

MEMORANDUM: by Mark Frederick and David LeDrew of Miller Thomson
Advocat/Lawyers, Toronto

Date: January 16, 2018

Subject: Alberta Case Law – Building Compliance and Insurance Policy By-Law
Inclusions

The Alberta Court of Appeal's decision in *852819 Alberta Ltd v Sovereign General Insurance Company*, 2017 ABCA 76 clarified the distinction between warranty and insurance in all risk commercial property insurance. The Supreme Court of Canada recently denied leave to appeal.

In brief, this case involved ice damage to part of a commercial building's roof. The damaged areas were repaired by the insurers, but a subsequent municipal inspection required changes to the entire roof structure as the roof was not compliant with the *Alberta Building Code* on the date of the inspection and potentially on the date of the initial build.

The additional repairs cost \$527,497.46.

The plaintiff owner then sought indemnification for the additional repairs. The insurers denied coverage on the basis that the additional repairs were an unrelated deficiency in the roof that was pre-existing and not covered under the policy.

The plaintiff owner argued that the additional repair costs should be covered under the policy. The policy terms included the following:

4. PERILS INSURED

This Form, except as herein provided, insures against all risks of direct physical loss of or damage to the property insured.

2. Building By-laws: This Policy shall, and only as a result of a peril insured against, extend to indemnify the Insured without increasing the amount of insurance stated on the "Declarations Page" ... for:

(i) loss occasioned by the demolition of any undamaged portion of the building or structures;
or

(ii) the cost of demolishing and clearing the site of any undamaged portion of the building or structures; or

(iii) any necessary increase in the cost of repairing, replacing, constructing or reconstructing the building, or structures, on the same site or on an adjacent site, of like height, floor area and style, and for like occupancy; arising from the enforcement of the minimum requirements of any by-law, regulation, ordinance or law which:

(a) regulates zoning or the demolition, repair or construction of damaged buildings or structures; and

(b) is in force at the time of such loss or damage.

This extension, however, does not insure against:

(i) the enforcement of any by-law, regulation, ordinance or law which prohibits the Insured from rebuilding, or repairing on the same site or adjacent site or prohibits continuance of like occupancy ...

5.B. PERILS EXCLUDED

This Form does not insure against loss or damage caused directly or indirectly:

(l) proximately or remotely, arising in consequence of or contributed to by the enforcement of any by-law, regulation, ordinance or law regulating zoning or the demolition, repair or construction of buildings or structures, which by-law, regulation, ordinance or law makes it impossible to repair or reinstate the property as it was immediately prior to the loss.

NOR DOES THIS FORM INSURE:

(m) wear and tear, gradual deterioration, latent defect, inherent vice, or the cost of making good faulty or improper material, faulty or improper workmanship, faulty or improper design, provided, however, to the extent otherwise insured and not otherwise excluded under this Form, resultant damage to the property is insured

The plaintiff owner argued that this was not a case of a faulty roof, but the damages were linked to the peril that caused the failure of the roof in the repaired areas.

The insurers advanced two primary arguments:

1. the plaintiff did not prove that the claim related to a direct physical loss or damage that occurred during the policy period and that the loss was fortuitous; and
2. the additional repairs fell within the exclusions for latent defect, inherent vice and the cost of making good faulty or improper material, workmanship or design.

The insurers submitted that the policy was not a warranty that the building was free of defect.

At first instance and by way of summary trial, the judge held that the additional repair costs were a result of the peril insured against and the insurers were liable to pay.

In the Court of Appeal's decision, it was noted that the summary trial judge did not have a 2016 Alberta Court of Appeal decision of *Roth v. Economical Mutual Insurance Company*, 2016 ABCA 399, wherein the court held that extending coverage for pre-existing deficiencies in buildings would require that the insurer be satisfied that the property complied with all relevant by-laws. As such, aside from being an impossibility, this requirement would turn an insurer into a guarantor of construction defects and building code violations.

The Court of Appeal held in this case that the structural deficiency did not result from the ice damage and the insurers were not required to pay for the additional repair costs.

The Court of Appeal's decision is a sound synthesis of the principals of insurance, causation and damages in commercial property policies with by-law coverage. If damages stem from a building code deficiency that is not related to a covered peril, those damages should not be covered.