RENOVATION CONTRACTS: AN INSURANCE TRAP?

By: Bill Preston

For renovation contracts, Consultants often simply use a standard CCDC 2-2008 contract form without altering General Conditions GC 9.1.1 and 9.1.3 (in the 1982 rendition they are GC 21.1 and 22.1). It seems that no serious consideration is given to two important matters:

1. Is there a significant difference between replacement cost and depreciated value cost of the Owner's adjacent property, which the Owner doesn't or cannot expect to pay for if damage occurs during construction?

2. And, if damage does occur to this adjacent property of the Owner, is it sufficiently insured for cases where the damage was caused by an "Act of God" or by an uninsured third party rather than the negligence of the Contractor or the subtrades?

How can these issues be important? What are the available risk management options? I hope my following comments will shed some light.

It is not exceptional that Consultants will simply use an unaltered CCDC 2-2008 for a roof replacement project to a 30-year-old school. The below General Conditions of this form can be very troublesome:

> GC 9.1.1 The *Contractor* shall protect … *the Owner's* property … adjacent to the … *Work* from damage which may arise as a result of the *Contractor's* operations under the *Contract*, and shall be responsible for such damage, except …
>
> .1 errors in the *Contract Documents*;
>
> .2 acts … by the *Owner*, the *Consultant*, other contractors …
>
> GC 9.1.3 Should the *Contractor* in the performance of the *Contract* damage the *Owner's* property adjacent to the *Place of Work*, the *Contractor* shall be responsible for making good such damage at the *Contractor's* expense.

Further, elsewhere in CCDC 2 the trap is developed by the General Conditions which only require the Contractor to supply the following insurance:

All Risk Property Policy	**- which does not cover the Owner's adjacent property**
General Liability Insurance	**- which does not pay replacement value, nor cover "Acts of God" nor third parties (i.e. where the Contractor's performance was reasonable and careful)**

So, what happens if there is a tornado with more than record rainfall, and the "experts" agree that there is a $250,000 difference between replacement cost and depreciated value cost to fix damages to the school's interior? Or, what happens if the protection measures which the Contractor took were "reasonably cautious", yet harm occurred to the interior of the school because construction operations were on-going at the time of the rainfall?

Sure, by General Conditions GC 9.1.1 and 9.1.3 the Contractor is responsible. But, these General Conditions do not prescribe responsibility for replacement costs. Rather, the word used is "damage". In this situation, the School Board is going to suffer a $250,000 cash crunch unless it has independently carried replacement coverage for property damage, because it is my opinion that the word "damage" is a depreciated value measure, not a replacement cost measure. I have not been able to find any law cases specifically on point, but this interpretation is consistent with the common law cases of like circumstances (see: *Patrick* v. *Hagblom*, where the Saskatchewan Court of Appeal dealt with a deficient chimney construction which caused a fire destroying the whole house) but not involving CCDC 2. Also, making the Contractor only responsible for depreciated value costs is consistent with the type of insurance which the General Conditions of the CCDC 2 require from the Contractor.

In the latter case (i.e. a tornado where protection measures were reasonable), the Contractor has no insurance! That's not to say that the Contractor can avoid contractual liability to the Owner as per GC 9.1.1. and 9.1.3, but if the damage to the Owner's property is considerable, there is a real risk to the Owner that the Contractor will simply close its doors and become judgment-proof.

So, what are the available risk management options? It seems to me that, if replacement cost insurance is what the Owner's cash flow circumstances require, then Consultants ought to be recognizing this and, by Supplemental General Conditions, specify that the builder provide replacement cost coverage for both the Work and the Owner's adjacent property damage. That, or have the Owner buy such coverage naming the Contractor as a co-insured, and then, by a Supplemental General Condition, removing the requirement of the Contractor to provide an all-risk property policy. By either management tool, there is then only one insurance adjuster, while the hassle of delay and costs to answer the questions whether someone was negligent and who will pay the difference between depreciated value and replacement costs are obviated. Is there

much opportunity for lawyers to make a career out of working such disputes? You betcha! Just consider that the Kelsey Institute fire damage took the Court system at least 6 years to resolve.