The restricted scope of "other insurance" clauses

***Lambert Leasing Inc v QBE Insurance (Australia) Limited* [2016] NSWCA 254**

4 NOVEMBER 2016

WHAT'S IMPORTANT

The New South Wales Court of Appeal has unanimously confirmed that the operation of section 45 of the Insurance Contracts Act 1984 (Cth) (**ICA**) is limited to circumstances where the *"insured"* has *"entered into"* both relevant contracts of insurance.

This decision is important because it significantly restricts the operation of section 45, which may in turn lead to an increase in the use of *"other insurance"* clauses in Australian market wordings because contribution claims (based on double insurance) are viable in certain circumstances.

"Other insurance" clauses attempt to limit or exclude an insurer's liability, if the insured is entitled to cover under another policy. Section 45 has historically restricted the operation of such clauses, leading to a decline of the use of such clauses in the Australian market. In this case, the Court of Appeal decided that when two policies have *"other insurance"* clauses which cancel each other out (because they were not rendered void by section 45), an insured can pick which policy it claims cover under. A situation of double insurance then arises between the two insurers.

BACKGROUND

Contractual framework

Lambert Leasing Inc (**Lambert)** sold a Fairchild Metro 23 Aircraft (**Aircraft**) to Jalgrid Pty Limited and Dramatic Investments Pty Limited (**Partnership 8018**). Partnership 8018 leased the Aircraft to Lessbrook Pty Limited (**Lessbrook**).

The Aircraft subsequently crashed in northern Queensland killing all passengers. The relatives of the passengers brought proceedings against Lambert and Saab Aircraft Leasing Inc (**SAL**) in the United States of America (**US Proceedings**).

Insurance cover

Lambert and SAL were both subsidiaries of Saab AB (**SAAB**). SAAB held a policy with Global Aerospace Underwriting Managers Limited (**Global**). That policy covered SAAB as the named insured, and also its subsidiaries, including Lambert and SAL (**Global Policy**).

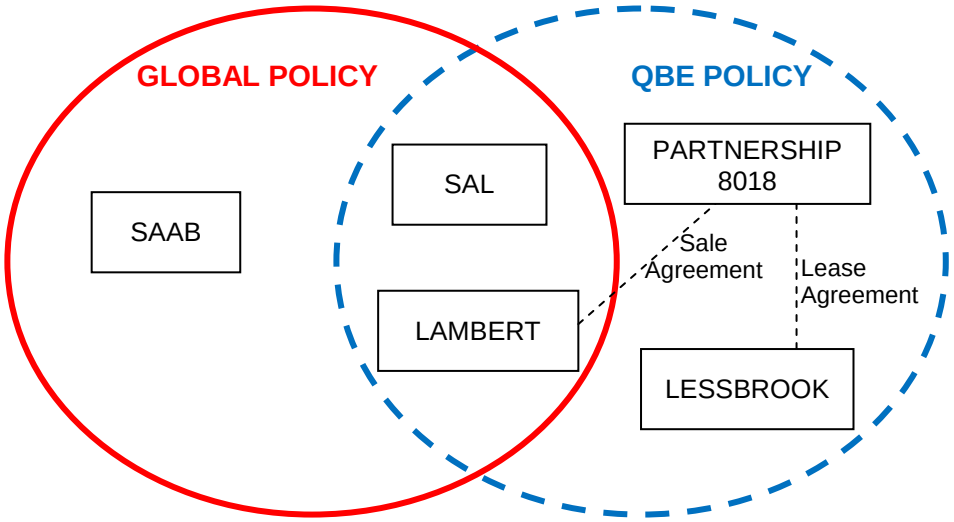
Lessbrook held an insurance policy with QBE Insurance (Australia) Limited (**QBE**). That policy named Lambert, SAL and Partnership 8018 as *"additional insureds"* (**QBE Policy**).

Lambert and SAL made a claim for indemnity under the Global Policy for cover for the US Proceedings. Global granted cover to Lambert and SAL. Lambert and SAL also made a claim for indemnity under the QBE Policy. Lambert and SAL said that the Global Policy operated as an excess policy and that the QBE Policy was the primary policy. In response, QBE relied upon an "*other insurance*" clause in the QBE Policy.

The primary issue was whether section 45 rendered the QBE "*other insurance*" clause void. Section 45 provides:

"Where a provision included in a contract of general insurance has the effect of limiting or excluding the liability of the insurer under the contract by reason that the insured had entered into some other contract of insurance, not being a contract required to be effected by or under a law, including a law of a state or territory, the provision is void…"

This diagram illustrates the contractual and insurance framework:



At first instance

The primary judge considered that the QBE "*other insurance*" clause was not rendered void by section 45 because:

- section 45 applied to cases where an insured is a party to <u>both</u> relevant contracts of insurance; and
- to be a party to a contract of insurance requires that party to have <u>entered into</u> the contract (in the sense of negotiating the contract and paying a premium etc). Merely being named as an insured is not enough.

The primary judge held that Lambert and SAL were not parties to the QBE Policy as they were merely "*additional insureds.*" Lambert and SAL appealed.

On appeal

The issues before the Court of Appeal were:

- did section 45 render the QBE *"other insurance"* clause void; and
- if section 45 did not render the QBE *"other insurance"* clause void, whether that clause and the *"other insurance"* clause in the Global Policy cancelled each other out?

THE COURT OF APPEAL'S DECISION

The QBE Policy

The Court of Appeal found that Lambert and SAL had not entered into the QBE Policy because that policy distinguished between *"insured"* and *"additional insured"*. The QBE Policy described to the *"insured"* as *"Lessbrook"*.

The *"additional insureds"* included Lambert and SAL. The Court concluded that it was clear that Lambert and SAL were third party beneficiaries of a contract of insurance, rather than the parties who had entered into the policy. Significant factors which bore upon the Court of Appeal's decision were the fact that Lambert and SAL had not paid any of the premium nor had entered into negotiation of the terms of the insurance contract.

The Global Policy

The Global Policy also contained an "*other insurance*" clause. There were a number of factors which the Court of Appeal considered relevant to whether Lambert and SAL had *"entered into"* the Global Policy. Those included:

- the policy distinguished between the *"insured"* and its subsidiaries;
- the correct inference was that SAAB's subsidiaries held an insurable interest, but were not contracting parties; and
- the doctrine of agency was not applicable to argue that SAAB contracted on behalf of itself and Lambert and SAL when entering into the Global Policy.

Accordingly, the Court of Appeal found that Lambert and SAL had not entered into the Global Policy.

Cancelling out and double insurance

Having concluded that section 45 did not void either the QBE *"other insurance"* clause or the Global *"other insurance"* clause, the Court of Appeal found that those clauses cancelled each other out. Where both "*other insurance"* clauses cancel each other out, the normal course is that the insured is entitled to choose which of its two insurers it requires indemnity from. A situation of double insurance then arises and that insurer may seek contribution from the other insurer.

CONCLUDING THOUGHTS

An appeal is unlikely given that the Court of Appeal's reasoning relies heavily on the High Court's decision in *Zurich Australian Insurance Ltd v Metal & Minerals Insurance Pty Ltd* (2009) 240 CLR 391. While legislative amendment to section 45 is possible, it is a notoriously slow process. It is less likely given that the ICA was substantially amended in 2013.

This case is significant because it confirms a restrictive operation of section 45. This may result in "*other insurance"* clauses being used more often in the Australian market, especially in the construction space where project specific insurance commonly includes "*additional insureds*". However, it should be remembered that section 45 is not intended to have application to policies which are genuine excess policies (such excess policies must specifically identify the primary policy and expressly state that the excess policy sits above the primary policy).

For further information please contact: **www.wottonkearney.com.au**

Andrew Moore
PARTNER
Sydney
T: +61 2 8273 9943
Andrew.Moore@wottonkearney.com.au

ROBERT FINNIGAN
SPECIAL COUNSEL
Sydney
T: +61 2 8273 9850
Robert.Finnigan@wottonkearney.com.au