusively to uncovered claims from those costs which arise from the defence of covered claims. At that time, there can be an apportionment of the costs of the defence for covered and not covered claims. This is consistent with the reasoning of the Court of Appeal in *Hanis v. University of Western Ontario* (2008), 241 O.A.C. 303 (Ont. C.A.).

38 However, at this time, given the stage of the proceedings, it is impossible in my view to apportion the costs between covered and non-covered claims. To attempt to do so would be pure speculation. Thus, Temple is obligated to pay all of the costs of the defence, subject to further order of this court.

The Choice of Counsel Issue

39 Counsel for the Applicant argues that given the initial refusal of Temple to respond to the claim, there is a legitimate concern that the counsel appointed by the insurer might attempt to conduct the defence so that any liability would be for non-covered damages. It therefore asks that **PCL** be afforded the opportunity to select its own counsel. Counsel for the respondent did not address this request in his materials nor in his argument.

40 In considering this submission, the Court must be sensitive to the rights of both parties. While I understand the apprehension of **PCL** to have Temple select and instruct counsel given the refusal of Temple to defend the claims to date, I am also mindful of the concerns of Temple and its contractual right to control the defence. I agree with the comments of Justice Thorburn in ***PCL*** *Constructors Canada Inc. v. Lumbermens Casualty Co.*, 2009 CarswellOnt 3695 (Ont. S.C.J.), where she noted:

> The Courts must seek to strike a balance in these circumstances recognizing the legitimate interests of both the insured and the insurer. The potential tension in the relationship between insured and insurer is not sufficient to require the insurer to surrender control of the defence. There must be a reasonable apprehension that if counsel were to act for both the insurer and the insured in defending the action, counsel would be in a conflict of interest.

41 On the facts of the case before me, I am not persuaded there is a real conflict of interest that would justify an order that Temple not be permitted to control the defence and appoint counsel of its choosing. Some portions of these claims may be covered while others may not. The mere fact that Temple denied a duty to defend does not demonstrate that there exists a conflict of interest and or that there is a real concern that Temple might appoint counsel that would attempt to move claims out of coverage. The Applicant's request for an order permitting it to select defence counsel is dismissed without prejudice to its right to seek such order from this Court at a further stage of the proceedings.

Conclusion

42 For the reasons set out above, a declaration shall issue that Temple Insurance Company is obligated to provide a defence to **PCL** in Ontario Superior Court of Justice action 06-CV-317325PD1 commenced in Toronto. An order shall issue requiring Temple to reimburse **PCL** for the fees and disbursements it has incurred in the defence of the action, including those billed by **PCL's** current defence counsel.

43 If the parties cannot agree on costs, I will accept brief written submissions of no more than three pages within 10 days, following which I will fix the costs.

Application granted in part.

END OF DOCUMENT