

RISK MANAGEMENT ON CONSTRUCTION PROJECTS

Presented by members of our Infrastructure, Construction & Procurement Group

*Satinder Sidhu – Moderator,
Scott Lamb, Samantha Ip,
Rosalie Clark, Kim Do*

CLARK WILSON Webinar: May 13, 2022



Risk Management on Construction Projects Overview

1. Builders Risk / Course of Construction Policy Coverage – Samantha Ip and Kim Do
2. Wrap-Up Liability Insurance – Satinder Sidhu
3. Construction Bonds – Scott Lamb
4. Warranties – Rosalie Clark

CLARK WILSON 2

Risk Management on Construction Projects

Builders Risk / Course of Construction Policy Coverage

 <p>Samantha Ip Partner 604 643 3172 sip@cwilson.com</p>	 <p>Kim Do 2021-22 Articling Student 604 643 3901 kdo@cwilson.com</p>
--	---

CLARK WILSON 3

**WHAT IS A COC OR
BUILDER'S RISK POLICY?**

CLARK WILSON 4

What is the Builders risk or course of construction policy?

- Intended to provide broad coverage for "all risks" that may arise during the course of construction for direct "physical loss" or "damage" to property.
- Only a property insurance (not liability insurance) policy that responds to property damage during the course of construction, not liability claims.
- Once property damage is established, there is often accompanying time element coverage for resulting business losses.

CLARK WILSON 5

What is the function of Builders risk policies?

- To provide certainty, stability, and peace of mind and ensure that construction projects do not grind to a halt because of disputes and potential litigation about liability for replacement or repair amongst the various contractors involved: *Ledcor Constructions Limited v Northbridge Indemnity Insurance Company*, [2016 SCC 37](#).
- "to provide to the owner the promise that the contractors will have the funds to rebuild in case of loss and to the contractors the protection against the crippling cost of starting afresh in such an event, the whole without resort to litigation in case of negligence by anyone connected with the construction, a risk accepted by the insurers at the outset. This purpose recognizes the importance of keeping to a minimum the difficulties that are bound to be created by the large number of participants in a major construction project, the complexity of which needs no demonstration. It also recognizes the realities of industrial life.": *Commonwealth Construction Co Ltd v Imperial Oil Ltd et al*, [1976 CanLII 138](#) (SCC)

CLARK WILSON 6

WHO CAN CLAIM FOR COVERAGE?

CLARK WILSON 7

Who can access the Builder's risk policy coverage?

- **Only Insureds:** Named Insureds, Additional Insureds but even potential Unnamed Insureds.
- Case law which holds that the policy will generally, by necessary implication, include Owners, General Contractors, and Subcontractors, and others, as Unnamed Insureds, unless such policy is worded to eliminate or limit direct coverage of any Unnamed Insureds. Other case law is more restrictive on who is an insured.
- Builder's risk policies are intended to provide broad coverage for construction projects as a whole, rather than to specific Insureds.
- **Risk management advice:** ensure you are named insured on Declarations Page or named in an Additional Insured Endorsement.

CLARK WILSON 8

WHAT DOES A BUILDER'S RISK POLICY COVER?

CLARK WILSON 9

First – Check the Declarations Page

- Summary of coverages purchased for the COC policy.
- Found at the beginning of the policy and contains important details, including:
 - Named Insureds;
 - Location of the insured premises;
 - Term;
 - Coverages and limits available;
 - Deductibles or self-insured retentions;
 - Endorsements added onto the policy.

Second – Satisfy the Insuring Agreement

- To make a claim under the policy and access coverage (whether basic or any extensions), that claim must satisfy the requirements of the Insuring Agreement.
- Multiple requirements.
- First "bridge" to cross for coverage.



Insuring Agreement – must be one of 5 types of insured property

1. Insuring Agreement

This Policy, subject to the limitations, exclusions, terms and conditions hereinafter mentioned or stated in the Declarations, is to insure, in respect of occurrences happening during the Policy Period, against all risks of direct physical loss of or damage, including general average and salvage charges, to:

- Property in course of construction, installation, reconstruction or repair including site preparation, excavation, testing & commissioning whilst at the risk of the insured and whilst at the location of the said construction, installation, reconstruction or repair operations (all of which are herein referred to as the construction operations). Where a limit is stated in the Declarations for Transit, coverage includes such property while in transit (including during loading, unloading and transshipment).
- Property of every kind and description (including expendable materials and supplies not otherwise excluded) owned by the insured and used or to be used in a part of, or incidental to, the construction operations including temporary works wherever the said property may be located within the Territorial Limits and including while in transit (including during loading, unloading and transshipment).
- Property of others used or to be used in, as part of, or incidental to the construction operations, for which the Insured may be responsible or shall, prior to any occurrence for which claim may be made hereunder, have assumed responsibility. Loss, if any, arising under this paragraph c) shall be adjusted with and paid to the Insured.
- Existing property for which the Insured may be responsible or shall, prior to any occurrence for which claim may be made hereunder have assumed responsibility.
- Tunnel Boring Machines

Insuring Agreements a) through e) apply only when specifically stated in the Declarations and shall be limited to a maximum recovery of the limit of Insurance stated on the Declarations Page in respect of any one loss.

Requirement for coverage – direct physical loss of or damage

1. Insuring Agreement

This Policy, subject to the limitations, exclusions, terms and conditions hereinafter mentioned or stated in the Declarations, is to insure, in respect of occurrences happening during the Policy Period, against all risks of **direct physical loss of or damage**, including general average and salvage charges, to:

[...]

Requirement for coverage – direct physical loss of or damage – cont'd

- “physical loss” and “damage” means an alteration in the appearance, shape, colour or other material dimension of the property insured.
 - *Acciona Infrastructure Canada Inc v Allianz Global Risks US Insurance Company*, 2014 BCSC 1568, aff'd 2015 BCCA 347
- Physical alteration must be harmful, resulting in the property insured becoming less functional, aesthetically pleasing, or valuable.
 - *Prosperity Electric v Aviva Insurance Co of Canada*, 2021 BCCA 237
- Physical loss does not include loss of use or pure economic loss, unless specifically provided for.
 - *MDS Inc v Factory Mutual Insurance Company*, 2020 ONSC 1924 rev'd 2021 ONCA 594

If Insuring Agreement is satisfied – coverage is for cost of remediation



- If the Insuring Agreement is triggered, cost of remediation is covered.
- Coverage is for remediation of damage with material of like kind and quality and for like occupancy:

5. Basis of Settlement
 In the event of loss or damage to Property covered hereunder, the measure of recovery shall be the full cost to repair or replace with new materials or like kind and quality at the construction site without deduction for depreciation. Coverage shall include necessary professional fees and profit charges. If the property is not repaired or replaced, the measure of recovery shall be the actual cash value of the property damaged at the time of the loss.

- Post loss enhancement is not covered.

Additional Coverage – Delayed Start Up (DSU)

- Covers loss of anticipated income in the event that the project suffers physical loss or damage during construction.
- In a way, a form of business interruption insurance for construction projects as it insures for the financial consequences of a delay to project completion arising from an insured peril.
- Cannot be triggered unless the loss is first covered by the insuring agreement.
- Extent of what it includes is based on wording of the endorsement.
- Expert evidence required to substantiate financial loss caused by property damage due to insured peril.

Delayed Start Up
[...]

Insuring Agreement
Subject to all its' stipulations, limitations and conditions, this Policy covers against the loss directly resulting from delay in the commencement of the commercial operation of the project described in the Declarations caused by loss, destruction or damage by the perils insured against by Section 1 of the Policy occurring during the Policy Period to the Property insured herein.

CLARK WILSON 19

WHAT DOES THE BUILDERS RISK POLICY NOT COVER?

CLARK WILSON 20

No Coverage for the Faulty Design or Workmanship

- These exclusions exclude the "cost of making good" or "damage caused by" faulty design or workmanship, subject to an exception for "resulting damage".
- For example, excludes the costs of making good **faulty workmanship** but the resulting damage exception will still cover the costs or damages apart from the cost of redoing the faulty work.
 - *Ledcor Construction Ltd v Northbridge Indemnity Insurance Co*, [2016 SCC 37](#)
- For example, excludes the costs of redoing the elements that were **faultily designed** but resulting damage is still covered (though encompassing damage done to something other than the property which is faultily designed.)
 - *Canadian National Railway v Royal and Sun Alliance Insurance Co of Canada*, [2008 SCC 66](#)

This policy section does not insure:
[...]

(b) The cost of making good faulty workmanship, construction materials or design unless physical damage not otherwise excluded by this policy results, in which event this policy shall insure such resulting damage.

CLARK WILSON 21

The “DE” and “LEG” exclusions

- Two sets of graduated wordings developed by London underwriting groups provide for different levels of coverage for defects and resulting damage, each subsequent iteration offering broader insurance coverage:

- Design Exclusion (DE) Clauses DE1-5;
- London Engineering Group (LEG) Clauses 1-3.



DE1 and LEG1: Outright Defects Exclusion

- DE1 and LEG1 are essentially a total exclusion of all loss or damage due to defective design, plan, specification materials or workmanship

DE1: Outright Defects Exclusion (1995)	LEG1/96: "Outright Defects" Exclusion
This Policy excludes loss of or damage to the Property Insured due to defective design plan specification materials or workmanship.	The Insurer(s) shall not be liable for loss or damage due to defects of material workmanship design plan or specification

DE2: Extended Defect Condition

- DE2 excludes damage to property that is in a defective condition, or property that relies upon it for support, but otherwise covers consequential damage (resultant damage) to any other property free of defective condition.

DE2: Extended Defective Condition Exclusion (1995)
This Policy excludes loss of or damage to and the cost necessary to replace repair or rectify
a) Property Insured which is in a defective condition due to a defect in design plan specification materials or workmanship of such Property Insured or any part thereof
b) Property Insured which relies for its support or stability on a) above
c) Property Insured lost or damaged to enable the replacement repair or rectification of Property Insured excluded by a) and b) above
Exclusion a) and b) above shall not apply to other Property Insured which is free of the defective condition but is damaged in consequence thereof.
For the purpose of the Policy and not merely this Exclusion the Property Insured shall not be regarded as lost or damaged solely by virtue of the existence of any defect in design plan specification materials or workmanship in the Property Insured or any part thereof.

DE3: Limited Defective Condition Exclusion, DE4: Defective Part Exclusion and LEG2: "Consequence" Defects Exclusion

- DE3 excludes damages to property which is defective, but gives cover for other property which is free of defect and is damaged by defective property.
- DE4 is similar to DE3 but restricts the exclusion to any "component part or individual item" which is defective but excludes damage only to the component part or individual item of the property that is deemed defective. It otherwise covers consequential damage to any other property free of defective condition.

CLARK WILSON 25

DE3: Limited Defective Condition Exclusion, DE4: Defective Part Exclusion and LEG2: "Consequence" Defects Exclusion

- LEG2 excludes all costs that would have been incurred if replacement or rectification of the defect had been carried out immediately prior to the damage occurring.

— *Acciona Infrastructure Canada Inc v Allianz Global Risks US Insurance Company, 2014 BCSC 1568, aff'd 2015 BCCA 347.*

DE3: Limited Defective Condition Exclusion (1995)	DE4: Defective Part Exclusion (1995)	LEG2/96: "Consequence" Defects Exclusion
This Policy excludes loss of or damage to and the cost necessary to replace repair or rectify:	This Policy excludes loss of or damage to and the cost necessary to replace repair or rectify:	The Insurer(s) shall not be liable for:
a) Property insured which is in a defective condition due to a defect in design plan specification materials or workmanship of such Property insured or any part thereof	a) Any component part or individual item of the Property insured which is defective in design plan specification materials or workmanship	All costs rendered necessary by defects of material workmanship design plan or specification and should damage occur to any portion of the Insured Property containing any of the said defects the cost of replacement or rectification which is hereby excluded is that cost which would have been incurred if replacement or rectification of the Insured Property had been set in hand immediately prior to the said damage.
b) Property insured lost or damaged to enable the replacement repair or rectification of Property insured excluded by a) above	b) Property insured lost or damaged to enable the replacement repair or rectification of Property insured excluded by a) above	
Exclusion a) above shall not apply to other Property insured which is free of the defective condition but is damaged in consequence thereof.	Exclusion a) above shall not apply to other parts or items of the Property insured which are free from defect but are damaged in consequence thereof.	For the purposes of this policy and not merely this exclusion it is understood and agreed that any portion of the Insured Property shall not be regarded as damaged solely by virtue of the existence of any defect of material workmanship design plan or specification.
For the purpose of the Policy and not merely this Exclusion the Property insured shall not be regarded as lost or damaged solely by virtue of the existence of any defect in design plan specification materials or workmanship in the Property insured or any part thereof.	For the purpose of the Policy and not merely this Exclusion the Property insured shall not be regarded as lost or damaged solely by virtue of the existence of any defect in design plan specification materials or workmanship in the Property insured or any part thereof.	

CLARK WILSON 26

DE5 and LEG3: Design Improvement Exclusion

- DE5 and LEG3 provide the broadest cover, providing full cover for damages resulting from a defect including for the defective property itself. It only excludes the costs to improvements to the original design, plan, specification, workmanship or materials.

DE5: Design Improvement Exclusion (1995)	LEG3/06: Design Improvement Exclusion
This Policy excludes:	The Insurer(s) shall not be liable for:
a) The costs necessary to replace repair or rectify any Property Insured which is defective in design plan specification materials or workmanship	All costs rendered necessary by defects of material workmanship design plan or specification and should damage (which for the purposes of this exclusion shall include any patent detrimental change in the physical condition of the Insured Property) occur to any portion of the Insured Property containing any of the said defects the cost of replacement or rectification which is hereby excluded is that cost incurred to improve the original material workmanship design plan or specification.
b) Loss or damage to the Property Insured caused to enable replacement repair or rectification of such defective Property Insured.	
But should damage to the Property Insured (other than damage as defined in b) above) result from such a defect this exclusion shall be limited to the costs of additional work resulting from and the additional costs of improvements to the original design plan specification materials or workmanship.	For the purpose of the policy and not merely this exclusion it is understood and agreed that any portion of the Insured Property shall not be regarded as damaged solely by virtue of the existence of any defect of material workmanship design plan and specification.
For the purpose of the Policy and not merely this Exclusion the Property Insured shall not be regarded as lost or damaged solely by virtue of the existence of any defect in design plan specification materials or workmanship in the Property Insured or any part thereof.	

CLARK WILSON 27

Other Notable Exclusions

- For example, a Terrorism Exclusion.

Notwithstanding any provision to the contrary within this insurance or any endorsement thereto it is agreed that this insurance excludes loss, damage, cost or expense of whatsoever nature directly or indirectly caused by, resulting from or in connection with any act of terrorism regardless of any other cause or event contributing concurrently or in any other sequence to the loss.

For the purpose of this endorsement an act of terrorism means an act, including but not limited to the use of force or violence and/or the threat thereof, of any person or group(s) of persons, whether acting alone or in behalf of or in connection with any organization(s) or government(s), committed for political, religious, ideological or similar purposes including the intention to influence any government and/or to put the public, or any section of the public, in fear.

This endorsement also excludes loss, damage, cost or expense of whatsoever nature directly or indirectly caused by, resulting from or in connection with any action taken in controlling, preventing, suppressing or in any way relating to any act of terrorism. [...]

- For example, an Asbestos Contamination Exclusion Endorsement.

This policy does not insure either directly or indirectly:

- a) the cost or expense arising out of testing for, monitoring of, clean up, removal, containment or treatment of Asbestos material, whether or not the Asbestos is:
 - i) airborne as a fibre or particle;
 - ii) contained in a product;
 - iii) carried on clothing or transmitted in any fashion whatsoever; or
- b) contained in any part of any building, building material, insulation product, insulation material or any component part of any building;
- c) costs of demolition or increased cost of reconstruction, repair, debris removal or loss of use necessitated by the enforcement of any law or ordinance regulating asbestos material;
- d) costs incurred in complying with any government direction declaring that asbestos material present in or part of or utilized on any portion of the project must be removed or modified.


**TAKE-AWAYS:
COC COVERAGE**

TAKE-AWAYS

- Not all property at the project is necessarily covered.
- Check the Declarations Page for available coverages.
- There are time and monetary limits to coverage.
- Expert evidence is often required to substantiate cause of failure or damage and business losses.
- What is considered "direct physical loss of or damage to" is evolving in Canada.

Risk Management on Construction

Wrap-Up Liability Insurance



Satinder Sidhu
Partner - Moderator
604 643 3119
ssidhu@cwilson.com

CLARK WILSON 31

WRAP-UP LIABILITY INSURANCE

CLARK WILSON 32

What is wrap up liability insurance (the “Wrap”)?

- General liability insurance for a specific construction project
Covers the insured for damages arising out of the insured’s operations in connection with the construction project (subject to the insuring agreement, conditions and exclusions)
- Covers all interested parties carrying out operations on the construction project: owner, contractor, subcontractors, and consultants under a single policy
- Either owner or contractor may purchase (should be set out in the contract/supplementary conditions)
- Complements a builder’s risk insurance policy, which covers damage to the property under construction

CLARK WILSON 33

ADVANTAGES OF THE WRAP

CLARK WILSON 34

What are the advantages of the Wrap?

- Time savings with only one policy at issue
- Uniformity of coverage, limits and deductible
- Deal with single insurer on claims
- Reduces disputes over liability between parties on the project and between their insurers
- May provide for higher limits than normally available for small contractors and subcontractors
- Less opportunity for duplicate coverage and premiums

CLARK WILSON 35

DISADVANTAGES OF THE WRAP

CLARK WILSON 36

What are the disadvantages of the Wrap?

- High deductibles
- May not be legally enforceable by unnamed insureds unless policy contains an agency and trustee clause
- Material suppliers may not be covered
- Liability for injury to property forming part of the project is limited to the completed operations period



CLARK WILSON

37

WHAT DOES THE WRAP COVER?

CLARK WILSON

38

Insuring Agreement

- The insurer agrees to pay on behalf of the insured all sums which the insured shall become legally obligated to pay as damages, arising out of the insured's operations in connection with the project insured, because of:
 1. Bodily/Personal Injury
 2. Property Damage
 3. Defense, Settlement, Investigation And Negotiation

CLARK WILSON

39

Definition of Bodily / Personal Injury

Bodily Injury

- Sickness, disease, mental anguish, mental suffering, or shock sustained by any person, caused by an occurrence (defined in the policy) during the policy period, including death.

Personal Injury

- Injury during the policy period arising out of (i) false arrest, detention or imprisonment, or malicious prosecution (ii) libel or slander (iii) wrongful entry or eviction (iv) humiliation or discrimination.

CLARK WILSON 40

Definition of Property Damage

Property Damage

- a. Physical injury to or destruction of tangible property caused by an occurrence during the policy period, including loss of use; or
- b. loss of use of tangible property which has not been physically injured or destroyed providing such loss of use is caused by an occurrence during the policy period.

Occurrence

- An accident, including continuous or repeated exposure to conditions which result in bodily injury or property damage neither expected nor intended from the standpoint of the insured . . .

CLARK WILSON 41

**WHAT THE WRAP
DOES NOT COVER?**

CLARK WILSON 42

No coverage for faulty workmanship

- The Wrap will not apply to liability for damage to that particular part of any property where:
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
- Property damage that occurs during the completed operations period is likely an exception to this exclusion

CLARK WILSON 43

No coverage for damage to the project

- The Wrap will not apply to liability for injury to or loss of use of property:
... forming part of or to form part of the project insured ...

This exclusion does not apply during any extension beyond the expiry date of this policy with respect to the Completed Operation Hazard as defined herein.

CLARK WILSON 44

Exception under the Completed Operations Hazard

- Generally the Wrap will extend completed operations coverage for a period of 24 months after the project is complete
- Definition of Completed Operations Hazard
... means liability arising out of the operations in connection with the project insured hereunder by or on behalf of the Insured because of Bodily Injury or Property Damage, but only if such Bodily Injury or Property Damage result from an Occurrence after such operations have been completed or abandoned by or on behalf of the Insured.
- Liability for injury to property forming part of the project is covered during the completed operations period

CLARK WILSON 45

Other Exclusions

The Wrap does not cover liability arising out of:

- Injury sustained by employees of the insured when entitled to benefits under any Worker's Compensation Statute
- Injury to property owned or occupied by or rented to the insured (including tools and equipment)
- The use and operation of a motor vehicle
- The discharge of pollutants
- The insured's intentional acts or criminal conduct
- The failure to render professional services

CLARK WILSON

46

OTHER INSURANCE

CLARK WILSON

47

General Liability Insurance

- Normally construction contracts require that parties must continue their general liability insurance
- There may be gaps in the insurance afforded under the Wrap or liability may continue after the Wrap has expired
- Existing and ongoing general liability insurance should not be reduced or terminated



CLARK WILSON

48

Other Insurance Provision in the Wrap

- The Wrap is intended to be primary:
***If any Insured hereunder has any other insurance against loss covered by this Policy** except for insurance which is written specifically to cover in respect of the project insured herein, it is agreed that **this Policy shall be primary insurance** and such other insurance shall be excess of the limits stated herein.*
- Subject to "other insurance" provisions in the competing policy


CLARK WILSON 49

CONCLUSION

CLARK WILSON 50

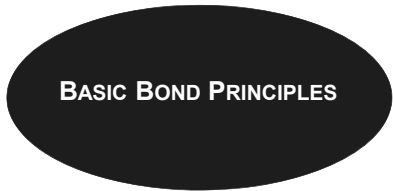
Risk Management on Construction

Construction Bonds



Scott Lamb
Partner
604 643 3103
slamb@cwilson.com

CLARK WILSON 51



BASIC BOND PRINCIPLES

CLARK WILSON
52

A Tripartite Relationship

- One party, the “**Surety**” will guarantee that another party, the “**Principal**”, will fulfil its obligations to the third party, the “**Obligee**”.
- If Principal defaults in its obligations to the Obligee, Surety will come to assist to remedy that default.
- Immediate financial burden associated with a Principal's default is transferred from Obligee to Surety.

CLARK WILSON
53

Not Insurance

Insurance	Bonds
<ul style="list-style-type: none"> • Two-party agreement between the Insured and an Insurer. • Triggered by an insurable (accidental) event. • Engage to pay the loss measured upon the happening of a defined contingency. • Typically exclude cover for fixing or finishing defective or incomplete work or materials and only cover resulting physical damage to other items. • Insurer who pays out on a policy cannot usually recover against the Insured who purchased the policy. 	<ul style="list-style-type: none"> • Three-party agreement between the Principal, a Surety and an Obligee. • Triggered by the Principal's default. • Bound to make good the default which the Principal was or should be liable to pay or make good. • Surety will pay for pure economic loss or the cost of completing the Principal's obligation, even if no damage. • Surety who pays on a construction bond is entitled to seek recovery from the defaulting Principal who purchased the bond by way of the indemnities the Surety likely required to issue such bond.

CLARK WILSON
54

For Example – Force and Effect

- Surety may not be liable for claims brought under a bond if a Principal fails to execute and deliver that bond to the Obligee.
- *Paul D'Aoust Construction Ltd v Markel Insurance Co of Canada*, [1999 CanLII 1732](#) (ON CA), aff'd [2001 SCC 84](#)



CLARK WILSON

55

Triggering the Bond and Giving Notice

- Bond is not triggered until Principal actually defaults on its obligations to Obligee. Obligee need not first exhaust other options, such as filing a lien claim or suing Principal.
- *Marigold Holdings Ltd v Norem Construction Ltd*, [1988 CanLII 3490](#) (ABQB)
- Once default confirmed, Obligee provides a Notice of Default within notice requirements set out in the bond, which typically requires such notice be in writing and delivered within a certain time.

CLARK WILSON

56

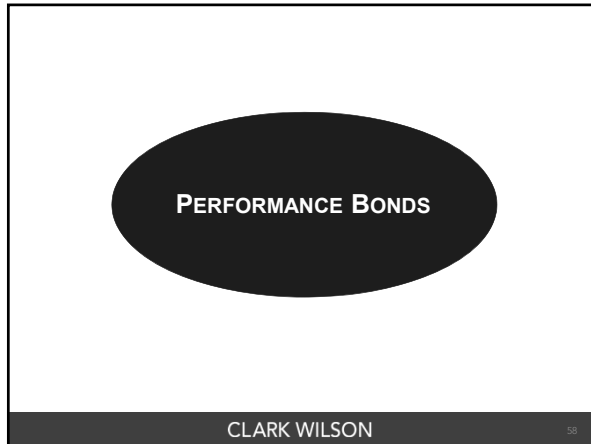
Triggering the Bond and Giving Notice – cont'd

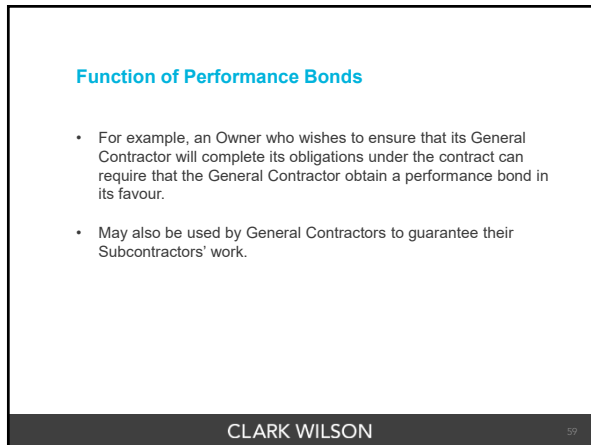
- However, Obligee who fails to strictly meet these notice requirements may not always forfeit their rights under the bond, since the Courts have before held that a "compensated" surety will not usually escape liability unless it can show that improper notice caused significant harm.
- *Citadel Assurance v Johns-Manville Canada Inc*, [1983 CanLII 52](#) (SCC)

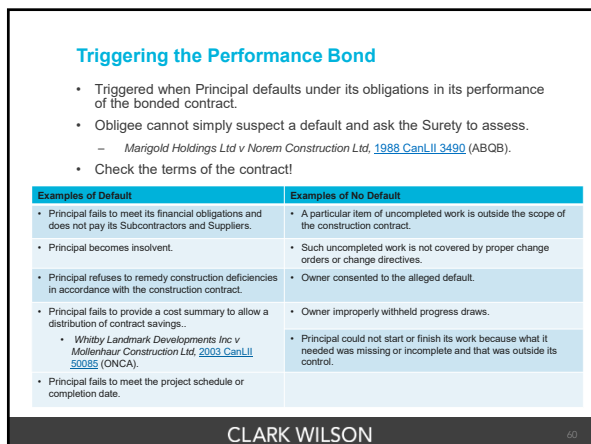


CLARK WILSON

57

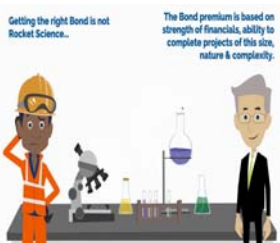






Making a Claim on the Performance Bond

- Obligees notify by way of a Notice of Default within the time required in the bond.
- If Obligees fail to give proper notice then they may lose their right under the bond where such delay prejudices the Surety.



CLARK WILSON

61

Suing on the Performance Bond

- If Obligees wish to sue on the performance bond, they must do so within the timeline stipulated on the bond.
- Often within two years from date on which final payment under the contract fell due, not when the last payment is made.
- But if no limitation period is provided for under the performance bond, then established by the appropriate legislation.

CLARK WILSON

62

Surety's Obligations to Investigate on the Performance Bond

- Surety conducts an investigation as to whether Principal has defaulted.
- Surety has a duty to Obligees, Principal and Indemnitors to investigate the default to determine whether amounts are payable under the terms of the bond.
- Surety may breach where it begins remedying the default when there is none, assumes any liability if Principal had a legitimate defence to Obligees' claims, does not complete work in a cost-effective way, or does more work under the contract than is necessary to be done to complete the contract.

CLARK WILSON

63

Surety's Defences on the Performance Bond

For example:

- If a bond was not executed or delivered by a party to it.
 - *Magna Contracting & Management Inc v Newfoundland*, [2001 CanLII 33783](#) (NLSC); *Larbonne v Shore*, [1928 CanLII 319](#) (BCCA); *Paul D'Aoust Construction Ltd v Market Insurance Co of Canada*, [1999 CanLII 1732](#) (ON CA), aff'd [2001 SCC 84](#).
- If Obligee did not give prompt notice to the Surety of the default and this prejudices the Surety.
 - *Whitby Landmark Developments Inc v Mollenhaur Construction Ltd*, [2003 CanLII 50085](#) (ONCA).
- If Principal is not actually in default of its obligations.
- If Obligee has also not met its obligations under the contract.

CLARK WILSON 64

Surety's Defences on the Performance Bond - cont'd

- If a material change to the bonded contract without the consent of Surety and is prejudicial to it. A variation will be often implied if there are provisions in the contract for changes in the work though consideration will be taken as to whether the change benefits Surety.
 - *Doe et al v Canadian Surety Co*, [1936 CanLII 9](#) (SCC); *Preload Co of Canada v City of Regina et al*, [1959 CanLII 94](#) (SCC); *Truro (Town) v Toronto General Insurance Co*, [1973 CanLII 169](#) (SCC); *Five-Fifty Beauty Street Ltd Partnership v Markwood Construction Ltd*, [1987 CanLII 2565](#) (BCCA); *St John's Metropolitan Area Board v William J Vokey & Sons Ltd et al*, [1988 CanLII 5448](#) (NLSC) aff'd [1991 CanLII 6860](#) (NLCA).

CLARK WILSON 65

Surety's Defences on the Performance Bond - cont'd

- Where Obligee takes remedial action following the default that prejudices the Surety's rights such as making improper payments to the Principal or fixing the default without Surety's knowledge or consent.
 - *Nickel Investments Ltd v Great American Insurance Co*, [1974 CanLII 603](#) (ONSC); *Town of Mulgrave v Simcoe and Erie General Insurance Co*, [1977 CanLII 1813](#) (NSCA).
- If at time the bond was issued, Owner misled Surety as to the risk it was undertaking to the prejudice of Surety.
 - *Doe et al v Canadian Surety Co*, [1936 CanLII 9](#) (SCC).

CLARK WILSON 66

Surety's Options to Remedy the Default on the Performance Bond

- For example, Surety may remedy the Principal's default.
- For example, Surety may complete the contract in accordance with terms and conditions.
- For example, Surety may submit a bid by a Contractor for completion.
 - Surety may issue tenders to identify a contractor who will complete the contract in accordance with its terms and conditions and put a bid to the Obligor. Once the bids are reviewed, a decision is made as to which bid will complete the contract in accordance with its terms and conditions and the Surety will make sufficient funds to pay the costs of completion.
 - Obligor must fulfill its obligation to attempt to work with the Surety to determine the most appropriate bidder. Some discretion to refuse the Surety's proposed replacement contractor depending on the wording of the bond such as if the bidder must be a "responsible bidder".
 - *Lac La Ronge Indian Band v Dallas Contracting Ltd*, [2004 SKCA 109](#);
Ellis-Don Construction Ltd v Halifax Insurance Co, [1996 CanLII 1588](#) (ONCA).

CLARK WILSON

67

Surety's Options to Remedy the Default on the Performance Bond – cont'd

- Bond may not cover more than the costs of completion of the project, such as liquidated damages, though the law on same has been conflicting on this issue.
 - *Whitby Landmark Developments Inc v Mollenhaur Construction Ltd*, [2003 CanLII 50085](#) (ONCA) vs. *Lac La Ronge Indian Band v Dallas Contracting Ltd*, [2004 SKCA 109](#).
 - *Vermilion & District Housing Foundation v Binder Construction Limited*, [2017 ABQB 365](#).
- For example, Surety can make a cash payment to the Owner and obtain a release.

CLARK WILSON

68

**LABOUR AND MATERIAL
PAYMENT BONDS**

CLARK WILSON

69

Function of the Labour and Material Payment Bond

- For example, Owner wishes to ensure General Contractor pays its Subcontractors so property remains free of liens and move according to schedule.



CLARK WILSON

70

A "claimant" under the Labour and Material Payment Bond

- Bond creates a trust relationship with the Obligee as Trustee for the benefit of Subcontractors as Claimants.
- S. 48 of BC's *Law and Equity Act, RSBC 1996, c 253* permits a Claimant to claim against the Surety.

CLARK WILSON

71

A "claimant" under the Labour and Material Payment Bond – cont'd

- To make a claim on the bond a Subcontractor or Supplier must first qualify as a "Claimant". To do so, must establish:
 - (1) that it has a direct contract with Principal;
 - (2) for labour or material or both;
 - (3) which is used or reasonably required for use in the performance of the contract between Principal and Obligee.

CLARK WILSON

72

Obligee's Duty to Disclose Existence of Labour and Material Payment Bond

- A lien holder or beneficiary of a trust under the BLA is entitled to demand from the owner the particulars of any available labour and material payment bond, under s. 41(1)(a)(iv) of BC's *Builders Lien Act*, [SBC 1997, c 45](#).
- Obligee as a Trustee has obligation to disclose the existence of this bond to a beneficiary:
 - *Valard Construction Ltd v Bird Construction Co*, [2018 SCC 8](#).

CLARK WILSON

73

Making a Claim on the Labour and Material Payment Bond

- Claimant can pursue payment under both a lien and bond at same time but need not first exhaust its builders lien rights.
- Claimant must provide notice to the parties and commence an action to claim under the bond within timeline and processes stipulated in the bond.
 - Typically written notice of claim to the Surety, the Principal and the Obligee within 120 days after the date on which the Claimant last provided work or furnished the materials for the project.

CLARK WILSON

74

Making a Claim on the Labour and Material Payment Bond – cont'd

- Legal action to enforce a claim under the bond usually prior to the expiry of one year following the date Principal ceases work on the bonded contract, after Claimant's work is completed or Claimant's materials are last supplied. Not always clear.
 - *Controls & Equipment Ltd v RAMCO Contractors Ltd et al*, [1998 CanLII 28525](#) (NBQB), aff'd [1999 CanLII 32511](#) (NBCA).
- Failure to give notice in timely fashion generally treated as imperfect compliance and a less serious breach than failing to bring an action within a stipulated time frame. If no prejudice to the Surety, the Claimant may be relieved.
 - *Falk Brothers Industries Ltd v Elance Steel Fabricating Co*, [1989 CanLII 38](#) (SCC).

CLARK WILSON

75

Amount of Claim on the Labour and Material Payment Bond

- Covers the cost of materials, labour, and services reasonably used in the furtherance of the work as required in the contract between the Principal and the Oblige and not damages relating to delay, increased overhead, or loss of profits.
- Bond provides a maximum liability. Claims may exceed the amount available under the bond and Surety will have to decide whether it makes a payment in accordance with the time of receipt of notice or whether or not payments should be made *pro rata*.

CLARK WILSON

76

Surety's Defences on the Labour and Material Payment Bond

For example:

- If Claimant fails to give notice or commence action within the required time.
- If party fails to constitute as a "Claimant".
- If the limits under the bond have been exceeded.

CLARK WILSON

77

LIEN BONDS

CLARK WILSON


78

Function of the Lien Bond

- S. 24 of BC's *Builders Lien Act*, [SBC 1997, c 45](#) permits an Applicant to apply to have claims of lien cancelled upon the posting of sufficient alternative security. Often cash, a letter of credit, or a lien bond.
- Lien bonds guarantee that a lien claimant will be paid if it is ultimately able to prove that it has a valid construction lien and at the same time will ease the cash burden and allow project funds to flow while the dispute between the parties are being resolved.
- Suitable security where there is no concern about the financial stability of the Surety and the Surety is authorized by the Registrar of the BC Supreme Court.

– *IDL Projects Inc v M3 Steel (Kamloops) Ltd*, [2011 BCSC 1600](#)

CLARK WILSON 79



HOLDBACK BONDS

CLARK WILSON 80

Function of the Holdback Bond

- Intended to stand in the place of the holdback retained by an Owner, Contractor, or Subcontractor under BC's *Builders Lien Act*, [SBC 1997, c 45](#).
- Advantageous because it would provide a General Contractor or Subcontractor with increased working capital and thus enhance its ability to perform work or reduce its financing costs.


CLARK WILSON 81

CONCLUSION

CLARK WILSON 82

Risk Management on Construction Projects

Warranties



Rosalie Clark
Partner
604 643 3190
rdark@cwilson.com

CLARK WILSON 83

CONTRACTUAL WARRANTY OBLIGATIONS

CLARK WILSON 84

Contractual Warranty Obligations

- In addition to the general, common law obligation of a contractor to perform specific construction work in a "good and workmanlike manner", construction contracts will typically also include requirements for specific, contractual warranty obligations.
- In standard form construction contracts, the typical warranties include requirements for the Contractor to:
 - perform the work as required by the construction documents;
 - correct any defects or deficiencies that occur within the warranty period; and
 - obtain any extended warranties that may be required for specific products or materials as specified in the Contract Documents (such as a manufacturer's warranty)

CLARK WILSON

85

Contractual Warranty Obligations – cont'd

- The standard form of warranty obligations may be modified by supplementary conditions.
- Owners and Contractors should consider:
 - when the running of the warranty period will be triggered (for example, at Substantial Completion, Ready-for-Takeover, or Early Occupancy?)
 - is there an extension to the warranty if a repair becomes necessary within the warranty period?
 - is there any holdback obligation that accompanies the warranty obligation?

CLARK WILSON

86

**NEW HOME WARRANTY –
LEGISLATIVE SCHEME**

CLARK WILSON

87

New Home Warranty – Legislative Scheme

- BC introduced legislative warranty requirements for new residential construction that came into effect in July 1999 under the Homeowner Protection Act, S.B.C. 1998, c. 31 – often referred to as the “2 – 5 – 10 Warranty”.
- The Homeowner Protection Act contains specific regulations (the Homeowner Protection Act Regulations) that detail certain specific mandatory warranty conditions, standards of coverage, permitted warranty terms and permitted exclusions.

New Home Warranty – Legislative Scheme – cont'd

- What is covered by the mandatory “2 – 5 – 10” warranty?
- 2 Year Coverage
 - materials and labour:
 - 12 months on detached homes and non-common property in strata units;
 - 15 months on common property of strata buildings;
 - defects in electrical, plumbing, HVAC delivery and distribution
 - defects in exterior cladding, caulking, windows and doors that may lead to detachment or material damage
 - defects which render the home unfit to live in
 - violations of the building code

New Home Warranty – Legislative Scheme – cont'd

- 5 Year Coverage
 - defects in building envelope – including water penetration
 - 10 Year Coverage
 - structural defects
- Note that policy coverage will vary – each policy should be considered in order to determine the coverages that are available.



New Home Warranty – Legislative Scheme – cont'd

When does coverage start?

- Detached Homes:
 - Contract / Custom Homes (build on land owned by homeowner) date of first occupancy, date of first occupancy permit, or date of transfer of legal title to first owner (whichever comes first)
 - Spec. Homes (build on land owned by builder / developer) date of first occupancy or date of transfer of legal title to first owner (whichever comes first)
- Strata Homes:
 - Strata units: earliest date of first occupancy or date of transfer of legal title to first owner
 - Common property: earliest of date of first-unit occupancy in strata building or date of transfer of legal title to first owner in building

New Home Warranty – Legislative Scheme – cont'd

- Homes exempt from New Home Warranty requirements:
 - homes built by owner-builders
 - manufactured homes that have not been significantly modified
 - non-stratified hotels, floating homes, motels, dormitories, care facilities
 - multi-unit rental buildings where sale of individual unit restricted by 10-year covenant registered against title
 - social housing

New Home Warranty – Legislative Scheme – cont'd

- **General Exclusions to 2 – 5 – 10 Warranty:**
 - Landscaping
 - Non-residential detached structures (i.e. parking structures)
 - Commercial use areas
 - Roads, curbs and lanes
 - Site grading and surface drainage
 - Operation of municipal services
 - Septic tanks and fields
 - Water quality and quantity



New Home Warranty – Legislative Scheme – cont'd

- Other typical exclusions:
 - Normal wear and tear
 - Shrinkage of materials from construction
 - Use of home for non-residential purposes
 - Labour, materials and design supplied by owner
 - Damage caused by others than residential builder






New Home Warranty – Legislative Scheme – cont'd

- Other typical exclusions (cont'd):
 - Damage caused by insects and rodents
 - Failure of an owner to prevent or minimize damage
 - Acts of nature
 - Failure to maintain
- Exclusions will be specific to the policy

New Home Warranty – Legislative Scheme – cont'd

- What happens when a claim is made?
- Claim must be submitted to warranty provider and builder
- Warranty provider may ask builder to investigate or send claims representative to evaluate claim
- Note that the New Home Warranty coverage is separate and distinct from any builder warranty or manufacturers warranty

Questions?

	Satinder Sidhu Partner - Moderator 604 643 3119 SSidhu@cwilson.com		
	Scott Lamb Partner 604 643 3103 SLamb@cwilson.com		Samantha Ip Partner 604 643 3172 Sip@cwilson.com
	Rosalie Clark Partner 604 643 3190 RClark@cwilson.com		Kim Do 2021-22 Articling Student 604 643 3901 KDo@cwilson.com

These materials are necessary of a general nature and do not take into consideration any specific matter, client or fact pattern.

CLARK WILSON
