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Case Alert

Shaping the future of insurance law

Court of Appeal offers further guidance on notified facts that might give rise to a claim

***P & S Kauter Investments Pty Ltd v Arch Underwriting at Lloyds Ltd* [2021] NSWCA 136**

12 JULY 2021

AT A GLANCE

- With the recent Kauter Investments decision, the NSW Court of Appeal has provided guidance on prior notified facts that might give rise to a claim under s 40(3) of the *Insurance Contracts Act 1984*.
- The matter involved actions by the trustees of SMSFs against a financial planner. When the financial planner was deregistered, the trustees joined the financial planner's professional indemnity insurers.
- The Court of Appeal, finding in favour of the insurers, upheld the decision of the primary judge that an insured cannot rely on s 40(3) when notifying mere possibilities (rather than facts).
- This article discusses the lessons learnt for insurers from this judgment and prior authorities on this issue.

Facts

From 2006 to 2009, Christopher Moylan, the principal of Moylan Retirement Solutions Pty Ltd (MRS), gave financial advice to four families and their self-managed superannuation funds (SMSFs) to make unsecured loans to corporate investment vehicles, primarily Moylan Investment Group (MIG). Mr Moylan was MIG's sole director and shareholder and used the funds advanced to MIG for other investment vehicles that conducted property development and land subdivision.

Mr Moylan's renewal proposal included the following information:

> *"A small number of clients have invested/lent funds to property investments and/or companies that have to date been unable to repay those funds in total.*

> *At the time of the investment all appropriate disclosures were made and clients invested/lent funds with full knowledge of the circumstances at the time.*
>
> *At this stage, no loss has been crystallised and no claim or complaint has been formally lodged.*
>
> *We wish to advise the insurance company that there is a chance of a claim against Moylan Retirement Solutions in relation to any loss that may be incurred."*

Subsequently, Mr Moylan was made bankrupt, MIG was wound up and MRS was deregistered. In some cases, the funds were also not used as instructed by the clients but were instead misapplied and used by MIG.

The trustees of the SMSFs commenced three separate actions from 2012 to 2015, which were heard together in *Esined No. 9 Pty Ltd v Moylan Retirement Solutions Pty Ltd (No 2)* [2020] NSWSC 359 (Esined No. 9). As a result of MRS' deregistration, the plaintiffs joined MRS' professional indemnity insurers to the proceedings seeking an indemnity through the mechanism of s 601AG of the *Corporation Act 2001* (Cth).

On 8 May 2020, the primary judge dismissed the claims against the insurers with costs. The claimants appealed this decision and on 2 July 2021, the Court of Appeal upheld the primary judge's decision and dismissed the appeal in favour of the insurers in *P & S Kauter Investments Pty Ltd v Arch Underwriting at Lloyds Ltd* [2021] NSWCA 136 (Kauter Investments).

First instance decision

In Esined No. 9, the primary judge determined that no "claim" had been made against MRS before May 2013, and the notification made in late January 2013 did not engage s 40(3) of the ICA.

The primary judgment also concerned non-disclosure, fraudulent misrepresentation and the application of the conflict of interest exclusion.

A notification needs to be of facts, rather than merely opinions or beliefs or of a possibility of a claim without any basis in fact.

The appeal

The primary ground of appeal was whether the 15 January 2013 notification was sufficient to trigger the operation of s 40(3) of the ICA. The appeal also considered issues of non-disclosure and fraudulent misrepresentation.

The Court of Appeal upheld the findings of the primary judge. Regarding the operation of s 40(3) of the ICA, the Court of Appeal made the following observations:

- s 40(3) is *"concerned with the notification of objective matters that bear on the possibility of a claim being made, rather than matters of belief or opinion as to that possibility";*
- there must be a "*sufficient correspondence*" between the facts notified and the subsequent claim made, such that one can say the claim arose or resulted from those facts (although this does not require that the potential claimants or quantum be identified);
- the notified facts must be assessed objectively. It is sufficient if the notified facts are of a kind that might, in common experience, be expected to give rise to a claim, even if that claim might only have limited prospects of success, and
- the necessary question to ask is: what is it about the notified facts that might give rise to a claim?

Considering the above principles, the Court of Appeal determined that Mr Moylan's notification was not a notification of "facts". It was only a notification of "possibilities" because:

- Mr Moylan did not elaborate on MRS' inability to repay the invested funds, including whether the time for repayment passed and whether it was likely that the funds would not be repaid in total;
- the timeframe was broad – Mr Moylan referred to *"advisory work"* between 2008 and 2011 in a business that was established in July 2005;
- no particular client was identified (which in itself is not fatal) but no loss had been "*crystallised*";
- there had not been a formal claim or complaint, and also no verbal claim or even verbal intimation of a claim (in contrast to *Darshn v Avant Insurance Ltd* [2021] FCA 706 discussed in the attached table); and
- the notification did not identify any defect in the advice given or disclosure made by MRS, and positively asserted that there was none.

Implications for insurers, brokers and their customers

This raises the question of when a claim will trigger the application of s 40(3) of the ICA. To answer this question, we look at the history of similar cases and their fact-specific notifications summarised in this downloadable table.

When considering whether a notification triggers the operation of s 40(3) of the ICA, ask:

- Has there been a notification of facts within the policy period? This can be a single notification or a collection of correspondence or information (if it is received before expiry of the policy).
- Has there been a claim or claims made against the insured outside the policy period?
- Consider the statements made in the notification(s):
  - Which statements are statements of fact, as opposed to statements expressing a belief or opinion?
  - What details have been provided by the insured, such as the description of possible claimants, what the insured has done or omitted to do which could give rise to claims, the defect or symptom observed, or the success of steps the insured is taking to rectify the issue? Note that not having all this information is not fatal to the notification.
  - Could the notified facts have led to the making of the claim against the insured?
- Is there a sufficient causal link or connection between the facts notified and the claim made?

As a claim progresses, it is important to also always consider whether the developments have a sufficient causal link or connection to the original facts notified.

The lessons from judicial guidance

The authorities summarised in the table "*Judicial guidance on notification of facts that may give rise to a claim"* table indicate that an insured can notify insurers of general facts, which may give rise to a claim, without having full knowledge of the causes or potential consequences of the problem. However, the notification needs to be of facts, rather than merely opinions or beliefs or of a possibility of a claim without any basis in fact.

Once facts that may give rise to a claim are notified, any claim that may later arise with a sufficient causal link to those facts will be deemed to be notified during the policy period within which the notification was given. A 'causal link' could be satisfied if it can be said that the claim arose, resulted from or was a consequence of those facts (as opposed to a mere coincidental link).

Need to know more?

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