

## Sorting Out *Whitby Landmark*

Duncan Glaholt & Markus Rotterdam  
Glaholt LLP

### 1. Introduction

Is this a case of irreconcilable appellate level decisions; or is it simply a tempest in a teapot? At the very least, it is a fascinating object lesson in the growth of common law. It has been observed that growth in common law occurs in a circular motion:

In the long run, a circular motion in judicial reasoning can be seen. The first stage is the creation of the legal concept which is built up as cases are compared. The period is one where the court fumbles for a phrase. Several phrases may be tried out; the misuse or misunderstanding of words itself may have an effect. The concept sounds like another, and the jump to the second is made. The second stage is the period when the concept is more or less fixed, although reasoning by example continues to classify items inside and outside of the concept. The third stage is the breakdown of the

concept, as reasoning by example has moved so far ahead as to make it clear that the suggestive influence of the word is no longer desired.

The process is likely to make judges and lawyers uncomfortable. It runs contrary to the pretense of the system. It seems inevitable, therefore, that as matters of kind vanish into matters of degree and then entirely new meanings turn up, there will be an attempt to escape into some overall rule which will make the reasoning look deductive.<sup>1</sup>

With *Whitby Landmark*,<sup>2</sup> and now *Lac La Ronge*,<sup>3</sup> we see the very beginning of this cycle and can expect, and predict, progress through the remaining two stages of this “circular motion” over the coming years.

## ***2. Whitby Landmark Development Inc. v. Mollenhauer Construction Ltd.***

When the trial decision in *Whitby Landmark* came down in October, 2000, it was hailed (in some circles, reviled in others) as an

---

<sup>1</sup> Edward H. Levi, *An Introduction to Legal Reasoning* (Chicago: University of Chicago Press, 1949) at pp. 8-9.

<sup>2</sup> *Whitby Landmark Development Inc. v. Mollenhauer Construction Ltd.* (2000), 4 C.L.R. (3d) 1 (Ont. S.C.J.); affirmed (2003), 67 O.R. (3d) 628 (C.A.).

<sup>3</sup> *Lac La Ronge Indian Band v. Dallas Contracting Ltd.*, 2004 SKCA 109 (C.A.).

incremental expansion of the rights of obligees under performance bonds, allowing them to look to the surety under standard bond language for not only “sticks and bricks”, but also bonus/penalty provisions of a bonded contract. *Whitby Landmark* was viewed by some lawyers as the thin end of a long-overdue wedge on surety liability. This prompted a strong, well-reasoned caution by one of the co-authors of the leading text on surety law.<sup>4</sup> Let us look at the case.

The facts in *Whitby Landmark* are common enough. Whitby Landmark, a developer, contracted with Mollenhauer, a contractor, to construct a condominium building. Whitby was entitled to 75% of any savings realized by Mollenhauer over the cause of the project. There was a recession. The cost savings were unexpectedly significant. The parties agreed that Whitby would begin to deduct its share of accrued savings from otherwise due monthly progress payments. Mollenhauer was obliged by its contract to provide a cost savings report within 150 days after the date of substantial completion. A certificate of the total cost of the work was to form the

---

<sup>4</sup> R. B. Reynolds, “Whitby Landmark: Much Ado About Nothing?” (2002), 12 C.L.R. (3d) 23.

basis of the final price adjustment. Mollenhauer never produced the required certificate. For various reasons, it was obliged to abandon the project. Mollenhauer was bonded by Zurich. After Mollenhauer left, Whitby tried to negotiate payment of the remaining unpaid savings from Zurich under the standard CCDC performance bond. Zurich argued that its obligations under the bond were limited to physical completion of the construction work, which had occurred before the bond was called upon. Zurich maintained that the bond did not respond to other terms of the underlying contract. Importantly, as it turned out, Zurich had another string to its bow. It argued that Whitby had not given it timely notice of the default, thereby prejudicing the surety and providing the surety with a complete defence. In the end, it was this defence that won the day for Zurich. The interesting part of the trial decision is *obiter*.

At trial, Lamak J. held that the bond *did* respond to claims under the contract:

I cannot accept the proposition that the language of the bond governs without reference to the provisions of the underlying contract. The bond is, properly and understandably, replete with references to the terms and conditions of the contract. I refer to the stated scope of the Surety's obligations quoted earlier in these Reasons. Zurich undertook, in the event of Mollenhauer's default, promptly to "complete the Contract in accordance with its terms and conditions" an undertaking whose scope can surely only be defined by reading and applying the contract. The fact that Zurich chose to assume that obligation without even checking or inquiring what those terms and conditions might be cannot, in my view, be taken as evidence - let alone compelling evidence - that the liability now alleged was never contemplated. The behaviour is equally consistent with the inference that the terms of the standard form contract were so familiar to the underwriter, that there was no need to review the contract before agreeing to undertake the stated obligation. Equally, the silence of the parties during negotiations for the bond on the issue whether the bond would respond to a claim such as that now made is utterly ambivalent. Certainly, it does not lead me to the conclusion that there was an intention that it should not respond.

[...]

If Zurich intended to restrict the obligations that it undertook or to eliminate certain of Mollenhauer's contractual obligations from the scope

of the bond, it could easily have done so. It did not. Instead, Zurich issued a bond that obliged it, in the event of Mollenhauer's default, to "complete the Contract in accordance with its terms and conditions". It would be difficult to formulate a provision that would more easily embrace all of the obligations of Mollenhauer's under its contract with Landmark.

However, Justice Lamek concluded that by failing to give notice of the default to the surety, Whitby had breached a condition precedent to payment by the surety under the bond, that the surety had been prejudiced thereby, and that Whitby could not recover under the bond for that reason.

The trial decision was a legal bombshell. It immediately attracted attention. J. Stephen Tatrallyay commented that the court's "finding in favour of Whitby Landmark to the effect that the surety bond was responsible for covering a contractual default not strictly arising out of the failure to complete construction will have a major impact on

the surety industry”.<sup>5</sup> On the other hand, R. Bruce Reynolds argued that *Whitby* was “much ado about nothing” and stood “solely for the proposition that if the obligee fails to notify the surety of its claim, and such late notice prejudices the surety, then the surety will be released”.<sup>6</sup> Mr. Reynolds argued that, based on a review of surety law principles and prior case law, the court’s statement that the CCDC performance bond clearly and unambiguously rendered the surety liable for collateral monetary obligations was just plain wrong. He cautioned readers to tread cautiously and await the Court of Appeal’s decision before banking on *Whitby Landmark*. There were a number of *Whitby Landmark* type cases under way at the time, several headed for mediation. The profession waited for the appeal with bated breath.

The Court of Appeal upheld the trial judge’s decision. Both sides argued U.S. case law. Zurich relied on cases from Florida and Pennsylvania, holding that a surety was *not* liable for delay

---

<sup>5</sup> J.S. Tatrallyay, “Sticks and Bricks Revisited: Performance Bond Liability After *Whitby Landmark*” (2001), 4 C.L.R. (3d) 13.

<sup>6</sup> R.B. Reynolds, “*Whitby Landmark*: Much Ado About Nothing?” (2002), 12 C.L.R. (3d) 23.

damages.<sup>7</sup> In the Court of Appeal, Feldman J.A. noted that there was U.S. law to the contrary.<sup>8</sup> She distinguished Zurich's U.S. cases on the basis that they dealt with "delay" *simpliciter*, whereas *Whitby Landmark* dealt with a cost savings provision. Justice Feldman held as follows:

In interpreting the intent of the parties as to the coverage of the bond and whether it extends beyond funding the cost of completing the physical work to the cost sharing provisions of the construction contract, the operation of the surety's third option is, in my view, particularly instructive.

Under the surety's third option, where bids are obtained for a new contractor to complete the work, the surety must "make available . . . sufficient funds to pay the cost of completion less the balance of the Contract price". The phrase "balance of the Contract price" is defined to mean "the total amount payable by the Obligee to the Principal under the Contract, less the amount properly paid by the Obligee to the Principal".

---

<sup>7</sup> *American Home Assurance Co. v. Larkin General Hospital Ltd.*, 593 So.2d 195 (Fla. 1992); *Dowington Area School District v. International Fidelity Insurance Co.*, 769 A.2d 560 (Pa. Cmwlth. 2001).

<sup>8</sup> *Amerson v. Christman*, 261 Cal. App. 2d 811, 825, 68 Cal. Rptr. 378 (1968); *Cates Construction Inc. v. Talbot Partners*, 53 Cal. App. 4th 1420, 1462, 62 Cal. Rptr. 2d 548 (1997), *revd on other grounds*, 21 Cal. 4th 28, 980 P. 2d 407 (1999); *Pacific Employers Insurance Co. v. City of Berkeley*, 158 Cal. App. 3d 145, 204 Cal. Rptr. 387 (1984); *Riva Ridge Apartments v. Robert G. Fisher Co.*, 745 P.2d 1034, 1987 Colo. App. NEXIS 77 (C.A. 1987); *R.J. Griffin & Co. v. Continental Insurance Co.*, 497 S.E. 2d 586, 230 Ga. App. 822 (C.A. 1998),

Therefore, where there is a cost-sharing arrangement in the contract, the balance of the contract price is reduced by the amount that may be owing by the contractor to the owner at the time of default as a result of cost savings; consequently, the amount that the surety is required to pay to complete the physical work is greater than it would have been had there been no cost sharing provision in the original contract. As a result, the surety effectively pays for the owner's share of the cost savings.

Following this analysis, the owner will only be able to recover its share of the cost savings if it has "properly paid" the contractor. If the owner has made payments not called for by the contract, or before they were due, and the contractor defaults, there may be an issue to what extent the surety will have to respond. A further issue is how the bond will operate if there is no further construction work left to be done at the time of default. I need not address either of these potential issues in this case because of my disposition of issue number two below.

In summary, subject to the operation of the bond in any particular circumstances, I conclude that there is no basis in the language of the bond or in the circumstances surrounding its negotiation or completion to suggest that the cost-sharing provisions of the construction contract are not included as bonded losses

For its part, Whitby argued *Thomas Fuller Construction Co. (1958) v. Continental Insurance Co.*<sup>9</sup> to the effect that failure to comply with the bond's notice requirement was not fatal to the claim. The Court of Appeal distinguished *Fuller* on the basis that Whitby had failed to give notice of the very default it relied upon in calling on the bond, not some minor default as was the case in *Fuller*:

Landmark also argues that it acted reasonably in not declaring a default under the bond on the basis that its perception at the time was that the default by Mollenhauer in not providing the Certificate was not a serious one. Landmark refers to *Thomas Fuller*, *supra*, at 218, where Houlden J. stated that it is up to the obligee under the bond to determine when a default by the principal is so serious that notice of default under the contract must be given to the surety.

Again, this argument does not bear scrutiny. In *Thomas Fuller*, the issue was whether the owner's failure to declare the contractor in default for smaller defaults that had occurred earlier was a breach of the owner's obligations under the bond. It was in that context that the court held, at 217, that:

---

<sup>9</sup> [1973] 3 O.R. 202 (H.C.).

[T]he bond negatives any obligation on the part of the obligee to notify the defendant of defaults by Singer unless the default was of so serious a nature that the obligee deemed it proper to make a declaration of default and to call upon the bonding company to perform its obligations under the bond. At this stage, the plaintiff was required to give notice of default to the bonding company, but not otherwise

In this case, the owner failed to make a timely declaration of the very default on which it relies in calling on the bond: failure of the contractor to pay the owner's share of the cost savings, the amount of which is determined by the Certificate of Total Cost, after audit. This is not a case of the obligee failing to acknowledge and alert the surety to other earlier minor defaults upon which the owner does not rely.

### ***3. Lac La Ronge Indian Band v. Dallas Contracting Ltd.***

And so it sat on Ontario. Meanwhile, “back at the ranch” in Saskatchewan, another remarkably similar fact situation was pending in the Saskatchewan Court of Appeal. *Lac La Ronge Indian Band v.*

*Dallas Contracting Ltd.*<sup>10</sup> presented a perfect opportunity for a reconsideration of *Whitby Landmark*.

Western Surety Ltd., a bonding company, provided a performance bond to secure the performance of Dallas Contracting Ltd. respecting a contract to build a sewage lagoon for the Lac La Ronge Indian Band. Dallas did not complete the contract on time and the Band terminated it. In the ensuing lawsuit, Dallas and Western denied any liability.

All the Saskatchewan trial judge had to go on was the *obiter* of Justice Lamak in *Whitby Landmark*, as the appeal in *Whitby Landmark* was not heard until two years later. He concluded that the surety *was* liable with respect to liquidated damages for delay. The key points of the trial judge's reasoning were as follows:

---

<sup>10</sup> 2004 SKCA 109.

- (i) the phrase “complete the Contract” does not confine the surety’s liability to completing the “work” described in the Contract;
- (ii) by the terms of the Contract, the Band may deduct liquidated damages from the amount otherwise payable to Dallas under the Contract and, therefore, may deduct them from the remaining funds; and,
- (iii) the definition in the Bond of the term “balance of the Contract price” confirms the ability to deduct liquidated damages from the amount otherwise payable to Dallas.

The decision was appealed to the Saskatchewan Court of Appeal on a variety of points. The key issue of the extent of the surety’s obligations was squarely before the Saskatchewan Court of Appeal.

Madam Justice Jackson, for the Court, held as follows:

The Band's claim against Western arises in the context of an action for a breach of contract. The measure of contract damages is that amount which will place the Band in the position it would have been in if Western had performed its obligation under the Bond. In this case, Western had two means to fulfil its obligation: (i) complete the Contract; or (ii) find some other responsible person to complete it. Western did neither, but the measure of damages can be no greater than if it had fulfilled either option. A surety's obligations cannot be greater under Option 2, i.e., completing the Contract, than under Option 3, i.e., the responsible bidder option, because no surety would assume the obligation of "completing the Contract" if it meant it was liable for greater damages or, in this case, liquidated damages. The extent of the surety's exposure must be the same regardless of which option it chooses.

I am reinforced in my view by these words by R. Bruce Reynolds in *"Whitby Landmark: Much Ado About Nothing?"*:

... Surely, however, where there has been a denial of liability which is subsequently found to have been wrongful, the measure of damages to which the obligee is entitled should not vary depending upon whether the court arbitrarily chooses to look to option 1 as opposed to option 2, or vice versa. Rather, the two options should be read together in order to identify the "package" of obligations which the surety has failed to perform, and with

respect to which, therefore, the obligee is entitled to be compensated in damages.

The significance of this observation is that Option 2 must be read in light of Option 3. The surety's obligation under Option 3 is "to pay the cost of completion less the balance of the Contract price." "[B]alance of the Contract price" is defined in Option 3 to mean "the total amount payable by the Obligee to the Principal under the Contract, less the amount properly paid by the Obligee to the Principal."

This is where the trial judge, in my respectful view, erred by interpreting "balance of the Contract price" to mean the Band could deduct its damages award from the amount available to pay to complete the Contract.

The Court of Appeal in *Lac La Ronge* relied heavily on *Saskatchewan Housing Corp. v. Canadian Surety Co.*,<sup>11</sup> in which the Saskatchewan Court of Appeal had concluded that delay damages were *not automatically* the surety's responsibility. The trial judge had distinguished *Saskatchewan Housing* on the basis that it dealt with delay damages rather than liquidated damages. The Court of Appeal, however, ruled that liquidated damages were nothing more than a

---

<sup>11</sup> (1998), 64 Sask. R. 158 (C.A.).

genuine pre-estimate of delay damages, and held *Saskatchewan Housing* to be indistinguishable for this reason.

Again, Jackson J.A. adopted and relied upon Reynolds' article:

In this regard, the decision in *Whitby Landmark* is arguably inconsistent with a line of judgments which stand for the proposition that even if a Performance Bond does not contain exclusory wording the surety will not be obligated to perform, or be responsible for certain of the contractor's obligations contained in the underlying contract: see for example, *Re Bodner Road Construction Ltd.* (1963), 5 C.B.R. (N.S.) 293 (Man. Q.B.) and *R. v. Canadian Indemnity Co.* (1963), 41 D.L.R. (2d) 617, 43 W.W.R. 641, 5 C.B.R. (N.S.) 283 (Man. Q.B.), where it was held (following the unreported decision of Bastin J. in *Canada Oil Companies Ltd. v. Scottish Canada Assurance Corp.* which was unanimously affirmed by the Manitoba Court of Appeal in a further unreported decision) that notwithstanding a term of the underlying contract requiring the contractor to pay its subcontractors, the CCDC Performance Bond surety was not liable to perform or be responsible for such term following the default of the contractor (but see *Dawson & Hall Ltd. v. United States Fidelity & Guaranty Co.* (1963), 38 D.L.R. (2d) 53 (B.C. C.A.) with relation to a federal contract); and see

*Saskatchewan Housing Corp. v. Canadian Surety Co.* (1988), 64 Sask.R. 158 (Sask. C.A.), where the Performance Bond surety was not held liable to meet the defaulted contractor's completion schedule; and see *Kvaerner Enviropower Inc. v. Tanar Industries Ltd.* 21 Alta. L.R. (3d) 182, [1994] 9 W.W.R. 228, 17 C.L.R. (2d) 70, 157 A.R. 366 (Alta. Q.B.); affirmed (1994), 24 Alta L.R. (3d) 365, [1995] 2 W.W.R. 433, 157 A.R. 363, 17 C.L.R. (2d) 70n (Alta. C.A), for a case where a Performance Bond surety was found not to be bound to the mandatory arbitration provisions of the underlying contract.

Finally, the Saskatchewan Court of Appeal reviewed the pertinent United States authorities. Four U.S. cases held a surety *not* liable for delay damages.<sup>12</sup> Eight held that the surety *was* liable for such damages.<sup>13</sup> Jackson J.A. preferred the first line of cases:

---

<sup>12</sup> *United States Fidelity & Guaranty Co. v. Gulf Florida Development Corp.*, 365 So.2d 748 (Fla.1<sup>st</sup> D.C.A. 1978); *American Home Assurance Company v. Larkin General Hospital Ltd.*, 593 So.2d 195 (Fla. 1992); *L & A Contracting Co. v. Southern Concrete Services, Inc.* 17 F.3d 106 (5<sup>th</sup> Cir. Miss. 1994); and *Downingtown Area School District v. International Fidelity Insurance Co.*, 769 A.2d 560 (Pa. Commw. 2001).

<sup>13</sup> *Mason v. City of Albertville*, 158 So.2d 924 (Ala. 1963); *Southern Roofing & Petroleum Co. v. Aetna Insurance Co.*, 293 F.Supp. 725 (E.D. Tenn. 1968); *Amerson v. Christman*, 261 Cal.App.2d 811 (3 App. Dist. 1968); *Aetna Casualty & Surety Co. v. Butte-Meade Sanitary Water Dist.*, 500 F.Supp. 193 (D.S.D. 1980); *Pacific Employers Insurance Co. v. City of Berkeley*, 204 Cal. Rptr. 387 (C.A. 1984); *Riva Ridge Apartments v. Robert G. Fisher Co.*, 745 P.2d 1034 (Colo. App. 1987); *Cates Construction v. Talbot Partners*, 53 Cal.App.4<sup>th</sup> 1420 (2 App. Dist. 1997), *aff'd* 21 Cal.4<sup>th</sup> 28 (Sup. Ct. 1999); and *R.J. Griffin & Co. v. Continental Insurance Co.*, 497 S.E.2d 586 (Ga.App. 1998).

I do not find any of the American authorities in either list to be particularly helpful. There is little analysis in any of the cases. On balance, I find the cases in the first list to be closer to the Canadian approach to performance bonds and those in the second list to be more readily distinguishable. For example, in California, the courts have concluded that performance bonds are a form of insurance and should be strictly construed against the surety and in favour of the insured.

In summary, with respect to the American authorities which take a different view, I do not find them to be persuasive. Where not governed by statute or modified wording, they tend to speak in terms of conclusions and rely on the surety's obligation to "complete the Contract" or the "incorporation by reference clause" while ignoring the balance of the Bond.

Thus, the Saskatchewan Court of Appeal held the surety *not* to be liable for Dallas's obligation to pay liquidated damages.

#### **4. Conclusion**

What we have, then, are two Canadian appellate courts heading in opposite directions. In Ontario, for the moment, the law seems clear:

a standard CCDC performance bond *may* be answerable to claims for payment of collateral monetary obligations of the principal. In Saskatchewan, it will not.

If we were keeping a tally, we would have to keep in mind a recent, prior decision by the Saskatchewan Court of Appeal that would seem to head in *Whitby Landmark's* direction. In *Regina (City) v. Graham Construction & Engineering Ltd.*,<sup>14</sup> the Saskatchewan Court of Appeal assumed that the surety's and the contractor's liability were the same.

The Court in *Lac La Ronge* simply rejected this decision and others like it out of hand because "none of these authorities appear to have considered the arguments raised before this Court".<sup>15</sup> The situation in Saskatchewan is less clear than it appears.

There was a collective sigh of relief from the surety industry after the Saskatchewan Court of Appeal decision in *Lac La Ronge*. It remains to

---

<sup>14</sup> 2001 SKCA 3 (C.A.).

<sup>15</sup> *Lac La Ronge*, para. 76.

be seen whether the industry will still attempt to change the wording of the standard documents to avoid the *obiter* in *Whitby Landmark*.

It might be helpful to see this in table format:

	<i>Whitby</i>	<i>Lac La Ronge</i>	<i>Regina</i>
<b>Type of Bond</b>	CCDC Performance	CCDC Performance	Performance
<b>Contractual Obligation Claimed Under Bond</b>	Share in costs savings	Liquidated damages	Any damage award against contractor
<b>Surety Liable?</b>	Yes	No	Yes
<b>Court's Reasoning</b>	<p>Bond incorporates contract by reference, therefore contract terms form part of the bond. In case of default, surety has 3 options:</p> <ul style="list-style-type: none"> <li>- remedy default</li> <li>- complete contract</li> <li>- obtain new bids</li> </ul> <p>There was no qualification on type of default referred to. Third option did not limit surety's obligation to funding the completion of physical construction, but included other costs and damages. Third option required surety to pay costs of completion less balance of contract price, which was defined as total amount payable by obligee to</p>	<p>In case of default, surety has 3 options:</p> <ul style="list-style-type: none"> <li>- remedy default</li> <li>- complete contract</li> <li>- obtain new bids</li> </ul> <p>Surety did neither, but the measure of damages can't be greater than if it had fulfilled either option. Surety's obligation can't be greater under option 2 than under option 3, because no surety would ever use option 2 if it meant greater liability. "Balance of contract price" does not mean damages award can be deducted from amount payable. "Total amount payable" is amount of contract.</p>	<p>"It is common ground that if Graham breached the contract specifications for the pavement, Pasqua, as subcontractor for the pavement, would be obligated to indemnify Graham and Seaboard against any damage award obtained by the City against them, and that if Graham is</p>

	principal less amount paid by principal to obligee. Therefore, amount surety had to pay to complete was higher than it would have been without cost sharing agreement.	Words “complete the contract” can more easily be interpreted as “complete the work” than as “perform all obligations under the contract”.	liable to the City for damages, Seaboard is also liable pursuant to its performance bond.”
--	--	---	--

As if that is not confusing enough, consider what follows:

**5. The Latest Word on Bond Alternatives**

**(a) Default Insurance**

Scarcely a construction law conference recently has gone by recently without some comment upon subcontractor or contractor default insurance as an alternative to performance bonds.

Despite all this interest, it would appear that such policies are still quite rare in Canada. In the United States, subcontractor default insurance has recently evolved into contractor default insurance for

the benefit of owners.<sup>16</sup> Default insurance is *not* a form of surety bond. It is insurance, plain and simple. Consequently the rules for interpreting insurance contracts apply, not the arcana of bond law. Very little is certain with respect to coverage issues. There is virtually no case law on point and no claims history to offer any kind of precedent.

The surety industry is quick to point out the following disadvantages of default insurance:

- Minimal pre-qualification performed by the insured
- Coverage limited to the aggregate limit
- Deductibles apply
- Insured must pay loss before getting reimbursed
- Insurer can cancel
- Insured must complete, *then* claim
- Subcontractors and suppliers cannot make a direct claim

---

<sup>16</sup> See H.K. Johannsen, “Subcontractor and Contractor Default Insurance”, paper presented at the 2<sup>nd</sup> Annual Conference of the Canadian College of Construction Lawyers, Montebello, Quebec, June 19, 1999.

- No case law or claims history<sup>17</sup>

On the other hand, subcontractor default insurance says that it will typically cover the following losses:

- the cost completing the subcontractor's obligations
- the cost of correcting defective or non-conforming work or materials
- legal and other professional expenses
- costs, charges and expenses incurred in the investigation, adjustment and defence of disputes
- indirect costs such as liquidated damages, acceleration and extended overhead<sup>18</sup>

Depending on the policy wording, uncertainty about coverage of the kind created by the decisions in *Whitby Landmark* and *Lac La Ronge* might therefore avoided.

---

<sup>17</sup> Surety Association of Canada, <http://www.surety-canada.com/contractors/riskcomp.html>.

<sup>18</sup> H.K. Johannsen, supra, note 12 at p. 8.

Contractors interested in default insurance face three major problems: first, many tenders specifically require performance and payment bonds from bidders, and offering default insurance instead of bonds may lead to non-compliant bids; second, owners are used to having sureties screen bidders through the bonding qualification process and insurers do not do this; third, lenders usually require bonding as a prerequisite to lending, which pretty much rules out contractor default insurance on most projects.<sup>19</sup>

### **(b) Delay in Start-Up Insurance**

One other type of insurance should be addressed, even though it seems more esoteric than contractor default insurance. A policy that has been around for some time, but is rarely used, is “delayed start-up insurance”. Delayed start-up coverage is designed for major infrastructure projects and is usually based on a builder’s risk policy. A typical “DSU” cover could look like this:

---

<sup>19</sup> Ibid. at p. 16-17.

The Insurers agree that if, at any time during the Period of Insurance stated in the Schedule, any or all of the property insured specified under item ... of the material damage section be physically lost or physically damaged at the contract site by an Accident or (Accidents) as insured under the material damage section, thereby causing an interference in the construction/erection works and/or testing schedule resulting in a delay of commencement of and/or interference with the business to be carried on by the principal, herein referred to as Delay.

Then subject to the provisions, terms, exceptions, conditions and memoranda contained herein, the Insurers will indemnify the Principal in respect of the actual loss sustained from deferred receipt or partial receipt of revenues as a result of the Delay in completion of the permanent works beyond the scheduled commencement date of the business. Actual loss sustained shall mean:

*Fixed Costs*

Fixed costs that would have been paid or payable out of the revenues that would have been received or receivable had the delay not occurred.

*Debt Service*

The interest, scheduled principal payments, commitment fees, agency fees, etc in respect of advances made or monies borrowed that would have been payable out of the revenues that would have been received had the delay not occurred.

*Net Profit*

Net profit that would have been earnable from the revenues that would have been received had the delay not occurred less any sum saved in respect of such of the foregoing amounts as may cease or be reduced in consequence of the delay.

*Insurers will also pay as increased cost of working*

Additional expenditures necessarily and reasonably incurred by the Principal or on his behalf (with the consent of Insurers) for the sole purpose of avoiding or diminishing the amount for which the insurer would have been liable with-out such expenditures, but not exceeding the amount of loss thereby avoided.<sup>20</sup>

Typically, DSU provides protection against delays arising from physical damage caused by a peril included in the builder's risk

---

<sup>20</sup> See Swiss Re, "Delay in Start-Up Insurance", available online @ <http://www.swissre.com/INTERNET/pwswpspr.nsf/fmBookMarkFrameSet?ReadForm&BM=../vwAllbyIDKeyLu/ESTR-5KYCDA?OpenDocument>.

policy. Once an insured peril has caused physical damage and this damage causes a delay beyond the scheduled business commencement date, then the principal will be indemnified for the resulting actual loss of gross profit, limited as described in the cover.<sup>21</sup>

Never before has the principle “buyer beware” seemed more appropriate.

---

<sup>21</sup> Ibid., page 8.