SUPREME COURT OF YUKON

Citation: *Yukon Energy Corporation* v. *Narrow Gauge Contracting Limited, et al.*, 2010 YKSC 38

Date: 20100719
S.C. No. 99-A0194
Registry: Whitehorse

Between:

YUKON ENERGY CORPORATION

Plaintiff

And

NARROW GAUGE CONTRACTING LIMITED, DOUGLAS GILDAY and ARCRITE NORTHERN LTD.

Defendants

Before: Mr. Justice R.S. Veale

Appearances:

James W. Rose, Q.C. and David Goult	Counsel for Yukon Energy Corporation
Ronald T. Smith	Counsel for Narrow Gauge Contracting Limited and Douglas Gilday
William G. Neen	Counsel for Arcrite Northern Ltd.

REASONS FOR JUDGMENT
(Waiver of Subrogation)

INTRODUCTION

[1] In 1996, Yukon Energy Corporation ("Yukon Energy"), contracted with Narrow Gauge Contracting Limited ("Narrow Gauge") to build a power plant expansion. Narrow Gauge contracted with Arcrite Northern Ltd ("Arcrite") as the electrical subcontractor. Yukon Energy alleges that the faulty installation of a heat trace system caused a fire (the "Fire") destroying the power plant (the "Plant"). Yukon Energy's insurers have paid out the damage claim and bring this action by way of subrogation against the contractor

and subcontractor and their insurers. Subrogation simply means that the insurer can stand in the place of the insured and claim against others at the insurer's expense and for the insurer's benefit.

[2] Narrow Gauge and Arcrite bring this stated case to determine whether the express waiver of subrogation rights clause in the Yukon Energy Corporation Insurance Policy applies to prevent a claim by way of subrogation against the Defendants.

[3] A six-month trial date is set in 2011.

THE FACTS

[4] The parties have filed an Agreed Statement of Facts which states the following:

1. The plaintiff, Yukon Energy, was the owner of a P125 power generating plant and the building in which it was contained (the "Plant").
2. The Defendant Narrow Gauge is a General Contractor which contracted with the Plaintiff to undertake an expansion of the Plant in 1996 (the "Expansion"). The Expansion involved the building of an addition to the building as well as some alterations to the mechanical and electrical systems in other parts of the Plant as set out in the Plant Expansion Contract.
3. The Defendant Arcrite is an electrical subcontractor which entered into a subcontract with Narrow Gauge to perform some of the electrical work required by the Plant Expansion Project.
4. As part of its subcontract with Narrow Gauge, in the late summer of 1996 Arcrite installed and energized an electrical heat trace system which was

to be used to heat a fuel line running from an exterior fuel tank to the inside of the Northwest corner of the Plant.

5. The work contemplated by the Plant Expansion Contract commenced in or about the spring of 1996 and was declared substantially complete on or about December 3, 1996.

6. Work to correct some deficiencies in respect to the Plant Expansion Contract was completed in the early months of 1997.

7. The City of Whitehorse issued an occupancy permit for the Expansion on April 1, 1997. The Plaintiff and its employees moved into the Expansion shortly thereafter.

8. On or about July 1, 1996, the Plaintiff obtained an Insurance Policy providing All Risks property coverage as well as Course of Construction coverage. The Insurance Policy was stated to be for a three-year term to July 1, 1999.

9. On or about October 30, 1997, a fire ignited in the Northwest corner of the Plant and substantially destroyed the Plant.

10. The fire is alleged to have been caused as a result of the faulty installation of the heat trace system which the Plaintiff alleges amounted to a breach of the Plant Expansion Contract and of a duty of care owed by Narrow Gauge, and a breach of a duty of care owed by Arcrite and others.

11. At the time of the fire, the “Consultant”, as defined in the Plant Expansion Contract, had not certified “Total Performance of the Work”, as defined in the Plant Expansion Contract.

12. The insurers who issued the Insurance Policy indemnified the Plaintiff for its loss under the Insurance Policy in an amount in excess of $15 million.

13. General Condition 8.1 of the tender Narrow Gauge submitted for the Plant Expansion Contract (which tender forms part of the Plant Expansion Contract) required that Narrow Gauge provide and maintain insurance that was written to insure the work to be performed under the Plant Expansion Contract on an “All Risks” basis granting coverage similar to that provided by the form known and referred to in the insurance industry as “All Risks” Builder’s Risk”. Narrow Gauge did obtain such insurance, but no claim was made under that policy by Narrow Gauge or any other insured.

14. The insurers who issued the Insurance Policy have brought this action as a subrogated action in the name of the Plaintiff.

[5] A letter dated December 3, 1996, from the Consultant, and attached to Paragraph 6 of the Agreed Statement of Facts, indicated that the project was “Substantially Complete” on December 3, 1996 and set out other details about holdbacks.

[6] An e-mail from the Consultant’s Solicitor, attached to paragraph 11 of the Agreed Statement of Facts, suggested that the final certificate had not been completed as of the date of the fire as no final inspection had been requested by Yukon Energy. The Plant Expansion Contract provided for a certificate of Substantial Performance (clause 14.3) and a certificate of Total Performance (clause 14.7). The certificate of Total Performance has never been issued.

The Waiver of Subrogation

[7] As this case must be decided on the actual wording of the Insurance Policy, I will set out the relevant terms.

DECLARATIONS

...

4. COVERAGE:	Section A	(i) ALL PROPERTY (ii) BOILER EXPLOSION AND MACHINERY BREAKDOWN
	Section B	COURSE OF CONSTRUCTION
	Section C	EXTRA EXPENSE

...

GENERAL CONDITIONS

(Applicable to all Sections of this policy except where specified to the contrary)

...

2. SUBROGATION:

Upon the payment of any claim under this policy the Insurers shall be subrogated to the extent of such payment to all rights and remedies of the Insured against any third party whose fault or negligence caused or contributed to the loss or damage.

It is understood and agreed that the Insurers hereby waive their rights of subrogation as against:

...

(c) any Insured (including their directors, officers, employees, servants or agents) whose fault or negligence caused or contributed to the loss or damage sustained by any other Insured;

...

(e) any contractors and/or subcontractors (including their directors, officers, employees, servants or agents) whose fault or negligence in the performance of work on behalf of the Insured during Course of Construction operations caused or contributed to the loss or damage, however, this shall not apply to architects and engineers with respect to course of construction operations.

...

8. AGENCY:

The Named Insured who obtained this policy and paid the premium therefor [as written] did so on his own behalf and as agent for others insured herein, including those referred to by general description. It is further acknowledged and agreed by the Insurers as evidenced by their acceptance of the premium paid that any person, firm or corporation coming within the description of an unnamed person insured by this policy may ratify such agency at any time for the purpose of entitlement to coverage granted by its terms for good consideration. This insurance shall not be invalidated should the interest of the Named Insured or other Insured be other than sole or unconditional ownership.

...

SECTION B

PROPERTY IN COURSE OF CONSTRUCTION OR INSTALLATION

1. INSURING AGREEMENT:

Subject to an initial estimated completed value of no more than the limit as specified in Clause 5 and in the event of loss or damage by a peril insured against in Section A, this policy covers:

> (a) Property in the course of construction, including start up and testing, installation, fabrication, alteration, erection, reconstruction, demolition, repair or undergoing any test or while completed and operational but still at the risk of any named Insured hereunder;
>
> ...
>
> 8. TERMINATION OF LIABILITY:
>
> All property in course of construction shall be deemed to be included during the period of construction operations and covered until the said property has been finally completed, tested and accepted (and during any further period provided for under the contract entered into by the Insured) irrespective of the policy expiry or cancellation.

ISSUES

[8] The following are the issues:

1. Should the waiver of subrogation clause be interpreted to waive subrogation against contractors and subcontractors when the date of fault or negligence occurred during the Course of Construction and the date of loss occurred after construction was substantially completed?
2. If the waiver of subrogation clause is interpreted so that both the date of fault and date of loss must be within the course of construction, was the plant expansion in the course of construction at the date of loss on October 30, 1997?

Interpretation of Insurance Policies

[9] The parties are in agreement about the general principles of interpretation of insurance policies:

1. Insurance policies are to be interpreted using the normal principles of contractual interpretation: *Consolidated Bathurst Export Ltd. v. Mutual Boiler & Machinery Insurance Co.,* [1980] 1 S.C.R. 888, at para 26. The court confirmed that a proper interpretation requires that:

   a. the whole of the contract must be considered to determine the true intent of the parties at the time of entry into the contract;

   b. a literal meaning should not be applied where to do so would bring about an unrealistic result or a result which would not be contemplated in the commercial atmosphere in which the insurance was contracted;

   c. where the words may bear two constructions, the more reasonable one which produces a fair result, or a sensible commercial result should be preferred.

2. Where a contract is unambiguous, a court should give effect to its clear language, reading the contract as a whole: *Non-Marine Underwriters, Lloyd's of London v. Scalera*, 2000 SCC 24 at para. 71.

3. The court should construe ambiguities found in the insurance contract in favour of the insured (the *contra proferentem* rule) *Scalera*, cited above, at para. 70.

4. A corollary of the *contra proferentem* rule is that coverage provisions should be construed broadly and exclusion provisions narrowly: *Scalera*, para. 70.

Position of the Insurer

[10] Counsel for Yukon Energy states that the Defendants are not named as Insured and must rely on the General Condition 2(e) to argue that subrogation against them has been waived.

[11] General Condition 2(e) specifically refers to work during Course of Construction operations, which counsel says links it to Section B coverage.

[12] Counsel for Yukon Energy submits that the principle established in *Commonwealth Construction Co. v. Imperial Oil Ltd.*, [1978] 1 S.C.R. 317, applies to recognize that all tradesmen have an insurable interest during the completion of construction to avoid the necessity of fighting between themselves should an accident occur involving the responsibility of one of them (para. 16). However, counsel submits this loss did not occur during the course of construction.

[13] Counsel for Yukon Energy relies on *Daishowa-Marubeni International Ltd. v. Toshiba International Corp.,* 2003 ABCA 257, at para. 59:

> The special relationship which contractors, subcontractors and other non-owners have with the property under construction ceases, however, upon completion of the project. This was made clear in Commonwealth where it was held that the insurable interest was based on the joint efforts of the parties in achieving the common goal of completion of construction.

[14] As to the timing of the negligent act and the argument that General Condition 2(e) merely requires that the negligent act occur during the course of construction, counsel submits that the phrase “during course of construction operations” applies not only to the negligent act but also temporally to the “loss or damage”. Thus, counsel

submits that the waiver of subrogation applies only for losses during construction and not after. This was the result in *Toshiba*.

The Position of the Contractors

[15] Counsel for the contractors submit that the wording of the waiver of subrogation in General Condition 2(e) is clear and unambiguous that the Insurer has waived its right of subrogation for fault or negligence of a contractor or subcontractor during the course of construction regardless of when the loss or damage actually occurs.

[16] Counsel submit that this literal interpretation is consistent with the Course of Construction coverage in Section B which extends coverage to property “while completed and operational but still at the risk of the named Insured hereunder.”

[17] Counsel for the contractors submit that to the extent there is any ambiguity, it should be construed against the Insurer.

[18] Alternatively, counsel for the contractors submit that the Course of Construction coverage was in effect at the time of the fire thereby prohibiting the insurers’ subrogation claim. In this submission, the contractors accept the principle relied on by the insurer in *Commonwealth Construction*, cited above, but submit that the wording of the Course of Construction coverage extends to the date of the fire.

ANALYSIS

Issue 1: Should the waiver of subrogation clause be interpreted to waive subrogation against contractors and subcontractors when the date of fault or negligence occurred during the Course of Construction and the date of loss occurred after construction was substantially completed?

[19] It is my view that the waiver of subrogation contained in General Condition 2(e) should be interpreted to apply to fault or negligence of contractors and subcontractors during course of construction operations whether the loss or damage occurred during or after the course of construction.

[20] General Condition 2(e) states that the insurer waives subrogation:

a) against any contractor or subcontractor;

b) whose fault or negligence in the performance of work during the course of construction operations;

c) caused or contributed to the loss or damage.

[21] The insurer contends that the words “loss or damage” are “temporally” connected to the words “Course of Construction operations”. I do not agree. The words “fault or negligence” are modified by the words “during the Course of Construction operations” but there is no such wording following “loss or damage.” Furthermore, if the Insurer intended to limit the loss or damage covered by the waiver of subrogation clause, express wording to that effect is required. In any case, even if I concluded that the wording was ambiguous, which I do not, it would be interpreted in favour of the contractors and subcontractors (the *contra proferentum* rule) and against the insurer.

[22] The General Conditions in the Insurance Policy were expressed to apply to all Sections of the policy “except where specified to the contrary.” Thus, General Condition 2(e) cannot be linked to the course of construction coverage unless expressly stated.

[23] The insurer submits that the words “Course of Construction” refers to Section B Course of Construction Coverage. That may be the case but it does not follow that the loss or damage must therefore occur in the course of construction.

[24] The insurer relies upon the case of *Commonwealth Construction*, cited above. In that case, Commonwealth was subcontracted to install process piping in a fertilizer plant constructed for Imperial Oil Ltd. During the course of the installation a fire occurred that, for the purpose of the case, was the responsibility of Commonwealth. The Supreme Court of Canada concluded that the “Trustee Clause”, included the owner was insured “as trustee for the benefit of any and all Contractors ... relating to the construction of the project ...” was sufficient to give all the trades involved in the construction of the plant an insurable interest.

[25] The Court also expressed the underlying policy reason as follows:

> ... On any construction site, and especially when the building being erected is a complex chemical plant, there is ever present the possibility of damage by one tradesman to the property of another and to the construction as a whole. Should this possibility become reality, the question of negligence in the absence of complete property coverage would have to be debated in court. By a recognizing in all tradesmen an insurable interest based on that very real possibility, which itself has its source in the contractual arrangements opening the doors of the job site to the tradesmen, the courts would apply to the construction field the principle expressed so long ago in the area of bailment. Thus all the parties whose joint efforts have one common goal, e.g., the completion of the construction, would be spared the necessity of fighting between themselves should an accident occur involving the possible responsibility of one of them.

[26] It is significant in my view that the court considered it a general common law principle that subrogation is not permitted against contractors and subcontractors. However, as stated in *Somersall v. Friedman*, 2002 SCC 59, at para. 56, equitable insurance principles of subrogation may be altered by the terms of the contract between the parties.

[27] The issue of the timing of Imperial Oil's loss was not specifically discussed in *Commonwealth Construction* because the "Trustee Clause" extended the benefit of the Insurance Policy to "all Contractors who heretofore or hereafter enter into a contract with the Owner, or other insured contractor relating to the construction of the project described in Clause 1 of the wording." Clause 1 covered "all materials, machinery, equipment including labour charges ... to be used or incidental to the fabrication, installation, completion, upkeep, expansion, modification, and all other changes or extensions" pertaining to the fertilizer plant. In other words, the loss in *Commonwealth* was clearly included in the actual wording of the Insurance Policy under the word "installation". In my view, the trigger for coverage was loss or damage incidental to installation. This must be contrasted with the wording in Yukon Energy Insurance Policy which focusses upon "fault or negligence in the performance of work on behalf of the Insured during Course of Construction operations". As I stated earlier, the wording of the Insurance Policy in the case at bar does not require the loss or damage to occur during the course of construction.

[28] The insurer of Yukon Energy also relies on the case of *Toshiba International Corp.*, cited above. Again, this case is distinguishable on its facts and in the wording of the applicable insurance policy. In *Toshiba*, Toshiba designed and delivered a turbine generator to the pulp mill which commenced operation in 1990. In October 1994, Toshiba conducted maintenance and overhaul which was completed on or about October 31, 1994. The generator operated for a further year without incident, but on November 5, 1995, it failed, causing irreparable damage to the generator and economic loss to the pulp mill (paras. 7 – 12).

[29] The Alberta Court of Appeal concluded that the failure in 1995 did not occur while the pulp mill was “undergoing alterations, renovations, construction, reconstruction, installation or maintenance”, as per the insurance policy in place.

[30] In *Toshiba*, the Court confirmed at paras. 48 and 49 as follows:

> [48] In the case at bar, the respondents were entitled to status as insureds under the Policy when the pulp mill was under construction and during the maintenance shutdown in October 1994. Coverage did not, however, extend beyond completion of the project or completion of the October 1994 maintenance and overhaul.
>
> [49] The wording of the Schedule specifically limited the respondents' insurable interest in the insured property to times when it was "undergoing alterations, renovations, construction, reconstruction, installation, or maintenance". The loss payable provision adopts the same wording. The intention to limit the status of the respondents as insureds to periods when certain operations were in progress is clear.

[31] Thus, in *Toshiba*, the loss payable provision adopted the same wording as the clause setting out the insurable interest. In the Yukon Energy Insurance Policy by contrast, there is no alignment of the timing of the fault or negligence with the loss or damage. The *Toshiba* case is also distinguishable to the extent it did not involve the interpretation of a waiver of subrogation at all.

[32] I conclude that the Yukon Energy’s insurer cannot rely upon the cases of *Commonwealth Construction* and *Toshiba* because the policy wording is not the same as in the case at bar. It is the precise wording of the waiver of subrogation clause that must be interpreted rather than applying the common law principle of waiver of subrogation in general terms.

[33] There is also a valid policy reason for concluding that the Insurer waived its right to subrogation based on negligence that occurred during the course of construction

even where the damage did not occur at the same time. Loss or damage in complex construction projects does not necessarily occur at the same time as the negligent act. It makes little sense, for the purpose of a waiver of subrogation, to provide coverage for immediate damage but not latent or delayed damage or loss such as may occur with the deterioration of a heat tape. The result would be that damage occurring on the last day of the course of construction would be protected from subrogation but damage or loss one day after would result in litigation. This interpretation would encourage long and costly litigation rather than reduce the frequency of litigation in complex construction projects.

[34] There is one further argument that arises in the Agreed Statement of Facts. It could be argued that the existence of General Condition 8.1 in the Instruction for Tenderers, which required the Contractor (Narrow Gauge in this case) to take out comprehensive General Liability Insurance and comprehensive “All Risks” Builder’s Risk supports the interpretation of the Insurer that it was the intention of the parties that the Contractor would take out its own property insurance and therefore could not rely upon the waiver of subrogation.

[35] This submission has been answered in *Sylvan Industries Ltd. v. Fairview Sheet Metal Works Ltd.*, [1994] 5 W.W.R. 449 (B.C.C.A.). The facts there were that the owner had a policy covering unnamed insureds. A fire allegedly caused by a subcontractor was paid out under the owner’s policy and the insurer brought a subrogated claim against the contractor and subcontractor. Both the owner and the contractor were required by contract to provide insurance, albeit coordinated between themselves. The

insurer for Sylvan argued that to be covered as an unnamed insured, the party must prove an intention to insure itself.

[36] The British Columbia Court of Appeal concluded that the policy used language that conferred unnamed insured status on contractors and subcontractors by necessary implication (paras. 16 and 17).

[37] In my view, the requirement for Narrow Gauge to provide insurance coverage does not negate the precise wording of the Yukon Energy Insurance Policy. The same conclusion was reached in *Janeland Developments Inc v. Michelin Masonry Inc.*, [1996] O.J. No. 513 (Gen. Div.), at para. 15.

[38] In summary, I find that the proper interpretation of the waiver of subrogation clause in the Yukon Energy Insurance Policy is that it is triggered by the date of the fault or negligence and not the date of loss. Therefore the Insurer of Yukon Energy cannot claim in subrogation against the contractors and subcontractors on this power plant expansion contract.

Issue 2: If the waiver of subrogation clause is interpreted so that both the date of fault and date of loss must be within the course of construction, was the plant expansion in the course of construction at the date of loss on October 30, 1997?

[39] Alternatively, counsel for the Defendants submit that if the interpretation is that the loss or damage must occur in the course of construction, the wording of the Insurance Policy itself extends the course of construction coverage to include the warranty period.

[40] This submission is based upon the wording of Section B Property in Course of Construction or Installation where Section 1 states that the policy covers:

> Property in the course of construction, including start up and testing, installation, fabrication, alteration, erection, reconstruction, demolition, repair or undergoing any test or while completed and operational but still at the risk of any named Insured hereunder;

[41] The words “Property ... while completed and operational but still at the risk of any named Insured hereunder” can only refer to Yukon Energy as it is the only named Insured in the Insurance Policy.

[42] This alternative submission also relies on the Section 8 Termination of Liability clause under Section B (“Property in Course of Construction or Installation”) which extends the construction operations to include “any further period provided for under the contract entered into by the Insured.”

[43] The Instruction to Tenderers has relevant provisions to a warranty period:

> 6. WARRANTY HOLDBACK
>
> (a) Upon substantial completion of the contract all funds due to the Contractor will be released except five percent of the final contract amount which will be held for the one year from substantial completion of the contract. This one year period shall be known as the “Warranty” period.
>
> ...
>
> **GENERAL CONDITIONS**
>
> 13. SUBSTANTIAL PERFORMANCE OF THE WORK
>
> Substantial Performance of the Work is as defined in the lien legislation applicable to Place of the Work. If such legislation is not in force or does not contain such definition, Substantial Performance of the Work

> shall have been reached when the Work is ready for use or is being used for the purpose intended and is so certified by the Consultant.
>
> 14. TOTAL PERFORMANCE OF THE WORK
>
> Total Performance of the Work means when the entire Work, except those items arising from the provisions of GC24 – WARRANTY, has been performed to the requirements of the Contract Documents and is so certified by the Consultant.

[44] I conclude that the Section B references to “course of construction”, read in conjunction with the warranty period of one year in the Instruction to Tenderers, extend the course of construction coverage for at least one year after substantial completion/performance of construction, which would include the date of this Fire and bar any subrogation claim against Narrow Gauge and Arcrite.

SUMMARY

[45] To summarize, the subrogated claim of the Plaintiff is dismissed with costs. The express wording of the waiver of subrogation clause prohibits a claim against the contractor and subcontractor for fault or negligence that occurred during the course of construction even where the damage did not arise until a later date.

VEALE J.