wotton kearney

Insurance Year in Review 2013

The Year in Review – An Overview

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Welcome to the 2013 Wotton + Kearney Insurance Year in Review publication addressing topical developments in 2013 across a broad range of commercial insurance products and in relation to insurance law generally.

2013 was another busy year for those of us who practise day to day in insurance claims. From amendments to the Insurance Contracts Act, to keeping pace with changes in the class action space, to the usual common law developments; insurance law certainly did not rest for long as the calendar year progressed!

As well as being an important year in terms of developments in insurance law, 2013 was also a year of considerable change at Wotton + Kearney.

At last year's launch of this publication I announced the opening of our Brisbane office, which subsequently opened on 1 July 2013.

In addition, both the Sydney and Melbourne offices moved to new locations at the end of the year to reflect significant growth in both offices. We now occupy new premises at 85 Castlereagh Street (Sydney) and 600 Bourke Street (Melbourne). We hope to have the opportunity to welcome you to our new offices in the near future.

Enjoy the 2013 Insurance Year in Review publication.

David

12 February 2014

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Wotton + Kearney

Wotton + Kearney is a leader in the provision of insurance legal solutions in Australia

Our sole focus is insurance law and with a team of more than 80 specialist insurance lawyers we are preferred by clients consisting of some of the largest insurers, brokers, private companies and industry participants in Australia and globally.

As the only Australian law firm based in more than one city practising solely in insurance law, we have a detailed understanding of the domestic insurance industry and of the litigation landscape relevant to the successful resolution of insurance claims. Our commitment to the insurance and reinsurance industry extends to overseas markets, particularly the London insurance market which continues to play a significant role in the writing of Australian risks.

Our service offering is broad. We specialise in reinsurance, regulatory and compliance advice and policy drafting. We have expertise in all forms of insurance claims litigation including claims relevant to:

+ Professional Indemnity
+ Public and Products Liability
+ ISR/Commercial Property
+ Directors & Officers Liability
+ Class Actions
+ Life Insurance and Superannuation
+ Trade and Transport
+ Accident and Health
+ Reinsurance and Regulatory

Contents

Wotton + Kearney
Insurance Year in Review - 2013

The Year in Review – An Overview

David Kearney, Chief Executive Partner 3

Developments for Insurers Generally

The ICA gets a makeover - amendments to the Insurance Contracts Act 1984 (Cth) 16
Simon Black and **Hayden Gregory** provide an overview of some of the key amendments to the **Insurance Contracts Act 1984** brought about by the **Insurance Contracts Amendment Act 2013**.

Section 54 offers no remedy for Prepaid 19
In ***Prepaid Services Pty Limited and Ors v Atradius Credit Insurance NV*** the NSW Court of Appeal continued the judicial debate on the application of section 54 of the **Insurance Contracts Act 1984**. **Sean O'Connor** and **Tara Weinman** examine the Court's findings.

Upping the ante: changes to offers of compromise in Victoria and NSW give defendants more options 22
Jonathan Maher considers the changes made in Victoria and NSW to the rules regarding offers of compromise and their effect on the options available to defendants to resolve claims.

Offers of compromise - enough already! Is silence really a virtue? Plus costs or not? 24
Exactly what constitutes a valid offer of compromise is a hotly contested issue. **Jacqueline Grace** and **Amanda Cefai** explore recent amendments to the **Uniform Civil Procedure Rules** and ***Whitney v Dream Developments***.

Waving goodbye to inadvertent waiver of privilege? 26
Peter Hamilton and **Jonathan Katsanos** examine the recent High Court case of ***Expense Reduction Analysts Group Pty Ltd v Armstrong Strategic Management and Marketing Pty Ltd*** addressing discovery issues in large scale litigation.

Is a consent judgment a judgment at all? 29
Charles Simon and **Alexis King** consider the High Court's decision in ***Newcrest Mining Limited v Thornton*** addressing the implications of consent judgments for subsequent actions.

Expanding rights of subrogation – Bupa blooper? **31**
Noa Zur and **Natasha Sung** discuss the case of ***Bupa Australia Pty Ltd v Gloria Shaw and James Walker (as Joint Executors of the Estate of Norman Shaw) & Anor***, in which the Victorian Supreme Court considered the interaction between the contractual and equitable principles in the well established doctrine of subrogation.

Cutting either way: Courts both extend and limit the scope of proportionate liability in 2013 **34**
In 2013 2 important appeal decisions were handed down, both of which dealt with questions regarding the scope and applicability of Part 4 of the **Civil Liability Act 2002**. **Jonathon Lees** considers the judgments of the NSW Court of Appeal in ***Perpetual Trustee Company Ltd v CTC Group Pty Ltd (No. 2)*** and the High Court in ***Hunt & Hunt v Mitchell Morgan***.

Claim not covered? No defence costs **37**
Raisa Conchin and **Troy Greig** discuss the decision of the Queensland Court of Appeal in ***Bank of Queensland Limited v Chartis Australia Insurance Limited***, which serves as a timely reminder of the principles of policy construction.

Acting outside your employment **39**
Susan Ougham and **Hayden Gregory** consider the recent case of ***Zakka v Elias***, in which the NSW Court of Appeal considered several questions relating to vicarious liability and causation.

Public + Product Liability

When the circumstances are unknown, how far can inferences take the Court? **43**
Charles Simon and **Rebecca Hosking** consider the decision of the Court of Appeal in ***Minogue v Rudd*** relevant to the use of circumstantial evidence.

Had a slip while choosing some dip – *Coles Supermarkets Australia Pty Ltd v Meneghello* **46**
Claire Tingey and **Danielle Skinner** discuss the importance of establishing causation and the specificity of pleadings.

Agency and vicarious liability **48**
Justin Carroll and **Melissa Tan** consider the decision of ***Day v The Ocean Beach Hotel Shellharbour Pty Ltd*** which considered whether the **Liquor Act 2007** had the effect of rendering the occupier of licensed premises vicariously liable for the conduct of an independent security contractor.

To care, or not to care **50**
In catastrophic injury cases, a question often arises as to the quality and nature of care for which an injured person ought to be compensated. **Rebecca Hosking** and **Michael Fung** consider ***Dang v Chea*** in which the NSW Court of Appeal held that the key issue is what meets a plaintiff's reasonable needs.

Risk in recreational activities **52**
Greg Carruthers-Smith and **Kim Ong** discuss 2 recent cases addressing the question of negligence in the context of dangerous recreational activities and risk warnings.

Contents

Bullying: make it stop! **55**
Karen Jones and **Ben Bronneberg** examine the decision of the NSW Court of Appeal in ***Oyston v St Patrick's College*** which confirmed the difficulties educational facilities will face in seeking to avoid liability for student bullying.

Property owners' liability for unknown hazards or defects that cause injury **57**
In ***Jodie Smith v Body Corporate for Professional Suites Community Title Scheme 14487*** the Queensland Court of Appeal determined whether the Body Corporate was liable for injuries suffered by the plaintiff when she fell through a glass panel in the ground-floor facade of an office building. **Paul Spezza** and **Anna Sheely** consider the decision.

Cost caps for intentional torts **60**
Belinda Henningham and **Jane de Saint Simon** discuss the High Court decision in ***Certain Lloyd's Underwriters Subscribing to Contracts No IHOOAAQS v Cross*** regarding the application of cost caps to intentional torts.

The sharp end of an inadequate system of cleaning **62**
In ***Wright v KB Nut Holdings Pty Ltd*** the Queensland Court of Appeal considered the liability of a manager of a serviced apartment complex for psychiatric injury suffered by the plaintiff after she sustained a needle stick injury while cleaning her apartment. **Paul Spezza** and **Anna Sheely** consider the decision.

Return to the status quo ante: *QBE v Orcher; Bowcliff v Orcher* **65**
Paul Spezza and **Justin Carroll** examine this NSW Court of Appeal decision which confirms that for an occupier of licensed premises to have a duty to anticipate and/or intervene in disputes occurring beyond those premises, it must be shown that the occupier was aware of and had the ability to control the relevant risk.

Blameless motor accident provisions – *Ingram v Axiak* **68**
Michelle MacMahon and **Nicole McConochie** examine ***Ingram v Axiak*** in which the High Court considered the application of the *"blameless accident"* provisions in the **Motor Accidents Compensation Act 1999**.

Shifting liability to a statutory insurer: the *"use of a registered motor vehicle"* **70**
Andrew Seiter and **Peter Hamilton** consider the importance for insurers of carefully considering whether claims for injury arising out of incidents relating to the *"use of a registered motor vehicle"* can be passed onto statutory insurers.

Current trends in personal injury litigation in Victoria **73**
Andrew Seiter discusses some of the recent trends seen in personal injury litigation in Victoria.

A second bite of the cherry? **76**
Lisa Sylvan and **Melissa Teo** examine the recent trend of litigants in Victoria attempting to circumvent jury verdicts against them, the means employed by those litigants and the Courts' response to this development.

Remediation costs not capable of being covered under liability insurance policies **81**
Julie Bowker discusses the case of ***Hamcor Pty Ltd & Anor v The State of Queensland & Ors***, in which the Queensland Court of Appeal considered whether an insured could recover costs incurred to remediate its own land.

Victorian bushfire litigation update: Issues involving damage to trees **84**
Litigation arising from the 2009 Victorian bushfires has challenged the status quo when it comes to assessing damages for mature trees. While the Courts have yet to produce a judgment on the issue, **Robin Shute** and **Aisha Lala** comment on the development of the argument in the litigation and the recent decision of the Victorian Supreme Court in ***Roads Corporation v Love***.

Financial Lines

Claim against financial advisor fails **87**
Gabrielle Levette and **Julie Bowker** discuss the decision of the Federal Court in ***Jordan v HLB Mann Judd Wealth Management***, in which the Court considered whether a financial advisor's advice to an *"unsophisticated"* investor was negligent.

Blanket notifications – to cover or not to cover? **89**
The issue of blanket notifications has vexed insurers of *"claims made"* policies for some time. **Graham Jackson** and **Thomas Byrne** examine the recent English High Court decision of ***McManus and Others v European Risk Insurance Co***, which follows the trend in the English courts of finding that blanket notifications can be an effective notification of circumstances.

***"Claims made"* policies and section 601AG of the Corporations Act 2001 (Cth)** **91**
Raisa Conchin and **Troy Greig** discuss the decision of the NSW Supreme Court in ***Sciacca v Vero Insurance Limited***, in which the Court considered the application of section 601AG of the **Corporations Act 2001**, which allows a plaintiff to claim directly against an insurer in circumstances where the insured defendant has been deregistered.

Damages and compensation – what's in a claim? **94**
Chris Busuttil and **Bhrig Chauhan** consider the decision of the Victorian Court of Appeal in ***Kyriackou v ACE Insurance Limited***, in which the Court was required to decide whether defence costs coverage under a professional indemnity policy was triggered.

The FOFA reforms **97**
On 1 July 2013 the Future of Financial Advice reforms became mandatory. **Cain Jackson**, **Jane O'Neill** and **Dearne Matheson** consider the key reforms and their impact on insurers and insureds.

NSW Court of Appeal bridges the gap on section 6 charges – *Chubb Insurance Company of Australia Ltd v Moore* **99**
In a successful outcome for the insurers of failed timber investment company Great Southern, the NSW Court of Appeal determined in ***Chubb Insurance Company of Australia Ltd v Moore*** that s6 of the **Law Reform (Miscellaneous Provisions) Act 1946** did not apply on a threshold issue, since the third party claims against Great Southern were issued outside of NSW. The Court also provided some long-awaited guidance on the problems thrown up by the New Zealand decision in the ***Bridgecorp*** case. **Patrick Boardman** and **Jonathon Lees** examine the likely consequences of the Court's findings.

Contents

Federal Court rules that *"dispute splitting"* at FOS is not *"claim splitting"* **103**
The Financial Ombudsman Service Terms of Reference specify the maximum financial remedies which may be awarded by FOS *"per claim"*. While FOS has issued guidelines about *"claim splitting"*, its approach had not been subject to judicial consideration until the recent case of ***Wealthsure Pty Ltd v Financial Ombudsman Service Pty Ltd***. **Michael Bath** and **Mark Hughes** examine the decision of the Federal Court.

Striking a balance between legitimate claims and the cost of defending proceedings – granting security for costs against unfunded applicants in class actions **105**
Madgwick v Kelly marks a departure from the courts' usual reluctance to award security for costs against individual class action applicants who are not represented by a litigation funder. **Hamish Baddeley** and **Bradley Meyerowitz** discuss the Federal Court's judgment.

Class action terms – ASIC intervenes **108**
In ***ASIC v Richards*** the Full Federal Court considered whether the settlement orders made by the primary judge in ***Richards v Macquarie Bank Ltd (No 4)*** were fair and reasonable. **Hamish Baddeley** and **Karina Mandinga** examine the decision of the Full Federal Court, which is notable in overturning the primary judge's settlement terms on the basis that they were unreasonable for certain members of the class action.

Class actions and multiple insurance claims **110**
In ***Morgan, in the matter of Brighton Hall Securities Pty Ltd (in liq)***, the Federal Court held that each individual plaintiff's claim in a class action proceeding against a financial services company, would be treated as a separate claim for insurance purposes. **Patrick Boardman** and **Gemma Houghton** consider the Court's decision and its implications for insurers and insureds.

The only Australian decision in a securities/investors class action – the Timbercorp decision **113**
On 10 October 2013 the Victorian Court of Appeal handed down its decision in ***Woodcroft-Brown v Timbercorp Securities Ltd (in liq) & Ors***, upholding the original decision of Judd J, which had dismissed the investor class action against Timbercorp. This is the only Australian judgment to have dealt with an investor/security class action and, in particular, the Court considered the extent to which the investor or shareholder has to prove reliance on the alleged wrongful conduct. This is a key issue in this type of class action and the Court ultimately upheld the importance of the plaintiff establishing such reliance and causation as a prerequisite of a claim for damages. **Patrick Boardman** examines the Court's decision.

Reinsurance + Regulatory

Section 562A(4) of the Corporations Act revisited: obtaining priority in respect of reinsurance proceeds where the insurer is in liquidation **117**
Graham Jackson discusses the decision of the NSW Supreme Court in ***HIH Casualty & General Insurance Ltd (in liquidation and subject to schemes of arrangement),*** in which the Court considered an application under section 562A(4) of the **Corporations Act**.

The reinsurance broker's continuing duty to remit funds 119
The English case of ***Equitas Ltd v Walsham Bros & Co Ltd*** will have a significant impact on claims against reinsurance brokers for failure to promptly remit funds. **Matthew Foglia** and **Melissa Tan** examine the Court's decision.

Principles of construction and interpretation: reinsurance contracts 122
Matthew Foglia and **Melissa Tan** consider 3 recent English judgments that provide a useful reminder of the principles applied by the courts when construing and interpreting reinsurance contracts.

Construction

An extension of the duty of care to subsequent owners for defective building works 128
Paul Spezza and **Jennifer Jones** consider the decision of the NSW Court of Appeal in ***Owners Corporation Strata Plan No 61288 v Brookfield Multiplex Limited***, in which the Court found the existence of a general duty of care extending to pure economic loss, provided that certain principles entitling one to recover such loss are established.

Will your dispute resolution clause cause a dispute? 131
In ***WTE Co-Generation & Anor v RCR Energy Pty Ltd & Anor*** the Victorian Supreme Court looked at the enforceability of a contractual dispute resolution clause. **Gemma Houghton** and **Hayden Gregory** discuss the Court's ruling and its implications.

Perpetual issues in construction: proportionate liability 133
Justin Carroll and **Michael Fung** consider the implications for insureds of the recent decision of ***Perpetual Trustee Company Ltd v CTC Group Pty Ltd (No 2)*** which found the operation of the proportionate liability regime under the **Civil Liability Act 2002** excluded from a contract despite a party's claim to the contrary.

Construction contracts and the Personal Property Securities Act – the importance of registering 135
The **Personal Property Securities Act 2009** represented a substantial shift in the way businesses need to treat contracts that might give rise to rights of security over personal property. **Mark Hughes** examines a recent case from New Zealand, where very similar legislation has been in force for more than a decade, which demonstrates the care needed to ensure that a security interest is properly registered.

The Victorian Building Authority – new authority, new power, new impacts on construction litigation 137
In July 2013 the Victorian Building Authority commenced work as the new integrated regulator of the plumbing and building industries. **Nick Lux** and **Connor Burdon-Bear** highlight some of the changes likely to impact the insurance and construction industry having particular regard to the Authority's broad new powers.

Contents

Victorian security of payment legislation – clarification of the issue of *"excluded amounts"* 140
Andrew Brennan considers the decision of Justice Vickery in ***Maxstra Constructions Pty Ltd v Joseph Gilbert & Ors***, which provides clarification on a perceived incompatibility between 2 sections of the **Building and Construction Industry Security of Payment Act 2002** that outline the matters that can be taken into account when adjudicating a payment claim under the Act.

Property / Industrial Special Risks

Payment of indemnity value – before or after reinstatement? 143
In ***TJK (NZ) Limited v Mitsui Sumitomo Insurance Company Limited*** Miller J of the High Court of New Zealand considered the effect of an optional extension providing for reinstatement in the event of earthquake damage and whether the insurer must pay the indemnity value before the insured incurs the cost of reinstatement. **Adam Chylek** and **Lauren Fieldus** examine the Court's decision.

A *"wild"* decision seeks to clarify automatic reinstatement clauses and deductibles 145
Michael Bath and **Bradley Meyerowitz** consider the decision of the New Zealand High Court in ***Wild South Holdings Ltd & Maxims Fashion Ltd v QBE Insurance (International) Ltd***, in which the Court sought to provide clarity around the application of automatic reinstatement clauses and deductibles.

Interpreting the policy – individual provisions or the policy as a whole? 148
The decision of the NSW Court of Appeal in ***Australian Rail Track Corporation Limited v QBE Insurance (Europe) Limited*** highlights the importance of construing the provisions of a policy as a whole rather than each provision in isolation. **Michael Bath** and **Katie Shanks** discuss the Court's decision.

Suspicious fire claims – a hunch is not enough 151
If an insurer is seeking to rely on circumstantial evidence of an insured's misconduct to deny a claim for indemnity, the onus of proof is on the insurer. **Susan Ougham** and **Jack Geng** examine the decision in ***Mutual Community General Insurance Pty Ltd v Khatchmanian***, which demonstrates the difficulty insurers face in satisfying this burden.

Dewatering explained 153
Phillip Wotton and **Thomas Byrne** consider the decision of the NSW Court of Appeal in ***Vero Insurance Ltd v Australian Prestressing Services Pty Ltd***, which is instructive on questions of construction arising under a contract works and public liability insurance policy.

Causation: a case of "Elementary, my dear Watson"? 155
Rebecca Craig and **Stephen Doherty** examine the English case of ***Nulty v Milton Keynes Borough Council***, in which the Court considered whether the so-called "*Sherlock Holmes causation dictum*" is a sound test of causation when not all the relevant facts are known.

When flooding is not a flood – *LMT Surgical Pty Ltd v Allianz Australia Insurance Ltd* [2013] QSC 181 **158**
Susan Ougham and **Jack Geng** consider the case of ***LMT Surgical Pty Ltd v Allianz Australia Insurance Ltd***, a decision that could have potentially wide-ranging implications for all ISR insurers.

Trade + Transport

Arresting developments: existence of foreign proceedings no basis to resist ship arrest **161**
Simon Black and **David Park** examine the decision of the Federal Court in ***Atlasnavios Navegacao, LDA v The Ship "Xin Tai Hai" (No 2)***, in which the Court was asked to determine whether attempts to arrest a vessel in Australian waters could be prevented by the fact that proceedings had already been commenced in another jurisdiction.

Federal Court packs a punch with interpretation of marine insurance cargo clauses **164**
In ***Alstom Ltd v Liberty Mutual Insurance Company (and Others) (No 2)*** the Federal Court found that a deeming provision in a marine insurance policy applied so that the insurer could not rely on an exclusion clause to exclude cover for losses caused by *"insufficiency or unsuitability of packaging or preparation"*. **Faith Geraghty** and **Melissa Tan** discuss the Court's decision.

Federal Court provides guidance on procedures for charterparty termination **167**
Simon Black and **Suzanne Craig** consider the decision of the Full Court of the Federal Court in ***Ships "Hako Endeavour", "Hako Excel", "Hako Esteem" and "Hako Fortress" v Programmed Total Marine Services Pty Ltd***, which provides useful guidance on the issues surrounding the termination of bareboat charters and the rights of entities to pursue actions *in rem* for the recovery of crew wages.

Australia makes an about turn on international arbitration position **169**
Andrew Moore and **Faith Geraghty** examine the decision of the Full Court of the Federal Court in ***Dampskibsselskabet Norden A/S v Gladstone Civil Pty Ltd*** which recognises the difference between a *"sea carriage document"* and a *"charterparty"*.

Yu can't always get what Yu want **171**
Simon Black considers the decision in ***Yu v STX Pan Ocean Co Ltd (South Korea), in the matter of STX Pan Ocean Co Ltd (receivers appointed in South Korea)*** in which the Federal Court confirmed that a creditor's attempts to arrest an insolvent shipowner's vessel in Australian waters will not necessarily be prevented by operation of the **Cross-Border Insolvency Act 2008**.

Navigating recent developments in Australian maritime law **173**
Simon Black examines the recent raft of maritime legislative amendments that have been implemented in Australia.

WA Court of Appeal provides useful guidance on the principles governing the incorporation of terms and conditions applied in commercial dealings 175
Faith Geraghty and **Melissa Tan** consider the decision of the WA Court of Appeal in ***La Rosa v Nudrill Pty Ltd***, in which the Court held that an exclusion clause printed on the reverse of an invoice was not, by a previous course of dealings, incorporated into a cartage contract.

Never let the truth get in the way of a valid claim – a little white device rings alarm bells to hull underwriters 178
Faith Geraghty and **Laura Tulloch** examine the recent English case of ***Versloot Dredging BV SO DC Merwestone BV v HDI Gerling Industrie Versicherung AG & Ors***, in which the High Court held that a *"fraudulent device"* completely deprived the claimant owners of an otherwise valid marine insurance claim.

Accident + Health

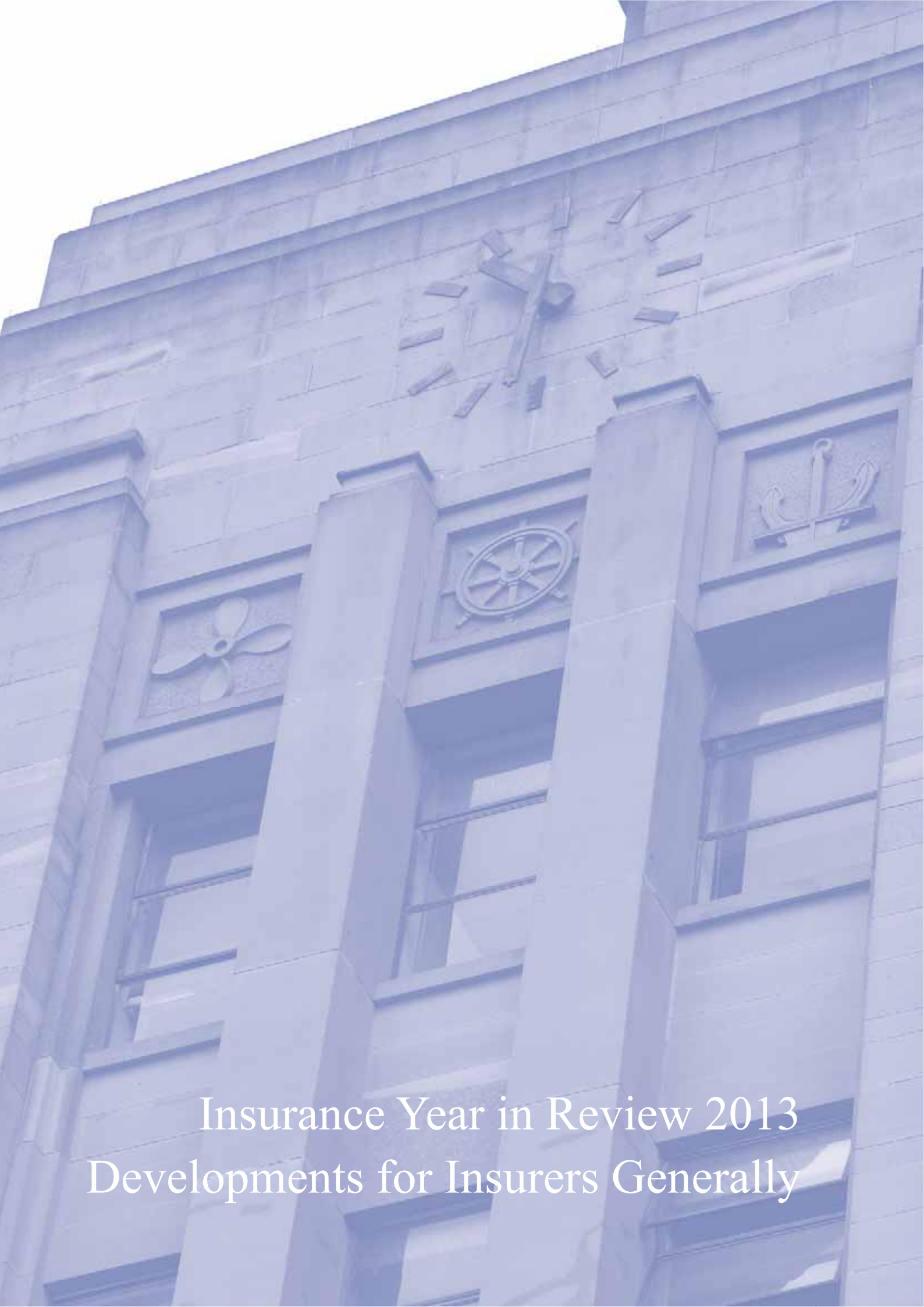
TPD or not TPD? That is the question 182
Sean O'Connor considers 2 recent decisions of the NSW Courts in claims made for total and permanent disablement benefit following injuries sustained in the workplace.

Pro Bono

Community Footprint – a year in review 185
Pro Bono Coordinator **Heidi Nash-Smith** provides a summary of Wotton + Kearney's pro bono and corporate social responsibility program, "Community Footprint", in 2013.

A lawyer's experience of a pro bono legal secondment 188
Heidi Nash-Smith and **Amanda Cefai** share their experience of providing pro bono legal services to newly arrived migrants, asylum seekers and refugees at an outreach clinic in Sydney.

Wotton + Kearney's pro bono work in practice: *SZRZM v Minister for Immigration & Border Protection* 190
Since 2011 Wotton + Kearney has partnered with Justice Connect to assist people in immigration detention in Australia seek judicial review of Independent Merits Review decisions regarding their claims for asylum. **Heidi Nash-Smith** discusses a recent case in which the client's claim for judicial review was successful.



Insurance Year in Review 2013
Developments for Insurers Generally

The ICA gets a makeover – amendments to the **Insurance Contracts Act 1984 (Cth)**

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Introduction

The **Insurance Contracts Amendment Act 2013** (**the Act**), seeks to improve the overall operation of the **Insurance Contracts Act 1984 (Cth)** (**the ICA**) by correcting a number of perceived deficiencies and clarifying several ambiguities. The Act received Royal Assent on 28 June 2013, and its various provisions will commence at different times.

Summary of changes

Of most relevance, the Act seeks to amend the provisions of the ICA relating to:

- the duty of utmost good faith;
- third-party beneficiaries;
- the duty of disclosure;
- the powers of the Australian Securities and Investments Commission (**ASIC**);
- electronic communications; and
- subrogation.

Duty of utmost good faith – sections 11, 13, 14 and 14A of the ICA

The ICA previously provided that the parties to an insurance contract were to deal with each other in *"utmost good faith"*. The amendments incorporated by the Act now clarify that a breach of the duty of good faith will be a breach of the ICA as well as a breach of contract. However, the Act does not go so far as to expressly define the duty of utmost good faith.

Although the Act does not prescribe penalties for breaching the duty of good faith, section 14A of the ICA now gives ASIC new powers to change, cancel or impose conditions on an insurer's Australian Financial Services Licence (**AFSL**) when the insurer breaches its duty of utmost good faith. This is a significant legislative development and one that insurers should make themselves familiar with.
The Act also makes it clear that the duty of utmost good faith extends to third-party beneficiaries under an insurance policy.

Third-party beneficiaries – sections 41, 48 and 48AA of the ICA

Prior to the Act, third-party beneficiaries to a policy enjoyed relatively little protection under the ICA. Third-party beneficiaries will now be afforded much the same rights as an insured under a contract of insurance.

"Third-party beneficiary" is now to be defined as:

"a person who is not a party to the contract but is specified or referred to in the contract, whether by name or otherwise, as a person to whom the benefit of the insurance cover provided by the contract extends."

Third-party beneficiaries who make a claim under a contract of liability insurance will be entitled to request that an insurer informs them, in writing, of:

- any decision on indemnity; and
- any intention by the insurer to conduct negotiations or legal proceedings on behalf of that third-party beneficiary.

The Act also provides that ASIC may bring representative actions on behalf of a third-party beneficiary to a policy.

The amendments also remove the uncertainty surrounding the question of whether a claim for indemnity by a third-party beneficiary can be adversely affected by the pre- or post-inception conduct of an insured. The revised ICA makes it clear that an insurer can rely on the conduct of an insured (for example pre-inception non-disclosure) in defending a claim made by a third-party beneficiary.

Duty of disclosure

The Act makes it easier for insureds to understand and comply with their duty of disclosure. It amends section 21(1) of the ICA to specify that disclosure by an insured must include all matters a reasonable person in the circumstances could be expected to know to be relevant "*having regard to factors including, but not limited to, the nature and extent of the insurance cover to be provided under the relevant contract of insurance*".

Amendments to section 22 of the ICA are aimed at ensuring that an insured is aware of their ongoing duty of disclosure, particularly in circumstances where there is a delay between initial pre-inception disclosure (for example, the submission of a proposal form) and the commencement of a contract of insurance.

Where there is a delay of more than 2 months between the most recent disclosure and the commencement of a contract of insurance, the insurer is now required to provide a formal notice to the insured, reminding the insured of their ongoing duty.

These provisions place an additional onus on insurers, as well as an additional administrative burden. However, insurers should ensure they comply with these new provisions, to avoid prejudicing any rights they may have to limit cover based on an insured's relevant non-disclosure.

ASIC's powers – section 11F of the ICA

Previously, ASIC had only limited administrative responsibilities in relation to insurance contracts. Under the new amendments, ASIC has increased intervention powers, in a similar vein to those already afforded to it in respect of other matters under the **Corporations Act 2001 (Cth)**.

Insurers should be aware that any breach of the ICA may now result in intervention by ASIC, and the imposition of conditions on, or the cancellation of, an insurer's AFSL.

Electronic communications – sections 71 and 72 of the ICA

Together with amendments in the **Electronic Transactions Regulations 2000 (Cth)**, insurers will now be formally entitled to provide written notices to insureds and/or third-party beneficiaries electronically. This sensible amendment removes any ambiguity surrounding this area.

Subrogation

The Act also introduces into the ICA, at section 67, a regime for the division of moneys recovered by an insurer by way of a subrogated recovery action. In short, the amendments seek to link the risks associated with the cost of these proceedings with the distribution of any moneys recovered. However, these revised rules may be contracted out of or modified in an insurance contract.

Conclusion

The amendments to the ICA, implemented by the Act, provide clarity in a number of areas that were previously clouded in confusion and ambiguity. The amendments relating to electronic communications, for example, appear sensible and should result in increased efficiencies for insurers.

Insurers should take particular note of the rights now afforded to third-party beneficiaries under policies of insurance, and the increased powers afforded to ASIC.

Insurers should also ensure that they have the necessary procedures in place to monitor the amount of time that passes between the submission of a proposal form and the inception of a relevant policy. If this period exceeds 2 months, failing to provide a prospective insured with notice setting out their ongoing disclosure obligations may prejudice the insurer's rights down the track. ■

Section 54 offers no remedy for Prepaid

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Background

Judicial determination of disputes surrounding the application of section 54 of the **Insurance Contracts Act 1984 (Cth)** (**ICA**) have largely been fact-specific and subject to subjective analysis by the courts based on the nature, purpose and wording of the particular insurance contracts involved.

The New South Wales Court of Appeal has continued the judicial debate on section 54 with its decision in ***Prepaid Services Pty Limited and Ors v Atradius Credit Insurance NV*** [2013] NSWCA 252 (***Prepaid Services***), by analysing the circumstances in which section 54 applies.

The claim

Prepaid Services Pty Limited (**Prepaid**), Optus Mobile Pty Limited (**Optus Mobile**) and Virgin Mobile (Australia) Pty Limited (**Virgin Mobile**) all supplied prepaid mobile recharge vouchers to Bill Express Limited (**Bill Express**), which in turn sold the vouchers to customers. Atradius Credit Insurance NV (**Atradius**) issued a trade credit policy to Prepaid, Optus Mobile and Virgin Mobile, which indemnified them for Bill Express' failure to meet payment obligations during the policy period (**the policy**). Bill Express defaulted on payments to the 3 companies , each of which made a claim on the policy.

As is relevant to the section 54 analysis, the *"Causes of Loss"* for which the policy provided cover included *"the failure of* [Bill Express]*, under the terms of the Contract, to pay any invoiced payment obligations to the Insured ... on Due Date"*. *"Contract"* was stated to mean the agreement identified in item 6 of the Declarations, which in turn stated:

> *"Contract(s): Sub Agency Agreement between*
> *(i) Prepaid, Optus Mobile, Optus Internet and Bill Express*
> *(ii) Optus Mobile and Bill Express; and*
> *(iii) Virgin Mobile and Bill Express for open account sales of Goods Insured* [recharge vouchers] *up to thirty (30) days from date of invoice."*

A proposal submitted by the companies

prior to the policy being issued was expressly incorporated into the policy terms. The proposal provided that credit terms for supply to Bill Express were *"21 days with weekly settlement"*.

Although written agreements in respect of contracts identified at (i) and (iii) above were included with the proposal, no written agreement between Optus Mobile and Bill Express was provided to Atradius prior to the policy being issued. *"Due date"* was defined to mean the date Bill Express was required to make payment to the insured *"under the terms of the Contract"*.

Atradius denied the claim made by Optus Mobile in respect of unpaid invoices it issued to Bill Express. It adopted the position that the policy only insured defaults under a contract requiring Bill Express to pay up to 30 days from the date of the invoice. However, the unpaid amounts claimed by Optus Mobile arose under a contract requiring payment by Bill Express 30 days from the date Optus Mobile issued a statement to Bill Express (which amounted to more than 30 days from the date of invoice). Atradius maintained that the claim did not therefore arise under a contract between Optus Mobile and Bill Express that was insured by the policy, and accordingly, that it fell outside the scope of the policy's cover.

Optus Mobile argued that its supply of recharge vouchers to Bill Express under a contract requiring payment more than 30 days from invoice was an act or omission by Optus Mobile to which section 54 applied, preventing Atradius from denying the claim.

The decision

In analysing the application of section 54 to Optus Mobile's claim, the Court emphasised the importance of defining the nature of the risk insured. In doing so, it considered and discussed several authorities including ***FAI General Insurance Co Ltd v Australian Hospital Care Pty Limited*** [2001] HCA 38 (***Australian Hospital Care***); ***Johnson v Triple C Furniture & Electrical Pty Ltd*** [2010] QCA 282 (***Johnson***); and ***Maxwell v Highway Hauliers Pty Limited*** [2013] WASCA 115 (***Highway Hauliers***).

The Court distinguished between ***Highway Hauliers*** and ***Johnson*** based on the way in which each court had characterised the effect of the insurance contract and the risk insured. In ***Johnson***, the nature of the risk insured was based on the operation of an exclusion regarding the pilot's qualifications; in Highway Hauliers, the Court considered that the substance of the risk insured did not include the condition regarding the driver's qualifications.

The Court considered the legislative history of section 54 and observed that it was:

> *"intended to prevent reliance upon temporal exclusions, such as those considered in* [***Johnson*** and ***Highway Hauliers***]*, as well as other provisions which operated, because of an act or omission occurring after the insurance was entered into, to suspend cover or entitle the insurer to deny a claim irrespective of whether the insurer had suffered any prejudice as a result."*

Because it took into account the operation of an exclusion when identifying the risk insured, the ***Johnson*** decision was not considered to be in accord with the approaches taken in Australian Hospital Care, Highway Hauliers or legislative intent.

With respect to Optus Mobile's claim, the Court of Appeal determined that the policy provided indemnity against Bill Express's failure *"to meet a payment obligation under, and by the time required by, a specified contract"* and that in the absence of Optus Mobile identifying

that contract, the parties adopted the description contained in Item 6 of the Declarations, which itself was based on the substance of the proposal. The Court concluded that Atradius refused Optus Mobile's claim because it was for a payment default not covered by the policy, not because Optus Mobile had contracted with Bill Express on different terms. Accordingly, section 54 did not apply and Atradius was free to deny the claim.

Implications

Prepaid Services emphasises the importance of determining the nature of the risk insured – and the substance and effect of the insurance contract – in analysing the application of section 54. The decision looks at the legislative intent behind the section and suggests that policy exclusions should not be relied on when characterising the effect of a policy and defining the risk insured. Optus Mobile's claim fell outside the scope of the policy cover because the specified contractual terms formed part of part of the risk insured. Through its analysis, the Court implicitly approved of the approach taken in Highway Hauliers and offers some guidance in analysing future claims.

Upping the ante: changes to offers of compromise in Victoria and NSW give defendants more options

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Introduction

During 2013 changes were made to the rules regarding offers of compromise in both Victoria and NSW. The amendments were introduced in part to clarify confusion about whether offers of compromise could include – or even refer to – costs.

The amendments are mostly to the advantage of defendant insurers, as they provide greater scope to apply pressure regarding costs, and thereby resolve disputes.

Victoria

Previously an offer of compromise was invalid if stated (or suggested) to be inclusive of costs. However amendments to the **Court Rules** now allow *"all in"* offers. From 1 September 2013 (7 October 2013 for County Court matters), an offer of compromise must state that it is inclusive of costs, or that costs will be paid in addition.

Other amendments to the Rules provide that:

- if a plaintiff unreasonably refuses an offer of compromise and the claim is ultimately dismissed (as opposed to merely achieving a less favourable outcome), the defendant will obtain standard costs up to the date of the offer, and indemnity costs thereafter; and
- the courts can take into account pre-litigation offers when determining costs. A Court has the discretion to order a refusing party to pay costs in much the same way as a Calderbank offer, except one that is made before litigation commences.

At first blush, the amendments are a positive development for defendants. Costs-inclusive offers are attractive because they provide certainty as to the final sum to be paid, and enable claims to be more promptly finalised. Such offers could previously only be made in the form of Calderbank letters, leaving the question of costs to the Court's discretion. As such, the amendments now allow parties to make costs-inclusive offers *"with teeth"*.

However some caution is required. Short

of succeeding on liability, a defendant needs to establish its offer is *"more favourable"* that the ultimate outcome. Costs-inclusive offers of compromise will be more difficult for the Court to assess when determining whether one outcome is *"more favourable"* than another. The Court will have to assess the costs at the time the offer was refused.

This issue has previously plagued judicial assessment of Calderbank offers and litigation on this point has already arisen since the amendments came into effect, acknowledging that full taxation of costs may be required before the issue can be determined (***Metricon Homes Pty Ltd v Frederick Sawyer & Ors*** [2013] VSC 518). As such, offers of this kind are likely to be used sparingly.

New South Wales[1]

By contrast, the amendments to the **Uniform Civil Procedure Rules** have moved NSW in the opposite direction.

As of 7 June 2013, offers of compromise in NSW cannot include any amount for costs and must not be expressed to be inclusive of costs.

The amendments attempt to address the confusion that surrounded the previous rule – that offers of compromise had to be *"exclusive of costs"*.

Relevantly, an offer may now propose:

- judgment in favour of the defendant with no order as to costs, or with a provision that the defendant will pay the plaintiff a specified sum in relation to costs (see below); or
- that the offeror will pay costs as agreed or assessed up to the time the offer was made.

In other words, an offer of compromise may still be made *"plus costs"*, as long as no figure for costs is specified.

The amendments also confirm that where an offer of compromise is accepted and is silent as to costs, the party for whom the offer proposes judgment will be entitled to costs on the ordinary basis, up to the time the offer was made.

It is worth noting that although the amendments prohibit offers of compromise from including *"any amount for costs"*, this prohibition is excluded in the case of an offer that proposes judgment for the defendant along with a payment of costs to the plaintiff.

This provides an additional option for defendants to encourage settlement of claims by offering to pay the plaintiff's costs, despite having a judgment entered against that plaintiff.

Conclusion

Amendments to the Victorian and NSW rules regulating offers of compromise have increased the options available to defendants to encourage the resolution of claims.

In Victoria, offers of compromise can now be made on an "*all in*" basis, affording defendants greater certainty in terms of the ultimate amount of the settlement offer. This may be tempered somewhat by the potential complication of enforcement by the Courts, due to the need to assess costs at the time of the offer.

In NSW, the confusion over the status of costs has been removed for offers of compromise made after 7 June 2013. Furthermore, defendants now have the ability to serve a plaintiff with an offer of compromise that proposes resolution of the proceeding in favour of the defendant, together with an offer by the defendant to pay the plaintiff's costs. ■

1 For a discussion of the law in NSW prior to the amendments, see the article "Offers of compromise - enough already! Is silence really a virtue? Plus costs or not?" by Jacqueline Grace and Amanda Cefai at page 24.

Offers of compromise - enough already! Is silence really a virtue? Plus costs or not?

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Exactly what constitutes a valid offer of compromise has been a hotly contested subject for some time. This article explores the amendments to the **Uniform Civil Procedure Rules** that came into effect on 7 June 2013, the recent Court of Appeal Case of ***Whitney v Dream Developments*** [2013] NSWCA 188 and the implications for insurers.

Formerly, Rule 20.26 of the **Uniform Civil Procedure Rules (NSW) 2005** (**UCPR**) specified that *"an offer must be exclusive of costs, except where it states that it is a verdict for the defendant and that the parties are to bear their own costs".*

Pursuant to the rationale in ***Old v McInnes*** [2011] NSWCA 410, an offer that provided for a payment of costs *"as agreed or assessed"* was invalid.

The amendment

The UCPR now provides that an offer *"must not include an amount for costs and must not be expressed to be inclusive of costs"* (Rule 20.26(3)(c)) and may propose *"that the costs as agreed or assessed up to the time the offer was made will be paid by the offeror"* (Rule 20.26(3)(b)).

At face value, it appears that an offer made on the basis that one party will pay the other's costs *"as agreed or assessed"* does not fall foul of the new rules. In ***Council of the City of Canterbury v Milich*** (unreported) NSWSC (10 July 2013), Basten JA made this very comment in obiter; however, as yet there is no direct judicial consideration of this section.

Pre-amendment Offers – *Whitney v Dream Developments Pty Ltd*

Given the amendments to the UCPR, this case is only relevant to offers made before 7 June 2013. In this case, a bench of 5 judges considered:

- whether an offer expressed as *"plus costs as agreed or assessed"* or similar complies with Rule 20.26; and
- if not, whether such an offer can take effect as a Calderbank offer when

considering whether a special order as to costs ought be made.

In this case, the relevant offer, which was bettered at trial, was made by Dream Developments Pty Ltd (**DD**) and included the wording *"... the Defendant to pay the Plaintiff's costs as agreed or assessed"*. DD claimed its costs from the date of that offer. Ultimately, it was held that the offer of compromise was invalid because it was articulated to be *"plus costs as agreed or assessed"*. Bathurst CJ went on to hold that an offer of compromise cannot operate as a Calderbank offer unless there was an indication from the covering letter or in the surrounding circumstances that would bring into play the Calderbank principles.

Implications for insurers

In summary, where an offer of compromise that includes the words *"plus costs as agreed or assessed"* or similar is made:

- before 7 June 2013, it will be held to be invalid unless it is accompanied by a Calderbank letter containing words such as:
  "If for any reason the enclosed offer of compromise is found to be not validly made under the UCPR, then this letter is intended to be a Calderbank offer in the sum of $[insert figure] plus costs on the ordinary basis to the date of the offer, open for acceptance for 28 days from the date of this letter"; or
- after 7 June 2013, it appears that offer will be valid whether or not these words are used; however, for abundant safety, until this rule has been judicially tested it would be wise to serve such offers under cover of a Calderbank letter.

Judgments for the defendant

The amendments to the UCPR (in Rule 20.26(3)(a)) have provided further options for insurers seeking a judgment entered for the defendant. Under the new rules, an offer may propose a judgment in favour of the defendant with:

- no order as to costs, with each party paying its own costs of the proceedings to date;
- the defendant to pay to the plaintiff a specified sum in respect of the plaintiff's costs; or
- the costs as agreed or assessed up to the time the offer was made being paid by the offeror.

These amendments allow greater flexibility for insurers by enabling them to offer a resolution to the proceedings on the basis that a judgment is entered for the defendant, with those offers potentially attracting the benefits of rigid cost sanctions if not accepted. ■

Waving goodbye to inadvertent waiver of privilege?

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Introduction

Large-scale proceedings often breed ancillary disputes, which can overshadow the main litigation. These disputes can be hotly contested, particularly when they relate to discovery.

The recent High Court of Australia case of ***Expense Reduction Analysts Group Pty Ltd v Armstrong Strategic Management and Marketing Pty Ltd*** [2013] HCA 46 (6 November 2013) (***Armstrong***) is a case in point. Indeed, the High Court did not hold back in expressing its concern that litigation of this type would even make it through the Court's doors.

In this case, Armstrong sought to rely on documents inadvertently disclosed by a defendant during the discovery process. In a unanimous decision, the High Court found that Armstrong had to return documents inadvertently disclosed to it and could not rely on their contents in the proceeding.

It is important that lawyers and insurers are aware of the ramifications of this decision and that they know how to act when they either inadvertently disclose or receive *"privileged"* documents.

The case has greater ramifications. The High Court criticised Armstrong and its lawyers for raising a dispute when it was not appropriate to do so having regard to the Civil Procedure obligations for parties to resolve disputes. The High Court noted that *"*[u]*nduly technical and costly disputes about non-essential issues are clearly to be avoided"*.

Background

Armstrong issued proceedings in the Supreme Court of New South Wales against 10 parties, including Expense Reduction Analysts (**ERA**). The proceedings related to a dispute surrounding a failed business transaction.

The parties were ordered to make discovery. ERA produced approximately 60,000 documents. With the assistance of computer software, the documents were vetted in terms of privilege. Documents were flagged either as being privileged or non-privileged. Non-privileged documents were then automatically migrated into a list of documents that were subsequently provided to Armstrong.

While reviewing copies of ERA's discovered documents, Armstrong realised ERA had disclosed certain *"privileged"* documents. Armstrong wrote to ERA advising of the disclosure, but refused to return the documents, instead claiming privilege had been waived.

In response, ERA advised that:

- the privileged documents had been provided inadvertently; and
- there was no intention to waive privilege.

ERA sought the return of the documents and an undertaking that Armstrong would not rely on the documents in the proceedings. Armstrong refused.

ERA subsequently applied for an injunction preventing Armstrong from relying on the documents.

The lower courts

At first instance, Bergin CJ in Eq considered the relevant question for determining the dispute was whether ERA had formed the view that the documents were privileged at the time of compiling the list of documents, but then inadvertently produced the documents. Her Honour said that if ERA formed this view and mistakenly produced the documents, privilege would not be waived.

Her Honour found that ERA had not waived privilege over some of the documents in question – the documents were listed as privileged in the list of documents, but duplicates of those documents were inadvertently produced to Armstrong. This, her Honour held, was evidence that the documents were disclosed by mistake. On the other hand, her Honour found there was no express or implied intention to maintain privilege of some of the other documents at the time of disclosure, and therefore ERA could not claim the documents were inadvertently disclosed.

On appeal

The Court of Appeal took a very different view. Campbell JA (with Sackville AJA and MacFarlane JA agreeing) rejected the Supreme Court's analysis. His Honour held the proper path of enquiry was in relation to the law of *"confidential information"*.

Campbell JA was unable to find any authority dealing directly with the return of privileged documents produced by mistake. However, relying on the English decision of ***Guinness Peat Properties Ltd v Fitzroy Robinson Partnership***[1], his Honour considered the relevant test was whether the disclosure of the documents imposed on Armstrong an *"obligation of conscience"* not to rely on them.

When considering the circumstances of this case, Campbell JA was not satisfied that Armstrong should have realised there was a mistake in the disclosure of documents, as it had a right to believe that ERA would have thoroughly considered the documents provided in the context of discovery before disclosing them. Campbell JA found ERA's failure to thoroughly consider the issue was its fault, not Armstrong's. Accordingly, no injunctions were granted.

The High Court

In a unanimous decision, the High Court took a critical view of the lower courts' approaches. The Court was of the view that ERA's mistake was obvious. It considered that the technical approaches to waiver and the law of confidentiality were not appropriate in this case.

The High Court focused on the obligations imposed on parties under the **Civil Procedure Act 2005 (NSW)** (**CPA**).

It held that the lower courts should have exercised their authority to ensure the issues were determined in a speedy and inexpensive fashion, and that the courts should have rectified ERA's mistake by preventing Armstrong from relying on the documents.

The High Court said:

"[w]*hat the Court was faced with was a mistake which had occurred in the course of discovery. It was necessary that the mistake be corrected and the parties continue with their preparation for trial...*

The documents disclosed during the discovery process were privileged, and [ERA's] *claim that disclosure occurred by mistake was not disputed. Any allegation of waiver was going to turn on a legal, technical argument tangential to the main proceedings, and should not have been made."*

1 [1987] 1 WLR 1027

Implications

Insurers often face situations where multiple parties hold sensitive documents. Solicitors, brokers, experts and loss adjustors all have access to documents over which privilege can be claimed.

From time to time, documents can be inadvertently disclosed, particularly when there are vast numbers of documents passing electronically between parties in large-scale litigation. Despite best endeavours, mistakes do happen and documents will end up in the hands of an opponent, but insurers can take some comfort in the High Court's decision on this potential cause of serious headaches.

In the absence of an express intention to disclose a document, and provided prompt steps are taken to correct the inadvertent disclosure, the documents should probably be returned to the party that made the inadvertent disclosure and it is probably safe to assume that they cannot be relied on. However, this will depend on the circumstances.

In ***Armstrong***, the Court was influenced by the large scale and complexity of the litigation, as well as ERA's prompt attempt to have the documents returned. However, the Court may not be willing to forgive lawyers' mistakes in all circumstances, especially if a document assumes especial importance and the knowledge gained from the inadvertent disclosure cannot easily be put to one side. [2]

The Courts can also use the CPA as a sword to place sanctions on parties seeking to benefit from another's mistake in circumstances where it is not appropriate to raise the issue of the mistake.

It is clear that when a privileged document has been obtained in the course of litigation and there is a real issue as to whether it was an intentional disclosure, solicitors and insurers should be careful how they use that evidence and should probably return the evidence if promptly requested to.[3] The potential consequences of not doing so could involve sanctions under the CPA.

Indeed, the High Court has sent a clear message that courts should take a pragmatic view when dealing with simple errors that occur in complex litigation. Parties taking an aggressive or technical approach in an ancillary dispute are likely to fall on the wrong side of the courts. ■

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2 As the High Court said:

"[t]*he courts will normally only permit an error to be corrected if a party acts promptly. If the party to whom the documents have been disclosed has been placed in a position, as a result of the disclosure, where it would be unfair to order the return of the privileged documents, relief may be refused. However, in taking such considerations (analogous to equitable considerations) into account, no narrow view is likely to be taken of the ability of a party, or the party's lawyers, to put any knowledge gained to one side. That must be so in the conduct of complex litigation unless the documents assume particular importance.*"

3 The High Court's determination is in line with the current *"Inadvertent Disclosure Guidelines"* published by the Law Institute of Victoria. Paragraphs 2 and 4 provide (at www.liv.asn.au/PDF/Practising/Ethics/2008GuideInadvertentDisclosure.aspx):

"[a] *practitioner is under a duty to pass on to a client (and use) all information which is material to the client's interests, regardless of the source of that information* ***unless the practitioner knows that the information has been accidentally, unlawfully, improperly or surreptitiously obtained.***

...

Where it is immediately obvious to a practitioner that confidential documents have been mistakenly disclosed, the practitioner should not read the documents and should inform the other side of the mistake and make arrangements for the return of the confidential documents..." [emphasis added]

Is a consent judgment a judgment at all?

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Introduction

If a plaintiff obtains a consent judgment against a defendant and the judgment is paid in full, can the plaintiff bring a second action to try to recover more damages from another alleged tortfeasor, or is the plaintiff restricted to bringing one and only one action?

In ***Newcrest Mining Limited v Thornton*** [2012] HCA 60 (delivered 13 December 2012), the majority of the High Court determined that a plaintiff can bring more than one action, as a settlement agreement is not subject to a judicial determination of liability nor a consequential award of damages.

Background

In 2004, Michael Thornton injured his knee in the course of his employment at a mine site in Western Australia. His claim for workers compensation payments and common law damages against his employer was settled. A consent judgment was filed in his favour in the District Court of Western Australia, with no admission as to liability.

More than a year after the settlement, Mr Thornton commenced proceedings against Newcrest Mining Limited (**Newcrest**) as owner and operator of the mine site.

Summary judgment

Newcrest applied for and obtained summary judgment in the District Court of Western Australia on the basis that section 7(1)(b) of the **Law Reform (Contributory Negligence and Tortfeasors' Contribution) Act 1947 (WA)** (**the Act**) operated to preclude Mr Thornton from bringing the action. This section provides that sums recoverable under judgments given in successive actions *"shall not in the aggregate exceed the amount of the damages awarded by the judgment first given"*.

Court of Appeal decision

The Court of Appeal overturned the summary judgment by ruling that Mr Thornton had not been *"awarded"* damages in his initial action against his employer when the consent judgment was entered.

High Court decision

In considering the appeal by Newcrest, the High Court of Australia was asked to consider whether the restrictions on the recovery of damages in multiple actions

under the Act (and equivalent legislation in New South Wales, Queensland and the Northern Territory) only applied to damages awarded after a judicial assessment rather than a judgment entered by the consent of the parties. Newcrest submitted that the findings of the Court of Appeal could enable a plaintiff, knowing that a consent judgment is no bar to future pursuit of claims, to adopt a scattergun approach to litigation and seek to improve his or her position against potential tortfeasors.

Mr Thornton contended that the interpretation of the phrase *"damages awarded by the judgment first given"* must require judicial determination of the damages recoverable by a plaintiff.

The majority of the High Court found that a consent judgment merely gives effect to a settlement agreement between the parties and cannot amount to an award of damages.

Implications

The High Court has made it clear that the filing of a consent judgment does not preclude a plaintiff from pursuing multiple tortfeasors for damages arising from the same facts and circumstances.

The High Court judgment is a reminder to take care when settling claims that involve multiple tortfeasors, to ensure the consent judgment adequately disposes of all claims, including potential claims. ■

Expanding rights of subrogation – Bupa blooper?

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Introduction

The doctrine of subrogation is well established. It allows an insurer to exercise the rights of an insured against a third party who caused or contributed to a loss sustained by the insured. Generally speaking, an insurer's right of subrogation crystallises once indemnity has been extended to an insured under a policy of insurance.

The doctrine is not a legal right; rather, it is seen as a right that is contractual and equitable in nature (***Woodside Petroleum Development Pty Ltd v H & R – E & W Pty Ltd*** (1999) 20 WAR 380).

The interaction between these contractual and equitable principles was recently considered in the Victorian Supreme Court decision of ***Bupa Australia Pty Ltd v Gloria Shaw and James Walker (as Joint Executors of the Estate of Norman Shaw) & Anor*** [2013] VSC 507.

Background

In September 2005, the insured, Norman Shaw, underwent surgery. Due to consequences arising from that procedure, he required hospitalisation and ongoing treatment until his death in May 2010. His health insurer, Bupa Australia Health Pty Ltd (**Bupa**), paid almost $340,000 in treatment expenses pursuant to Mr Shaw's health insurance policy (**the policy**). The policy was a *"policy of indemnity"*, which indemnified Mr Shaw in respect of his liability to pay medical expenses.

Mr Shaw commenced proceedings against the surgeon, seeking damages for medical negligence (**the negligence claim**). After Mr Shaw's death, his estate continued the negligence claim.

Mr Shaw's lawyers had notified Bupa that a claim was being pursued. However, the negligence claim was ultimately settled in December 2011 without Bupa's knowledge and without accounting to Bupa. Instead, Mr Shaw's estate entered into a release with the surgeon, which – although it purported to carve out Bupa's potential entitlements (if any) – essentially required the surgeon to indemnify Mr Shaw's estate in any recovery action for any amount to which Bupa was entitled to recover. After Bupa learnt of the settlement, it sought reimbursement from Mr Shaw's estate.

However, the estate's lawyers denied that the estate was liable to account to Bupa (and it appears the surgeon also refused to meet Bupa's claim, for reasons that are not clear). Bupa then issued proceedings against Mr Shaw's estate.

The parties' arguments

The estate denied that it was liable to repay Bupa. It argued that if Bupa had a right of subrogation (noting there was no specific statement in the policy recognising this entitlement), that right was excluded or modified by the terms of the policy and, as such, was effectively waived.

The Court accepted Bupa's submission that as the policy was a policy of indemnity – in this case a policy indemnifying the insured for medical and like expenses – Bupa was entitled to exercise a right of subrogation notwithstanding the absence of an express contractual term in the policy.

In considering this issue, Almond J followed the decision of ***Barwick CJ in State Government Insurance Office (Qld) v Brisbane Stevedoring Pty Ltd*** (1969) 123 CLR 228, which stated (at 240) that:

> *"It is settled law that an insurer who has paid the amount of a loss under a policy of indemnity is entitled to the benefit of all the rights of the insured in the subject matter of the loss and by subrogation may enforce them. This right of subrogation is inherent in the contract of indemnity.*
>
> *"It is also settled law that an insured may not release, diminish, compromise or divert the benefit of any right to which the insurer is or will be entitled to succeed and enjoy under his right of subrogation. On occasions an attempt by the insured to do so will be ineffective against the insurer because of the knowledge of the circumstances which the person under obligation to the insured may have. On other occasions when the insured's act has become effective as against the insurer, the insured will be liable to the insurer in damages, or possibly, on some occasions for money had and received."*

Mr Shaw's estate argued that no right of subrogation existed because:

- the policy did not impose a legal obligation for Bupa to indemnify Mr Shaw for medical expenses that Bupa had paid, which meant that benefits must have been paid in error; and
- if the payments were made in error, then the indemnification provided for under the policy was made in error, so no right of subrogation attached to it.

In the alternative, Mr Shaw's estate also argued that certain terms in the policy limited the rights of subrogation to the effect that Bupa had waived such rights.

The allegedly mistaken payments

Mr Shaw's estate relied on the following terms in the policy, which provided that:

- the insurer had a right to cease paying benefits to the insured once a third party had been identified (in this case, the surgeon); and
- the policy allowed Bupa to *"take over"* the insured's proceeding against the surgeon, and in doing so, Bupa would have ceased paying benefits to the insured.

The estate said that because Bupa could have ceased making payments in March 2010 (when it became aware of the negligence claim), any payments made after that time were made in error, even if they were made in good faith.

The Court did not accept the estate's arguments. It found that Bupa:

- had not made payments to the insured in error;
- was acting in good faith by honouring the terms of the policy (and providing the insured with benefits at a critical time); and
- had sufficiently placed the estate on notice of its intention to seek reimbursement of the benefits paid to or on behalf of the insured.

The alleged contractual limitation

As already mentioned, the policy terms did not expressly state that Bupa had a right of subrogation.

However, the Court accepted that the rules of equity recognise that a right of subrogation would arise if, under a policy of indemnity, an insured was indemnified in respect of his or her loss.

Mr Shaw's estate argued that because Bupa did not recover any payments made *"in error"* to the insured within a 2-year period even though the policy expressly stated that it could do so, this imposed limits on its rights of subrogation (the recovery term).

The Court disagreed with the estate's arguments.

The Court said that although *"an insurer's right of subrogation, whether as a contractual term implied by law, or a right that arises in equity as a necessary incident of an indemnity contract, may be expanded, modified or excluded either expressly or impliedly by the terms of the contract"*, it did not view the recovery term as being expressly or implicitly in conflict with the general right of subrogation.

The net effect was that Mr Shaw's estate was ordered to reimburse Bupa for the whole of its liability, leaving the estate with only a modest balance.

Comments

The decision in this case makes it clear that:

- a right of subrogation may arise because of the express terms of the contract but, even in the absence of such a term, an insurer may exercise this right in accordance with the principles of equity;
- unless an insurer has expressly waived its right of subrogation through the terms of the policy, the insurer's right of subrogation may remain intact; and
- if an insured compromises the insurer's rights of subrogation, the insured may be liable to the insurer in damages, which may include money had and received.

This clarification of the law relating to subrogation is no blooper, but the insured's failure to account to the insurer from the outset certainly was!

It is important to note that although it was not relevant to the Court's deliberations in this instance, the **Insurance Contracts Act 1984 (Cth)** — and the recent amendments to that Act – contain provisions regarding subrogation, including for the prioritisation of proceeds following recovery.

Cutting either way: Courts both extend and limit the scope of proportionate liability in 2013

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Introduction

2013 saw important appeal decisions with similar facts pull in opposite directions.

These cases posed 2 important questions regarding the scope and applicability of Part 4 of the **Civil Liability Act 2002 (NSW)** (**the NSW Proportionate Liability Regime**). The 2 essential questions thrown up for the Courts and the answers given were:

- Where co-defendants have each technically harmed the plaintiff in different ways but each type of harm sounds in the same ultimate economic damage to the plaintiff, should the NSW Proportionate Liability Regime apply? The High Court decision of ***Hunt & Hunt v Mitchell Morgan*** [2013] HCA 10 (***Hunt & Hunt***) has confirmed that if co-defendants cause the same ultimate economic damage, proportionate liability will apply.
- Is it possible for parties to contract out of the NSW Proportionate Liability Regime through contractual indemnities without expressly referring to the legislation? The NSW Court of Appeal decision of ***Perpetual Trustee Company Ltd v CTC Group Pty Ltd*** (No. 2) [2013] NSW CA 58 (***Perpetual Trustee***) has confirmed this is possible.

The effect of ***Hunt & Hunt*** is to broaden the applicability of the NSW Proportionate Liability Regime which will be welcome news to insurers and insured defendants. On the other hand, the effect of Perpetual Trustee is to limit the application of proportionate liability where the insured has granted an indemnity. This raises issues as to contractual assumption of risk by insureds.

In ***Hunt & Hunt*** the High Court also held that the Victorian Court of Appeal decision of ***Quinerts***[1] which involved a similar factual scenario, was wrongly decided. Victorian Courts will also now

1 ***St.George Bank Limited v Quinerts Pty Ltd & Anor*** (unreported, County Court of Victoria, Judge Kennedy, 4 August 2008 (***Quinerts***)

be bound to follow the High Court ***Hunt & Hunt*** decision.

Hunt & Hunt

This was a mortgage fraud case in which the plaintiff lender sued fraudsters for fraudulently obtaining certificates of title and Hunt & Hunt solicitors for failing to secure the loan by registered mortgage.

The plaintiff could not recover its loan moneys because:

- it had paid the loan moneys out due to the fraudsters' wrongdoing; and
- it had no security for the loan due to Hunt & Hunt's wrongdoing.

The question was whether the paying out of the loan money on one hand, and lack of security on the other, were:

- two distinct losses; or
- only conditions necessary for the ultimate economic damage to the plaintiff, namely the loss of the loan monies.

Minds differed in the NSW Courts. The Victorian Court of Appeal in ***Quinerts*** also waded into the argument, finding that there were 2 losses rather than just one loss in both the facts of the ***Quinerts*** case and (by analogy) on the facts in ***Hunt & Hunt***.

On appeal, the majority of the High Court in ***Hunt & Hunt*** gave a very broad interpretation of the economic damage or loss which concurrent wrongdoers must cause by defining it as *"the injury and other foreseeable consequences suffered by a plaintiff"*. The High Court disagreed that there were 2 distinct losses. It defined the plaintiff lender's damage as *"its inability to recover the moneys it advanced"* and found that the actions of the fraudsters and Hunt & Hunt were both necessary conditions for that singular damage. In doing so, the High Court held that ***Quinerts*** was wrongly decided. Victorian Courts will now have to follow the High Court decision unless a particular case can be distinguished on its facts.

Perpetual Trustee

In NSW parties may contract out of proportionate liability. However, there has been great uncertainty for many years as to whether a contractual indemnity is effective to contract out of the NSW Proportionate Liability Regime without expressly referring to the legislation.

In Tasmania, this question was answered in the 2010 decision of ***Aquagenics Pty Ltd v Break O'Day Council*** [2010] TASFC3. That case held that an indemnity need not expressly refer to contracting out of the Tasmanian proportionate liability regime to be effective.

Now NSW has followed Tasmania by confirming that:

- an indemnity provision can be effective to contract out of the NSW Proportionate Liability Regime as long as it makes express provision for the rights and liabilities of the parties;
- as a result, there was no need for the indemnity to expressly refer to the **Civil Liability Act 2002 (Cth)** (**the CLA**).
- it was irrelevant whether the indemnity was entered into before the **CLA**.

Implications

Hunt & Hunt

This case should be welcome news for insurers and defendant insureds alike. The broad definition of economic damage or loss given by the High Court will mean more defendant insureds will be able to limit their liability to the extent of their respective fault. With

Quinerts overturned, there is now clarity for insurers in both NSW and Victoria over the correct approach to determining the relevant loss or damage caused by defendants in cases involving similar facts to ***Hunt & Hunt*** and ***Quinerts***.

Perpetual Trustee

The implications of this decision are far-ranging and include:

- Principals under contracts will now rely on indemnity provisions as a way to contract out of the proportionate liability provisions in the CLA.
- Underwriters should enquire whether insureds have given contractual indemnities. Insureds may also start asking insurers' permission to grant indemnities.
- It is now clear that many indemnity clauses will create a contractual liability over and above the proportionate liability that would apply under the CLA. In giving an indemnity, an insured may now be assuming a liability that is greater than the underwriter agreed or intended. Many liability policies exclude cover for liability assumed under contract. As a result, an insured who grants an indemnity may find it triggers the contractual liability exclusion under the policy. The effect of the exclusion would be:
    - to limit the insurers' liability to the extent of the insured's proportionate liability; and
    - leave the balance of the liability (the difference between proportionate and indemnity liability) for the insured to pick up. ■

Claim not covered? No defence costs

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Introduction

On 12 July 2013, the Queensland Court of Appeal handed down its decision in ***Bank of Queensland Limited v Chartis Australia Insurance Limited*** [2013] QCA 183.

This case concerns an appeal by Bank of Queensland Limited (**BOQ**) from a decision of Jackson J in the Supreme Court of Queensland. His Honour held that Chartis Australia Insurance Limited (**Chartis**) was not liable to indemnify BOQ for defence costs where the relevant third-party claim was excluded from cover.

Background

The matter owes its origins to the infamous collapse of Storm Financial Limited. In 2010, the Australian Securities and Investments Commission (**ASIC**) commenced proceedings against BOQ in the Federal Court of Australia. The proceedings were brought on behalf of Barry and Deanna Doyle (**the Doyles**).

It was alleged that BOQ had acted unconscionably in entering into a number of home loan contracts and a mortgage with the Doyles, and by making advances pursuant to the contracts. ASIC and the Doyles also alleged that BOQ was a *"linked credit provider"* under the **Trade Practices Act 1974 (Cth)**, and on that basis was jointly and severally liable for certain conduct by Storm Financial Limited.

BOQ notified the claim under a professional services liability policy with Chartis (**the policy**). In April 2011, Chartis declined to indemnify BOQ. Chartis relied on the exclusion for claims arising out of any actual or alleged loan, lease or extension of credit (**the lending exclusion**).

The decision at first instance

BOQ applied to the Supreme Court for a declaration that Chartis was liable to indemnify it in respect of any *"loss"* regarding the Doyles' claim. *"Loss"* was defined in the policy to mean any damages, judgment or settlement.

BOQ also sought a declaration that Chartis was liable to cover the *"defence costs"* incurred in relation to the Doyles' claim. The term *"defence costs"* was defined to mean any reasonable fees, costs and expenses resulting from the investigation, adjustment, defence and appeal of any third-party claim.

Jackson J refused to declare Chartis liable to indemnify the loss arising from the Doyles' claim, concluding that the Court could not make this order because no loss had yet occurred.

His Honour otherwise declined to make any declaration about the operation of the lending exclusion, explaining that the underlying facts relevant to the exclusion were limited to the allegations made by ASIC and the Doyles in the Federal

Court. Until those facts were established or agreed, any declaration about the lending exclusion would be merely hypothetical.

Accordingly, the decision centred on whether or not Chartis was liable to indemnify BOQ for the defence costs. Chartis asserted that the lending exclusion applied equally to defence costs and loss. BOQ pointed to the wording of the exclusions section of the policy, noting that each exclusion was predicated by the words, *"The insurer shall not be liable to make any payment for Loss"*. BOQ argued that the absence of the term *"defence costs"* meant that the exclusions worked only to exclude cover for loss (and not defence costs).

Jackson J accepted that on the ordinary meaning of the language, the exclusions worked only to exclude indemnity for loss. However, his Honour confirmed that the proper construction of the contract required a business-like approach, and that any inconsistency was to be resolved on the basis that the different parts of the contract were intended to work harmoniously.

Applying these principles, Jackson J determined that it would be an unlikely commercial result if Chartis was liable to indemnify BOQ for defence costs in relation to a claim that was not covered by virtue of an exclusion.

His Honour also considered the wording of the insuring clause, noting the requirement that Chartis pay for loss and defence costs arising from a covered claim. His Honour concluded that overall, neither the subject matter nor the text of the policy indicated that it was intended to deal differently with loss and defence costs.

Finally, Jackson J examined the provision relating to advance payment of defence costs (**the advance clause**). This clause said that Chartis was required to advance defence costs, except where it had declined indemnity. However Chartis was not entitled to refuse to advance defence costs in reliance on a particular exclusion for certain types of wrongdoing.

Jackson J concluded that the advance clause was inconsistent with the absence of the words *"defence costs"* in the exclusions section. Under the advance clause, Chartis was entitled to refuse to advance defence costs where it had declined indemnity on the basis of an exclusion (other than the wrongdoing exclusion).

The Court held that, having denied indemnity on the basis of the lending exclusion, Chartis was not required to pay or advance defence costs until and unless the declinature was agreed or determined to be wrong.

On appeal

BOQ's appeal was confined to the issue of defence costs. BOQ maintained that even if the lending exclusion had the effect of excluding cover for the loss, Chartis was nevertheless required to pay (and advance) defence costs.

Shortly before the hearing, BOQ accepted that it was not entitled to have Chartis advance defence costs, and submitted that it was nevertheless entitled to be paid defence costs.

The Court of Appeal unanimously upheld the Supreme Court decision, finding that BOQ had failed to establish any error in Jackson J's findings. The Court of Appeal concluded that the position for which BOQ contended gave rise to apparently unintended and absurd consequences, including that Chartis would be required to pay defence costs for claims that it had plainly excluded from cover (such as personal injury claims).

Conclusion

This case serves as a timely reminder of the principles of policy construction. Insurance contracts must be given a commercial and business-like interpretation. Any inconsistency should be resolved on the basis that the different parts of the contract are intended to work harmoniously.■

Acting outside your employment

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Introduction

In the recent case of ***Zakka v Elias*** [2013] NSWCA 119, the New South Wales Court of Appeal considered:

- the issue of vicarious liability, and whether a solicitor with a restricted practising certificate, who was assisting a relative, was acting outside the course of her employment; and
- as to causation, whether a holistic warning to a client is itself sufficient, or whether the particular incidents giving rise to the warning must be provided.

Background

Delilah Rahe (**Ms Rahe**) had been employed as a solicitor by a sole practitioner, George Elias (**Mr Elias**) (**Cadmus Lawyers**). Ms Rahe had a restricted practising certificate. Mr Elias had told Ms Rahe that he did not permit his staff to accept instructions from existing or new clients or to open new files without his knowledge or approval.

Ms Rahe was consulted by a relative, Victor Zakka (**Mr Zakka**) in a social and family context to assist him in relation to two loan transactions as a favour and at no cost. Mr Elias was unaware of the assistance that Ms Rahe provided to Mr Zakka. Ms Rahe went to some trouble to actively conceal from Mr Elias the steps she took on behalf of Mr Zakka in relation to the loan transactions.

In the first loan transaction, Zakka borrowed $50,000 from Permanent Trustee Australia in June 2003. The proceeds of this transaction went directly to Ms Rahe's brother, by way of an undocumented loan (**the Permanent loan**). Ms Rahe was not aware that the $50,000 was being lent to her brother until she received the directions for settlement of the Permanent loan.

The second loan transaction occurred later that year in October 2003, when Mr Zakka borrowed a further $304,000 from First Mortgage Company Home Loans Pty Ltd (**the First Mortgage loan**). The proceeds of the First Mortgage loan were used to repay the Permanent loan, and to provide a loan of $250,000 by Mr Zakka to a company called Alispur Pty Ltd (**the Alispur loan**). Alispur was a company associated with Louis Allem (**Mr Allem**), who had arranged the original finance for the Permanent loan.

The Permanent loan and the First Mortgage loan were secured by a mortgage over Mr Zakka's home. Some time after the Permanent loan transaction, Mr Zakka telephoned Ms Rahe and sought her assistance with the

First Mortgage loan documentation. Mr Zakka visited Ms Rahe at her home and brought with him the unsigned First Mortgage loan documents along with a signed but undated copy of the Alispur loan document (**the Alispur loan agreement**).

Ms Rahe warned Mr Zakka that she had *"heard Louis Allem is a con"* and warned him not to do any deals with him. Ms Rahe warned Mr Zakka during their telephone conversation and again when he came to see her. She also informed Mr Zakka that if he defaulted on the First Mortgage loan he would lose his house.

Mr Zakka received some small amounts of money from Alispur (on behalf of Mr Allem) in relation to the Alispur loan, but subsequently Alispur went into liquidation and Mr Zakka defaulted on the repayments due on the First Mortgage loan. As a consequence, the lender in the First Mortgage loan exercised its rights as mortgagee to take possession of Mr Zakka's home and it was sold, leaving $150,000 owing on that loan.

Mr Zakka brought proceedings in the New South Wales District Court against Mr Elias and Ms Rahe.

At first instance

The trial judge held that:

- Ms Rahe was liable for the loss suffered by the making of the Permanent loan, on the basis that at the time she became aware that Mr Zakka was borrowing money to lend to her brother, a competent solicitor in her position would have realised that there was a serious possibility of a conflict of interest, declined to assist Mr Zakka further and strongly advised him to obtain independent legal advice;
- Ms Rahe's breach of duty was causative of the loss resulting from the $50,000 transaction;
- any breach of duty on the part of Ms Rahe had not led to any loss in respect of the First Mortgage loan or the Alispur loan;
- there was no express or implied retainer between Mr Zakka and Mr Elias in relation to any of the loans; and
- Ms Rahe was not acting in the course of her employment in the ostensible pursuit of Mr Elias's business, and all claims against Mr Elias failed.

The appeal

Mr Zakka appealed but the Court of Appeal dismissed the appeal with costs. In doing so, the Court determined:

- whether the trial judge erred in not finding that Ms Rahe breached a duty of care owed to Mr Zakka in relation to the First Mortgage loan and the Alispur loan;
- whether causation was established in relation to the alleged breach of duty; and
- whether Mr Elias was vicariously liable for Ms Rahe's negligence on the basis that the torts committed by Ms Rahe were within the course of her employment.

Breach of duty

Mr Zakka contended that:

- Ms Rahe breached her duty of care to him by failing to advise him, in relation to the First Mortgage loan and the Alispur loan, to obtain independent legal advice and not to provide money without adequate security and an appropriate loan agreement; and
- the advice Ms Rahe gave to him in relation to the First Mortgage loan and the Alispur loan was not sufficient to discharge her of her duty of care.

The Court of Appeal found that the trial

judge did not err in her findings that Ms Rahe had satisfied any duty to warn Mr Zakka in relation to the risk that Mr Zakka might lose his home as a result of the First Mortgage loan and the Alispur loan. However, the Court found that there was a penumbral duty: a duty to advise a client to seek independent financial advice given the circumstances of the transaction. The penumbral duty was created once Ms Rahe became aware, in reviewing the Alispur loan agreement, of matters that a reasonably competent conveyancing practitioner would have seen as posing risks to the client. Ms Rahe's penumbral duty was to draw this to Mr Zakka's attention and warn him that he should consider – and perhaps obtain further advice regarding – whether the security for the First Mortgage loan and the Alispur loan would provide adequate protection.

The Court of Appeal found that Ms Rahe breached her duty of care in failing to alert Mr Zakka to the prudence of investigating the adequacy of the security for the Alispur loan agreement, or of seeking additional security if the unregistered second mortgage was found not to provide adequate protection.

The Court of Appeal also found that a solicitor only has a duty to cease to act if there is a subsisting or fresh conflict of interest. It is not the duty of a solicitor to decline to act for clients who wish to enter risky transactions or transactions that may be improvident.

Causation

The Court of Appeal found that the trial judge's finding on causation was correct, based on the likelihood that Mr Zakka would have proceeded with the transaction in any event. The onus was on Mr Zakka to establish, on the balance of probabilities, that had Ms Rahe given the advice or warnings, he would not have proceeded with the First Mortgage loan.

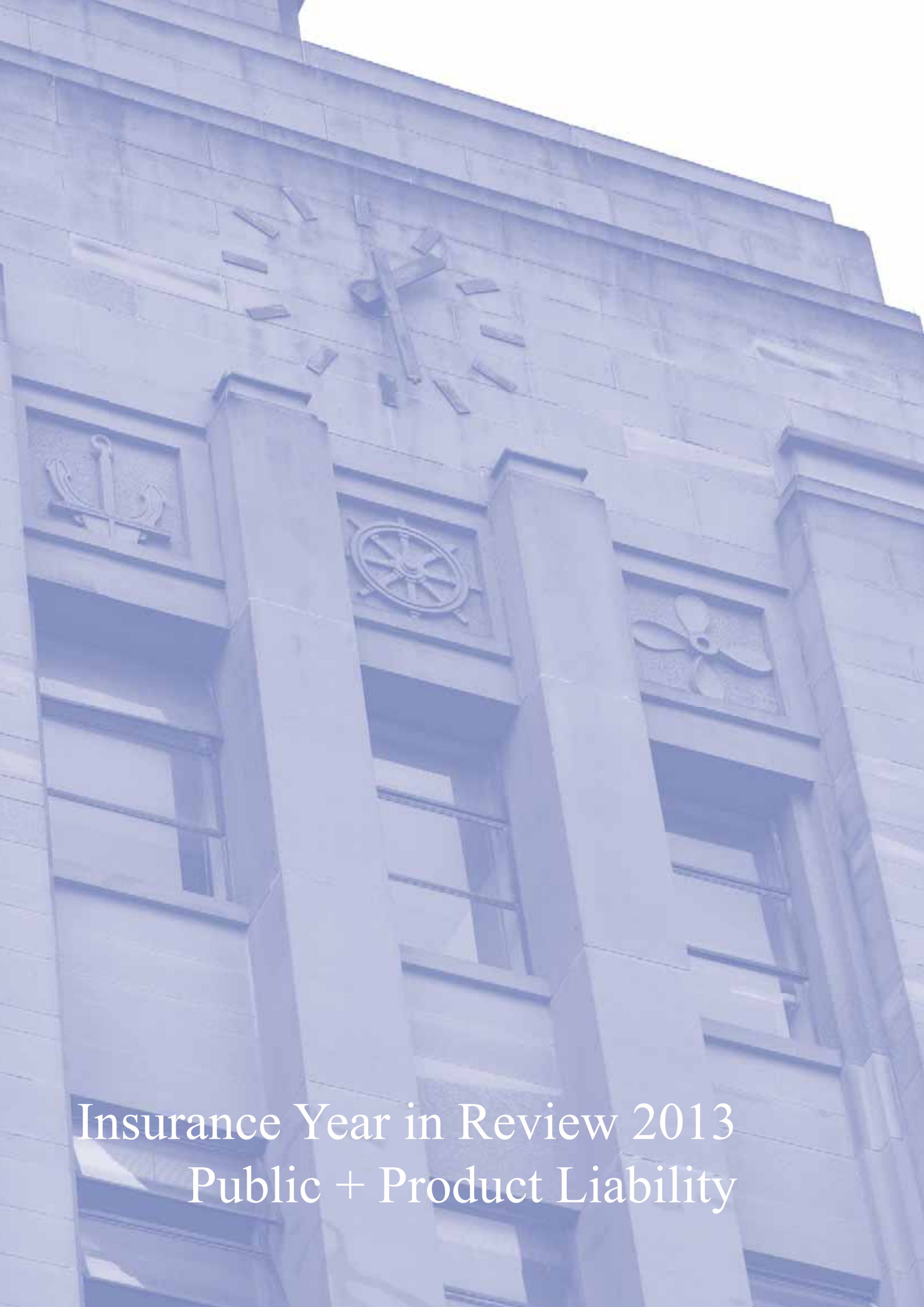
Ward JA (at paragragh 83) said *"The fact that a risk is expressed in general terms (such as 'you could lose your home') or that the warning is in general terms (such as 'don't enter into the transaction') does not mean that a solicitor will have failed to discharge a general duty to warn his or her client that the transaction was risky or as to the risks of the transaction."*

The Court of Appeal found that the real cause of Mr Zakka's loss was his decision to place his trust in Mr Allem and invest in Mr Allem's business.

Vicarious liability

The Court of Appeal upheld the trial judge's findings that Mr Elias was not liable for Ms Rahe's negligence and confirmed that the test as to when vicarious liability will arise will turn on whether there is the requisite closeness of connection between what the employee was employed to do – or was held out by the employer as employed to do – and the wrongful conduct (***Withyman v State of New South Wales*** [2013] NSWCA 10).

Ward JA reasoned that *"This, in my view, is a clear case of a solicitor engaging in a frolic of her own or at her own whim, to adopt the terminology used in the authorities. It is not an unauthorised mode of committing an unauthorised act. It is an act Ms Rahe was not authorised to take as an employed solicitor of the firm. There was not, in my opinion, a sufficient connection between that unauthorised conduct and Ms Rahe's employment to bring this within the scope of the doctrine of vicarious liability as explained in Lepore and Withyman."* ■



Insurance Year in Review 2013
Public + Product Liability

When the circumstances are unknown, how far can inferences take the Court?

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Background

The plaintiff in ***Minogue v Rudd*** [2013] NSW CLA 335, a 24-year-old Irish man on a working holiday in Australia, was injured on a residential building site at around 10:30am on 12 February 2004 when he fell about 3 metres through wooden joists in an unfinished kitchen to a concrete floor on the level below. There were no witnesses to the fall. The plaintiff suffered severe injuries including a brain injury, and was unable to provide any explanation as to why he was working in the kitchen or how the accident occurred. His employer gave evidence that he had not instructed the plaintiff to work in the kitchen and could not explain why he would be there.

In the kitchen area, timber floor joists had been installed and *"skew nailed"* to wall plates at each end. With one exception, between each 2 joists in the central area there was a timber *"noggin"* skew nailed to the joists at each end, preventing the joists from moving.

The exception was the space between 2 joists in the middle of the room where the noggin on the western side was moved before the accident (the missing noggin). One of these joists was found after the plaintiff's accident, unsecured at its northern end with its central part resting at an angle on top of an adjacent joist. There had recently been – but was no longer – a noggin on the eastern side of the joist. There was no floor covering the joists, as its installation was delayed pending a decision about the location of air-conditioning ducts.

Decision by Adamson J

The plaintiff commenced proceedings in the Supreme Court against the builder (**Mr Rudd**), the owner's building supervisor (**Mr Tilden**) and a subcontractor that had engaged the plaintiff to perform carpentry work on the site, DMW Carpentry Services Pty Limited (**DMW**).

At trial, evidence was given in relation to a barricade or warning at the entry to the kitchen. There was inconsistency as to the form of barricade or warning. However, the owner of the premises (who was not sued in these proceedings) and Mr Hardwick (an electrician who accompanied the owner through the

premises on the morning of the accident) gave persuasive evidence. The owner said a plyboard barricade was in place with warning tape. She attested to this fact in a file note prepared the day after the accident, which she and Mr Hardwick both signed.

After the accident, the scene was attended by a worker on-site who heard the fall, police and ambulance officers, and a WorkCover representative who took photographs after the plaintiff had been taken away.

The crux of the plaintiff's claim was twofold, that:

- the missing noggin posed a hidden danger to the plaintiff and caused or contributed to the plaintiff falling through a hole made larger when the unsecured joist moved; and
- temporary flooring ought to have been laid upon the joists, which would have ensured they were safe for access.

Expert opinions were tendered and the experts gave evidence concurrently. Much was made of the missing noggin and dust patterns in the WorkCover photographs, allegedly showing the movement of the joist.

Adamson J was unable to determine the manner in which the plaintiff's accident occurred. Her Honour found that the plaintiff was not in the kitchen area for any reason associated with his employment for DMW, aside from the fact that but for his employment, he would not have been on the site at all.

She concluded that a reasonable person in the plaintiff's position would not have gone into the kitchen area noting that it was cordoned off with a partition, tape and/or sign.

Her Honour formed the view that the plaintiff's accident – and therefore his injuries – had not been shown to be causally related to the missing noggin.

Her Honour held that:

> *"While it is not essential for a Plaintiff's success that the precise cause of the accident be demonstrated, he nevertheless needed to demonstrate that his accident and therefore his injuries resulted from the Defendant's assumed negligence in leaving one noggin missing."*

Her Honour also found that Mr Rudd *"did not breach the duty of care he owed to the Plaintiff by not installing a temporary floor in the kitchen area".* She rejected submissions that she should consider the risk the exposed joists posed to a child entering the kitchen area. Her Honour found that:

> *"The issue of breach of duty must be considered in the context of the particular plaintiff, bearing in mind what the defendant knew or should have known about the plaintiff or the class of persons of which the Plaintiff forms part (see Shaw v Thomas [2010] NSW CA 169 at 40)."*

Her Honour entered judgments in favour of all defendants.

The appeal

The Court of Appeal unanimously dismissed the plaintiff's appeal.

In accordance with ***Jones v Dunkel*** [1959] HCA 8; 101 CLR 298 at 304–5 (citing ***Bradshaw v McEwans Pty Limited*** (1951) 217 ALR 1 at 5; see also ***Luxton v Vines*** [1952] HCA 19; 85 CLR 352 at 359–360 and ***Condos v Clycut Pty Limited*** [2009] NSW CA 200 at 68), their Honours found that:

- *"The evidence does not reveal any likely cause of the Plaintiff's accident, much less a realistic one with which*

the absent noggin had any causal relation"; and
- a definite conclusion can't be drawn *"where the evidence gives rise to conflicting inferences of equal degree of probability so that the choice between them is* [a] *mere matter of conjecture"*.

Implications

This case reminds us that:

- inferences cannot be drawn at a whim; for the Court to make findings of fact in the absence of direct evidence, it requires sufficient circumstantial evidence clearly favouring one conclusion as being more likely than another; and
- the duty owed to a plaintiff is to be determined by reference to the class of persons to which the plaintiff belongs. For example, what may have amounted to a breach of duty of care owed to a child is not relevant if the plaintiff is an adult.

Wotton + Kearney acted for Mr Rudd in the proceedings. The plaintiff has filed an application seeking leave to appeal to the High Court.

Had a slip while choosing some dip – *Coles Supermarkets Australia Pty Ltd v Meneghello*

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Section 5D of the **Civil Liability Act 2002 (NSW)** (**CLA**) requires a Court to determine whether a defendant's failure to exercise reasonable care and skill was a necessary condition of the occurrence of harm. In this decision, the Court of Appeal unanimously found that a plaintiff failed to establish a causal connection between her fall and an alleged breach of a duty of care owed by Coles Supermarkets Australia Pty Ltd (**Coles**).

The facts

The plaintiff, Charlene Meneghello, slipped and fell while she was selecting a dip from the fridge aisle of the Coles supermarket in Neutral Bay. After the incident, she observed two small pieces of cardboard on the floor.

The plaintiff alleged that Coles was negligent in failing to take precautions to alleviate the risk posed by the presence of the cardboard on the floor.

In support of her claim, she served an expert report prepared by engineer Robert Fogg, who formed the opinion that the cardboard on the vinyl floor surface constituted a slip hazard. The plaintiff did not observe the pieces of cardboard before her fall, nor did she see any employee stocking shelves nearby or see any trolley containing cardboard boxes.

The plaintiff was successful at first instance and was awarded damages totalling $119,024. This included damages for non-economic loss, which was assessed at 20% of a most extreme case plus economic loss and future domestic assistance.

Coles appealed and challenged the

finding of negligence against it on the basis that the plaintiff's evidence did not establish that she had in fact slipped on the pieces of cardboard on the floor, nor that the pieces of cardboard lying on the floor posed a foreseeable hazard to patrons of the supermarket.

The appeal

Barrett JA, with whom Ward JA and Emmett JA agreed, noted that the plaintiff had the onus of proving on the balance of probabilities that Coles' negligence was causative of her loss.

Barrett JA found there was *"no direct evidence that the* [plaintiff's] *foot came into contact with cardboard or that cardboard was at any time between the sole of her* [shoe] *and the surface of the floor"*. Barrett JA cited ***Luxton v Vines*** [1952] HCA 19; (1952) 85 CLR 352, stating that if direct evidence is not available:

> *"it is enough if the circumstances appearing in evidence give rise to a reasonable and definite inference: they must do more than give rise to conflicting inferences of equal degrees of probability so that the choice between them is mere matter of conjecture."*

Barrett JA said that either the plaintiff stepped on cardboard lying on the floor, or the plaintiff stepped on a part of the floor devoid of cardboard. His Honour determined that the mere fact that the plaintiff observed the pieces of cardboard after her fall did not make it more probable than not that she had stepped and slipped on the cardboard rather than on the floor.

The Court of Appeal was of the view that the expert evidence of Robert Fogg, which found that the cardboard was hazardous, held no weight in circumstances where Mr Fogg had not undertaken any slip testing of the floor surface or provided reasons for his opinion that the cardboard on the floor surface constituted a slip hazard. His Honour found that Mr Fogg's opinion was *"mere assertion"* and stated that *"if the opinion evidence were to be of probative value, it would have to do more than simply assert that grip or resistance was reduced because of the presence of cardboard"*.

In addition to appealing the decision on liability, Coles appealed the quantum of damages. The Court of Appeal found the assessment of damages was excessive.

It determined that the plaintiff did not meet the threshold required by section 16(3) of the CLA in order to be entitled to non-economic loss, as she sustained only minor injuries. The Court of Appeal assessed the plaintiff's injuries at 10% of a most extreme case. Barrett JA also held that the awards for future domestic assistance on a commercial basis, and the past and future economic loss, were incommensurate. His Honour favoured the contemporaneous evidence of the plaintiff's treating medical providers rather than her medico-legal doctors.

Had the plaintiff succeeded in proving liability, the Court would not have allowed the plaintiff any amount for economic loss or domestic assistance on a commercial basis.

The implications

Consistent with the High Court decision of ***Strong v Woolworths*** [2012] HCA 5, Barrett JA reiterated that it is incumbent on a plaintiff to prove that a defendant's negligence was causative of his or her injuries.

Coles v Meneghello demonstrates that general pleadings of negligence will no longer suffice. Practitioners should ensure that the cause of a claim against an occupier is clearly identified and allegations of negligence are specific and properly particularised.

Agency and vicarious liability

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Introduction

In ***Day v The Ocean Beach Hotel Shellharbour Pty Ltd*** [2013] NSWCA 250 (***Day***), the NSW Court of Appeal was required to determine whether the regime under the **Liquor Act 2007 (NSW)** (**the Act**) had the effect of rendering the occupier and licensee of licensed premises vicariously liable for the tortious conduct of a security guard employed by an independent contractor.

The decision is significant in that it appears to confirm that while the obligations that a licensee owes under the Act are personal that does not mean the obligations are not delegable or that liability for performing them tortiously will be borne vicariously by the licensee when those obligations have been delegated to an independent contractor.

Background

In July 2008, Julia Day (**the plaintiff**) was drinking wine at the Ocean Beach Hotel in Shellharbour (**the hotel**) when the duty manager formed the view that she was intoxicated and requested that a security guard provided by Checkmate Security International Pty Ltd (**Checkmate**) remove her from the premises. Checkmate provided security to the hotel pursuant to an oral contract. Checkmate's security guard spoke to the plaintiff, then pulled her stool out from under her, causing her to fall to the floor and to suffer injuries.

The plaintiff sued Checkmate and the occupier and licensee of the hotel, alleging that all three were liable either directly or vicariously for the security guard's conduct. At first instance, the plaintiff failed against the occupier and the licensee but succeeded against Checkmate, which the trial judge found was vicariously liable for the security guard's conduct. After judgment was entered, Checkmate was deregistered and the plaintiff was unable to recover from it the damages she had been awarded. In response, she appealed the decision against the occupier and the licensee.

Decision

The crux of the plaintiff's argument on appeal was that the provisions of the Act rendered Checkmate's employee an *"agent"* of the occupier or the licensee of the hotel. Section 73(1) of the Act forbids a licensee to permit intoxication to occur on licensed premises and empowers the licensee or an *"employee or agent"* of the licensee to turn out an intoxicated person using *"such reasonable degree of force as may be necessary"* in furtherance of that obligation.

The plaintiff argued that Checkmate's security guard was an *"agent"* of the licensee or the occupier in this sense, and that the guard's conduct was in furtherance of the obligations of the licensee under the Act.

While the Court accepted that a security contractor may be retained by licensed premises to ensure that the licensee complies with his or her statutory obligations under the Act and that these obligations may extend to turning out people who are intoxicated, the Court did not accept that the use of the term *"agent"* in the Act turned the relationship

between Checkmate's security guard and the hotel's licensee or occupier into a relationship of agency. For the purposes of imposing vicarious liability, the Court maintained that the term *"agent"* was to be construed in its strict legal sense as someone with the authority to bind another in legal relations.

A further ground identified by the Court for dismissing the plaintiff's appeal was that Australian law does not recognise dual vicarious liability. Once one person has been found vicariously liable, no other person can be. Thus, as Checkmate had already been found vicariously liable, it followed that the licensee and the occupier of the hotel could not also be found vicariously liable.

Conclusion

On one level, the decision reaffirms the general rule that a principal is not liable for the tortious conduct of his or her independent contractor. This is subject to a limited number of exceptions, including certain relationships of true agency.

On another level, the decision appears to close the door on recent attempts to use the provisions of the Act to hold licensees vicariously liable for the tortious conduct of security guards on the basis that the latter have been enlisted to discharge personal statutory obligations owed by the former under the Act. The legal relationship between a licensee or occupier of licensed premises and a security contractor will not, without more, make the security contractor the agent of the licensee, notwithstanding the use of the word *"agent"* in the Act. ■

To care, or not to care

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In catastrophic injury cases, a question often arises as to the quality and nature of care for which an injured person ought to be compensated.

The background

In ***Dang v Chea*** [2013] NSWCA 80, on 7 September 2007, Mrs Chea was struck by Ms Dang's vehicle and suffered serious injuries including a brain injury. Two years after the accident, Mrs Chea fractured her left femur and, as a consequence, was moved from her home to the Canley Gardens Aged Care Facility (**Canley Gardens**).

Between 2010 and 2011, while residing at Canley Gardens, Mrs Chea suffered 6 falls. Balla DCJ had found, due to advanced dementia and cognitive deficits from her brain injury, Mrs Chea often showered and went to the toilet by herself, leading to an increased risk of falling.

At the trial, it was submitted for Mrs Chea that she should be awarded future care damages based on returning to suitable rental accommodation and being provided with 24-hour nursing assistance (**the in-home option**). It was submitted that Mrs Chea's falls at Canley Gardens evidenced the need for more intimate care than Canley Gardens could provide. This submission was opposed by Ms Dang, who submitted that damages should be calculated based on the cost of Mrs Chea remaining in Canley Gardens. Balla DCJ found for Mrs Chea on the issue, awarding $1,912,926 in damages including $1,095,691 for future accommodation and care. Her Honour concluded that there were *"real and significant health benefits in maximising the chance of avoiding Mrs Chea being injured in a fall which outweigh that difference in cost"*.

Ms Dang appealed, submitting that Her Honour's award for future accommodation and care damages was manifestly excessive.

The appeal

The appeal was unanimously upheld, with the leading judgment given by Garling J.

Garling J referred to ***Arthur Robinson (Grafton) Pty Ltd v Carter*** [1968] HCA 9, in which it was held that the aim of an award of damages was not to fulfil the ideal requirements for an injured plaintiff, but rather the *"reasonable requirements"*. Garling J observed that the touchstone of reasonableness requires matching the cost of the care with the health benefits to a plaintiff (***Sharman v Evans*** [1977] HCA 8).

Garling J found:

- that the 6 falls suffered by Mrs Chea between 2010 and 2011 did not

constitute *"many falls"*;
- for the expense of the in-home option to be warranted, the incidence of falls would need to be reduced by a significant extent, proportionate to the additional cost of that care;
- as Mrs Chea's age advanced, she would become progressively less mobile, less active and more likely to be confined to bed, such that in her later life the risk of falling would be reduced to nil;
- to determine whether a particular expense is warranted, it is necessary to consider:

    - the health benefits of the more expensive option;
    - the cost differential between the various options; and
    - what proportion of the overall damages assessment the cost differential would form; and

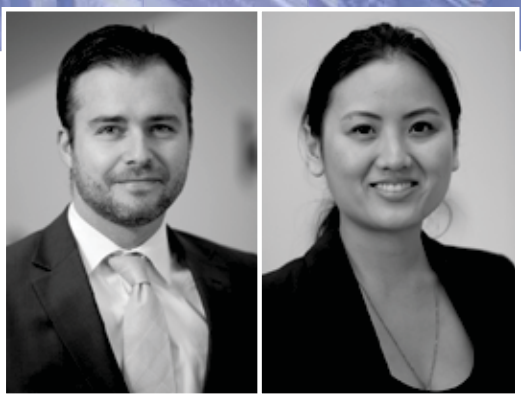
- in this case, the in-home option came at a cost of $6,092.50 per week, while the cost of remaining in Canley Gardens was $1,680 per week. Over the remainder of Mrs Chea's life, the total difference was calculated at $781,745, which was clearly a significant proportion of the overall award of damages (around 40%).

The Court of Appeal ordered that Mrs Chea's damages were to be reduced to reflect her being accommodated in Canley Gardens for the balance of her life.

The takeaway

In dealing with catastrophic claims, it is common for plaintiffs to seek future care and accommodation that represent their *"ideal"* requirements. The Court of Appeal emphatically held that the touchstone is what meets a plaintiff's reasonable requirements. To assist the courts to identify what is reasonable, insurers should obtain evidence regarding the extent of additional health benefits offered by the competing options so this may be weighed against the relative costs. ■

Risk in recreational activities



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Part 1A, Division 5 of the **Civil Liability Act 2002 (NSW)** (**CLA**) applies to liability in negligence for harm resulting from recreational activities. Two recent cases show that Division 5 can be troublesome for plaintiffs, particularly in the context of dangerous recreational activities and risk warnings.

Noel Campbell v Rodney Victor Hay [2013] NSWDC 11

In this case, the District Court of NSW considered whether injuries suffered in a light aircraft accident were a result of the materialisation of an obvious risk of a dangerous recreational activity.

The facts

The plaintiff was learning how to fly in the defendant's aircraft. The plaintiff had been in control of the aircraft when it experienced slight vibrations. When the vibrations occurred for a second time, the defendant took back control of the aircraft but the engine subsequently failed, forcing the defendant to perform an emergency landing in rough terrain. The plaintiff sustained injuries as a result.

The trial

The trial judge determined the defendant had failed to exercise reasonable care by not ensuring the aircraft was flown towards an appropriate landing strip immediately after the second set of vibrations.

The defendant contended that he could not be held liable in negligence by reason of section 5L of the CLA, which precludes liability for harm suffered from the materialisation of obvious risks of dangerous recreational activities.

In support of his claim, the defendant tendered statistics and media reports about the frequency of light aircraft accidents. To the contrary, the plaintiff gave evidence to the effect that the defendant was an experienced pilot, the aircraft was well maintained and pilots generally regarded the particular aircraft as safe to fly.

Marks J reviewed the authorities on what constitutes a dangerous recreational activity, and confirmed:

- the defendant bore the burden of establishing the defence;
- the issue is to be determined objectively and prospectively;
- the standard of risk to be proved lies somewhere between a trivial risk and one that is likely to occur;
- there must be a *"significant"* risk of physical harm, with the significance being informed by the elements of both risk and physical harm. The *"risk of physical harm"* may be *"significant"* if:
    - the risk is low but the potential harm is catastrophic; and
    - the likelihood of both the occurrence and the harm is more than trivial.

Conversely, the risk of *"physical harm"* may not be *"significant"* if, despite the potentially catastrophic nature of the harm, the risk is very slight;

- the activity in question needs to be identified at a relatively detailed level of abstraction by including not only the particular conduct actually engaged in, but also the circumstances in which that conduct occurs; and
- the type of evidence which may be relied on to establish the defence can include statistical evidence as well as matters of logic, common sense and a general understanding of the activity.

Marks J determined that travelling in a light aircraft was akin to parachuting: a *"statistically safe"* activity that nonetheless involved some risk of danger. Common sense dictated that if something went wrong there was a significant risk of physical harm. Furthermore, there was *"a not insignificant risk"* of something going wrong, which was sufficient to characterise flying a light aircraft as a dangerous recreational activity. Moreover, the risks that eventuated were *"obvious"* despite the low probability of them occurring.

A contrast to *Hume v Paterson*

It is interesting to note the contrasting fortunes of a plaintiff in another recent case, who was injured while waterskating: ***Hume v Paterson*** (2013) NSWSC 1203.

In this case, the plaintiff suffered C6 tetraplegia when he fell while waterskating (an adaptation of wakeboarding) in shallow water (approximately 1.1 metres deep) and struck his head on a sandbar. Expert evidence indicated that waterskating at any depth under 1.5 metres was unsafe.

The Court determined the boat driver was negligent in failing to navigate the boat wholly within the channel where the depth was at least 3 metres while towing the plaintiff.

The defendant sought to rely on section 5L of the CLA on the basis that the harm suffered by the plaintiff was a result of the materialisation of an obvious risk of a dangerous recreational activity. The Court noted that the question of whether an activity is a dangerous recreational activity must be assessed objectively, and that subjectively most people do not actually court danger even if a degree of risk adds to the exhilaration of a sport.

The Court determined that in the circumstances, waterskating was not a dangerous recreational activity, because:

- the activity was to be engaged in only in the relatively deep water of the channel;
- unlike waterskiing, waterskating is undertaken at a relatively slow speed; and
- the expert evidence did not support the idea that waterskating is an activity involving a significant risk of physical harm.

Furthermore, even if it was a dangerous recreational activity, there was an issue as to whether the risk was obvious. The Court highlighted that there was not necessarily a correlation between the significant risks that make an activity dangerous and the obvious risk that materialises. In this instance, given that the activity undertaken was waterskating in the channel, the risk of injury on a sandbar outside the channel was deemed not to be an obvious risk.

Action Paintball Games Pty Limited (In Liquidation) v Barker (2013) NSWCA 128

The facts

In this case, the NSW Court of Appeal considered the issue of risk warnings in the context of paintballing in bushland. The plaintiff, a 10-year-old girl, was

injured when she tripped on a tree root while playing paintball at an outdoor facility occupied by the defendant.

Before the game started, the defendant gave a general warning about the dangers of natural obstacles one might encounter during the activity.

At first instance

The District Court gave judgment in favour of the plaintiff and awarded her damages, primarily because the defendant had not removed the tree root.

The appeal

On appeal, the defendant submitted that the risk of tripping and sustaining injury was obvious, known to the plaintiff and her parents, and inherent given the natural characteristics of the bushland, so there were no additional precautions the defendant could have reasonably taken. The defendant relied on Division 5 of the CLA in its defence, specifically:

- section 5H, which states there is no duty of care to warn of an obvious risk;
- section 5I, which states there is no liability for the materialisation of an inherent risk; and
- section 5M, which states there is no duty of care where a recreational activity was the subject of a risk warning.

The Court of Appeal reinforced the view that it is possible to warn of a risk without instructing the recipient of all the steps necessary to avoid the risk. The Court considered that an adequate warning can be given at least in some circumstances by reference to the general kind of risk involved, without a precise description of each separate obstacle or hazard that may be encountered (section 5M(5)).

The Court of Appeal also stated that the risk of harm through tripping and falling is a common risk of daily life, and can occur inside a house, in a garden, on a pavement or roadway, or in the bush. The Court of Appeal determined that:

- not only would the obligation to remove all naturally occurring obstacles change the nature of the area or the recreational activity, but it would be an impracticable and unreasonable precaution;
- there was no obligation on the defendant to remove the tree root in exercising its duty of reasonable care; and
- there was no duty of care owed in respect of a risk of the activity if the risk were the subject of a risk warning, and the general risk warning about the natural obstacles provided by the defendant was considered sufficient.

Comment

Establishing liability for injuries suffered in recreational activities can be very difficult for plaintiffs, particularly where risk warnings have been provided – even if those risk warnings are only of a general nature. The question of what constitutes an adequate risk warning will depend on the nature of the recreational activity and the likelihood of injury occurring. When considering liability in the context of dangerous recreational activities, one must be mindful that each case is likely to be highly dependent on its facts and that the activity in question needs to be assessed at a reasonably detailed level of abstraction. ■

Bullying: make it stop!

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On 27 May 2013 the New South Wales Court of Appeal delivered its judgment in ***Oyston v St Patrick's College*** [2013] NSWCA 135, confirming that educational facilities will have difficulty escaping liability for student bullying unless they can demonstrate clear compliance with comprehensive anti-bullying policies.

At first instance

The plaintiff Ms Oyston was a student at St Patrick's College, Campbelltown (**the college**) from 2002 to 2005. She alleged that during that period she was subjected to persistent bullying which included being called names by girls in the *"popular group"*, being mocked for not wearing a bikini at a swimming carnival, and being jostled and elbowed in the school corridors. After reporting the incidents to teachers and counsellors, she was exposed to further bullying. She engaged in self-harm and had thoughts of suicide.

She was withdrawn from the college in 2005 and repeated Year 9.

At first instance, the college argued that the plaintiff had not been bullied, or that if she had, the college had not been aware of it. Furthermore, the college argued that a contributory negligence reduction must be made on account of the plaintiff's failure to complain.

Schmidt J found that while the college had written policies in place to respond to varying degrees of bullying, it failed to impose appropriate sanctions on the perpetrators and failed to maintain adequate records of instances of bullying in the student files. Her Honour considered the college was under a duty to educate and support students through adolescence and that there had been an overemphasis on supporting certain students who had engaged in bullying at the cost of supporting Ms Oyston. Furthermore, Her Honour found that there was no contributory negligence, noting contemporaneous written reports of Ms Oyston's complaints.

Her Honour awarded Ms Oyston $116,296.60, finding that the college's negligence had resulted in her suffering a depressive illness and adjustment disorder from which she did not recover for several years, and which made her vulnerable to future psychiatric illness.

Court of Appeal

Ms Oyston lodged an appeal based on damages and the college cross-appealed based on liability. The question of liability was addressed first.

The college submitted that Schmidt J erred in finding Ms Oyston was bullied as alleged, or that it had breached its duty of care by not dealing with known bullies. Ms Oyston submitted that she was a

reliable witness, that her testimony was supported by documentary evidence and, to the extent that any documents were lacking, this was a shortcoming of the college. Furthermore, she submitted that the college failed to take reasonable care to ensure her safety, demonstrated by the inconsistency between its anti-bullying policy and its actual response.

The Court of Appeal held that the college's appeal failed, because:

- Schmidt J was entitled to conclude that Ms Oyston was regularly bullied;
- the actions taken by the college in response to the reports of bullying clearly violated the words of the college's policies; and
- the risk of psychological harm to Ms Oyston from bullying was both foreseeable and not insignificant within the meaning of section 5B of the **Civil Liability Act 2002 (NSW)**.

The Court of Appeal subsequently delivered its judgment in ***Oyston v St Patrick's College (No 2)*** [2013] NSWCA 310 in relation to Ms Oyston's appeal on causation and damages. It held that Ms Oyston had established causation and was entitled to an increase in her damages for non-economic loss from 20% to 25% of a most extreme case, but was not entitled to an increase for past and future economic loss. Her overall award was therefore increased from $116,296.60 to $124,938.48. In a subsequent decision of ***Oyston v St Patrick's College (No 3)*** [2013] NSWCA 324, the judgment of $124,938.48 was set aside, with judgment then entered in favour of Ms Oyston for $162,207.34, reflecting an increase for non-economic loss and interest as agreed by the parties.

Implications

This case reaffirms that liability insurers will remain exposed to damages claims unless educational facilities set and enforce clear anti-bullying policies and keep adequate records of the process of complying with them. ■

Property owners' liability for unknown hazards or defects that cause injury

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Introduction

In ***Jodie Smith v Body Corporate for Professional Suites Community Title Scheme 14487*** [2013] QCA 80, the Queensland Court of Appeal considered whether the body corporate for Professional Suites Community Title Scheme 14487 (the body corporate) was liable for personal injuries suffered by Jodie Smith (**the plaintiff**) when she fell through a glass panel in the ground-floor facade of an office building at 138 Albert Street, Brisbane (**the building**). The plaintiff alleged that the body corporate was negligent in failing to undertake an audit of the glass panel – which would have identified that it did not comply with relevant Australian Standards – and replace it before the accident.

Facts

The plaintiff worked for a multimedia company that was a tenant in the building. The body corporate was the occupier of the building's common property, including the foyer entrance and the building's façade.

In December 2001, the plaintiff, a friend and two colleagues arrived at the building following a staff Christmas party. The plaintiff searched her handbag for her swipe key so she could access the building. While she was looking for the swipe key, she stumbled backwards and fell through a glass panel adjacent to the door. The glass panel broke into large pieces which fell onto the plaintiff and she sustained severe lacerations to her face, neck, arms and torso.

The plaintiff had consumed approximately 10 glasses of wine during the day and 6 pre-mixed spirits during the Christmas function. Expert evidence concluded that the plaintiff's blood alcohol concentration would have been 0.26% at the time of the incident and her balance and mobility would have been "*severely disturbed*".

The glass panel was installed in 1971 and was made of 6-millimetre annealed glass, which did not contravene any relevant building or Australian Standard in force at that time. The Australian Standard for the type of glass that should be used in premises such as the building was introduced in 1973 and revised in 1994 (**the 1994 Standard**). At the time of the incident, the 1994 Standard specified that safety glass was to be used in new buildings. The 1994 Standard did not require the replacement of existing glass that complied with any earlier Standard in force when the glass was installed; however, in the event that existing glass was replaced, it required that the new glass comply with the 1994 Standard.

The body corporate replaced the glass front doors of the building during renovations to

the foyer between 2000 and 2001. The body corporate's architect specified that the glass in the replacement front doors was to be safety glass in accordance with the 1994 Standard; however, the architect's plans retained the existing glass in the building's facade, including the glass panel.

There had been no reported problems with the glass panel since its installation. The body corporate did not commission an audit of the glass panel at any time prior to the incident. At the time of the renovations, audits were available for no more than $220. Such an audit would have revealed that the type of glass used did not comply with the 1994 Standard.

At trial

At trial, the plaintiff argued that the body corporate was liable for her injuries at common law and under the **Workplace Health and Safety Act 1995 (Qld)** (**WHSA**). The plaintiff alleged, among other things, that the body corporate had:

- acted unreasonably by failing to commission a glass audit by an appropriately qualified person to ascertain whether the glass panel complied with the 1994 Standard; and
- breached its statutory duty under sections 26(3) and 30(1)(c) of the **WHSA and the Workplace Health and Safety Risk Management Advisory Standard 2000 (Qld)** (**the Advisory Standard**) to act proactively to ensure safe access to the building by arranging a glass audit by an appropriately qualified person (**the WHS argument**).

The plaintiff alleged that had the glass been audited, the annealed glass would have been detected, the glass auditor would have recommended it be replaced with safety glass, the body corporate should have acted on such advice and the plaintiff would not have suffered serious injury when she stumbled backwards against the glass panel.

In the first instance, the District Court of Queensland dismissed the plaintiff's claim because she failed to establish that the body corporate had acted unreasonably in failing to organise an audit of the glass panel and replace it with safety glass. The trial judge did not consider the WHS argument.

Court of Appeal

The plaintiff sought leave to appeal on the basis that the trial judge had erred by not taking into account the WHS argument.

The Court of Appeal agreed that the trial judge had not considered the WHS argument and gave her leave to appeal. However, the majority (Fraser JA and Fryberg J) dismissed the appeal because the plaintiff failed to prove that the body corporate breached any duty to engage a suitably qualified person to audit the glass. There was no evidence that the glass panel was defective or hazardous. Even if there was a breach in failing to organise a glass audit, the majority was not satisfied that the plaintiff could establish that such a breach caused her injuries. The majority determined that there was no requirement under the prevailing 1994 Standard to replace existing annealed glass if there was no reason to think it was defective. Furthermore, there was no evidence that the glass would have been replaced even if an audit had been undertaken.

McMurdo P (dissenting) found in favour of the plaintiff on the basis that that the body corporate had breached its common law duty of care by not undertaking a safety audit of the glass panels during the renovations in 2001. In her Honour's view, the audit would have recommended replacing the glass panels with safety or laminated glass and a reasonable person in the body corporate's position would have replaced the glass as recommended, thereby preventing the incident in which the plaintiff was injured.

Implications

This case confirms the longstanding authority that a property owner – or an entity charged with the responsibility of property management – will not owe a duty of care to lawful entrants to that property to search for unknown hazards or defects. Further still, the law will not impose an obligation on property

owners to modernise fixtures or fittings on their properties to ensure they comply with the relevant Australian Standard. Although compliance with Australian Standards represents sound business practice, a failure to comply with a particular Australian Standard will not of itself be evidence of negligence. Compliance or otherwise with an Australian Standard is but one of a number of issues to be considered when determining whether the negligent acts or omissions of a property owner or manager materially caused or contributed to an injury. ■

Cost caps for intentional torts

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In ***Certain Lloyd's Underwriters Subscribing to Contracts No IHOOAAQS v Cross*** [2012] HCA 56 the High Court confirmed that intentional torts constitute *"claims for personal injury damages"*, attracting the application of the cost caps under the **Legal Profession Act 1987 (NSW)** (**the 1987 LPA**) and **Legal Profession Act 2004 (NSW)** (**the 2004 LPA**) (together, **the LPA**).

Background

In January 2001, John Cross, Mark Thelander and Jill Thelander (**the Claimants**) were injured by security guards at the Narrabeen Sands Hotel. Each commenced NSW District Court proceedings against, ultimately, the insurers of the security guards' employer.

Garling DCJ awarded each Claimant damages of less than $100,000. His Honour also awarded costs, but subject to the caps imposed by section 198D of the 1987 LPA, being the greater of 20 per cent of the damages awarded, or $10,000.

The Claimants appealed His Honour's finding that the LPA cost caps applied to intentional torts.

Court of Appeal

The Court of Appeal determined that the costs were in fact governed by section 338 of the 2004 LPA, which mirrors section 198D of the 1987 LPA. It then considered whether the cost caps applied to intentional torts.

Their Honours considered the wording of the LPA, which essentially:

- caps costs where *"the amount recovered on a claim for personal injury damages does not exceed $100,000"*; and
- defines *"personal injury damages"* as having *"the same meaning as in Part 2 of the Civil Liability Act 2002"* (**CLA**).

The Court held that the LPA cost caps do not apply to intentional torts, essentially because the CLA damages regime excludes those torts.

In reaching this view, their Honours adopted a contextual approach to the construction of section 338, observing, variously, that:

- it *"is not sufficient just to take the words of the definition from the source statute and apply them as they stand, without any regard for their context in the source statute"*;
- the authorities support the proposition that the term *"has the*

same meaning as in" permitted taking into account the operation of the phrase *"personal injury damages"* in the CLA, not merely picking up the words of the definition;

- the cost cap provisions were introduced by the CLA as part of a package of reforms. The CLA was enacted as part of *"a broader statutory scheme for limiting the costs of personal injury claims"*, which excluded certain claims, including intentional torts, and therefore did not apply to awards for damages for intentional torts; and
- personal injury claims founded on negligence provide *"the quintessential example of high volume litigation conducted or capable of being conducted along ... standardised lines",* and usually involve compulsory insurance cover, which could be contrasted with claims based on intentional acts.

The security guards were therefore ordered to pay costs at large. The insurer appealed.

The High Court

By majority, the High Court overturned the Court of Appeal's decision and confirmed that the LPA cost caps do apply to intentional torts.

The High Court observed that:

- the term *"personal injury damages"* in the LPA simply refers to the definition contained in the CLA, and is not informed by the operation or application of the CLA in claims for personal injury damages;
- the Court of Appeal should not have had regard to notions of legislative intention that were not based on the statutory text of either Act;
- the LPA and CLA both used the term *"personal injury damages"* as part of two differing, larger, composite phrases, and the operation of each Act turned on each of those composite phrases, not on the defined expression *"personal injury damages"*;
- there was no reason to limit the expression *"personal injury damages"* in the LPA to claims for personal injury damages regulated by the CLA; and
- by their very terms, the relevant provisions of each Act demonstrate a different area of operation.

Crennan and Bell JJ dissented, observing that:

- the mischief the CLA was intended to address, being the perceived crisis in negligence claims; and
- the express language of the LPA cost caps provisions;

weighed against a conclusion that personal injury resulting from an intentional tort constituted a claim for *"personal injury damages"* within the meaning of the LPA.

Implications for insurers

The High Court's decision means that, at least in NSW, where personal injury damages awards in claims involving intentional torts do not exceed $100,000, the claimant's costs will be subject to the LPA cost caps. ■

The sharp end of an inadequate system of cleaning

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In ***Wright v KB Nut Holdings Pty Ltd*** [2013] QCA 66, the Queensland Court of Appeal considered the liability of KB Nut Holdings Pty Ltd (**KB**), which managed Bonapartes Serviced Apartments in Brisbane, for psychiatric injury suffered by Robin Wright (**the plaintiff**) when she was cleaning her serviced apartment and sustained a needle stick injury.

The facts

The plaintiff had entered into a contract to rent a serviced apartment from KB. The plaintiff and her family arrived at the apartment at 5:00pm on 18 April 2009, and found the apartment in an unsatisfactory state of repair and cleanliness. In particular, the internal wooden staircase was covered in dirt and there was a noticeable layer of dust and fluff from corner to corner where the treads met the risers.

The following day, the plaintiff complained to KB about the condition of the apartment. When she returned home that evening, some cleaning had been done and some rubbish had been removed. However, the apartment remained in an unsatisfactory state so the plaintiff complained to KB again on 20 April 2009.

KB told the plaintiff that the cleaners (**the Bowens**) would be fired but did not offer to have the apartment cleaned. The plaintiff volunteered to clean the apartment herself. She purchased a number of cleaning items and KB also provided some cleaning supplies. Although the plaintiff requested that KB supply a vacuum cleaner, KB was unable to do so.

The plaintiff commenced a thorough clean of the apartment. When cleaning the internal stairs, she started at the top step and wiped each step individually. During this process, she wiped the corner of a step and suffered a needle stick injury. The plaintiff developed a psychiatric injury as a result.

Trial

At trial, the plaintiff gave evidence that no reasonable person could have seen the needle and that she and her family had used the stairs without noticing the needle. Mr Bowen gave evidence that he had no specific recollection of cleaning the apartment.

At first instance, the trial judge found in favour of KB on the basis that:

- the risk of harm to the plaintiff was not foreseeable, in that it was a risk that KB did not know or ought not to have reasonably known;
- in the event that the risk was foreseeable, a reasonable person in the position of KB would not have taken any further precautions than those which were taken, namely, engaging the Bowens to clean the apartment on 12 April 2009 and inspecting their work generally; and
- the needle was unobservable to the reasonable person and there was a low probability of harm.

The plaintiff appealed the decision.

Court of Appeal

The Queensland Court of Appeal found in favour of the plaintiff.

Muir JA gave the leading judgment, which was accepted by Margaret Wilson and Douglas JJ. His Honour made his own findings on the facts, as the trial judge had *"'failed to use or has palpably misused his advantage* [and] *has acted on evidence which was 'inconsistent with the facts incontrovertibly established by the evidence' or which was 'glaringly improbable'".* In this regard, the trial judge's findings in respect of the cleaning undertaken by the Bowens were considered unsustainable. Additionally, the trial judge had *"laboured under a misapprehension about, disregarded or failed to take into account, sufficiently"* the plaintiff's evidence about the build-up of debris on the stairs.

KB contended that the **Civil Liability Act 2003 (Qld)** (**CLA**) applied to the various claims brought against KB by the plaintiff under contract, tort and the **Trade Practices Act 1974 (Cth)**, and that the plaintiff could not establish that any breach of duty caused her injury and loss.

Muir JA accepted that the CLA applied. He affirmed that the duty of care owed to contractual entrants to premises was that stated in ***Watson v George***[1], namely, that the premises be rendered *"as safe for the purpose of residing in as reasonable care and skill on the part of anyone can make them"*.

His Honour found in favour of the plaintiff. In His Honour's view:

- KB breached the duty of care owed to the plaintiff by leaving the apartment in filthy condition. As a consequence, the needle was likely obscured from the plaintiff's vision when she was cleaning the stairs;
- it was likely that the area where the needle was located needed thorough cleaning. If KB had an appropriate system of cleaning and had engaged diligent and suitably qualified cleaners this would have likely ensured the needle would have been found and/or removed prior to the commencement of the plaintiff's stay;
- there was a foreseeable risk of injury to the plaintiff which KB knew or ought to have known. The risk was of an injury that may have had grave consequences – such as the plaintiff being cut, being impaled or falling as a result of unremoved objects or general debris. Further, the general state of the apartment gave rise to broader health issues and it was foreseeable that a person injured physically might consequently suffer psychiatric impairment;
- a reasonable person in the position of KB would have taken the precaution of properly cleaning the premises. Such cleaning would have been no more than what a serviced apartment provider would deem necessary to attract customers, and what would be considered appropriate by its users; and
- the plaintiff had established causation against KB under the *"but for"* test (section 11 of the CLA) and the practical or commonsense concept of causation discussed by

1 (1953) 83 CLR 409

Deane J in ***March v Stramare (E & MH) Pty Ltd***[2].

Implications

This case demonstrates the importance of rental managers and/or owners ensuring that:

- they engage suitably qualified and competent cleaners in circumstances where they arrange for serviced apartments to be leased by third parties for reward; and
- an adequate system of cleaning and inspection is in place and properly monitored to prevent foreseeable risks of injury.

2 (1991) 171 CLR 506 at 552

Return to the status quo ante in *QBE v Orcher; Bowcliff v Orcher*

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Introduction

In the 2012 Insurance Year in Review[1], we reported on the decision of ***Orcher v Bowcliff Pty Ltd*** [2012] NSWSC 1088, in which the NSW Supreme Court found an occupier of licensed premises liable for the injuries sustained by a patron who had left the premises and was assaulted on the other side of the road. The decision was notable for the fact that the occupier and the independent contractor retained to provide security at the licensed premises were both found liable for a failure to prevent an assault on the patron, despite the assault not having been preceded by any aggressive conduct on the licensed premises or immediately outside them.

Following the decision, the occupier[2] and the security contractor both appealed the finding of liability. In December 2013, the NSW Court of Appeal allowed both appeals, finding that neither the occupier nor the security contractor had breached their respective duties of care to the patron. In so finding, the Court confirmed that, while the duty of an occupier of licensed premises to its patrons is not confined to the curtliage of the premises, knowledge and control of the relevant conduct remain the critical elements of the duty. Where an occupier neither knows of nor has the ability to control that conduct, the occupier will not have breached its duty of care to the patron.

Facts

John Orcher (**the plaintiff**) was assaulted on the morning of 25 November 2007 after he, his partner and a friend left the Bridge Hotel in Rozelle (**the hotel**) and crossed the road. Shortly after doing so, the plaintiff and the friend started arguing (**the altercation**). Seeing the altercation from the other side of the road, Tamiano Paseka (**Mr Paseka**) – who was employed at the hotel as a glass collector but who was then standing on the footpath outside the hotel – crossed the road with the apparent intention of defusing the situation. On seeing Paseka, the plaintiff assumed a boxing stance and challenged him to *"have a go"*. Paseka punched the plaintiff in the face, causing him to fall back and hit his head on the kerb (**the assault**). The assault resulted in the plaintiff suffering severe head injuries.

1 See 'Pushing the Boundaries – ***Orcher v Bowcliff Pty Ltd*** [2012] NSWSC 1088' in Wotton + Kearney, 2012 Insurance Year in Review.

2 The licensee was also a party to the appeal. For the sake of brevity, we will refer to both as *"the occupier"*.

Trial

At trial, the plaintiff alleged that the occupier of the hotel, the licensee and the hotel's independent security contractor were negligent for failing to prevent Mr Paseka's assault on the plaintiff. It was common ground at the trial that at the time of the assault:

- Mr Paseka did not know the plaintiff or his friend;
- neither Mr Paseka nor the plaintiff were intoxicated; and
- nothing had occurred between Mr Paseka and the plaintiff that should have alerted the hotel or its security guards that Mr Paseka posed a risk to the plaintiff.

Further, while the trial judge did not accept that Mr Paseka had ceased work at the time of the assault, his Honour did not find the hotel vicariously liable for Mr Paseka's conduct. Rather, all three defendants were found liable for *"failing either to take steps to intervene in the disturbance* [between the plaintiff and his friend] *in the first place, or to prevent* [Mr Paseka] *from doing so himself"*. The trial judge found that this failure had given rise to the risk that others like Mr Paseka, who lacked security training and who were liable to react impulsively, might intervene and cause harm to the plaintiff. Thus, the basis of the defendants' negligence was that they had failed to exercise reasonable care in preventing Mr Paseka from assaulting the plaintiff.

Appeal

On appeal, the plaintiff conceded that the trial judge had erred in finding that the hotel's own security guard (as distinct from the security guard employed by the independent contractor) was present on the street at the time Mr Paseka crossed the road. The effect of that error was that the trial judge's finding that the hotel must have seen Mr Paseka approach the plaintiff could not stand. [3] Therefore, the only issue was whether the independent contractor's security guard should have anticipated the assault. On this issue, the Court unanimously agreed that the evidence did not show that he should have.

Although not decisive of the outcome of the appeal, the Court noted that the scope of the duty of the occupier was to take reasonable care to *"prevent injury to patrons from the violent, quarrelsome or disorderly conduct of other persons"* (emphasis added). As the majority observed, the *"other person"* in the circumstances of the present case was Mr Paseka. Yet the only evidence of *"violent, quarrelsome or disorderly conduct"* shown by Mr Paseka to the plaintiff was Mr Paseka's assault of the plaintiff. However, this was not the conduct that the trial judge had found triggered the occupier's duty. The trial judge had found that the duty was triggered by the altercation between the plaintiff and his friend which, it was said, had caused Mr Paseka to cross the road.

The authors consider that the focus on the altercation between the plaintiff and his friend caused the trial judge's evaluation of the evidence of Paseka's own conduct towards the plaintiff prior to the assault to fall into hindsight reasoning. As the majority of the Court of Appeal found, it did not follow that just because the plaintiff and his friend were arguing on the other side of the road, the hotel and the security contractor should have anticipated that Mr Paseka (or anyone else) who crossed the road posed a risk to the plaintiff. The enquiry as to breach of duty was whether there had been anything in Mr Paseka's conduct prior to his crossing the road that called for a response from the occupier or the security contractor. It is submitted that the trial judge's error was to approach that enquiry retrospectively rather than prospectively.

3 Despite this concession, the plaintiff tried to argue that the independent security contractor had been so subsumed into the security system of the hotel as to have lost its character as an independent contractor. The majority of the Court (Tobias AJA with McColl JA agreeing) did not accept that argument. Macfarlan JA accepted it but agreed with the majority that the security guard had not seen Mr Paseka cross the road, and therefore did not breach his duty of care.

Implications

Although the decision turns on its own facts, it should reassure key players in the hotel industry that for an occupier to have a duty to anticipate and/or intervene in disputes occurring beyond licensed premises, it will need to be shown that the occupier was aware of and had the ability to control the relevant risk before it materialised.

By the same token, it would be wrong to read into the judgment a sanctioning of inaction on the part of industry players in the face of antisocial behaviour occurring around licensed premises. This is particularly so given present community concerns surrounding alcohol and violence. Indeed, had the requisite knowledge and control been established against the occupier and/or the security contractor in the present case, the result would likely have been very different.

We understand that the plaintiff may apply for special leave to appeal to the High Court against the Court of Appeal's decision. Time will tell as to whether that application succeeds.

(Wotton + Kearney acted for the occupier and the licensee in the appeal.) ■

Blameless motor accident provisions – *Ingram v Axiak*

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Amendments to the **Motor Accidents Compensation Act 1999 (NSW)** (**the Act**) allow claimants seeking damages stemming from motor vehicle accidents to make a claim even in situations where a driver is deemed not to be *"at fault"*.

These *"blameless accident"* provisions were introduced to safeguard the interests of claimants injured in sudden or *"inevitable"* circumstances caused by a driver. For example, the provisions cover claimants injured by drivers suffering an instantaneous and unforeseeable medical event such as a stroke. However, the provisions do not extend to pre-existing medical conditions such as diagnosed epilepsy.

The facts

The 14-year-old claimant alighted from a school bus with her 12-year-old sister and walked around to the rear of the bus. The bus pulled back onto the road and the sisters emerged, running, from behind the bus. The defendant, travelling in the opposite direction, saw the bus and slowed to 40km/h. However, the bus obscured any view of the sisters that he might otherwise have had. The claimant was struck by the defendant's vehicle.

There being no disputing that the accident was not caused by the fault of the driver, the claimant abandoned her allegation of negligence. She amended her statement of claim to allege the accident was a blameless accident pursuant to section 7A of the Act, which defines a blameless accident as *"a motor accident not caused by the fault of the owner or driver of any motor vehicle involved in the accident in the use or operation of the vehicle and not caused by the fault of any other person"*. The provision effectively gives the claimant the same right to damages as if the defendant had been negligent.

Supreme Court Proceedings – ***Axiak v Ingram*** [2011] NSWSC 1447

At first instance the claimant failed, as Adamson J found that the concept of *"the fault of another person"* in section 7A extended to include the fault of the claimant, and held that if the claimant is guilty of negligent acts or omissions that cause the accident, wholly or in part, then the accident cannot be said to be *"blameless"*. Even if the claimant

had been entitled to damages, Adamson J would have reduced them by 100% on account of her contributory negligence.

The Court of Appeal Proceedings – ***Axiak v Ingram*** [2011] NSWCA 311

The claimant successfully appealed. The Court of Appeal held that the word *"fault"* for the purposes of section 7A does not include non-tortious negligence such as the claimant's contributory negligence. The expression *"any other person"* excludes the person who has been injured. The claimant was therefore entitled to rely on the blameless accident provisions and to claim damages.

The Court then addressed contributory negligence. The blameless accident provisions proceed on the assumption that the driver is not at fault, and consequently a comparison of the culpability of each party in causing the claimant's injuries is inappropriate. The concept of contributory negligence is therefore an inquiry as to how far the claimant has departed from the standard of care he or she is required to observe in the interest of his or her own safety. The 14-year-old claimant's damages were reduced by 50%.

Special leave application – ***Ingram v Axiak*** [2013] HCA Trans 64 (15 March 2013)

The High Court refused the driver's application for special leave, stating that:

- the Court of Appeal's interpretation of *"fault"* under Part 1.2 of the Act was an available construction of the provisions; and
- it is for Parliament to amend the Act if that construction extends the operation of the provisions beyond what was intended.

Comments

The effect of the High Court dismissing the special leave application is that the Court of Appeal's decision extends the benefit of the blameless accident provisions to every pedestrian, bike rider and passenger of any age injured in a motor accident.

The NSW Government was recently unable to gain the support of the Upper House of the NSW Parliament to proceed with its proposed reforms to compulsory third-party insurance laws. These reforms included the creation of a no-fault statutory benefit scheme for claimants who cannot establish greater than 10% whole person impairment.

The reforms also incorporated amendments to overcome the result of ***Axiak v Ingram***, including provisions that would mean no entitlement to recover damages on the grounds that the accident is blameless if the motor accident was *"caused by an act or omission of that person"*. It remains to be seen whether the NSW Government will introduce further amendments addressing the effects of the case.

Shifting liability to a statutory insurer: the *"use of a registered motor vehicle"*

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Introduction

Most insurance policies exclude cover for personal injury arising out of the *"use of a registered motor vehicle"*. (Coverage may also be excluded for vehicles that should have been registered but were not; however, this article is only concerned with shifting liability to a statutory insurer.) It is a powerful but under-utilised exclusion, and the courts have applied a wide definition of *"use of a registered motor vehicle"*, far beyond merely driving the vehicle.

It is therefore imperative that insurers and their representatives carefully consider whether a claim may be shifted to a statutory insurer for incidents relating to the *"use of a registered motor vehicle"*.

Statutory indemnity in Victoria

In Victoria, the Transport Accident Commission (**TAC**) administers a statutory scheme of compensation established for people injured in transport accidents. The TAC was established by the **Transport Accident Act 1986 (Vic)** (**TAA**).

Under section 94 of the TAA, the TAC is liable to indemnify:

> *"the owner or driver of a registered motor vehicle in respect of any liability* [for] *an injury or death of a person caused by or arising out of the use of the motor vehicle in Victoria or in another State or in a Territory."*

In short, TAC is required to provide statutory indemnity if:

- the insured is the owner or driver of the motor vehicle;
- the motor vehicle is registered in Victoria; and
- a person is injured or killed arising out of the *"use"* of that motor vehicle in Australia.

All other Australian states and territories have their own statutory provisions that would need to be assessed for incidents arising out of the *"use of a registered motor vehicle"*.

While section 45 of the **Insurance Contracts Act 1984 (Cth)** (**ICA**) prevents insurers from providing insurance that limits or excludes liability if the insured has some *"other insurance"*, it does not apply to insurance that is required to be provided by law. Therefore, insurers are entitled to exclude cover for incidents where liability is *"picked up"* by a statutory scheme, such as section 104 of the TAA.

Registered vehicles

As section 104 of the TAA applies only to registered motor vehicles, when an incident occurs arising out of the *"use"* of a motor vehicle, it is important to identify the type of vehicle and whether it is registered.

The **Roads Safety Act 1986 (Vic)** (**RSA**) sets out which motor vehicles must be registered in Victoria. The RSA is broadly worded to include motor vehicles driven on public roads or related areas, including buses, cars, forklifts, mobile cranes, motorcycles, trailers and trucks.

Vehicles that cannot be registered – or are not required to be registered – include:

- railway trains or trams;
- motorised wheelchairs that cannot go faster than 10 kilometres per hour;
- golf carts, golf buggies or ride-on mowers primarily not taken on roads;
- vehicles without a motor, such as bicycles;
- self-propelled vehicles used for construction that travel at less than 10 kilometres per hour; and
- most electronic scooters.

"Use" of a registered motor vehicle, not *"driving"* a registered motor vehicle

The word *"use"* of a registered motor vehicle must not be confused with the threshold test in relation to *"driving"* a registered motor vehicle. This is a narrow test, which in Victoria is the threshold test for entitlement to *"no-fault compensation"*. Claims for indemnity under section 104 of the TAA apply to more than merely *"driving"* a registered motor vehicle because of the wide interpretation of the word *"use"* of a registered motor vehicle.

The application of *"use"* of a registered motor vehicle is aptly explained in ***Transport Accident Commission v Road Construction Authority*** [1990] VR 989, where the Court stated that:

> *"the Act* [which was a precursor to, but to the same effect as section 104 of the TAA] *is not concerned with fine distinctions and its reference to the use of a motor car should be taken as including everything that falls fairly within the conception of the use of a motor car."*

For example, an injured worker may make a claim against the insured, arising out of a workplace accident that occurred when the worker was loading a registered vehicle on a building site. In this scenario, the incident did not relate to driving a motor vehicle and did not occur on a road.

The injured worker may be entitled to make a claim under workplace accident legislation, but if the incident could be said to have arisen out of the *"use"* of the registered motor vehicle, section 104 of the TAA would apply.

Other examples of the *"use"* of a motor vehicle

A number of cases illustrate the wide application of the word *"use"* in relation to motor vehicles.

- In ***Transport Accident Commission v Road Construction Authority*** (introduced above) a worker was injured raising the tailgate of a trailer connected to a registered motor vehicle. The Court found the injury arose out of the *"use"* of the registered truck. Loading the machine was incidental to using the truck to transport the machine by trailer.
- In ***QBE Insurance Ltd v Stoobridge & Ors*** [2000] TASSC 172, a worker was injured in an accident when unloading a horse float that had just been towed by a registered motor vehicle, and the process of unloading was deemed to be *"use"* of the vehicle.
- In ***Dickinson v Motor Vehicle Insurance Trust*** (1987) 74 ALR 197, an infant was severely burnt when the interior of her father's car caught fire. Her father had parked the car temporarily to buy records at a nearby record shop. The infant's brother began to play with a box of matches. A floor mat caught alight, the fire spread, and the infant was trapped and injured. The father was deemed to have been *"using"* the car at the time.

- In ***Commercial and General Insurance Co Ltd v Government Insurance Office (NSW)*** (1973) 129 CLR 374, a rigger was injured by a mobile crane that was in a fixed position. The High Court of Australia held that although the mobile crane was stationary, *"use"* of a motor vehicle included its intended use as a crane, even though the vehicle itself was in a fixed position at the time of the incident.

Summary

As claims including liability arising out of the *"use of a registered motor vehicle"* are potentially covered by a statutory scheme – in Victoria, under section 104 of the TAA – it is imperative that insurers:

- consider if insurance policies should simply exclude insurance cover for incidents relating to the *"use of a registered motor vehicle"*, to prevent double insurance becoming the core issue;
- turn their mind to potential cover by a statutory scheme when a registered or potentially registered motor vehicle is connected to an insured's claim made under a policy. This includes, for example, subcontractors making a claim under a head contractor's policy of insurance, if a subcontractor provided a registered forklift or other registered vehicle connected to the incident; and
- notify the statutory insurer as soon as possible if the statutory insurer may be obliged to provide indemnity. It is often in an insured's best interests to pursue recovery under this scheme as there are no excesses, nor are there claims-history cost penalties. ■

Current trends in personal injury litigation in Victoria

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Introduction

In Victoria, most claims brought for personal injury fall into one of two categories.

The first is general liability claims, which are usually standard *"slip and trip"* cases, sports or recreational injuries, medical negligence claims and claims by injured hotel patrons.

The second category involves claims arising from injuries sustained in the course of employment. This category includes two subcategories of claims, being:

1. actions brought by seriously injured workers, known as serious injury proceedings under section 134AB of the **Accident Compensation Act 1985** (**ACA**); and
2. actions brought by the Victorian WorkCover Authority (**VWA**) against negligent non-employer third parties, to recover the compensation it has paid a worker pursuant to the provisions of the ACA, known as a section 138 actions.

General liability claims

An injured person's entitlement to make a general liability claim was substantially altered in 2003 as a result of sweeping tort law reform. 10 years on, the Victorian Government is now reviewing whether these changes remain appropriate.

In Victoria, the tort law reforms introduced thresholds before a claim for general damages could be maintained.

It was thought this would throttle claim volumes, reducing pressure on insurance availability and rising premiums. Many other states also implemented tort law reform, but preferred to address the issue by placing caps on entitlements, which controlled claims values.

The changes in Victoria worked as planned. The number of general liability claims slowed to a trickle after the reforms were enacted. We estimate claims volumes are less than 10 per cent what they were before the reforms.

In large part, this is due to Part VBA of the **Wrongs Act 1985 (Vic)** (**the Wrongs Act**), which says that a claimant can only claim damages for pain and suffering (known in Victoria as general damages) if the injury is assessed by a medical practitioner as resulting in more than 5 per cent permanent physical whole-person impairment (**WPI**), or more than 10 per cent permanent psychiatric impairment. There are also detailed procedural requirements, including the need to obtain a Certificate of Assessment (**a certificate**), which can be subject to independent review by a Medical Panel.

Experience has told us that the method of assessment used to determine WPI – the American Medical Association Guides Edition 4 (**the AMA Guides**) – favours certain injury types. The AMA Guides focus on the impairment resulting from injury, not the pain levels. For example, significant and painful back injuries may not satisfy the threshold, despite the permanency of the injury. However, cervical injuries that restrict movement of the neck or shoulder might qualify. Elderly claimants are much more likely than other demographics to sustain injuries that meet these thresholds.

Earlier this year, the Victorian Government appointed the Victorian Competition and Efficiency Commission (**VCEC**) to undertake an inquiry into whether perceived inequities in the current scheme – in particular the current thresholds for entitlement to general damages – ought to be revisited.

Plaintiff firms and lawyer groups such as the Law Institute of Victoria (**LIV**), argued the threshold should be a lower percentage figure, or alternatively, for the introduction of a *"narrative"* or subjective test so those who have a serious injury might still be entitled, even if they do not meet the AMA Guides' requirements.

The VCEC has now issued its draft report. It has indicated it will not recommend moving to a narrative test. However, it has suggested some changes by:

- reducing the threshold requirement for spinal injuries, because it considered that the AMA Guides too onerously assess these serious injuries; and
- reducing the psychiatric injury threshold from more than 10 per cent to 10 per cent or less.

Despite lobbying by plaintiff groups and the LIV, it appears the VCEC is unlikely to introduce exceptions to the threshold for psychiatric injury resulting from:

- the a loss of a close relative;
- being infected with a blood-borne disease;
- undergoing unnecessarily invasive treatment due to negligent misdiagnosis; and
- traumatic injuries suffered by children who eventually substantially recover.

Although the VCEC considers the changes to the threshold will have a modest impact on premiums (between 0.2 and 1.8 per cent), it is likely that other amendments (such as improvements to procedural aspects) might offset any detriment felt by public liability insurers.

The VCEC has indicated it will also look to implement legislative changes to the procedural scheme, which has been plagued with uncertainties and widely litigated upon. Wotton + Kearney has been one of only a few firms invited to participate in roundtable conferences with VCEC members, to work through current problems with the system.

Other proposed amendments may include altering some caps for general damages and economic loss claims. However, these changes should have marginal impacts on insurers. The VCEC has recommended changes to gratuitous attendant care thresholds to include only claimants who establish a need for care for 6 months and 6 hours a week, because in Victoria (unlike other states) the threshold has been applied disjunctively – to those requiring 6 hours a week or 6 months of care.

The VCEC's final report should be handed down by March 2014.

Claim costs on the increase

We have previously reported that over the last 5 years, general damages awards have increased significantly across the board.

In that period, we estimate that assessments have at least doubled. However, we have seen some tempering – but not lowering – of expectations and judicial outcomes.

That said, claim costs generally continue to increase.

The source of current upward pressure comes from substantially increased claimant costs entitlements, and a continuing litigious environment. The introduction of the **Civil Procedure Act 2010 (Vic)** – and the imposition of overarching obligations for all parties to only take such steps as are in the interest of resolving disputes – is having some positive impact. However, other legislative changes (such as substantially revised scale costs entitlements in the Supreme Court) are resulting in a substantial increase in claims costs overall.

In April 2013, for instance, the scaled hourly rate that will be applied in a costs recovery when a party is entitled to a costs order increased to $360 plus GST, up from $315. There is now more focus on assessing the hours the lawyer spends on the case, rather than placing a fixed fee on certain work performed, as had been the norm under the scale costs approach.

We have already noticed a substantial increase in plaintiffs' costs expectations (of between 50 per cent and 100 per cent over the last 12 months). We expect this upward trend will continue, at least in the short term, as lawyers and costs consultants get used to the new scale.

It is worth noting that already the Transport Accident Commission – the sole insurer of motor vehicle personal injury liability in Victoria – has taken the unusual step of implementing caps on costs recovery for actions involving the Commission. Unfortunately, insurers do not have the same ability to take steps towards limiting costs claims against them.

Other notable trends

The overwhelming feeling is that claims volumes have generally remained stable over the last 12 months. Yet we appear to be seeing more speculative claims which, on their face, seem unmeritorious.

It is hard to say whether this is a result of personal injury law firms vying for work in a tighter market. Otherwise, it may reflect what we perceive is an attempt – by firms and claimants alike – to take advantage of the general lowering of the 'bar' for a finding of negligence or liability, or a deliberate strategy to take advantage of insurers' commercial pragmatism. Regardless of the cause, it is a concerning trend.■

A second bite of the cherry?

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Introduction

"Centuries of experience before this present age taught the general wisdom and reasonableness of the verdicts of civil juries. Only in a clear case should the judge assume the responsibility of depriving all parties of the jury's verdict and directing or entering judgment in favour of one party."[1]

In Victoria, a party to a claim in contract or tort may elect to be tried before a jury of 6.[2]

In a trial with a jury, the verdict of the jury forms the basis for the Court's judgment.[3] The courts have traditionally taken a robust view in considering the capacity of a jury, properly instructed, to reject or ignore evidence or information irrelevant to the performance of its duties.[4]

More recently, there has been an increasing trend for plaintiffs to challenge the jury's capability to fairly decide the case. This had led to a large number of applications to discharge the jury, or alternatively, applications for judgment notwithstanding the jury's verdict (judgment *non obstante veredicto*). Aggrieved parties (usually plaintiffs) are also appealing more jury outcomes. In the last 12 months, appeals against jury verdicts comprised about 60 per cent of the Court of Appeal's injury appeal business. Although the Court's response to these applications has varied, in an increasing number of recent cases (if not at first instance, then on appeal) the jury's reliability has been second guessed.

Background

It is well established that the courts have the discretion to discharge a jury if there has been inflammatory, irrelevant and/or prejudicial material in counsels' addresses, and the trial judge concludes that a fair trial is not possible.[5] However, *"the discharge of a jury is a serious step which should only be taken where real injustice cannot otherwise be avoided."*[6]

1 ***Naxakis v West General Hospital*** [1999] VSC 389 per Kirby J.

2 Rule 47.02 (1) and (4) of the **County Court Civil Procedure Rules 2008** and **Supreme Court (General Civil Procedure) Rules 2005**.

3 See ***Phillips v Ellinson Bros Pty Ltd*** (1941) 65 CLR 221 at 231; ***Russell v Victorian Railways Cmrs*** [1948] VLR 118 at 120; ***Antoniadis v Ramsay Surgical Ltd*** [1972] VR 323 at 324.

4 See ***X v Amalgamated Television Services Pty Ltd (No 2)*** (1987) 9 NSWLR 575 at 590; ***G & J Shopfitting & Refrigeration Pty Ltd (in liq) v Lombard Insurance Co (Aust) Ltd*** (1989) 16 NSWLR 363 at 372; ***BP v Australian Red Cross Society*** (Unreported, Supreme Court of Victoria, Nathan J, No 5495/91, 21 August 1991).

5 ***Hudspeth v Scholastic Cleaning and Consultancy Services Pty Ltd & Ors*** (Unreported ruling, Supreme Court of Victoria, Dixon J, 4 December 2012).

6 ***Allard v Murwillumbah Bowling Club Ltd*** [1976] 1 NSWLR 275 at 284 (Glass

For example, a fair trial may be prejudiced where:

- facts alleged in opening cannot be established[7];
- counsel transgresses Court rulings[8];
- counsel asks an improper question[9]; or
- irrelevant evidence is introduced, possibly distracting the jury from its true function.[10]

Alternatively, circumstances may be revealed that reflect on the capacity of the jury – or one juror – to give an impartial verdict.[11] Questions of impartiality may arise from:

- an association between a juror and a witness[12] or a party[13]; or
- a juror's statement of intention to find for one party, regardless of the evidence.[14]

In such circumstances, if it is thought that the interests of justice so require it, a trial judge may discharge the jury. A case of interest is ***Messade v Baires Contracting Pty Ltd***[15], where the trial judge discharged the jury after 8 hearing days on application by the plaintiff's counsel, after it was brought to the Court's attention that 3 jurors had raised concerns because the plaintiff had been at Flagstaff train station where they were catching the train on 2 different occasions, seemingly without purpose. The judge commented that when first apprised of the interaction, he was particularly concerned that the plaintiff may have in some way deliberately orchestrated the events.

JA); ***Wellington v Lake George Mines Pty Ltd*** (1961) 62 SR (NSW) 326.

7 ***Taylor v Edwards*** [1967] 1 NSWR 689; (1967) 85 WN (Pt 1) (NSW) 386.

8 ***Tringali v Stewardson Stubbs & Collett Ltd*** (1966) 66 SR (NSW) 335.

9 ***Levett v Perry*** (1960) 78 WN (NSW) 158.

10 ***Cucinotta v Nominal Defendant*** [1960] NSWR 9; (1960) 61 SR (NSW) 23.

11 ***Hodgetts v Purser*** [1958] VR 414.

12 *Ibid.*

13 ***Keddie v Foxall*** [1955] VLR 320.

14 ***Watson v Hammence*** [1957] VR 319 at 325.

15 (Rulings Nos. 2, 3 & 4) [2011] VSC 75.

However, his Honour concluded that although highly coincidental, his Honour could not say why the plaintiff came to be in the same area as the jurors on 2 successive dates. His Honour ultimately determined that as credit was such a key issue in the case, his Honour could not be satisfied that the jurors could act impartially (despite advising the Court they would). The jury was discharged.

Non obstante veredicto

When a jury delivers its verdict, it will ordinarily be binding on the Court and the parties. However, in some cases, a party may apply to the trial judge for judgment not to be entered in accordance with the jury verdict. This step should only be taken in exceptional circumstances, when the evidence upon which the jury made its decision did not support its verdict.

The principles were recently summarised by ***Kyrou J in King v Amaca Pty Ltd***[16], as follows:

- In order for a party's application for judgment notwithstanding the jury's verdict to succeed, that party must establish that there was no evidence upon which a reasonable jury, properly directed, could return a verdict for the other party.
- Where there is evidence to support the jury's verdict, the verdict cannot be disregarded even if the trial judge was strongly against the jury's conclusion.
- A trial judge hearing an application for judgment notwithstanding the jury's verdict should determine the application on the evidence most favourable to the party that carries the onus of proof.
- A trial judge should proceed with great caution and only exercise the power to give judgment disregarding the jury's verdict in the clearest of cases.
- The Court has been more reluctant to enter judgment contrary to a jury's verdict, that is, judgment *non obstante veredicto*.

In ***Duma v Mader International Pty Ltd***[17], the

16 [2011] VSC 422.

17 [2013] VSCA 23.

jury found in favour of the defendant. The trial judge rejected the plaintiff's application for judgment *non obstante veredicto*. The Court of Appeal dismissed the plaintiff's appeal and found that the jury was entitled to accept that there were shortcomings in the plaintiff's evidence. Further, the jury was entitled to accept the evidence relied on by the defendant.

The Court of Appeal held that the appeal must be determined based on the evidence most favourable to the defendant, and on that basis the verdict of the jury was open.

The case of ***Drew v Clyne & Clyne***[18] again involved an application by a plaintiff for judgment notwithstanding the jury's finding of contributory negligence. In that case, the plaintiff's counsel submitted that although there was evidence of a system of work, there was no evidence that the plaintiff was informed of or instructed in relation to the system of work. As such, it was suggested that he could not have contributed to his own injury. The trial judge dismissed the application. His Honour found that there was evidence before the jury that the plaintiff had knowledge of the system of work. In all the circumstances, his Honour formed the view there was evidence upon which a reasonable jury, properly directed, could return a verdict in relation to contributory negligence on the part of the plaintiff.

In ***Kiriwellage v Best & Less Pty Ltd***[19], after the jury concluded that the plaintiff was 20 per cent responsible for contributory negligence, the plaintiff applied for a judgment to be entered in her favour disregarding the jury's finding of contributory negligence on the grounds that no reasonable jury, properly instructed, could have concluded that she was guilty of any such negligence. The trial judge refused the application, stating that his Honour was not:

> *"satisfied that this is 'the clearest of cases' of there being no evidence upon which a jury properly instructed could have concluded that the plaintiff did not take reasonable care for her own safety. Heeding the warning that I should proceed with great caution and should only exercise the power to give judgment in this regard of the jury's verdict in the clearest of cases, I must therefore reject the plaintiff's application."*

However, in ***Pasqualotto v Pasqualotto***[20], the jury found the plaintiff guilty of contributory negligence and reduced the plaintiff's entitlement by 70 per cent. The trial judge rejected the plaintiff's *non obstante veredicto* application. On appeal, 2 of the 3 judges of the Court of Appeal agreed that the jury's finding was not open, and allowed the appeal.

Losing the jury

Where there is an objection to Counsel's address or the capacity of the jury is questioned, the trial judge must consider the extent of any prejudice inflicted, and whether appropriate directions could cure that prejudice.[21] In many cases a trial judge's direction may be capable of curing any perceived unfairness that may otherwise have arisen.[22]

Juries are assumed to accept and faithfully apply judge's directions.[23] Unless the contrary is demonstrated, it is assumed that juries understand and comply with the trial judge's directions.[24]

In the 1909 case of ***David Syme & Co v Swinburne***[25], it was held that a statement in closing submissions claiming that the defendant and its counsel had engaged in *"tricks and machinations"* in having *"crept out of court"* and left the trial before its conclusion

18 (Ruling) [2012] VCC 1551.
19 [2012] VSC 620.
20 [2013] VSCA 21.
21 ***Morgan v John Fairfax & Sons Ltd*** (1988) 13 NSWLR 208 at 211–12 per Kirby P.
22 ***Fitzpatrick v Walter E Cooper Pty Ltd*** (1935) 54 CLR 200 at 211 per Latham CJ, 217 per Dixon J.
23 ***Demirok v The Queen*** (1977) 137 CLR 20 at 22 per Barwick CJ.
24 ***Reza v Summerhill Orchards Ltd*** [2013] VSCA 17 at [50] (and the authorities there cited).
25 (1909) 10 CLR 43.

could not be said to give rise to prejudice.[26] However, over the last few years, juries have been discharged, or verdicts set aside, on the basis of much less.

In ***Li v Toyota***[27], the plaintiff (who had been receiving compensation through workers compensation) successfully applied for the jury to be discharged after the employer's counsel told the jury that *"in this case,* [the plaintiff] *is seeking more, he is seeking pain and suffering damages and economic loss damages over and above his worker's compensation entitlements..."* The trial judge concluded that the comments made by defence counsel constituted unnecessary references to the plaintiff's right to obtain workers compensation, leading the jury to conclude that the plaintiff was endeavouring to seek more than what was his proper entitlement by bringing a common law claim, and that the plaintiff was being greedy. However, in ***Reza v Summerhill Orchards Ltd***[28], the Court of Appeal said proper directions by the trial judge could overcome any potential prejudice to a claimant as a result of comments by defence counsel that because of the plaintiff's receipt of *"compensation payments"* the jury *"might think that it lessens his urgency to work"*.

In ***Mould v ABM Plastics Pty Ltd***[29], the plaintiff's counsel made 2 applications to discharge the jury. The first application was made on the basis that the factual issues to be determined were too complex for the jury. This application was not successful. The second application was based on multiple grounds, including the implication of collusion and recent invention regarding how the incident occurred, and comments made by defence counsel in the opening address. In his opening, the defence counsel had stated that:

"In our modern society you might think that there is an increasing tendency for members of that society to find someone to blame for their own mistakes and you might think that that has particular application in this case where a person performs a task which they know they ought not to do and indeed, as is the fact in this case, you might think, they did this task specifically contrary to a certified capacity which had been authorised by their general practitioner".

The trial judge accepted that this gave rise to a prejudice that could not be confidently *"cured"* by a direction to the jury to ignore the comment.

In ***Christodoulou v Tunstall Square Fruit & Vegetables Pty Ltd***[30], the plaintiff made an application to discharge the jury on a number of bases, including because of comments by the defence counsel. Defence counsel regularly referred to the fact that the plaintiff and her husband were both represented by the same group of lawyers and had been treated by and consulted the same or similar doctors for the purposes of their respective claims. The trial judge discharged the jury. His Honour said that this led to a risk of the jury perceiving that there was something improper about the case, or something in the nature of a conspiracy.

In a recent matter in the County Court[31], the trial judge determined (after 15 days of hearing and when all of the evidence had been led) that the matter was too complicated for the jury. The consequence for the parties, quite apart from being denied the jury's verdict, was an enormous waste of time and money. It is widely viewed that a jury trial takes at least twice as long as a trial before a judge alone[32].

Even in cases where the trial judge has decided not to discharge the jury, plaintiffs (in particular) have sought to have the decision overturned on appeal.

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26 ***David Syme & Co v Swinburne*** (1909) 10 CLR 43 at 59 per Griffith CJ, 61 per Barton J.
27 (Ruling No. 3) [2010] VSC 448.
28 [2013] VSCA 17.
29 (Ruling No. 1) [2010] BCC 1474.
30 (Ruling No. 5) [2010] VCC 1618.
31 ***De Bever v MB Marlow Engineering Pty Ltd & Anor*** (Ruling No. 3) [2013] VCC 1925.
32 See e.g. ***Trevor Roller Shutter Service*** [2011] VSCA 16, 14 [38]-[44].

In ***Baulch v Lyndoch Warrnambool Inc***[33], a case where the jury found no negligence on the part of the defendant, there was an application to discharge the jury on the basis of the defence counsel's closing address. The defence counsel's conduct was impugned on many grounds, having said that the plaintiff could have called any evidence she wanted to rebut an allegation of recent invention but had not done so, and that the jury should conclude that the plaintiff and her counsel were *"grasping at straws"*. The defence counsel had not made this allegation previously.

In that case, the Court of Appeal said that even with the trial judge's directions, it was impossible to be satisfied that the jury was not irretrievably prejudiced against the plaintiff's case. The decision was overturned and a new trial was granted.

In ***Hudspeth v Scholastic Cleaning and Consultancy Services Pty Ltd & Ors***[34], again a case in which the jury returned a verdict of no negligence, there were 2 applications to discharge the jury. One was on the basis of the defence counsel's comments in closing. The comments related to the involvement of the plaintiff's *"legal team"* in preparing expert witness reports, to the effect that the legal team had acted in a misleading and/or deceptive manner. The trial judge was of the view that a false issue had been raised, attacking the honesty of the plaintiff's legal team, which was irrelevant to determining the plaintiff's or expert's credibility. The trial judge rejected the application to discharge the jury. His Honour preferred to direct the jury about the impugned closing submission and provide instructions about how the jury could assess the evidence of the expert and the plaintiff.

This matter is currently on appeal.

Conclusion

There is no dispute that every litigant has a right to have their case fairly tried, free from bias and prejudice. Where litigants receive the benefit of having their case heard before a body of their peers, the Court plays an important role in managing the process so an impartial verdict may be reached. Jury trials are incredibly time-consuming and expensive to run, and there has always been a recognised need to neutralise improper influences and temper potential impropriety.

However, the trend towards litigants questioning the capacity of persons (who are intended to represent the community conscience) to decide cases fairly is worrying. The growing incidence of challenging the robustness of juries in an attempt to *"take a second bite of the cherry"* and begin the proceedings again could in fact lead to the slow erosion of faith in the jury system, thereby chipping away at the capacity of the people to be involved in administering justice. ■

33 (2010) 27 VR 1.
34 Above at 5.

Remediation costs not capable of being covered under liability insurance policies

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Introduction

In ***Hamcor Pty Ltd & Anor v The State of Queensland & Ors*** [2013] QCA 262 the Queensland Court of Appeal considered whether an insured could recover costs incurred to remediate its own land under specified liability policies or an industrial special risks (**ISR**) policy.

Background

Hamcor Pty Limited (**Hamcor**) owned land containing a chemical manufacturing plant operated by Binary Industries Pty Limited (**Binary**). The plant and its contents were destroyed by fire. Large quantities of water used by the Fire Service in fighting the fire became contaminated with chemicals from the plant. The contaminated water overflowed bungs and dams, contaminating neighbouring properties and a creek. A large quantity of contaminated water also remained on Hamcor's land.

The Environmental Protection Agency issued a notice requiring Hamcor *"to conduct or commission work to remediate the contaminated land ... and nearby affected land"* (**the notice**), and obtained orders in the Planning and Environmental Court requiring Hamcor to remove contaminated substances and clean structures (**the orders**).

Hamcor spent over $10 million performing the remediation work. It did not have an insurance policy in place that provided cover for the remediation costs. At a preliminary issue trial Hamcor sought to recover the costs from:

- the Fire Service (as the State of Queensland) alleging that it was negligent in the manner in which it fought the fire, and that the contamination had been caused by its negligence; and
- Marsh Pty Ltd and its authorised representative, Otago Pty Ltd (the brokers), alleging that the brokers owed it a duty of care to ensure it had appropriate insurance cover in place.

Hamcor argued that the costs it incurred to comply with the notice and the orders constituted an event that would fall within the insuring clauses of specified liability policies that the brokers had placed for Binary. It claimed that it should have been named as an insured in the liability policies or, alternatively, that the brokers should

have arranged an ISR policy that would have provided cover.

The brokers argued that the specified primary and excess policies (which provided indemnity for public liability, pollution liability and products liability) would not respond because an *"Insured Event"* had not occurred. The policies only responded to claims where there was liability at law to pay damages, and that required a claim by a third party. In terms of the ISR policy, it was argued that indemnity for remediation was excluded.

First instance decision

At first instance, Boddice J determined that even if Hamcor had been named in the specified liability policies or an ISR policy, it would not have been entitled to indemnity for the costs incurred in remediating its own land. His Honour made the following points:

- a primary composite policy that provides indemnity for public liability, pollution liability and products liabilities does not cover the costs of remediating an insured's own property, since:
  - *"liability to pay compensation" has a broader definition than legal liability to pay damages to another. A liability to pay compensation is conceptually distinct from "damages";*
  - for the policy to respond, liability must be in respect of "*claims ... made against the insured*". That requirement can only be consistent with claims for compensation made by third parties against an insured; and
  - when considered in the context of the policy as a whole, the primary policy provides pollution cover for damage to property belonging to third parties but not to property owned by an insured;
- if there is no liability under the primary policy, there is no cover under an excess policy that provides that liability only attaches after the primary insurers have paid or been held liable to pay the full amount of their liability; and
- an ISR policy provides cover for *"costs and expenses necessarily and reasonably incurred in respect of ... removal, storage and disposal of debris"* and not the costs of remediating an insured's own property, since:
  - *"debris"* is an accumulation of physical items, not an accumulation of contaminated water; and
  - the policy contained an exclusion that cover *"does not extend to any liability that the Insured may incur as a consequence of pollution of any kind"*.

The Appeal

Hamcor appealed Boddice J's decision. The Court of Appeal accepted that the notice and orders were both a *"liability"* on Hamcor. However, the primary composite policy required a *"liability to pay compensation"*. The Court of Appeal referred to dictionary definitions of *"compensation"* and found that *"compensation"* necessarily contemplated the recompensing of the third party. The liability therefore had to be in respect of loss and damage suffered by a third party. The Court of Appeal upheld Boddice J's determination in relation to the primary composite policy. Hamcor did not appeal Boddice J's findings in relation to the excess policy.

In terms of the ISR policy Hamcor argued that the use of the word *"debris"* was not inconsistent with the provision of an indemnity for costs of remediation of polluted property, and that the exclusion of *"pollution of any kind"* was

not applicable. The Court of Appeal accepted Hamcor's contention about *"debris"* and determined that the word *"debris"* is capable of describing various forms of residue from the destruction by fire of premises, including ash and water damaged materials. While the court considered that the arguments advanced in relation to cover possibly provided by an ISR policy to be entirely hypothetical, it commented that the wording of the exclusions in an ISR policy are not synonymous with an exclusion of all loss and damage, costs and expenses arising from pollution.

Hamcor's appeal was partially successful, in that the Court of Appeal made a finding that an ISR policy could have provided an indemnity in relation to the costs associated with complying with the notice and the orders.

Comments

This case provides useful guidance to the Australian insurance industry on the approach taken by the Courts to the interpretation of policy terms and provisions. Policy wordings are to be given their plain meanings in accordance with the following legal principles:

- a policy of insurance is a commercial contract and should be interpreted having regard to the language used and the objects it was intended to secure (***McCann v Switzerland Insurance Australia Ltd*** [2000] 203 CLR 579);
- in the event of ambiguity, a liberal approach favouring an insured is to be adopted. The interpretation of policies is to be determined by what a reasonable person would have understood by the language used (***Toll (FGCT) Pty Ltd v Alphapharm Pty Ltd*** (2004) 219 CLR 165);
- although evidence of surrounding circumstances is admissible to assist with the interpretation of a contract, it is not admissible to contradict the plain meaning of the language used (***Codfelfa Construction Pty Ltd v State Rail Authority (NSW)*** (1982) 149 CLR 337); and
- the ordinary rules of contractual interpretation apply but where there is ambiguity, a court may place reliance on parties' intentions (***Australian Casualty Co Ltd v Federico*** [1986] 160 CLR 513).

Hamcor alleged that the brokers should have advised it to obtain a separate policy providing appropriate insurance cover in relation to pollution and environmental risks associated with its ownership of the land. While this aspect was not considered at trial, the case serves as a reminder of the need to fully consider the nature of the risks to which an insured is exposed, and the possibility of obtaining appropriate cover including cover for environmental risks. That said, whether cover is available in relation to penalties imposed by statute remains a contentious issue, as does whether policies providing such cover are enforceable as a matter of public policy.

Victorian bushfire litigation update: Issues involving damage to trees

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Introduction

Litigation arising from the 2009 Victorian bushfires has challenged the status quo when it comes to assessing damages for mature trees by advancing single-tree amenity-based valuations using the modified Burnley method (**MBM**) and the Thyer method (**TM**). These methods have the ability to generate significantly high individual values for trees, without reference to underlying land values.

While Victorian courts have yet to produce a comprehensive judgment on the issue, we comment on the development of the argument in the litigation and a recent decision of ***Roads Corporation v Love*** [2013] VSC 176, where the Court declined to apply the MBM.

Trees and the bushfire class actions

The loss of trees and vegetation in the 2009 Victorian bushfires was immense. The resulting civil class actions encompass a total damaged area of 206,186 hectares – (168,542 hectares in Kinglake–Murrindindi, 33,577 hectares in Beechworth–Mudgegonga, 2,346 hecatres in Horsham, 1,008 hecatres in Weerite–Pomborneit and 713 hectares in Coleraine) – including private, commercial and wilderness areas.

The bushfire litigation has raised a plethora of complex issues in the area of damages. This article explores one area of significant contention: the assessment of compensation for damage to trees, particularly established and mature trees.

The classical view

Trees, like other fixtures on land, have classically been regarded as appurtenant, or part and parcel of the land. At law, the measure of loss for damage to real property caused by tort is:

- the diminution (reduction) in value of the land before and after the fixture; or
- in some cases where property has some special value to the claimant, the cost of reinstatement. The reasonableness of a claimant's desire to reinstate the property (trees) is a factor to be considered.

Individual tree-based valuation methods

An area of controversy in the bushfire litigation is the use of formulaic methods to value trees on an individual basis. The MBM and TM are the two valuation methodologies sought to be used in Australia.

The MBM and TM are mathematical calculations that give a monetary value to an individual tree

by reference to a number of physical attributes and external factors. The factors considered in the MBM include tree volume, form, vigour, useful life expectancy, location and base value (nursery prices). The TM uses a series of factors including size, age, environmental benefit, social benefit and planting cost.

These methods can result in significantly high values for individual trees, in some cases collectively eclipsing the underlying value of the property. This outcome has recently been the subject of judicial consideration.

In ***Roads Corporation v Love*** the Court declined to adopt the MBM for valuing trees on the claimant's property in the context of a compulsory acquisition of land. McMillan J commented that the MBM *"artificially inflates the value of trees and characterises them as having an intrinsic value regardless of whether the trees are situated in industrial or residential land"*.

The Court's concern about the inability of the MBM to differentiate values for trees based on their location and the underlying value of the land was raised in a previous decision in the litigation (***Roads Corporation v Love*** [2010] VSC 32). In that judgment, Osborn J said that while the MBM may be appropriate for valuing specimen trees in parks and gardens, it was inappropriate in the context of the case, as it did not draw a distinction in value based on the location. In the circumstances of that case, which involved trees on a rural property, valuing the trees using the MBM resulted in a sum of $20 million just for loss of the trees, which was regarded as completely disproportionate to the underlying value of the land.

The Court did not apply MBM.

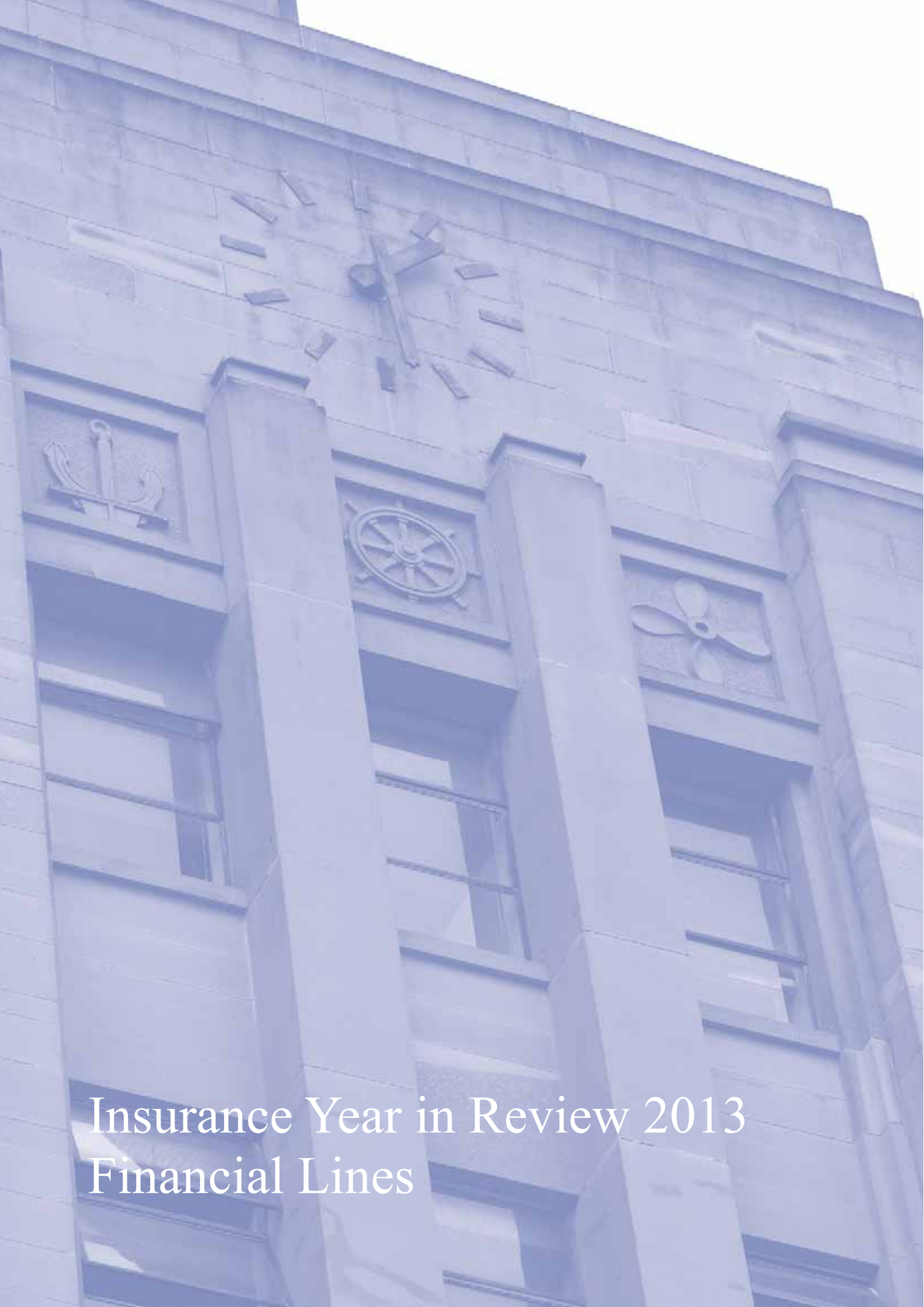
Australian courts have referred to but have not applied the TM (see ***Blythe v Hamblin*** [2009] WADC 192). Peter Thyer, the author of the method, has since developed a variation on the TM, which the plaintiff in the Kinglake bushfire class action (***Matthews v SPI Electricity Pty Ltd & Ors***) advanced this year.

Summary

In some cases trees are a prominent feature of private and public properties. Like other physical and geographical attributes of the land, trees and vegetation can enhance the value of the underlying property. In certain circumstances, individual tree-based valuation methods may have merit and application, but not, it seems, in the area of damages for their destruction.

There is no current definitive Australian judgment on how to assess damages for loss of trees. The preferred approach in the case of replacement of trees is to adopt a *"cost of cure"*, that is to say replanting with juvenile vegetation which will quickly establish and ultimately replace the lost landscape. Such an approach is consistent with reinstatement in the context of damage to real property. In ***Roads Corporation v Love*** the award made was to all intents and purposes the basis of diminution in value.

It is only a matter of time before the courts are asked to accept the application of the MBM and TM. Until then – to the relief of property liability and utility insurers – the classical view prevails. ■



Insurance Year in Review 2013
Financial Lines

Claim against financial advisor fails

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In ***Jordan v HLB Mann Judd Wealth Management (NSW) Pty Limited*** [2013] FCA 315 the Federal Court of Australia considered whether a financial advisor's advice to an "*unsophisticated*" investor to invest in 2 Basis Capital funds (a Basis Aust-Rim Fund and a Basis Yield Fund) (**the Basis Capital Investments**), both of which failed, was negligent.

Background

In 2005 Ms Vicki Jordan approached HLB Mann Judd Wealth Management (NSW) Pty Limited (**HLB**) requesting financial advice. She had received in the region of $7 million from a divorce settlement, and intended to invest between $5.21 million and $5.5 million with the assistance of HLB. Her goal was to invest in funds that would provide her with an income of around $15,000 a month. She relied entirely on Mr Hutton of HLB as her advisor. Mr Hutton's advice to Ms Jordan was to spread her money across a number of investments with varying degrees of risk. In order to achieve the income required, he recommended that her portfolio should include the Basis Capital Investments. Ms Jordan followed Mr Hutton's advice and invested $537,500 (around 10% of her total investment) in the Basis Capital Investments. In 2007 the Basis Capital Investments failed and Ms Jordan lost the money she had invested in those funds.

Ms Jordan sued HLB and Lonsdale Financial Group Limited (**Lonsdale**) for damages in respect of the financial losses she suffered when the Basis Capital Investments failed. Lonsdale is a financial services licensee and HLB is Lonsdale's authorised representative. Lonsdale and HLB are in business together providing financial services.

Ms Jordan alleged that HLB should not have recommended that she, an "*unsophisticated*" investor, should invest in the risky Basis Capital Investments. She alleged that HLB and Lonsdale had:

- breached the contractual and tortuous duties of care they owed to her;
- engaged in misleading or deceptive conduct or conduct that was likely to mislead or deceive by representing to her that the investment recommendations made were suitable for her having regard to her risk profile when they were clearly not; and
- breached section 945A of the **Corporations Act 2001 (Cth)** (**the Corporations Act**) as they made recommendations to her without having a proper basis for doing so.

Ms Jordan also alleged that HLB had breached section 12DA of the **Australian Securities and Investments Commission Act 2001 (Cth)**, and section 1041H of the Corporations Act, as they had engaged in trade or commerce that was misleading or deceptive, or likely to mislead or deceive in relation to a financial service.

HLB and Lonsdale denied all allegations. At trial Mr Hutton gave detailed evidence, assisted by his diary, and attendance notes he had kept on file. HLB and Lonsdale were also able to adduce evidence in the form of reports from Lonsec Limited (Lonsec) showing that the Basis Capital Investments received a "*highly recommended*" assessment of sound performance up to the time of the investment. Lonsec is a corporation associated with Lonsdale that carries out research, and provides analysis and reports in respect of potential investments.

Foster J did not find Ms Jordan's evidence particularly credible. His Honour said "*I have no difficulty accepting that Ms Jordan is unsophisticated*", and considered that she must have appreciated her investments were not risk-free.

Foster J determined that Mr Hutton had made a reasonable and substantially accurate assessment of Ms Jordan's risk profile, and had relied on Lonsec's reports, which were reasonable and pertinent to the assessment. His Honour also said it was "*highly artificial*" to argue that 2 products within a diverse portfolio of investments were too risky when Ms Jordan made no claim that the other investments in the portfolio were unreasonable. Foster J determined that the level of risk in relation to an investment in a particular fund had to be balanced in the context of the portfolio as a whole. His Honour made the following comments:

> *"The provision of investment advice requires a good deal of judgment and, although based upon information which may to some extent be described as objective, is largely a subjective exercise. A critical factor in providing reasonable investment advice is making a reasonably accurate assessment of the goals and objectives of the investor who has come to the advisor for that advice. The process is interactive in the sense that there are no absolutes. What might suit one investor's circumstances, goals and aims may not suit those of another investor. Different investors have different levels of tolerance of risk."*

Ms Jordan's case failed in its entirety. She failed to establish that no reasonable financial advisor asked to advise her in November 2006 should have included the Basis Capital Investments in their investment recommendations. She also failed to show that it was misleading for HLB to suggest that the recommendations were suitable for her, or that it was misleading for HLB to describe a Basis Yield Fund as a fixed-interest investment.

Comments

Financial advisors can take some comfort from this case as it shows that a court will take into consideration the reasonableness of relying upon research and external ratings of investment risk. However, sole reliance on reports or ratings agency research may still be a dangerous course to take.

This case reinforces the importance of keeping contemporaneous file notes, and taking the time to accurately record the details of discussions with clients. If Mr Hutton had not kept detailed notes and diary entries, the outcome may have been different. ■

Blanket notifications – to cover or not to cover?

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Introduction

The issue of blanket notifications has vexed insurers of *"claims made"* policies for some time.

In the context of blanket notifications, it can sometimes be difficult to gauge whether the notification is sufficiently informative and precise to amount to a valid notification. While there has been very little judicial scrutiny in Australia, a number of UK cases have found that a *"blanket"* notification of circumstances can be an effective notification of circumstances so that any claims subsequently made will be regarded as having been made at the time the circumstances were notified.

The recent English High Court decision of ***McManus and Others v European Risk Insurance Co*** [2013] EWHC 18 has followed this trend and found that a blanket notification by an Insured of circumstances that might give rise to a claim was a sufficient notification under a professional indemnity policy.

Facts

In mid-2011, a firm of solicitors, McManus Seddon, took over another firm called Runhams. The new firm was called McManus Seddon Runhams (**McManus**). Runhams had itself recently taken over and acquired all of the mostly conveyancing files of a firm called Sekhon Firth.

In November 2011, McManus received its first claim from a former client of Sekhon Firth. Further claims arrived, and by May 2012 a total of 17 claims – all relating to files handled by Sekhon Firth, had been made. McManus notified these 17 claims to its professional indemnity insurer. Thereafter, McManus retained a risk consultancy firm (**Consultant**) to carry out a review of a range of Sekhon Firth files. The Consultant issued a report, which concluded that there had been a consistent pattern of breaches by Sekhon Firth.

McManus issued a letter to its professional indemnity insurer headed *"Blanket Notification of Circumstances which may give rise to claims"* (**Notification**). The Notification cited:

- the 17 claims already notified;
- similarities between those 17 claims and a number of other files; and
- the conclusion of the Consultant

and the results of its own internal investigation, which found that inadequate practices were endemic or extremely common in the files of Sekhon Firth.

McManus sought to notify each and every Sekhon Firth file as a circumstance that may give rise to a claim, on the basis that the files more likely than not contained examples of malpractice negligence. More than 5,000 files fell into this category.

With the exception of the 17 existing claims and the 32 files identified by the Consultant, the insurer rejected the Notification as a valid notification of circumstances, on the basis that on each individual file, McManus had not identified any specific incident or transaction.

The decision

The Court found that the Notification was valid even though it did not identify specific matters relating to individual files (apart from the 32 files that were the subject of the Consultant's report).

The Court, following the decisions of ***J Rothschild Assurance plc & Ors v Collyear & Ors*** [1998] C.L.C. 1697 and ***HLB Kidsons v Lloyds Underwriters and others*** [2008] EWCA Civ 1206, held that:

- the insurer's rejection of the Notification was wrong, to the extent that it purported to rule out the prospect of future claims being covered under the policy unless a specific incident had been notified;
- whether or not a future claim arising from other Sekhon Firth files would be covered under the policy:
  - would depend on the nature of that future claim and whether it arose from circumstances that were validly notified;
  - would not be conditional on McManus having separately notified an incident on that particular file as being a separate circumstance under the policy.

Comment

It is not always easy to extract a universal application as to when a notification will be sufficient. Blanket notifications need to be seen in their specific factual context.

It remains to be seen whether the Australian courts will follow the approach of the UK courts. The cases of ***John Connell Holdings Pty Ltd v Mercantile Mutual Holdings Limited*** (1988) 10 ANZ Insurance Cases 61-407 at 74,472–3 and ***TBI Pty Ltd v Aon Financial Planning Ltd*** (2004) 13 ANZ Ins Cas 61-601, although not blanket notification cases, are examples of where the Australian courts have taken a narrow view on whether a claim can be said to have arisen as a result of notified circumstances.

The key lesson for insurers is to look at each notification carefully and not reject a blanket notification out of hand simply because an insured has failed to state the precise basis upon which a future claim may be made. ■

"Claims made" policies and section 601AG of the **Corporations Act 2001 (Cth)**

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Overview

On 10 September 2013, the Supreme Court of New South Wales handed down its decision in ***Sciacca v Vero Insurance Limited*** [2013] NSWSC 1285.

The decision involved the application of section 601AG of the **Corporations Act 2001 (Cth)**, which allows a plaintiff to claim directly against an insurer in circumstances where the insured defendant has been deregistered.

In this case, the insurer applied for summary dismissal of the plaintiffs' claim pursuant to section 601AG. The insurer argued that the claim against the insured defendant did not trigger the relevant insurance policy (a *"claims made"* policy) because the claim had not been made until after the policy had expired.

The Court refused the insurer's application, holding that the plaintiffs did not need to prove that the policy in fact responded to the insured's liability in order to claim under section 601AG. It was enough for the plaintiffs to prove that the insured's liability to them was within the scope of the policy.

The arguments

On 21 April 2011, the plaintiffs claimed against Vero Insurance Limited (**Vero**) pursuant to section 601AG. The basis for the claim was that Vero's insured, Integrity Mortgage Professionals Pty Ltd (**IMP**), was liable to the plaintiffs in connection with a loan transaction. The period of the policy in favour of IMP was from 31 May 2007 to 31 May 2008. IMP was deregistered in April 2009.

Section 601AG states that:

> *"A person may recover from the insurer of a company that is deregistered an amount that was payable to the company under the insurance contract if:*
> *(a) the company had a*

liability to the person; and

(b) *the insurance contract covered that liability immediately before deregistration."*

Vero conceded that IMP had a liability to the plaintiffs which satisfied the first limb of section 601AG.

Vero's application for summary dismissal of the plaintiffs' claim turned on the second limb of section 601AG. Vero argued that the policy did not cover IMP's liability immediately before the deregistration in April 2009 because the policy had expired on 31 May 2008. Vero explained that the policy was a *"claims made"* policy, and that no claim had been made during the policy period.

Vero's argument hinged on the use of the word *"covered"* in the second limb of section 601AG. According to Vero, the plaintiffs needed to establish that the policy responded to IMP's liability – in other words, that Vero was liable to indemnify IMP immediately before the deregistration.

Vero submitted that the Court should distinguish between occurrence-based policies and *"claims made"* policies. It argued that section 601AG was designed to assist a plaintiff claiming against an occurrence-based policy, under which the insurer's liability to indemnify the insured arose at the same time as the insured's liability to the plaintiff. So long as the 2 liabilities arose prior to the insured's deregistration, the plaintiff could claim under section 601AG.

Vero distinguished this situation by comparing it with a *"claims made"* policy, where the insurer's liability to indemnify often does not arise until some time after the insured's liability to the plaintiff. The insurer's liability arises when a claim is made against the insured. Where this situation arises, as it did in these facts, the plaintiff cannot use section 601AG, and the plaintiff should seek to have the insured reinstated under section 601AH. Vero claimed that the legislature had deliberately distinguished between the types of policies when it enacted section 601AG.

Finally, Vero accepted that but for the insured having been deregistered, Vero could not have obtained summary dismissal of the plaintiffs' claim. If IMP had still been registered, Vero would have declined to indemnify IMP on the basis that no claim had been made during the policy period. The viability of the declinature would have been a triable issue between insurer and insured.

The plaintiffs submitted that the second limb of section 601AG only required that there be a policy in existence immediately prior to deregistration, covering the insured's liability. They argued that the word *"covered"* was a broad term, intended to refer to the type of liability owed by the insured. The word *"covered"* did not require proof that the insurer was liable to indemnify. The plaintiffs submitted that although the policy had expired in May 2008, it continued to exist as at the date of deregistration.

The decision

The Court held that the purpose of section 601AG was to put Vero in IMP's position for the purpose of responding to the plaintiffs' claim.

In interpreting the second limb of section 601AG, the Court preferred the plaintiffs' submission. The plaintiffs only needed to show that at the time of the insured's deregistration, there existed a policy that might potentially respond to the insured's claim. The plaintiffs were not required to establish that the insurer was liable to indemnify IMP (at least

not for the purpose of invoking section 601AG).

Concluding remarks

The decision confirms that an insurer cannot run a declinature point (which would have been available against the insured) to defeat a plaintiff's claim under section 601AG. The question of indemnity is a triable issue between the insurer and the plaintiff, just as it would have been between the insurer and the insured.

It is worth noting that the decision did not consider the first limb of section 601AG, which requires that the insured is liable to the plaintiff. Vero admitted this fact. Without this admission, the plaintiffs may have been required to prove the insured's liability for the purpose of invoking section 601AG. Alternatively, the Court may have preferred a broader construction (as it took with the second limb), in which case the plaintiffs would only have needed to prove a potential liability of the insured.■

Damages and compensation – what's in a claim?

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In ***Kyriackou v ACE Insurance Limited*** [2013] VSCA 150, the Victorian Court of Appeal was called on to decide whether defence costs coverage under a professional indemnity policy was triggered, in relation to a claim brought by the Australian Securities and Investments Commission (**ASIC**) against the insured director, Michael Kyriackou.

Background

The appellant, Mr Kyriackou, was a director of a series of companies against which ASIC commenced proceedings in the Federal Court. ASIC sought a declaration that the defendants, including Mr Kyriackou, were operating an unregistered managed investment scheme. ASIC also sought consequential relief, including an order pursuant to section 1324(1) of the **Corporations Act 2001 (Cth)** that Mr Kyriackou be permanently restrained from further operating or promoting the scheme, and an order that the scheme be wound up.

ASIC ultimately discontinued its proceedings against the companies and Mr Kyriackou. No order for costs was made. Mr Kyriackou was significantly out of pocket and looked to his ACE Insurance Limited (**ACE**) professional indemnity policy to cover him for his legal costs.

ACE denied indemnity on the basis that the claim fell outside the insuring clause of the policy. Alternatively, ACE contended that the claim was subject to a number of exclusions.

At first instance, the Victorian Supreme Court found in favour of ACE on the basis that the relief ASIC sought did not include a claim for civil compensation or civil damages. As such, the insuring clause was not triggered because ASIC had merely sought declaratory and injunctive relief against Mr Kyriackou.

In addition, the Court held that Mr Kyriackou was not entitled to indemnity because the claim did not arise from a breach of duty owed in a professional capacity.

Mr Kyriackou appealed the decision.

The Court of Appeal's decision

Mr Kyriackou submitted that ASIC's application was based on a claim for civil damages or civil compensation even though ASIC's originating process

did not expressly seek relief by way of damages or compensation. Mr Kyriackou argued that the claim for declaratory relief was one step in a series, the aim of which was to bring to light conduct that might ultimately result in a claim by some or all of the investors in the scheme. Mr Kyriackou argued that the very purpose of ASIC's application was to preserve the assets of the companies, thereby allowing investors to enforce any future judgment.

Mr Kyriackou also relied on the definition of *"claim"* in the ACE policy, which included the phrase *"a written intimation of an intention to seek such compensation or damages"* (emphasis added). Seizing on this wording, Mr Kyriackou submitted that the ASIC proceedings constituted a written intimation because at a minimum, ASIC's originating motion contemplated or hinted that it intended to make an application for damages or compensation.

In response, ACE submitted that Mr Kyriackou's argument was based on nothing more than conjecture. A proper analysis of the originating process and the material ASIC relied on showed that ASIC had sought neither civil compensation nor civil damages, and that had the Court ultimately determined the proceeding, this relief would not have been granted. Properly characterised, ASIC's application was concerned with shutting down the managed investment scheme and preserving the assets before they were dissipated. It was intended to do no more than protect the assets during an interim period.

The Court of Appeal unanimously agreed with ACE's submissions and found that pleadings in a civil action are, by their very nature, intended to inform the opposite party of the claim it is asked to meet. In the circumstances, it could not be said that there was any *"intimation"* of an otherwise *"undisclosed intention"* of a claim not clearly expressed in the pleadings or the originating process.

The Court of Appeal went further by stating that even if it could be argued that the ASIC proceedings were intended to safeguard assets to allow aggrieved investors to recover lost funds, this action would be for the restitution of borrowed funds or the enforcement of contractual rights. In these circumstances, the claim would be for a restitution of money had and received, or recovery of a debt due or payable under the contract, neither of which would constitute payment of compensation or damages.

The Court of Appeal concluded that ASIC's claim was not a claim for civil liability, and accordingly the definition of the word *"claim"* was not met. As such, Mr Kyriackou was not entitled to indemnity.

In obiter, the Court also considered whether Mr Kyriackou was acting in his professional capacity as a broker, as required by the insuring clause in the policy. The Court of Appeal departed from the first instance decision and although not determinative of the appeal, found that:

- it is necessary to make a broad assessment of the overall activity undertaken by the insured; and
- this *"is not answered by concentrating on the specific task which has not been performed or badly performed so as to give rise to liability".*

If there was liability in this case, it arose in the overall context of Mr Kyriackou operating the group's business as a finance originator.

Implications

In upholding the Supreme Court's

decision, the Court of Appeal showed that it will consider the substance of the claim, but will also give careful regard to the terms in which the claim is made – whether that be a letter of demand or, as in this case, the originating motion or pleadings that give rise to the claim.

Importantly, the Court of Appeal also continued to endorse a broader characterisation of the phrase *"professional capacity"*. Noting that policies are often sold to persons who are not acting as traditional professionals, it is now likely that the courts will give regard to the business the policy was intended to cover, as well as the overall context in which that business was conducted, to determine whether a claim falls within the term of an insuring clause.

The FOFA reforms

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Introduction

In the wake of the global financial crisis and huge losses suffered by investors as a result of advice given by financial advisers, the Future of Financial Advice (**FOFA**) reforms have emerged. On 1 July 2013, the FOFA reforms became mandatory. They have been implemented through amendments to the **Corporations Act 2001 (Cth)**.

The FOFA reforms aim to improve consumer trust and confidence in the financial advice industry following the fallout of a series of product failures affecting retail investors underpinned by "*non-traditional*" and often highly leveraged products, significant levels of client borrowings and questionable commission and remuneration models for the advisers concerned. The reforms are directed at conflicts of interest, improving competency, and quality and affordability of advice, encouraging greater ethics, standards and professionalism and enhancing ASIC's regulatory (particularly enforcement) powers for providers of financial services to retail clients.

The key reforms

The key FOFA reforms include:

- **The best interests duty.** The introduction of a statutory best interests duty requires financial advisers to act in the best interests of their clients and place their clients' objectives, financial situation and needs ahead of their own when developing and providing personal advice. This duty is based on the notion of "*reasonableness*". Financial advisers can establish that they have satisfied this duty by undertaking specified steps to assist in determining what the best interests of the client are – referred to as "*safe harbour*" provisions. Those steps include identifying the client's objectives, financial situation and needs; making relevant inquiries to obtain complete and accurate information; and assessing whether the financial adviser has the expertise required to provide the relevant advice sought.
- **A ban on conflicted remuneration.** The reforms introduce a prospective ban on conflicted remuneration, including commissions. Licensees and authorised representatives will not be allowed to give or receive payments or non-monetary benefits if the payment or benefit could reasonably be expected to influence financial product recommendations or financial product advice. The ban also applies to asset based fees on geared (or borrowed) amounts (although it will still be permissible to charge a flat fee on geared

amounts and/or an asset based fee on that portion of a client's investment that isn't subject to gearing).

- **A ban on soft-dollar benefits.** The reforms also ban non-monetary ("*soft-dollar*") benefits – such as holidays and gifts – given to advisers who provide financial advice to retail clients. There are some exceptions to the ban, such as IT support or software relating to the provision of financial product advice, or a benefit for genuine education and training purposes.
- **Scaled advice.** The reforms introduce a new concept of "*scaled advice*". The reforms are directed at simplifying the advice process for simple, limited, single product advice within specific areas. The reforms are expected to improve consumers' access to, and the affordability of, financial advice and will have the most impact in the superannuation space by giving fund managers the opportunity to provide scaled advice to members.
- **Opt-in and fee disclosure.** Advisers are required to request that their retail clients opt in or renew their advice agreements every 2 years if the client is paying ongoing fees. Advisers must also provide an annual statement outlining the fees, charges and services provided in the previous 12 months. The aim is for clients to be fully aware of the fees they are paying and the value of the services being provided, resulting in a more competitive advice market.

In addition to the reforms outlined above, a number of other initiatives have been implemented. ASIC has been given enhanced enforcement powers and a new limited Australian Financial Services Licence will see accountants licensed and able to provide a range of financial advisory services beyond the former self-managed superannuation fund exemption.

Impact for insureds and insurers

The reforms have been met with mixed responses from professional indemnity insurers of financial advisers. While there appears to be a general acknowledgement that reforms directed at conflicted remuneration were necessary, the enhanced level of regulation is viewed as a "*double-edged sword*".

On the one hand, the reforms may improve the general quality of advice being provided by financial advisers. However, on the other hand, the reforms represent a further layer of potential liabilities for financial advisers and, therefore, their insurers. The effective removal of commissions also raises questions about how the industry as a whole will react and introduces some uncertainty into the impact of alternative arrangements which appear to be contributing to the nervousness around the reforms.

It is also notable that minimum education and qualification requirements, the role of the Financial Ombudsman Service and the relationship between financial product issuers and financial product advisers remain "*big ticket*" issues for professional indemnity insurers which have not been addressed in any meaningful way by the reforms. On one view, therefore, the reforms will not translate into anything meaningful either from an insurance product or pricing perspective.

In this context, 2014 ought to see a more stable environment for professional indemnity insurers in this space with the last round of "*GFC claims*" drawing to a conclusion but from a regulatory and liability perspective there remains real potential for another "*interesting*" year. ■

NSW Court of Appeal bridges the gap on section 6 charges - *Chubb Insurance Company of Australia Ltd v Moore*

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Introduction

In a successful outcome for the insurers of failed timber investment company Great Southern, the New South Wales Court of Appeal (**NSWCA**) in ***Chubb Insurance Company of Australia Ltd v Moore*** [2013] NSWCA 212 (***Chubb v Moore***) determined that section 6 of the **Law Reform (Miscellaneous Provisions) Act 1946** (**the Act**) did not apply on a threshold issue, because the third-party claims against Great Southern were issued outside of New South Wales.

The NSWCA also provided some long-awaited guidance on the problems thrown up by the New Zealand decision in the ***Bridgecorp***[1] case by providing some obiter commentary that section 6 of the Act does not:

- attach to defence costs; or
- prevent claims payments where there are multiple claimants with competing charges.

1 ***Steigrad v BFSL 2000 Ltd.***

The collapse of Great Southern led to various class actions brought by different groups of investors for alleged non-disclosure in Great Southern's Product Disclosure Statements, and alleged failures to act in investors' best interests during a company restructure. After those investor claimants asserted competing section 6 charges over relevant professional indemnity and directors' and officers' insurance policies, the ***Chubb v Moore*** declaratory proceeding was brought by Great Southern's insurers: Chubb, Liberty, Allianz, AIG, Dual, QBE and AXIS.

Issues

The intended purpose of section 6 is to ensure a claimant receives the fruits of any judgment by creating a charge over relevant insurance moneys and a corresponding statutory right to enforce the charge directly against the insurer. However, the scope and operation of section 6 is notoriously unclear as reflected by Ball and Emmett JJ's comments in the judgment that

the section should be repealed or rewritten to meet its objectives. Since there was previously no Australian case law on point, the first instance ***Bridgecorp*** decision (despite being overturned on appeal in New Zealand[2]) added to the uncertainty plaguing the insurance industry over the past 2 years.

The NSWCA grappled with three major issues in ***Chubb v Moore***:

- **The territorial scope of section 6.** Does it apply only where the governing law of the policy was New South Wales[3], where the insurer's principal place of business was in New South Wales[4] or when some other combination of territorial connections to New South Wales existed?
- **Defence costs.** Does section 6 attach to all insurance money (including defence costs) so that if the claim(s) exceeded the policy limits the insurer must run the risk of paying ex gratia payments or leave the insured unfunded[5].
- **Payment of multiple claims.** Was the first-instance decision in ***Bridgecorp***[6] correct in determining that the charge takes full effect immediately at the time of the event giving rise to the claim? If so, where there are multiple claimants with competing charges, could an insurer follow the usual rule of paying the first claimant to establish a liability[7] or must the insurer instigate *"claims paralysis"* by refusing to pay any claimants until all had established liability, and then pay in accordance with the priority of competing charges?

2 Although subsequently reinstated by the New Zealand Supreme Court.

3 ***Ludgater Holdings Limited v Gerling Australia Insurance Company Pty Limited*** [2008] 3 NZLR 885.

4 ***Cambridge Credit Corporation Ltd v Lissenden*** (1987) 8 NSWLR 411.

5 As is now the case with the recent NZ Supreme Court decision.

6 And subsequent Supreme Court decision.

7 The *"first past the post"* principle set down in ***Cox v Bankside*** [1995] 2 Lloyd's Rep 437

Findings

In relation to the territorial scope of section 6, the NSWCA adopted a simple and clear approach: section 6 only applies where the claim against the insured is issued in New South Wales. While this may temporarily limit the number of cases where section 6 applies, the jurisdiction of the New South Wales courts is very wide and many claimants may in future issue claims in New South Wales solely to assert section 6 charges.

In relation to defence costs, the NSWCA provided authoritative commentary, stating that even if section 6 did apply to the Great Southern insurance policies, any charge under the section would not extend to defence costs because:

- the charge under section 6 attaches to *"all insurance moneys that are or may become payable in respect of that liability"* (the liability being that owed to the claimant) and defence costs were not payable in respect of the insured's liability, but rather under a contractual obligation to defend the insured; and
- there is nothing to which a section 6 charge can attach unless and until a liability to pay damages or compensation has been determined. That liability is not determined unless and until a determination has been made by a judgment of award or settlement, and defence costs are payable before that judgment or settlement.

In relation to settlement of multiple claims, the NSWCA commented that even if section 6 applied to the Great Southern insurance policies, any payment to some claimants could be a valid discharge (thus eroding the policy limits) if made before judgment or settlement of other claimants' claims (i.e. the NSWCA appears to have approved the *"first past the post"* principle.

Chubb v Moore also provides guidance on 2 other important issues, by stating that:

- section 6 does not apply to claims arising before the inception of the relevant policy

(rejecting the submission of one third party claimant that the previous NSWCA decision of ***The Owners of Strata Plan No. 50530 v Walter Construction Group Ltd (in liquidation) & Ors*** [2007] NSWCA 124 (***Walter Construction***) was wrongly decided); and

- receipt by insurers of letters from the claimants asserting section 6 charges constituted *"actual notice"* of the existence of a charge under section 6 because it provided *"notice of the circumstances that give rise to the charge"*.

Consequences

This decision is good news for insurers and insureds alike, because it is the first Australian authority on the issue and alleviates some of the uncertainty created by the ***Bridgecorp*** decision. Insurers who are paying defence costs and/or settling with the first of multiple claimants with competing charges will welcome the clarification – and the fact that the NSWCA considers that insurers can do so without the risk of paying twice. However, the reasoning of the judgment is not particularly strong and is currently the subject of an application for special leave to the High Court (see below).

As it presently stands, ***Chubb v Moore*** should result in:

- insurers being able to advance defence costs, allowing claims to be properly defended;
- fewer delays in paying claims where there are multiple claimants seeking close to or more than the limit of liability; and
- the end of ad hoc arrangements that were proposed to avoid the risk of double payments by insurers, such as global settlements with every known claimant, payments into Court or stays of execution on judgments, and insureds effectively acting as uninsureds.

The NSWCA's view that section 6 only applies to claims arising after the inception of insurance policies will also significantly limit the number of future section 6 charges.

Finally, the territorial determination that section 6 applies where proceedings are issued in New South Wales at least provides a *"bright light"* test, rather than the tests in previous case law that included a patchwork of multiple territorial triggers for the application of section 6. However, the territorial determination will no doubt increase *"forum shopping"* by claimants who will seek the benefit of section 6 charges (and the correlating right to sue insurers) by bringing proceedings in New South Wales (and potentially the ACT and/or Northern Territory) rather than elsewhere.

However, the NSWCA effectively accepted that its previous judgment in ***Walter Construction*** (which was a predominant basis of its finding as to the effect of section 6) was open to significant criticism, although the NSWCA also considered that ***Walter Construction*** was not so wrong that it was not bound to follow and apply it in this matter.

The third party claimants in ***Chubb v Moore*** have sought special leave to appeal to the High Court. The real danger to insureds and insurers alike is if the High Court:

- similarly criticises ***Walter Construction*** in circumstances where it is not bound to follow that judgment;
- considers that ***Walter Construction*** and ***Chubb v Moore*** do not give sufficient weight to the words *"... all insurance moneys that ... may become payable in respect of that liability"*; and
- adopts the reasoning of Lindgren J in ***FAI v McSweeney***.[8]

Accordingly, we consider that the section 6 ***Bridgecorp*** issue is not as dead as some have asserted. There is an initial question as to whether special leave to appeal the NSWCA decision will be granted in relation to the interpretation and application of a New South Wales statute with no corresponding provision in other states (although similar provisions

8 [1997] 73 FCR 379, which for a long time was the Federal Court's view on the application of section 6 – and was contrary to the NSW Supreme Court's view

occur in the ACT and the Northern Territory).

However, given the importance of the decision, its potential application outside New South Wales (in relation to the New South Wales legislation and corresponding legislation in the ACT and Northern Territory), the High Court could be persuaded to grant special leave. The possibility of leave being granted has since increased, as on 23 December 2013 the New Zealand Supreme Court upheld the original first-instance ***Bridgecorp*** decision.

If special leave is granted, then given the amount of times the NSWCA has been overturned in the High Court in recent years, and the equivocal basis of the NSWCA judgment, we consider that there would be substantial uncertainty in predicting which way the High Court would go. We will closely monitor and advise on the application for special leave and any appeal to the High Court. ■

Federal Court rules that *"dispute splitting"* at FOS is not *"claim splitting"*

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The Financial Ombudsman Service (**FOS**) Terms of Reference specify the maximum financial remedies which may be awarded by FOS *"per claim"*. For disputes involving financial advice lodged between 1 January 2010 and 31 December 2011, the maximum remedy is $150,000 per claim. For disputes lodged on or after 1 January 2012, the maximum remedy is $280,000 per claim. Individuals whose losses exceed these financial caps often argue that their dispute involves *"multiple claims"* and is therefore subject to multiple limits. Unsurprisingly, that position is disputed by Financial Services Providers (**FSPs**) and their insurers.

While FOS has issued guidelines about *"claim splitting"*, its approach has not been subject to judicial consideration until recently, when the Federal Court of Australia considered the issue in ***Wealthsure Pty Ltd v Financial Ombudsman Service Pty Ltd*** [2013] FCA 292 (**Wealthsure**).

The facts

The circumstances of the case are relatively common for financial advice disputes in the post–GFC environment. Between November 2005 and March 2007, Wealthsure's authorised representatives provided investment advice to Mr and Mrs Box. The advice was provided in 3 separate Statements of Advice (**SOA**). The investments recommended in each SOA were based on an assessment of the Box's risk profile that had been undertaken prior to the issue of the first SOA. That assessment was revisited and confirmed prior to issuing each subsequent SOA. The investments lost substantial value and the Boxes lodged a dispute with FOS, alleging that their losses were caused by Wealthsure's deficient advice.

The Boxes argued that, since their losses arose from investments recommended in 3 separate SOAs, their dispute comprised 3 separate *"claims"* and therefore a separate compensation cap of $150,000 applied to each claim. The combined value of the losses claimed exceeded $150,000 but was less than $450,000.

Wealthsure argued the losses arose from the initial assessment of the Box's circumstances in 2005 and any subsequent advice was merely a continuation of any breach of duty that arose from that assessment. Therefore, Wealthsure argued, the dispute comprised a single indivisible claim to which a single cap of $150,000 applied.

FOS determined that the dispute comprised 3

"claims" which were each subject to a separate compensation cap. Wealthsure sought a declaration from the Federal Court that the dispute was a single claim and therefore the maximum amount that could be awarded by FOS was $150,000.

The decision

In reaching his decision, Justice Gilmour of the Federal Court noted that:

- the FOS Terms of Reference make it clear that a *"Dispute"* can comprise more than one *"claim"* with each *"claim"* subject to a separate monetary cap; and
- the FOS Operational Guidelines provide that:

> *"... the expression "Claim" refers to the set of facts that, put together, give an Applicant a right to ask for a remedy. This means a set of separate events or separate facts that lead to the alleged losses. FOS does not aggregate a number of claims into one claim just because the claims all arose from an ongoing relationship between a FSP and an Applicant..."*

After considering the various common law rules in relation to claim splitting (and determining that those rules were not infringed), His Honour held that:

- Wealthsure had a duty under section 945A of the **Corporations Ac 2001 (Cth)** to have a reasonable basis for its advice;
- the duty under s945A arose when each SOA was issued; and
- the duty required Wealthsure to revisit the Box's risk profile before each SOA was issued.

His Honour concluded:

> *"...If there was negligence in the attribution of an inappropriate risk profile at the outset, then the generic error was repeated on two further occasions. That it was an error in each case requires to be adjudged upon the personal circumstances of the Boxes at those different occasions. There would then have been not one but three errors, albeit from the same generic error.*
>
> *That the duty of care or statutory duty might be similar in each instance does not alter the position that the giving of each SoA ... constituted a discrete set of facts that gave the Boxes the right to ask for a remedy which is in the language of a 'claim' as expressed in the Operational Guidelines..."*

It followed that there was no splitting of claims and that the Dispute before FOS comprised 3 separate *"claims"*, each subject to a separate monetary cap.

Implications

FSPs often argue before FOS that where there is an ongoing advice relationship with their client, a single error perpetuated through a series of subsequent SOAs is a single breach of duty, and so it is a single claim subject to a single limit. The Federal Court's decision in ***Wealthsure*** means that argument is now unlikely to be successful before FOS (at least in disputes where the claimant's circumstances do not change over time). With the monetary cap increasing to $280,000 per *"claim"* for financial advice disputes lodged with FOS after 1 January 2012, this is a concern for FSPs and their insurers.

Many FSPs have separate endorsements to their professional indemnity policies that provide discrete terms of cover for FOS matters. In many instances those endorsements, while written with FOS jurisdictional limits in mind, are drafted to limit insurance cover and/or apply deductibles based on a single dispute being a single claim for the purpose of the policy. Insurers and FSPs should carefully review the terms of their professional indemnity policies to determine if the cover for FOS disputes remains appropriate. ■

Striking a balance between legitimate claims and the cost of defending proceedings – granting security for costs against unfunded applicants in class actions

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Introduction

In ***Madgwick v Kelly*** [2013] FCAFC 61 (***Madgwick***), the Full Federal Court awarded security for costs in a class action where the applicants were individuals and not represented by a litigation funder. In awarding security, the Full Federal Court overturned the primary judge's decision in ***Kelly v Willmott Forests Ltd (in liquidation)*** [2012] FCA 1446 (***Kelly***) on the grounds that the applicants had not established that such an order would *"stultify"* the proceedings.

The decision in ***Madgwick*** marks a departure from the Courts' usual reluctance to award security for costs against individual class action applicants who are not represented by a litigation funder.

Background

On 6 September 2010, Australia's troubled agribusiness sector lost yet another participant when the timber group Willmott Forests Ltd (**Willmott**) was placed into liquidation. Willmott joined a long list of recently failed agribusiness managed investment schemes (**MISs**) including Great Southern, Timbercorp, Environinvest and Forestry Enterprises Australia.

In late 2011, Macpherson + Kelly Lawyers (**M+K**) commenced 3 class action proceedings in the Federal Court on behalf of over 400 investors in Willmott.

The 3 proceedings all arose out of investments in MISs based around long-term forestry

plantations in which Willmott and Bioforest Ltd (**Bioforest**), a subsidiary of Willmott, were the responsible entities. The 3 class actions involved:

- an action by an unspecified number of investors pursued in the names of David Kelly, Margaret Kelly and Aaron Grant, against Willmott, Bioforest and 5 former directors of those companies;
- a claim by David and Margaret Kelly against MIS Funding No 1 Pty Ltd (**MIS Funding**) on their own behalf and on behalf of all persons who acquired an interest in the relevant schemes, to set aside loan agreements with MIS Funding for financing the acquisition of the relevant scheme interests; and
- an action against the Commonwealth Bank of Australia (**CBA**) by Aaron Grant on his own behalf and on behalf of all persons who acquired an interest in the relevant schemes, to set aside loan agreements with the CBA for financing the acquisition of the relevant scheme interests.

Security for costs in class actions

In class action proceedings where the applicants are represented by a litigation funder, the Courts have readily awarded security for costs which is paid by the funder.

However, where class action applicants are not represented by litigation funders, the Courts have been reluctant to order security for costs. Consequently, when class action applicants are not represented by a litigation funder and the respondents successfully defend the proceedings, the respondents face the daunting task of recovering millions of dollars in legal costs from the applicants.

Notwithstanding this trend, the respondents in ***Kelly*** applied for security for costs in each of the 3 class actions. In support of their applications, the respondents filed affidavits by lawyers and cost consultants outlining the estimated amount of party-to-party costs that would likely be awarded if the respondents were successful. Those estimates ranged from $7.4 million to $9.2 million.

Relevant legislation and case law

Section 56 of the **Federal Court of Australia Act 1976 (Cth)** (**the Act**) provides the Court with general power to order security for costs.

However, in the context of class actions there is a tension in the rules relating to the granting of security for costs under the Act because:

- section 43(1A) provides that the Court may not award security for costs against represented persons on whose behalf the proceeding has been commenced; and
- section 33ZG(c)(v) provides that nothing in Part IV of the Act (which includes section 43(1A)), can affect the operation of any law in relation to awarding security for costs.

This dichotomy was explored in ***Bray v F Hoffmann-La Roche*** [2003] FCAFC 153 (***Bray***). In ***Bray***, Finkelstein J stated that it would be *"incongruous and anomalous"* to make an order for security under section 33ZG(c)(v) of the Act in light of section 43(1A). Despite this, Finkelstein and Carr JJ held that an order for security for costs did not necessarily involve removing the immunity provided under section 43(1A) of the Act. As a result, security for costs may be awarded in class actions commenced in the Federal Court.

Carr J went on to explain that in determining whether to grant security for costs, the Court must strike a balance between the legitimate claims of applicants and the risks of injustice to the respondents as a result of having little chance of recovering very substantial costs from the applicants if they successfully defend the proceedings.

In ***Hall v Australian Finance Direct Ltd*** [2005] VSC 306 (***Hall***), Hollingworth J summarised the general considerations relevant to exercising the discretion to award security for costs in the context of a class action.

Decision at first instance

In a judgment handed down on 17 December 2012, Murphy J dismissed the applications for security for costs on the basis of the factors outlined in ***Hall***.

A survey provided by M+K demonstrated that:

- 80 per cent of the applicants were *"relevantly impecunious"* as they were unable to cover the proposed costs order; and
- 65 per cent of the applicants were unwilling to be part of the class actions if they had to meet the proposed costs order.

In light of that evidence, Murphy J held that granting the proposed order for security for costs would stifle the action and shut the applicants out from pursuing their claims.

Murphy J further found that:

- the claims made by the applicants had reasonable prospects of success and were *bona fide*;
- the applicants were not deliberately selected as *"persons of straw"* to protect group members with substantial means from paying security for costs;
- no party, including M+K, funded the litigation or stood behind the litigation in the sense that they would gain an additional fee in the event of success; and
- the applicants were natural persons.

Appeal

The respondents appealed and on 14 June 2013 the Full Federal Court reversed Murphy J's decision, ordering security for costs against the unfunded applicants.

In overturning Murphy J's decision, the Full Federal Court took a different view on a number of issues including the relevance of the availability of third-party funding. The Full Federal Court held that in the absence of evidence demonstrating the lengths to which the applicants had gone to secure litigation funding, Murphy J should not have come to the conclusion that the proceedings would be stifled by an order for security for costs.

Crucial to the Full Federal Court's decision, Allsop CJ and Middleton J explained that Murphy J had also failed to undertake the balancing exercise outlined by Carr J in Bray. Their Honours found that Murphy J had not expressly taken into consideration the risk of the respondents being out of pocket by up to $9.2 million if they successfully defended the proceedings.

Implications

The decision in ***Madgwick*** should provide some relief to respondents in class actions in which the applicants are not represented by a litigation funder. In determining whether to award security for costs in class action proceedings, the Courts are reminded to take into account the substantial costs burden imposed on the respondents defending the action.

The decision in ***Madgwick*** has also affirmed the growing importance of litigation funding in class actions. In the absence of evidence outlining the lengths to which applicants have gone to secure funding, the Courts should not readily find that awarding security for costs will stifle proceedings.

Class action terms – ASIC intervenes

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Introduction

In ***ASIC v Richards*** [2013] FCAFC 89, the Full Federal Court considered whether the settlement orders made by the primary judge in ***Richards v Macquarie Bank Ltd (No 4)*** [2013] FCA 438 were fair and reasonable. The Full Federal Court's decision is notable in overturning the primary judge's settlement terms on the basis that they were unreasonable for certain members of the class action. These proceedings were the first time the Australian Securities and Investments Commission (**ASIC**) had intervened in a class action settlement agreed between all the parties and approved by the Court.

Background

Class action proceedings against Macquarie Bank Ltd were commenced on behalf of investors in Storm Financial products. The primary judge made settlement orders distributing the $82.5 million settlement between the class action members, led by Mrs Richards. There were around 1,050 class action members, roughly one-third of whom contributed to funding the litigation. The primary judge's settlement orders ensured that the group members that contributed to funding the litigation would receive approximately 42 per cent of the amount lost on their investments. The remaining two-thirds (being those class action members who did not contribute to funding the litigation), would only recover around 17.6 per cent of their investment losses. The difference in the amounts payable was attributed to a *"funding premium"* of 35 per cent of the settlement pool, which was awarded to the litigation-funding group members.

ASIC appealed the primary judge's decision, and the issue on appeal was whether the distribution between the group members was fair and reasonable.

The decision on appeal

The Full Federal Court unanimously upheld ASIC's appeal to set aside the settlement. The basis of the Full Federal Court's decision was that the members who did not contribute to funding the action had been subjected to an unfair and unreasonable settlement.

There were two aspects of the settlement distribution that the Court considered unfair:

- the non-funding group members lost the opportunity to share the *"funding premium"* on the terms offered to the litigation-funding group members. Essentially, the merits of each of the members were analogous, yet there was a large disparity in the settlement outcome; and
- the calculation of the 35 per

cent premium (by reference to the success fees achieved by the commercial litigation funders) was not based on any rational or mathematical foundation. Furthermore, the possibility of obtaining a premium was not mentioned until around 2 years after the litigation commenced, and those who funded the litigation did so without the prospect of receiving a premium in mind.

Implications

ASIC's intervention to appeal the primary judge's settlement terms was a pivotal move, showing that it will intervene to contest settlements where it considers an outcome for a representative class is unreasonable.

Although the premise of the Full Federal Court's judgment centres on the fairness of the allocation and amount of the *"funding premium"*, this decision does not necessarily prevent members of a class from being awarded a premium if they have contributed to funding the litigation. Rather, the case emphasises that when awarding settlement, the Court must ensure fairness between those who do and those who do not fund the litigation.

This decision will undoubtedly affect the way future class actions are managed and structured. Although it ensures that settlements are made on fair and reasonable terms, this precedent provides an additional hurdle in settling any class action, as the settlement not only has to be agreed by the claimants and the courts, it may also be reviewed by ASIC.■

Class actions and multiple insurance claims

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Introduction

In ***Morgan, in the matter of Brighton Hall Securities Pty Ltd (in liq)*** [2013] FCA 970 (***Brighton Hall***), the Perth Federal Court held that in class action proceedings against a financial services company, each individual plaintiff's claim would be treated as a separate claim for insurance purposes, with each claim attracting a separate claim excess.

The facts

The facts are a somewhat familiar tale: a financial services company provides advice to investors, investors invest, the investment goes bad and the investors sue the financial services company for their loss.

Between late 2001 and late 2005, Brighton Hall Securities (**Brighton**) advised multiple clients to invest in property development schemes developed and marketed by the Westpoint Group of Companies (**Westpoint**). In or around late 2005, Westpoint collapsed. The Brighton clients who had invested in Westpoint made claims against Brighton on the basis that the investment advice they received was negligent or misleading. Two separate class actions were commenced against Brighton, which amalgamated those individual claims (**the class actions**).

The insurance element

Brighton had the benefit of a Professional Indemnity Policy (**the Policy**), which provided cover in respect of the class actions. The Federal Court was asked to decide whether the class actions should be treated as one claim under the Policy, or whether each class action constituted multiple claims.

The Policy relevantly provided that:

> *"…all claims that arise from any one act, error or omission, or series of related acts, errors or omissions, are deemed to constitute one claim."*

The Court's findings

McKerracher J found that each of the class actions constituted groups of multiple individual claims, which would be treated as separate claims under the Policy and would attract a separate excess per claim.

In reaching this decision, his Honour stated that:

> *"...the whole essence of the representative claim is that there are multiple claims before the Court. The character of each claim is not changed by the proceeding which embraces it. The representative proceeding is simply designed to facilitate an efficient and cost-effective way to resolve multiple individual claims..."*

His Honour further stated that, in order to invoke the *"aggregation of claim"* provisions of the Policy, it was not sufficient to simply identify common features of the class action claims. Importantly, his Honour specified that in these circumstances, multiple claims did not arise out of any one act, error or omission because:

> *"...there were different products, different clients, different times of investment, different circumstances of taking advice, different levels of investment and perhaps most importantly, different circumstances and times and amounts of sustaining loss. Without the loss, there can be no course of action in each instance."*

For similar reasons, McKerracher J also found that there was no *"series"* of related claims (which would be deemed to constitute one claim under the Policy). Whilst there was limited commentary on the issue of a *"series"* of claims, it was stated that there could be no series because it was probable that each decision made to recommend the products in question was brought about by different circumstances.

Commentary

The findings in ***Brighton Hall*** bear a strong resemblance to the leading UK case on aggregation, ***Lloyds TSB General Insurance Holdings and Others v Lloyds Bank Group Insurance Company Limited*** [2003] 4 All ER 43 (***Lloyds TSB***), notwithstanding that ***Lloyds TSB*** was not referred to in McKerracher's judgment. In ***Lloyds TSB***, multiple claims had been instigated against Lloyds TSB relating to pensions (superannuation) mis-selling. The House of Lords considered whether for the purposes of the claim under the insurance policy, the claims against Lloyds TSB should be aggregated. The policy in question provided for aggregation of claims that were a *"related series of acts or omissions"*. The House of Lords found that the claims were not aggregated because the policy wording required that a single act or omission be the proximate cause of every claim and this requirement was not fulfilled on the facts. The result was that Lloyds TSB effectively had no cover for the claims against it, as each individual claim fell below the policy deductible.

To date, ***Lloyds TSB*** has not been adopted by the Australian Courts; however, the Federal Court decision in ***Brighton Hall*** is a step towards the position adopted in that case and in particular indicates a willingness of the Australian Courts not to construe aggregation clauses solely against insurers (subject to the particular wording of the aggregation clause).

Implications for insureds

An insured who seeks cover under its insurance policy for multiple claims against it which are connected but arise from different events, may be obliged to pay a separate excess for each of those individual claims, notwithstanding that those claims may be made in a single class action.

The worst-case scenario for an insured is where none of the individual claims exceed the policy excess and the insured is thereby left with little or no effective insurance cover.

Implications for insurers

Although the most obvious implication of ***Brighton Hall*** is its effect on insured parties, there are also 2 potentially significant implications for insurers.

Firstly, for insurers of policies with *"per claim"* limits and automatic reinstatement, exposure for multiple similar claims, such as a class action, may be greater than previously anticipated or intended (depending on the specific policy wording). For instance, where connected claims are treated as single claims under a policy because of an aggregation provision, and that policy allows for automatic reinstatement, an insurer cannot necessarily rely on a policy limit to cap its total exposure to multiple connected claims (because of the reinstatement provisions).

Secondly, aggregation provisions may be interpreted in a way that may be contrary to the insurer's intentions either by providing too few or too many applicable retentions. To avoid this situation, insurers should ensure that claims aggregation provisions are carefully worded so as to accord with the intended coverage.

Summary

Brighton Hall provides an important reminder to insurers and insureds to take particular care when negotiating and drafting aggregation clauses, to ensure the extent of cover received and provided accords with the relevant intent. ■

The only Australian decision in a securities / investors class action – the *Timbercorp* decision

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Introduction

On 10 October 2013 the Victorian Court of Appeal handed down its decision in the important case of ***Woodcroft-Brown v Timbercorp Securities Ltd (in liq) & Ors*** [2013] VSCA 284 (***Timbercorp***), upholding the original decision of Judd J[1], which had dismissed the investor class action against Timbercorp on the basis that:

- the product disclosure statement (**PDS**) allegedly relied on by investors was not misleading or deceptive;
- Timbercorp had complied with its disclosure obligations; and
- the representative plaintiff investors had not established any reliance on the PDS or any alleged failure to disclose.

Background

The original decision was the first in Australia regarding the liability of defendants in a major investors/securities class action. As such, it is an important indicator of the issues that are relevant to a Court's decision in such actions.

The proceedings arose following the April 2009 collapse of the Timbercorp Group, which had offered tax-efficient forestry and horticultural investment schemes and also provided finance for investing in those schemes. At the time of its collapse, Timbercorp had outstanding loans of $477.8 million to over 14,500 investors. McPherson & Kelly solicitors (**M&K**) commenced the proceedings without a litigation funder, on behalf of the lead plaintiff (**Woodcroft-Brown**) and 2,000 group member investors who had invested between 6 February 2007 and 23 April 2009.

The basis of the class action was relevant "*structural risks*"[2] and "*adverse matters*"[3] were not disclosed in the PDS, contrary to section 1013C of the **Corporations Act 2001 (Cth)** (**the Act**) which requires that a PDS include all significant risks and other information that either affects, or would have a material influence on, an investor's decision of whether or not to acquire a financial product. It was alleged that if proper disclosure had occurred, no investments would have been made and no loss would have occurred. It was also alleged that Timbercorp's actions were misleading and deceptive contrary to section 1041 of the Act.

1 [2011] VSC 247.

2 Regarding Timbercorp's ability to maintain sufficient cash flows, including the potential for investors to default on payments and the possible inability to renew funding arrangements.

3 Including an Australian Taxation Office announcement that upfront deductions of application fees for non-forestry schemes would no longer be allowed, together with the general tightening of the global credit markets as a result of the global financial crisis.

Judd J dismissed the class action on the grounds set out in the opening paragraph of this note. The appellant lodged 14 grounds of appeal, the majority of which related to the required content of a PDS and what constitutes a "*significant risk*".[4]

The Appeal Court

While the Court of Appeal judgment is important in determining those 2 issues, namely whether proper disclosure in a PDS has been made and/or whether a PDS is misleading or deceptive – the most important aspect of the decision is the Court of Appeal upholding the original finding on reliance and causation.

As noted above, Judd J held that the representative plaintiff investor had not established any reliance on either the PDS or any alleged failure to disclose the stipulated information. The Court of Appeal confirmed that in order to recover damages on the basis of a defective PDS[5] or for misleading or deceptive conduct[6] a plaintiff:

> *"… must establish that he relied on the misleading or deceptive conduct, or the false or misleading statement or that he would have acted differently if the material omission had been disclosed, in other words, the vice aimed at by the legislation 'is not issuing misleading prospectuses, but misleading investors by issuing misleading prospectuses'."*

The appellant and one Mr Van Hoff were the only investors to give evidence at trial, and provided witness statements that were "*virtually identical and which echoed the allegations in the statement of claim*". The Court of Appeal noted that "*… unsurprisingly, the trial judge ... placed little reliance on this formulaic evidence*". Notably, that evidence was to the effect that the appellant and Mr Van Hoff did not read each PDS carefully or completely. Judd J held that the appellant and Mr Van Hoff were not induced to invest by reason of the PDS; rather, they chose the schemes on the basis of the advice from professional advisors and perhaps in search of tax relief.

The Court of Appeal held that the fact that the appellant and Mr Van Hoff were anxious to obtain tax deductions was relevant to the question of reliance, and that the trial judge did not reach his conclusion on reliance merely because of that desired tax avoidance. Indeed, Judd J relied on all the evidence and that played an important role in determining the issue of reliance.

Notably, both the appellant and Mr Van Hoff retained and relied on financial advisors who identified the tax deduction schemes. The appellant sought to argue that there was indirect reliance on that advice in circumstances where those advisors had presumably read and relied on the PDS in providing their advice. However, the Court of Appeal found that no such argument was raised at trial, and no evidence from any financial advisor was adduced at trial. Accordingly, it considered the submission to be mere speculation. However, the Court of Appeal did not have to comment or consider whether or not it would follow:

- the NSW Court of Appeal decisions that rejected indirect reliance as a form of reliance that could be relied upon by an investor claimant[7]; and/or

4 Notably, a risk that is being successfully managed was held not to be a significant risk, unless there was a likelihood that management would not prevent that risk occurring. It was also held that a risk does not necessarily have to be disclosed if it is otherwise available in a public document.

5 Pursuant to section 1022B (2)1) or section 1041I(1) for a breach of section 1022A regarding a defective PDS.

6 Contrary to section 1041H.

7 ***Digi-Tech (Australia) Ltd v Brand*** [2004] NSWCA 58 and ***Ingot Capital Investments Pty Ltd v Macquarie Equity Capital Markets*** (2008) 73 NSWLR 653.

- the "fair inference" principle.[8]

Accordingly the Court of Appeal dismissed the appeal.

Summary

While the case largely turned on its facts and the manner in which evidence was adduced at trial, it is still a most important judgment, being the only Australian judgment to have dealt with an investor/security class action. One of the most important outstanding issues in such class actions is the extent to which the investor or shareholder has to prove reliance on the alleged wrongful conduct. The Court of Appeal considered this issue, and upheld the importance of the plaintiff establishing such reliance and causation as a prerequisite of a claim for damages.

8 ***Smith v Chadwick*** (1884) 9 APP CAS 187 at 196, to the effect that *"… if it is proved that the defendants, with the view to induce the plaintiff to enter into a contract, made a statement to the plaintiff of such nature as would be likely to induce a person to enter into a contract, and it is proven that the plaintiff did enter into the contract, it is a fair inference of fact that he was induced to do so by the statement".* This principle was accepted by the High Court in ***Gould v Vaggelas*** (1985) HCA85 and was referred to, without criticism, by the full Federal Court in ***De Bortoli Wines Pty Ltd v HH Insurance Limited (in liq)*** [2012] FC 28.

Insurance Year in Review 2013
Reinsurance + Regulatory

Section 562A(4) of the **Corporations Act** revisited: obtaining priority in respect of reinsurance proceeds where the insurer is in liquidation

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Introduction

When an insurer is in liquidation and the liquidator receives reinsurance proceeds under reinsurances that predate the winding up, sections 562A(2) and (3) of the **Corporations Act 2001 (Cth)** (**the Act**) provide for those proceeds to be applied to claims arising from the insurer's liabilities under contracts of insurance written before the winding up commenced.

Although the regime provides recovery options for insurance creditors generally, it can have disadvantageous consequences for an insured in respect of whose claim the reinsurance proceeds were received. Rather than allowing the insured to receive all of the proceeds, the proceeds must be shared between all creditors under contracts of insurance, and these other creditors do not need to establish a link between their insurance contracts and the reinsurance proceeds.

To overcome the hardship this may create, section 562A(4) of the Act enables a creditor under a contract of insurance to apply to the Court for an order varying the effect of subsections (2) and (3) on the basis that to do so would be *"just and equitable"*.

Section 562A(5) sets out the factors the Court may take into account when considering whether to make an order under section 562A(4).

Recent examples of an insured successfully applying for relief under section 562A(4) include a series of cases involving former James Hardie companies and the liquidators of HIH companies: ***Amaca Pty Ltd v McGrath*** [2011] NSWSC 90, ***Amaca Pty Limited v McGrath*** [2012] NSWSC 176 and ***Amaca Pty Ltd v McGrath*** [2012] NSWSC 1523 (***the Amaca cases***).

In ***HIH Casualty & General Insurance Ltd (in liquidation and subject to schemes of arrangement)*** [2013] NSWSC 741; BC20130303049 (12 June 2013, Nicholas J), the Supreme Court of New South Wales distinguished the Amaca cases and was not satisfied that the insured had demonstrated

that it was just and equitable to vary the regime in section 562A(2) and (3).

Facts

Sydney Water Corporation (**SWC**) was the insured pursuant to various contracts of insurance with HIH over a number of years. HIH reinsured the majority of the relevant risks with a number of London reinsurers. On each renewal of the relevant contracts of insurance, there were extensive negotiations between SWC, its broker and HIH, and on the reinsurance side, between HIH and the reinsurers.

SWC made various claims under the policies, including a $14.5 million claim relating to water contamination. Before going into liquidation, HIH made payments of $2.5 million in respect of the contamination claim. SWC's claims were acknowledged in the HIH Schemes for a total of $7.6 million.

The reinsurers made various payments to the liquidators, including under commutation agreements. None of the payments were specifically allocated to SWC's claims. The liquidators made payments to SWC after prorating SWC's claims against other claims HIH owed to other insurance creditors, pursuant to the set-off provisions in the Act.

SWC sought an order under section 562A(4) that the provisions of section 562A(2) and (3) did not apply to moneys received from the reinsurers in respect of specific claims, and that the liquidators pay such moneys to SWC.

Decision

Nicholas J adopted the following reasoning of Barrett J in the first of ***the Amaca cases***, regarding the principles that apply when the Court exercises its discretion under section 562A(4):

> *"In deciding whether an order affecting a particular 'amount received under the contract of reinsurance' should be made, the court must thus focus on the amount itself, the circumstances prevailing at the time the court is asked to make the order and what, in those circumstances, is 'just and equitable' with regard to the application or disposition of the amount. The inquiry is, of its nature, directed to an existing and established factual situation involving the 'amount received'. A necessary factor in the decision as to what is just and equitable – and an element of the 'circumstances' to be taken into account – may be, in some cases, the quantum of the amount."*

On reviewing the evidence, Nicholas J found that:

- SWC had not directly participated in the negotiations for reinsurance;
- unlike in the Amaca cases, there was no support for a suggestion that HIH was merely a conduit to facilitate direct negotiations between SWC and the reinsurers;
- the relationship between SWC and HIH was neither extraordinary nor unusual;
- correspondence established that the reinsurer was not willing to deal directly with SWC in respect of the contamination claims; and
- there was no evidence that SWC was instrumental in procuring the reinsurance cover, that the reinsurer's willingness to reinsure was attributable to the efforts of SWC, or that there was a direct relationship between SWC and the reinsurers.

Comment

In the second of ***the Amaca cases***, the Court found that there was an *"unusually direct relationship"* between the insured and reinsurer. The insured had actively assisted HIH to obtain the reinsurance cover.

The nature of the relationship between insured and reinsurer will be critical in determining whether the Court grants relief under section 562A(4). In the absence of a direct relationship between insured and reinsurer – and the absence of a high level of involvement by the insured in negotiating the reinsurance cover – the insured is unlikely to obtain relief under the section. ■

The reinsurance broker's continuing duty to remit funds

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Introduction

The English Commercial Court in ***Equitas Ltd v Walsham Bros & Co Ltd*** [2013] EWHC 3264 found that the duties Lloyd's reinsurance brokers owed – to remit funds reasonably promptly to reinsureds and reinsurers in contract, restitution and tort – were continuing duties. This had implications for the reinsurance brokers' recourse to a limitation defence.

Background

Equitas is the successor to the Lloyd's syndicates writing non-life insurance business for the 1992 and all prior years of account. This was a result of a settlement agreement entered into in or around September 1996 as part of Lloyd's Reconstruction and Renewal plan which required Equitas to reinsure 100% of the Lloyd's syndicates' liabilities in respect of non-life insurance business for the 1992 and all prior years of account. In return, Equitas was assigned all the syndicates' rights and interests in relation to that business, including any claims the syndicates had against brokers.

Walsham was one of the largest Lloyd's reinsurance brokers.

Equitas' case was that Walsham had received substantial sums, which it ought to have remitted to the syndicates before September 1996 or to Equitas thereafter, and its failure to do so resulted in Equitas' loss of substantial investment income. The total claim amounted to £14.9 million; the majority (£11.8 million) was a claim for lost investment income.

Equitas argued that Walsham had breached its duties – in contract, tort and restitution – to remit these funds reasonably promptly, and that the duties owed were continuing duties. As such, Walsham would be precluded from relying on a limitation defence for breaches more than six years before the commencement of the litigation on 9 September 2011.

Walsham accepted that it had an obligation to remit funds received for the syndicates reasonably promptly, but it did not accept that it had failed to remit the payments to Equitas. Further, Walsham argued that Equitas' claims were time-barred as its duty in contract and restitution (but not tort) was absolute, and accrued once and for all when it failed to remit any funds reasonably promptly.

The decision

The Commercial Court decided several key issues of principle; the most important are set out below.

Nature of duties owed by Lloyd's reinsurance brokers

Males J held that the Lloyd's reinsurance brokers had a duty to:

- collect all premiums reasonably promptly from the reinsured and pay these premiums reasonably promptly to the reinsurers, net of any applicable brokerage (and claim refunds);
- notify the reinsurers reasonably promptly of any potential claims advised by the reinsured, and notify the reinsured reasonably promptly of any questions raised by the reinsurers;
- collect reasonably promptly from the reinsurers all valid claims (and returns of premium), and pay them reasonably promptly to the reinsured; and
- administer the reinsurance contract in a professional and business-like manner – including maintaining and preserving proper and adequate records, and providing the relevant records, or copies thereof, to the reinsured and/or to the reinsurers if requested.

His Honour went on to hold that Walsham's duty in contract and restitution was absolute, and not merely a duty to exercise due diligence. His Honour also found a concurrent duty in tort to exercise reasonable care, provided that such a duty was not excluded by or inconsistent with the contract, as the syndicates had relied on Walsham to administer their reinsurance policies, and Walsham had assumed that responsibility.

Continuing duty and limitation defence

More importantly, Males J held that Walsham's obligation to remit the funds was a continuing obligation, which Walsham breached on the first day those funds ought to have been remitted, with a fresh breach committed each successive day when no remittance was made.

According to his Honour, a determination whether an obligation is continuing is dependent on the relationship between the parties and the nature of the obligation in question.

The *"starting point"*, as Males J put it, is that an obligation to remit funds is likely to require performance once and for all on the due date, and therefore will not be a continuing obligation. However, this will depend on the particular features of the relationship in question.

A combination of features of the relationship between the syndicates and Walsham led Males J to conclude that Walsham's obligation was continuing. First, the parties' relationship was a long-term continuing relationship in which Walsham's role in collecting and remitting funds was central. Second, Walsham was under a continuing obligation to maintain accounts and administer the syndicates' reinsurance policies with knowledge that the syndicates relied on Walsham heavily. Third, Walsham's obligation was essentially to administer the syndicates' accounts in a manner that ensured the syndicates would not be deprived of funds to which they were entitled.

Males J held that the same duties in contract, tort and restitution were owed directly to Equitas, since Equitas' roles as successor to the syndicates was fully understood in the market, and Walsham had, in substance, understood that it was acting as Equitas' broker.

The consequence was that a fresh cause of action accrued each day that Walsham failed to remit the funds. It followed that Equitas' claim for funds that were still not remitted – and for damages for breaches committed 6 years preceding the commencement of the action – were not time-barred, and Walsham had no recourse to the limitation defence in relation to those claims. However, Males J noted that any claim for investment income lost as a result of failing to remit funds at an earlier stage was not necessarily recoverable as a result of this conclusion, and recovery would be dependent on Equitas' success on one or more of its arguments about limitation, which was to be decided at a later stage.

Comment

While this is an interim decision by the English Commercial Court, it nevertheless has a significant impact on claims against reinsurance brokers for failure to promptly remit funds. Reinsurance brokers, including those in Australia, should be aware that they may have a continuing duty to remit funds to reinsureds and reinsurers reasonably promptly, which may affect their ability to invoke a limitation defence.

As such, as a prudent risk management strategy, reinsurance brokers should make sure they have an up-to-date accounting and processing system that efficiently tracks all movements of funds. This would help prevent any unremitted funds being overlooked, especially in times where there is considerable pressure for reinsurance brokers to process claims rapidly. ■

Principles of construction and interpretation: reinsurance contracts

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Introduction

Three recent English decisions – ***Tokio Marine Europe Insurance Ltd v Novae Corporate Underwriting Ltd*** [2013] EWHC 3362 (Comm) (***Tokio***), ***Beazley Underwriting Ltd v Al Ahleia Insurance Co*** [2013] Lloyd's Rep. I.R. 561 (***Beazley***) and ***Amlin Corporate Member Ltd v Oriental Assurance Corp*** [2013] EWHC 2380 (Comm) (***Amlin***) – provide a useful reminder of the principles the Courts apply when construing and interpreting reinsurance contracts.

Key principles

Under English law, the following principles apply when construing and interpreting reinsurance contracts:

- reinsurance contracts are to be construed by adopting the same principles applicable to the construction of commercial contracts;
- the first rule of construction is to consider what a reasonable person having all the background knowledge that would have been available to the parties at the time of contracting would have understood themselves to be agreeing to in using the language in the contract;
- the words must be given their ordinary and natural meaning unless the background indicates that such meaning was not the intended meaning;
- where parties have used unambiguous language, the Court must apply it, however improbable the result;
- if there are two possible constructions of a document or term, the Court is entitled to prefer the construction that is more consistent with *"business"* or *"commercial"* common sense. However:
  - *"commercial common sense"* must not be elevated as an overriding criterion of construction;
  - the parties should not be subjected to the individual judge's own notions of what might have been the sensible solution to the parties'

conundrum; and
- the issue of construction should not be determined by what seems like "*commercial common sense*" from the point of view of one of the parties to the contract.

Back-to-back?

A particular issue that arises in this context is the extent to which a Court can presume that reinsurance or retrocession contracts are intended to operate *"back-to-back"* with the underlying insurance or reinsurance.

Courts have frequently emphasised that reinsurance contracts are separate and independent bargains entered into between different parties, and that they potentially cover different risks. As such, for proportional reinsurance – that is, where the reinsured cedes a share of the risk to the reinsurer – it is presumed that the parties intend the insurance and reinsurance to be back-to-back. On the other hand, for non-proportional reinsurance contracts, there is no presumption that the reinsurance contract is intended to be back-to-back with the underlying insurance contract.

In ***Tokio***, the issue was whether the term *"Loss Occurrence"* in the retrocession contract should be construed in the same manner as *"Occurrence"*, as defined in the Master Policy i.e. back-to-back.

In this case, a Thai subsidiary company of the supermarket chain Tesco had suffered property and business interruption losses amounting to £125 million following severe floods in Thailand in 2011. Tesco and its subsidiaries were insured under an ACE Master Policy for up to £100 million for any one *"Occurrence"*, which was defined as *"any one Occurrence or any series of Occurrences consequent upon or attributable to one source or original cause"*.

ACE was reinsured under a facultative reinsurance policy (**the reinsurance**). Tokio Marine, which had a 12.5 per cent share of the reinsurance, reinsured its share of the reinsurance through a facultative *"excess of loss"* reinsurance policy with Novae (**the retrocession**). The retrocession provided that the sum reinsured was *"£25 million each and every Loss Occurrence in excess of £53 million each and every Loss Occurrence which in turn is excess of Original Policy Deductibles."*

Tokio paid its share of the settlement sum and sought to recover from Novae its 12.5 per cent share of losses in excess of £53 million. Novae denied liability on the basis that the claims that were the subject of the underlying settlement should not be aggregated for the purpose of the *"Loss Occurrence"* deductible in the retrocession.

The key issue was the proper construction of the phrase *"Loss Occurrence"* in the retrocession and whether the term had the same aggregating effect as the term *"Occurrence"*. Tokio argued that it had the same meaning as *"Occurrence"* in the Master Policy. Novae argued that *"Loss Occurrence"* should be given the meaning ordinarily attributed to *"occurrence"* or *"event"* in the insurance context – that is, it is *"something which happens at a particular time, at a particular place, in a particular way"*.

The decision

Hamblen J decided that the term *"Loss Occurrence"* in the retrocession should be construed in the same manner as the term *"Occurrence"* in the Master Policy. In coming to this decision, his Honour applied the ordinary principles of construction to identify the intention of the parties as expressed by the natural and ordinary meaning of the words used, in the context of the commercial purpose of the contract.

As a matter of construction, *"Loss Occurrence"* was held to have the same meaning as *"Occurrence"*. The retrocession was expressly stated to be subject to *"the same terms, clauses and conditions as original"* and expressed to follow the *"Original Policy Wording"*, which was defined by reference to the Master Policy. As such, Hamblen J held that the retrocession was intended to incorporate the Master Policy definition of *"Occurrence"*.

His Honour also considered that it made far more commercial sense for the parties to have adopted a consistent approach, with the result that it could not have been the parties' intention to produce a *"radical mismatch"* in the cover, with the retrocession only covering individual losses while the underlying insurance covered aggregated losses attributable to a single cause. According to his Honour, if the parties had intended otherwise, they would surely have spelled that out expressly, which they did not do.

Claims control clauses

In ***Beazley***, the central issue was the scope and effect of the claims control clause (**CCC**).

The insured had made a claim for losses attributable to a defective crude-oil storage tank. The insurer/reinsured, Al Ahleia (**the reinsured**), then notified its reinsurers – including Beazley and AIG as co-leads, among others. The reinsurance contract contained a CCC stating that compliance with the CCC was a condition precedent to the reinsurers' liability.

The CCC required that:

- the reinsured furnish the reinsurers with all information available regarding losses that might give rise to a claim under the policy – and that the reinsurers had the right to appoint adjusters, assessors or other experts, and to control all negotiations, adjustments and settlements in connection with such loss or losses that might give rise to a claim (subparagraph (b)); and
- no settlement, compromise or liability was to be admitted without the reinsurers' prior approval (subparagraph (c)).

AIG settled its exposure to the underlying claim without the approval of the other reinsurers. The reinsured then sought cover from Beazley and the other reinsurers.

Beazley argued that the reinsured breached the CCC by failing to allow it to control the negotiations with the insured, and by admitting liability for and settling the insured's claim without Beazley's prior approval. In particular, Beazley argued that the wording of subparagraph (c) was *prima facie* unlimited, and that it prohibited any settlement, compromise or admission of liability under the underlying insurance policy without the reinsurers' approval, rather than being subject to the words in subparagraph (b).

The decision

Elder J held that the reinsured had not breached the CCC and was therefore not barred from pursuing its claim against the reinsurers.

His Honour applied the ordinary principles of construction to determine the scope and effect of the CCC. Based on the natural and ordinary meaning of the words, his Honour held that subparagraph (b) allocated a controlling role to reinsurers.

"It will be for the reinsured to say if and when negotiations are about to take place to enable the reinsurers to decide whether to exercise control at that stage. The position will be similar if it becomes apparent that a settlement can be made. This does not mean that there

is any obligation on the reinsured to inform reinsurers of any negotiations or settlement; it just means that if reinsurers do not control negotiations or settlement, then (subject to waiver or estoppels) reinsurers will not be liable."

Elder J held that there were no *"negotiations"* between the reinsured and the insured and, as such, the reinsured had not breached subparagraph (b).

In relation to subparagraph (c), Elder J emphasised that a purely literal construction was not necessarily the correct approach and that it was important to construe subparagraph (c) in the context of the CCC as a whole. Subparagraph (c) was not unlimited, and should be read subject to subparagraph (b). In other words, the reinsurers' approval was only required for any settlement, compromise or admission of liability in respect of loss or losses that might give rise to a claim under the reinsurance contract. Absent very clear words to the contrary, the reinsured was entitled to settle, compromise or admit liability in respect of AIG's share of the reinsurance and the reinsured's own retention, neither of which were settlements in respect of loss or losses that might give rise to a claim under the reinsurance contract.

Typhoon warranty clauses

In ***Amlin***, the issue was the proper construction of a typhoon warranty in a reinsurance contract, which provided cover for loss of or damage to cargo on scheduled vessels.

The relevant warranty provided as follows:

"...it is expressly warranted that the vessel carrying subject shipment shall not sail or put out of sheltered Port when there is a typhoon or storm warning at that port [which we refer to as limb 1] *nor when her destination or intended route may be within the possible path of a typhoon or storm announced at port or* [sic] *sailing, port of destination or any intervening point* [which we refer to as limb 2]."

In this case, before sailing, the captain of the vessel had received a severe weather bulletin and a Grade 1 *"Public Storm Warning Signal"* was hoisted in an area that would affect the vessel. The applicable Coast Guard Circular provided that the ship's owner and/or master had the responsibility and discretion to decide whether to sail when a Grade 1 signal had been given. The captain decided to set sail, and ultimately sailed into the eye of a typhoon with catastrophic results – the vessel capsized and most of the passengers died.

The reinsurers sought a declaration that there had been a breach of warranty and that the reinsurers were therefore not liable under the reinsurance contract.

The decision

The Commercial Court held that the both limbs of the warranty had been breached.

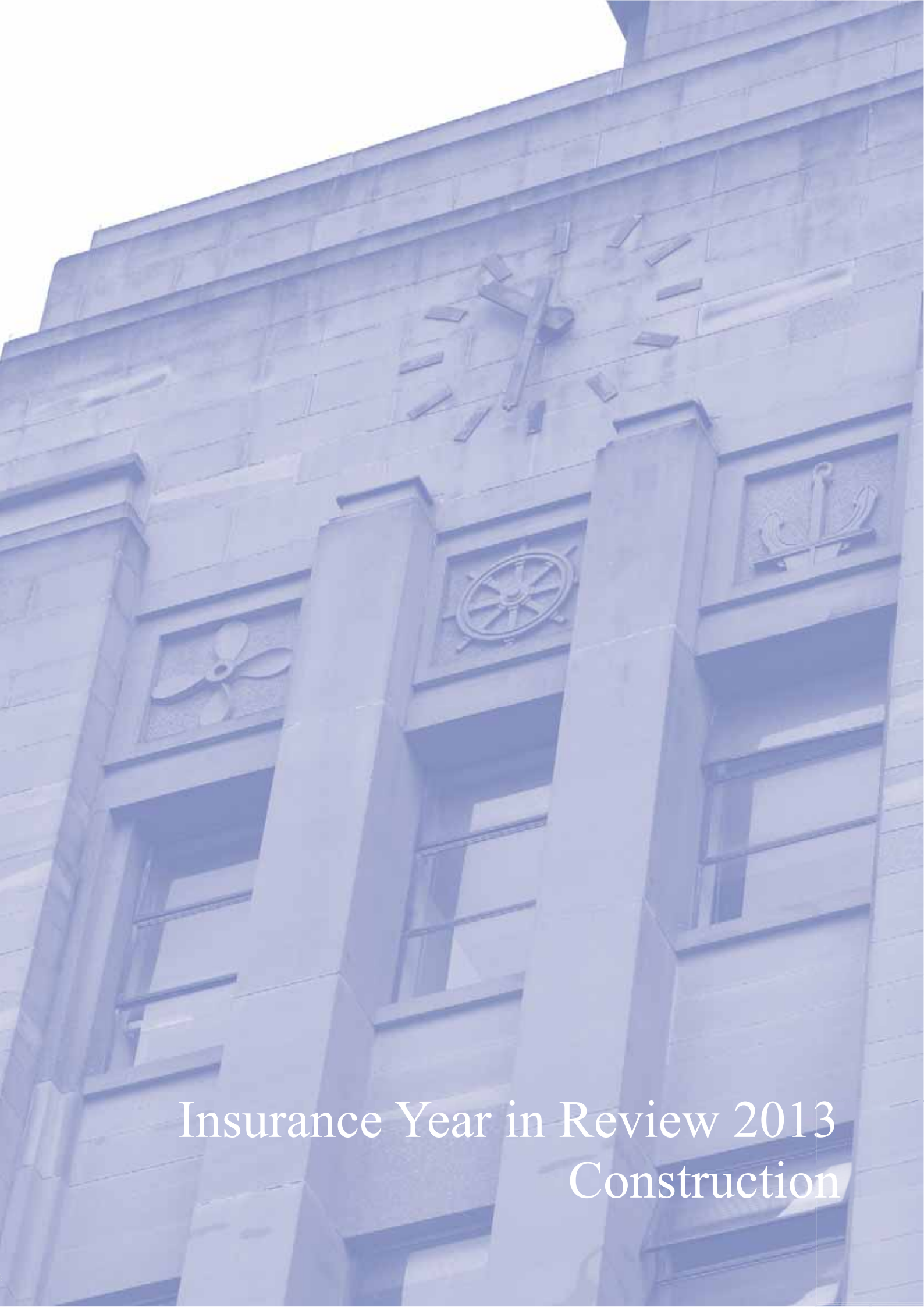
Field J emphasised the ordinary principles of construction in determining the proper construction of the typhoon warranty clause. His Honour held that the manifest object of the warranty was to protect the reinsurers from liability arising from the grave danger of typhoons, which could travel at varying speeds and in directions that could not be reliably predicted. The rationale for the warranty was *"safety first"* and the wording clearly expressed this. As such, the Court preferred the reinsurers' interpretation of the warranty; namely, that if a scheduled vessel sailed from a port while there was a typhoon or storm warning at that port, the warranty was breached. Accordingly, the Court found that limb 1 of the warranty had been breached.

Although it was not necessary to do so, Field J also considered limb 2, concluding that it would be breached if the usual route the captain took was the *"intended route"*. The evidence indicated that the captain had intended to follow the usual route but would have departed from it if the weather became very bad. The Court held that as the policy of the warranty was *"safety first"*, an intended route that could be changed in the event of bad weather was, for the purposes of limb 2, *"the intended route"*. As such, limb 2 had also been breached.

Comments

The English principles of construction applied to reinsurance contracts are not substantially different from those applied in Australia. It is important for Australian reinsureds who reinsure in the London market to be aware of these principles and their potential effect on claims.

At the end of the day, Courts are more likely to prefer the construction that is more consistent with *"business"* or *"commercial"* common sense. As such, it is important for reinsureds and reinsurers alike to ensure that their interests and requirements are set out in clear, simple and unambiguous terms. ■



Insurance Year in Review 2013
Construction

An extension of the duty of care to subsequent owners for defective building works

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Summary

In two decisions of the Supreme Court of NSW delivered in 2012 ***(Owners Corporation Strata Plan No 72535 v Brookfield Australia Investments Limited*** [2012] NSWSC 712 (***The Star of the Sea***) and ***Owners Corporation Strata Plan No 61288 v Brookfield Multiplex Limited*** [2012] NSWSC 1219 (***Chelsea***)) McDougall J considered the duty of care owed by a builder to subsequent owners of a property (specifically a Strata or Owners Corporation) in relation to latent defects.

In both cases, McDougall J held that no general duty of care existed which led to the result that the Owners Corporation in ***The Star of the Sea*** had a remedy against the builder under the **Home Building Act 1989 (NSW)** (**HBA**) but the Owners Corporation in ***Chelsea*** which comprised serviced apartments did not.

The NSW Court of Appeal has now determined the appeal from the decision in ***Chelsea*** and found the existence of a general duty of care extending to pure economic loss provided the principles that must be established to recover such loss are established.

The Supreme Court decision

Chelsea concerned a development of serviced apartments which were designed and constructed by Brookfield Multiplex Limited (**Brookfield**) pursuant to a contract with the developer, Chelsea Apartments Pty Ltd (**the developer**). Latent defects in the common areas were discovered and the Owners Corporation sought redress against Brookfield.

At first instance, McDougall J found that Brookfield did not owe the Owners Corporation a duty of care in circumstances where:

- a detailed contract had been negotiated between Brookfield and the developer to the extent that he found no underlying duty of care owed by Brookfield to Chelsea as the original owner of the development;

- in providing residential owners with statutory warranties under the HBA, Parliament had excluded from its scope serviced apartments and the Court should not impose a duty contrary to legislative policy;
- his Honour was not persuaded of any authority to establish a duty of care in these circumstances and a court of first instance could not establish the existence of a novel category of duty of care.

The Court of Appeal decision

The Court of Appeal decision from the first instance judgment in ***Chelsea*** was delivered on 25 September 2013.

Basten JA conducted a detailed analysis of relevant authorities on the existence of a duty of care for pure economic loss. He concluded that:

- the contract between Brookfield and the developer did not expressly exclude a tortious duty of care and accordingly there was a concurrent tortious duty of care between Brookfield and the developer alongside Brookfield's contractual obligations ;
- McDougall J had placed too much reliance on the terms of the **Home Building Regulation 1997** in force under the HBA when construing the HBA and it was wrong to derive the statutory intention underlying the legislation from delegated legislation ;
- The decision in ***Bryan v Maloney*** (1995) 182 CLR 609 was authority for the existence of a duty of care owed by a builder to a subsequent owner in certain circumstances, subject to an analysis of established principles relating to claims for pure economic loss;
- the Owners Corporation was '*vulnerable*' in the sense that it could establish a duty of care extending to pure economic loss in circumstances where:
  - the development was a significant financial investment to the developer and subsequently the Owners Corporation as subsequent owner of all of the common property;
  - the developer sought to protect itself from the defects complained of by virtue of the contract between it and Brookfield but the Owners Corporation and unit owners were not party to that contract;
  - the Owners Corporation did not exist at the time the building works were carried out and, unlike the developer, had no means of attempting form of self-protection; and
  - the nature of the defects was such that they were not readily identifiable or discoverable by the developer or subsequently the Owners Corporation;
- the duty of care extended to defects in respect of which rectification was reasonably required in order to avoid the possibility of personal injury or damage to property; and
- this was because if personal injury or property damage eventuated, it would give rise to a claim in tort against the builder and therefore recovery for pure economic loss was available on the basis that the work required constituted the cost of steps reasonably necessary to mitigate that risk.

Conclusion

The Court of Appeal decision represents a substantial expansion on the common law duty of care owed by builders. The decision will be of particular concern to professionals in the building industry in that it will likely result in an increase in claims in tort, and concurrent claims in tort and contract, concerning defects in residential and non-residential buildings.

While the effects of the decision may be ameliorated by the potential for contracting parties to expressly exclude tortious duties of care, the application of that duty will be unavoidable unless such contracts are carefully drafted.

An application for special leave is likely, so watch this space.

Will your dispute resolution clause cause a dispute?

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Introduction

In ***WTE Co-Generation & Anor v RCR Energy Pty Ltd & Anor*** [2013] VSC 314, the Victorian Supreme Court considered an application to stay proceedings because of a non-compliance with a contractual dispute resolution clause.

Background

RCR Energy Pty Ltd (**RCR Energy**) was engaged to supply a co-generation facility (a heat and electricity generation plant) that would be fired by paper mill residues. WTE Co-Generation (**WTE**) alleged a breach of the contract and ultimately commenced proceedings against RCR Energy in the Victorian Supreme Court.

Proceedings

In response, RCR Energy filed an application seeking a stay of the proceedings until the parties complied with the dispute resolution clause contained within the contract.

The clause in question provided as follows:

> *"If a difference or dispute (together called a 'dispute') between the parties arises in connection with the subject matter of the contract ... then either party ... shall give the other ... written notice of a dispute ... In the event the parties have not resolved the dispute then* [within a further 7 days] *a senior executive representing each of the parties must meet to* [attempt to resolve the dispute or to agree on the methods of doing so]."

WTE argued that the clause was uncertain and unenforceable, or alternatively that the parties had effectively agreed not to comply with the clause.

Decision

The Court held that a contract may validly include agreements to negotiate and that the question in this case was whether the clause of the contract was sufficiently certain that it required a dispute resolution process to be followed prior to the commencement of proceedings.

The Court stated that, in interpreting dispute resolution clauses, it would endeavour to construe contracts in a manner that would give commercial effect and would uphold the agreement reached by the parties.

The Court summarised a number of principles from recent case law that apply when construing the application of a dispute resolution clause. Of particular note:

- equity will not order specific performance of a dispute resolution clause;
- dispute resolution clauses should be construed robustly to be given commercial effect;
- business people should be bound by contracts entered into using their commercial judgment, even if broad and general, so long as they are sensible and ascribable;
- for the promotion of efficient dispute resolution, dispute resolution clauses should be upheld if the content is enforceable;
- the trend of recent authority is to favour construing resolution clauses so that the clauses work as the parties intended, and are slow to declare provisions void for uncertainty;
- the process for dispute resolution does not need to be overly structured;
- agreements to agree may be incomplete if they lack essential terms; and
- agreements to negotiate will be upheld if the clause has certain content.

In this instance, the Court found that the dispute resolution clause was uncertain because it failed to outline the method for resolving the dispute. The clause was an agreement to agree on the process of the dispute resolution to be employed and was therefore not enforceable.

Implications

Dispute resolution clauses in commercial agreements can play a very important role in preserving contractual relations and avoiding expensive litigation, provided they are enforceable.

This decision demonstrates that courts will broadly construe dispute resolution clauses in commercial agreements. However, if parties want to rely on dispute resolution clauses, they should take care that they sufficiently prescribe the dispute resolution process or method.

How do I make sure my dispute resolution clause is enforceable?

Dispute resolution clauses should clearly outline the process for resolving disputes. This can be achieved by ensuring the clause:

- contains all the relevant terms;
- sets out the dispute resolution method to be employed;
- does not depend on further agreements; and
- leaves no options for different types of dispute resolution unless there is a method to determine which process is to be used. ■

Perpetual issues in construction: proportionate liability

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Introduction

Section 3A(2) of the **Civil Liability Act 2002 (NSW)** (**CLA**) provides that, with the exception of Part 2 (which deals with damages for personal injury), parties to a contract are not prevented from *"making express provision for their rights, obligations and liabilities under the contract with respect to any matter to which this Act applies and does not limit or otherwise affect the operation of any such express provision"*.

Although it has been considerably qualified since the 19th century, the doctrine of freedom of contract remains central to contract law. That doctrine embodies the notion that individuals should be free to choose with whom and on what terms they contract. Section 3A(2) of the CLA preserves that freedom by providing that parties to a contract may exclude the operation of the proportionate liability regime in Part 4 of the CLA from the determination of their liabilities under contract.

In the recent decision of ***Perpetual Trustee Company Ltd v CTC Group Pty Ltd (No 2)*** [2013] NSWCA 58 (***Perpetual (No 2)***), the doctrine of freedom of contract and section 3A of the CLA were both in issue in a way that has direct implications for an insured under a policy that contains a clause excluding liability assumed under contract.

Facts

In the earlier decision of ***Perpetual Trustee Co Ltd v CTC Group Pty Ltd*** [2012] NSWCA 252, CTC Group Pty Ltd (**CTC**), a mortgage originator, was found to have breached its obligations under a mortgage origination deed (**MOD**) to Perpetual Trustee Company Ltd (**PTC**), the mortgagee under loans arranged by CTC. Later, CTC sought to argue that its liability to PTC was limited by the operation of the proportionate liability regime under Part 4 of the CLA. Had that argument been accepted, CTC's liability would have been limited to its contribution to PTC's loss which would have forced PTC to sue other tortfeasors where CTC's liability did not provide PTC full redress for its loss.

PTC resisted CTC's submission by arguing that a contractual indemnity in the MOD made provision for the rights and liabilities of PTC and CTC in a manner that was inconsistent with incorporation of the proportionate liability regime into the MOD.

The indemnity in the MOD provided that CTC agreed to indemnify PTC *"against any liability or loss arising from and any costs, charges and expenses incurred in connection with ... (d) any breach by* [CTC] *of any of its warranties or obligations under or arising from this deed or failure to perform any obligation under this deed"*.

One of the warranties that PTC alleged CTC to have breached under the MOD was that CTC would exercise reasonable care to identify borrowers and to ensure it had authorised the making of applications submitted by CTC to PTC's agent.

Decision

Macfarlan JA (with whom Meagher and Barrett JJA agreed) considered that if the proportionate liability regime limited CTC's liability to PTC as CTC contended, CTC's liability would have been so limited as to deprive PTC of its contractual right to a full indemnity for its loss. As it was clear that the contractual indemnity in the MOD made express provision with respect to a matter covered by the proportionate liability regime and was inconsistent with that regime's operation, it followed that the regime did not apply to PTC's claim for indemnity under the MOD.

The Court of Appeal's decision is consistent with the earlier decision in ***Aquagenics Pty Ltd v Break O'Day Council*** [2010] TASFC 3. There, the Full Court of the Supreme Court of Tasmania observed in relation to an identical provision to section 3A in the Tasmanian **Civil Liability Act (2002)** that the fact that a concurrent wrongdoer might emerge who is not a party to the contract between the principal and a contractor does not mean that the contractor can limit its liability to the principal pursuant to the proportionate liability regime. The plain purpose of section 3A of the Tasmanian Act was to *"ensure the primacy of express provisions of a contract as to the parties' rights, obligations and liabilities under the contract over any provision in relation to the same matter in the Act"*.

Conclusion

As the decision in ***Perpetual (No 2)*** shows, where an insured enters a contract containing terms that operate inconsistently with the operation of the proportionate liability regime, the insured may be found to have contracted out of the operation of that regime. That will be so irrespective of the insured's subjective intention that the proportionate liability regime would apply to the contract.

Where that occurs, an insured cannot subsequently assert that they did not intend that to be the effect of the contractual term. Under Australian law, parties are generally free to contract on whatever terms they like and their contractual intentions will be construed from the terms of the contract rather than from what they say their intentions were afterwards.

For that reason, insureds need to be alive to the potential effect on their insurance cover of provisions in construction or consultancy contracts to which they are a party. Where an insured assumes a liability under a contract, the effect may be to exclude the proportionate liability regime and put the insured in breach of the standard provision in a liability policy which excludes cover for a liability assumed under contract. If an insured is unsure as to whether a contract into which it has entered has that effect, they should seek legal advice. ■

Construction contracts and the **Personal Property Securities Act** – the importance of registering

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Introduction

The **Personal Property Securities Act 2009 (Cth)** (**PPSA**), now 2 years into operation, represented a substantial shift in the way businesses need to treat contracts that might give rise to rights of security over personal property.

A recent case from New Zealand, where very similar legislation has been in force for more than a decade, demonstrates the care needed to ensure that a security interest is properly registered.

Facts

In ***McCloy v Manukau Institute of Technology*** [2013] NZHC 936, the New Zealand High Court dealt with the issue of competing priorities where a construction contract was said to create a security interest by way of a *"step in"* right, but had not been registered.

Mainzeal Property & Construction Limited (**Mainzeal**) entered into a construction contract (**the contract**) with Body Corporate 177519 (**the body corporate**) to carry out remedial construction works. The contract contained a standard form of wording that, relevantly, included the right for the body corporate to terminate the contract if Mainzeal went into receivership and the receiver failed to take over the contract.

Importantly, clause 16 of the contract also provided that if the body corporate terminated the contract due to the receivership of Mainzeal, and where the receiver did not assume conduct of the works:

- the body corporate would be deemed to be in possession of the works;
- Mainzeal's interest in the onsite works, materials, fittings and machinery would be transferred to the body corporate; and
- the body corporate was entitled to complete the works (using the materials, fittings and machinery); recover reasonable costs from Mainzeal; and sell any surplus materials or fittings and its interests in the machinery to satisfy any claims it had against Mainzeal.

Mainzeal went into receivership before the works were completed and the receiver did not step in to complete the works.

The contract between the body corporate and Mainzeal was not registered as a security interest under the **Personal Property Securities Act 1999 (NZ)**, the New Zealand equivalent of the PPSA.

A dispute arose between the body corporate and the receiver (appointed by Mainzeal's banker, Bank of New Zealand (**BNZ**), which had the benefit of a registered security agreement securing Mainzeal's borrowings) as to which entity had priority to take possession of and sell the hoists Mainzeal had used for the works.

The decision

Collins J found that the rights afforded to the body corporate under clause 16 of the contract constituted a security interest for the purposes of the New Zealand Act, in that it was *"a transaction that in substance secures payment or performance of* [Mainzeal's] *obligations"*. This is the same language used to define a *"security interest"* under section 12 of the PPSA.

Having found that the terms of clause 16 constituted a security interest, and one that was not registered, it followed that the body corporate's interest in the disputed hoists must stand behind that of BNZ, which had an earlier security interest perfected by registration.

The Court made further findings that – given the rules of priority under the New Zealand legislation, which are mirrored in Part 2.6 of the PPSA – even if the body corporate had perfected its security by registering the contract, BNZ's earlier security would have prevailed, being earlier in time.

Implications

"Step in" or *"take out"* clauses or *"retention of title"* provisions that are used to secure the performance of obligations are a common feature of construction contracts.

The Court's decision in ***McCloy v Manukau Institute of Technology*** was later reinforced by the decision of the New South Wales Supreme Court in ***Maiden Civil (P&E) Pty Ltd (In Liquidation) v Queensland Excavation Service Pty Ltd*** [2013] NSWSC 852. In that case, the Court held that the rights of an owner of excavators were subordinated to the interests of the financier because the financier had registered its security interest created by the finance lease, and the owner had not registered its ownership interest.

Although it is now 2 years old, the PPSA still seems to be a relatively *"novel"* concept to many construction businesses. Nevertheless, the decision of the New Zealand High Court is a timely reminder that care needs to be taken when negotiating contracts, to ensure that anything falling within the scope of the PPSA is registered to properly secure the relevant party's interest.

It is important for all businesses, and in particular those in the construction industry, to recognise and register their security interests. A failure to register in time – or at all – may result in others getting in first when it comes to competing priorities.

The Victorian Building Authority – new authority, new power, new impacts on construction litigation

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Overview

On 1 July 2013, the Victorian Building Authority (**VBA**) commenced work as the new integrated regulator of the plumbing and building industries, replacing the Building and Plumbing Industry Commissions. The VBA is also earmarked to regulate architects.

At a recent presentation to the Building Dispute Practitioners Society (**BDPS**), the Honourable Attorney-General, Robert Clark MP, outlined the role of the VBA in the context of the Government's Domestic Building Consumer Protection Reform Strategy (**the strategy**). The changes to be implemented as a part of the strategy include enhancing dispute resolution processes, broadening the scope of domestic building insurance and strengthening the regulation of registered builders.

The strategy and its reforms will be implemented progressively throughout 2013 and 2014, with the effect of:

- expanding the scope of domestic building insurance;
- improving domestic building practitioner registration and re-registration standards;
- expanding the scope of regulation to include corporations and partnerships;
- expanding the disciplinary powers of the regulator;
- improving oversight of building surveyors and the building permit system;
- providing greater access to information for consumers in relation to building practitioners and their associated disciplinary history; and
- enabling the VBA to issue rectification orders where a VBA inspector assesses building work as defective or incomplete.

Arguably these changes represent the

most significant changes in 10 years in the building industry. Of particular interest is the VBA's power to issue rectification orders, and the proposed changes to domestic building insurance.

VBA rectification orders

The VBA will provide a conciliation service; if a resolution cannot be reached, consumers will be able to seek a binding rectification order from the VBA. A rectification order will be issued if a VBA inspector determines that the works are defective or incomplete.

Currently, an inspector has the power to prepare a report outlining the defects in a building with recommendations for rectification. However, they cannot make a binding rectification order.

An inspector will also be able to make orders in relation to building standards or contractual requirements. This is qualified in circumstances where the inspector believes that the issues require an assessment beyond the inspector's skill and competence. If this occurs, the inspector may issue a determination in relation to those aspects within their skill and expertise, and the remaining aspects of the dispute may be heard by the Victorian Civil and Administrative Tribunal (**VCAT**).

A rectification order can include an order for a consumer to make outstanding payments to a builder in the event that an allegation of defective work is not upheld, or does not justify the moneys being withheld.

If a builder fails to comply with a rectification order, they may receive *"demerit points"*, partial suspension or other sanctions. The partial suspension system should create significant incentive for builders to comply with a rectification order because they will be unable to enter into new contracts or works until they comply with the rectification order. Partially suspended builders will be able to continue working under existing contracts.

Builders will be able to appeal a rectification order to the VCAT. Interestingly, the VBA will not be the named party in the appeal; rather, it will be the consumer. The VCAT will have the power to order costs against a party that unjustifiably seeks a review of a rectification order – namely, if a party appeals a rectification order to the VCAT and does not achieve a better result than the original order.

Domestic building insurance

Currently, domestic building insurance in Victoria is triggered when the builder becomes insolvent, dies or disappears.

The previous Victorian Government released figures noting that in the 2010/11 financial year, more than 53,000 Victorians paid approximately $87.8 million in builders warranty insurance premiums. A total of 3 claims were paid, totalling $108,476.

The strategy proposes broadening the circumstances that will trigger builders warranty insurance to include those where a project is incomplete or there is a defect and:

- the builder or building entity has died or disappeared, or is insolvent;
- the VBA has certified that a rectification order has not been complied with or that order has been successfully appealed to the VCAT, and the building contract has been completed (with the exception of an incomplete rectification order) or terminated;
- the builder or building entity has been partially suspended, suspended or deregistered and cannot complete the project; or
- the builder is certified as permanently and significantly incapacitated and no substitute arrangements are available.

Further, the maximum benefit amount will increase from $200,000 to $300,000. Claims for non-completion of building work will still be limited to 20% of the original contract amount.

Comment

These changes are expected to result in increased premiums. However, the trade-off may be that successful claims against builders will reduce the current pressure placed on associated building practitioners – such as engineers and surveyors – where recoveries against builders traditionally haven't been available. ■

Victorian security of payment legislation – clarification of the issue of "*excluded amounts*"

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Synopsis

The decision of Justice Vickery in ***Maxstra Constructions Pty Ltd v Joseph Gilbert & Ors*** [2013] VSC 243 provides clarification on a perceived incompatibility between 2 sections of the **Building and Construction Industry Security of Payment Act 2002 (Vic)** (**the Act**) that outline the matters that can be taken into account when adjudicating a payment claim under the Act.

In doing so, Justice Vickery relied on the distinction between the common law concepts associated with *"claims for damages"* and the statutory concept of the "*estimated cost of rectification*" of a defect.

Background

The case arose out of the construction of a service station in Echuca, Victoria (**the project**). Maxstra, the head contractor undertaking the construction works, subcontracted the concreting works for the project to Joseph Gilbert (**Gilbert**).

During the project, Gilbert served Maxstra with a payment claim under the Act, seeking payment of $259,954.62 (**the payment claim**). Maxstra disputed the amount claimed and sought to set off various amounts, including amounts associated with completing certain items and rectifying damage. Maxstra also sought to set off an amount for "delay costs".

After taking these matters into account, Maxstra's payment schedule had the practical effect of not only refusing to make any payment to Gilbert, but actually seeking payment from Gilbert of $164,590.43.

Gilbert predictably took issue with Maxstra's assessment of the claim and referred the matter to adjudication pursuant to section 18 of the Act.

Adjudication

On adjudication, Maxstra asserted that it was entitled to set off $400,000 against Gilbert's payment claim on the basis that this was its estimated cost of rectifying defects (**the defect rectification costs**).

The adjudicator ultimately found that Maxstra was required to pay Gilbert $270,491.47 after concluding that the set-off claimed by Maxstra for defect rectification costs was, in fact, a claim for damages for breach of contract and was an item that, under the Act, the adjudicator was not entitled to consider in making its assessment. The adjudicator reached this conclusion after determining that the defect rectification costs were an *"excluded amount"* under the Act and on that basis, could not be taken into consideration.

Judicial review

The central issue in the proceeding for judicial

review was whether the adjudicator was correct in refusing to take into account the defect rectification costs when making its assessment on the basis that it was precluded from doing so under the Act.

The concept of *"excluded amounts"* is discussed in section 10B of the Act and includes at 10B(c) *"any amount claimed for damages for breach of the construction contract or for any other claim for damages arising under or in connection with the contracts"*.

On one view, this appears to present an inconsistency with section 11(1)(b)(iv) of the Act, which requires that regard should be had to whether any of the relevant work is defective and, if it is, the estimated cost of rectifying the defect.

Purpose of the Act

Vickery J provided a useful discussion of the objects and guiding principles of the Act, emphasising that it was aimed at enabling timely adjudication of payment claims. In particular, citing ***Hickory Developments Pty Ltd v Schiavello*** [2009] 26 VR 112 at 121, his Honour noted that the Act intended to:

- give *"full effect"* to the principal that a respondent to a payment claim for a progress payment *"should pay now and argue later"*; and
- *"demonstrate a pragmatic concern to provide a dispute resolution process which is not bedevilled with unnecessary technicality"*.

Inconsistency?

Vickery J found it unnecessary to resolve any apparent conflict between these provisions, instead applying a close examination of their text. In assessing the provision dealing with *"excluded amounts"*, his Honour found that *"the fulcrum of the provision"* was its reference to a *"claim for damages"*. His Honour noted that:

- the concept of *"damages"* has a particular meaning at law where there is a failure to discharge a contractual obligation;
- various principles apply in relation to damages resulting from the breach of a construction contract; and
- commonly, damages are rewarded arising from a breach of contractual warranty of *"good workmanship"*. This might include consequential losses – for example, those arising from delay in contract completion and losses from liabilities incurred to third parties arising from such delay.

In contrast, Vickery J held that section 11(1)(b)(iv) of the Act was of a different character, being a purely statutory concept, which provided that in the event of any work being defective, the estimated cost of rectifying the defect was to be taken into account in valuing the construction of the work.

This statutory concept differed from a *"claim for damages"*, because under section 11 it was only necessary that the *"cost of rectifying the defect"* be taken into account.

This only required the adjudicator to estimate the defect rectification costs. This was not the same as requiring an adjudicator to assess damages, as assessing damages does not require a mere estimate, but rather requires a claimant to prove its case to the usual civil standard, on the balance of probabilities, and on the admissible evidence adduced.

In reaching this conclusion, Vickery J noted that this approach was consistent with the approach taken to the equivalent statutory regime in New South Wales.

Ultimate decision

Vickery J ultimately found that the adjudicator had failed to take into account the defect rectification costs, which it was required to do, and remitted the matter for adjudication. ■

Insurance Year in Review 2013
Property / Industrial Special Risks

Payment of indemnity value – before or after reinstatement?

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Introduction

In ***TJK (NZ) Limited v Mitsui Sumitomo Insurance Company Limited*** [2013] NZHC 298, Miller J of the High Court of New Zealand considered the effect of an optional extension providing for reinstatement in the event of earthquake damage. The question before the Court was whether the insurer must pay the indemnity value before the insured incurs the cost of reinstatement.

Background

TJK (NSW) Limited (**TJK**) was the owner of an office building in Christchurch, which was damaged by two earthquakes in September 2010 and February 2011. The local earthquake authority pronounced the building dangerous and commissioned its demolition.

Under the material damage section of the insurance policy (**the policy**), TJK had selected an optional earthquake damage extension. This extension provided that the insurer would pay the cost of reinstating the building if TJK elected to pursue reinstatement. TJK had elected, but had not yet incurred, the cost of reinstatement. The cost of reinstatement would far exceed the building's lost market value following the earthquakes.

TJK argued that the insurer should pay the indemnity value before the reinstatement works. The insurer conceded that it was required to pay the indemnity value, but only after TJK incurred the cost of reinstatement. Both parties agreed that the building's lost market value following the earthquakes represented the least measure of the building's indemnity value.

TJK sought declaratory relief that the insurer was obliged to pay at least the indemnity value, regardless of whether TJK had incurred the cost of reinstatement.

The policy

The general indemnity clause in the policy provided that:

"We will indemnify you for damage to any of the insured property occurring during the period of insurance. You will be indemnified by payment or, at our option, by repair or by replacement of the lost or damaged property. Subject to the reinstatement of amount of insurance extension our liability will not exceed the total sum insured; or where more than one item is included in the schedule will not exceed in respect of each item the sum insured applicable to that item."

The policy also contained the following reinstatement clause:

"[The Insurer] *will pay the cost of reinstatement in the event of any insured property to which this extension applies suffering earthquake damage ... during the period of insurance."*

The reinstatement clause included the following special condition, which set out the circumstances in which the insurer would not pay the full reinstatement sum:

"No payment of more than the indemnity value will be made under this extension:

> *a) If the work of reinstatement is not commenced and carried out with reasonable despatch;*
> *b) Until the cost of reinstatement has been actually incurred; or*
> *c) If the property is damaged, but not destroyed, and the repair of the damage is not permissible by reason of any regulations or by any reason of the condition of the undamaged proportion of the property."*

The insurer argued that the obligation to pay the indemnity value arose only where TJK elected not to reinstate. Miller J was not convinced by this argument and found that the earthquake damage extension incorporated the general indemnity clause, to the extent that the latter is consistent with the former.

Furthermore, the wording of the policy distinguished between indemnity value and reinstatement cost, and contemplated that the insurer might have to pay indemnity value before TJK actually incurred the reinstatement cost. Having been paid the indemnity value, TJK would then credit repair or rebuilding costs against the indemnity value sum as and when incurred, making further claims for reimbursement once those costs exceeded the indemnity value.

The authorities

Miller J then turned to a number of Australian and international authorities where Courts had held that the indemnity value was payable before the insured incurred the cost of reinstatement. The authorities identified this obligation in the general indemnity clause.

The finding

Miller J concluded that ultimately the question of whether the indemnity value was payable before or after an insured had incurred the cost of reinstatement was guided by the terms of a particular policy. Although the overseas authorities fell short of establishing a rule of law, the similar wordings in local and overseas industrial special risks policies made the authorities highly persuasive.

On that basis, Miller J found that – subject to proof of loss and credit for sums already paid – the insurer was liable to pay TJK not less than the indemnity value of the building.

Conclusion

This decision provides support for the Australian authorities on this point, and encourages consistent interpretation across standard-form industrial special risks policies. The decision falls short of finding a rule that insurers are liable to pay indemnity value before reinstatement costs are incurred; ultimately that question still depends on the wording of each policy. ■

A *"wild"* decision seeks to clarify automatic reinstatement clauses and deductibles

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The Christchurch earthquakes in 2010 and 2011 raised a myriad of insurance issues. On 23 October 2013, the New Zealand High Court in ***Wild South Holdings Ltd & Maxims Fashion Ltd v QBE Insurance (International) Ltd*** [2013] NZHC 2781 sought to offer some clarity around the application of automatic reinstatement clauses and deductibles.

Background

Wild South Holdings Ltd (**Wild South**) and Maxims Fashion Ltd (**Maxims**) each owned a commercial building in Christchurch. The buildings were insured under separate but similar insurance policies issued by QBE Insurance Ltd (**QBE**). Both buildings were deliberately underinsured.

Following the Christchurch earthquakes on 4 September 2010, 22 February 2011 and 13 June 2011, Wild South and Maxims each claimed the sum insured and the automatic reinstatement cover. QBE accepted that the policies responded to the damage caused by the earthquakes, but disputed the application of the automatic reinstatement clause and the deductible.

Wild South and Maxims commenced separate proceedings against QBE. The proceedings were heard together and the parties agreed for several preliminary questions to be answered by the Court including:

- what is the proper interpretation and application of the automatic reinstatement clauses? (**Question 1**); and
- what is the proper application of the deductible? (**Question 2**)

The decision

Question 1

The automatic reinstatement clause in Wild South's policy provided that:

"... in the absence of written notice by QBE or the Insured to the contrary, the amount of insurance cancelled by loss will be automatically reinstated from the date of loss..."

The automatic reinstatement clause in Maxims' policy provided:

> *"... In the absence of written notice by the Insurers or the Insured to the contrary, the amount of insurance cancelled by loss or damage is automatically reinstated as from the date of loss or damage ..."*

Wild South and Maxims argued that QBE was not allowed to give notice that the limit was not reinstated. QBE maintained that it was entitled to give notice up until payment of the claim.

Fogarty J held that QBE was permitted to give written notice that the limit was not reinstated, but that notice had to be given within a reasonable period of time. Fogarty J explained that shortly after the Christchurch earthquakes, QBE and the insureds must have entered into discussions which would have resulted in QBE considering the ramifications of failing to give notice regarding automatic reinstatement. Having reached that conclusion, Fogarty J held that it was not reasonable for QBE to wait until the claim was paid before giving notice to the insureds.

Question 2

Question 2 essentially boiled down to whether the deductible should be subtracted from the loss or the sum insured limit. The relevant provision in Wild South's policy was as follows:

> *"Each Event will be adjusted separately. The adjusted loss will be net of salvage and other recoveries. From each adjusted loss the amount stated in Schedule A will be deducted."*

Wild South and Maxims relied on the decision of ***Australian Consolidated Press Holdings Pty Ltd v Royal Insurance (Global) & Ors*** (1997) 9 ANZ Ins Cas 61–351 (***ACP***) as authority that a deductible is to be taken off the total loss, to which the sum insured limit is then applied. The Court in ***ACP*** reached that conclusion because the policy did not state that the sum insured (that is, the maximum amount the insurer is obliged to pay) was subject to a deductible. Fogarty J considered that he was unable to rely on ***ACP*** because the terms of the policies were significantly different.

QBE argued that because the deductible is to be subtracted from *"each adjusted loss"* and the *"adjusted loss"* is the amount assessed as payable as a result of *"Each Event ...* [having been] *adjusted separately"*, it follows that the deductible is the last step in the adjustment process.

Fogarty J agreed with QBE, concluding that it did not make commercial sense to have the deductible subtracted from an amount that was larger than what the insurer had agreed to pay. His Honour's conclusion was heavily influenced by a clause in the policy stating that the sublimits were *"understood to be in excess of the relevant Deductibles"*. In His Honour's view, that clause confirmed the intent that the deductible was to be subtracted from the adjusted loss payable by the insurer to the insured.

Implications

This case should be a reminder for insurers to provide written notice against automatic reinstatement within a reasonable period of time. What is reasonable notice will depend on the circumstances of each case. However, waiting until the completion of the loss adjustment process and payment of the claim before giving notice is not likely to be deemed reasonable and may result

in automatic reinstatement of cover.

The decision regarding the application of the deductible was heavily influenced by the precise words used in the policies. Therefore its authoritative value (beyond policies with the same or similar wording) is unlikely to be significant and parties should carefully consider the wording of each policy to determine how deductibles should be applied.

Interpreting the policy – individual provisions or the policy as a whole?

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The New South Wales Court of Appeal decision in ***Australian Rail Track Corporation Limited v QBE Insurance (Europe) Limited*** [2013] NSWCA 175 highlights the importance of construing the provisions of a policy as a whole rather than each provision in isolation. The Court found that a claim for indemnity was subject to a large excess even when there was no excess prescribed in the policy in respect of the insured making the claim.

Background

Australian Rail Track Corporation Limited (**ARTC**) managed the New South Wales rail network known as the Country Regional Network (**the network**) under an agreement with State Rail Authority of New South Wales (**SRA**) and Country Rail Infrastructure Authority (**CRIA**). Under the agreement, SRA and CRIA were required to arrange third-party liability insurance. A policy of liability insurance was issued in respect of claims arising out of or in connection with the agreement (**the policy**). SRA, CRIA and ARTC were all insured entities under the policy.

ARTC brought 2 claims for indemnity under the policy as a result of property damage arising from a derailment, and a personal injury claim following injury to a worker during maintenance works on the network. The insurers accepted both claims but maintained that cover was subject to the application of a self-insured excess provision (in General Condition 1 and Item 6 of the Schedule to the policy).

ARTC sought a declaration that the self-insured excess provision did not apply to its claims for indemnity. The primary judge (Stevenson J) refused to make the declaration. ARTC appealed.

The policy

General Condition 1 of the policy provided:

> ***"Self-Insured Excess***
>
> *Insurers shall only be liable for that part of any one Occurrence/claim or series of such Occurrences/claims arising out of any one originating cause under this Policy, including Defence Costs, which exceeds the amount of the Self-Insured Excess (including Defence Costs) stated in Item 6 of the Schedule."*

Item 6 of the Schedule to the policy specified the excess to be applied depending on whether a claim or occurrence was *"in respect of"* Rail Corporation New South Wales, CRIA, SRA or Constructions (clearways) activities. No excess was specified in respect of ARTC.

ARTC submitted that its claims for indemnity were not subject to any excess since General Condition 1 provided that the self-insured excess was as stated in Item 6 of the Schedule and ARTC was not listed among the entities in Item 6.

The Court's interpretation of the policy General Condition 1 provided that insurers could be liable only for the *"part of"* any one occurrence or claim that exceeded the self-insured excess. The Court of Appeal held that the words *"part of"* meant that an excess must apply. An excess would therefore apply to any claim made by any named insured under the policy.

The excess was to be determined by reference to the wording in Item 6 of the Schedule to the policy. The Court found that Item 6 did not stipulate the excess for the entities as named because the words *"in respect of"* in Item 6 were not intended to identify the parties to bear the excess. Rather, the relevant excess was to be determined by reference to whether the relevant occurrence or claim was *"in respect of"* the named entities.

The Court considered that the excess that applied to a particular claim did not depend on a third party's decision to sue one particular insured. Rather, it depended on the named insured or the business activity in Item 6 with the closest connection to the relevant occurrence. This required an inquiry into the nature of the event and the circumstances in which that event occurred, to determine which named insured or which described business activity in Item 6 had the closest connection with the subject of the indemnity claim.

In this case, the Court found that ARTC's entitlement to cover under the policy arose only with respect to its liabilities in connection with the network, and its agreement with SRA and CRIA. Accordingly, any claim made by ARTC under the policy was *"in respect of"* either SRA or CRIA.

The Court concluded that both of the claims against ARTC were connected to CRIA because CRIA owned and operated the tracks, and neither incident had anything to do with the other insured entities in Item 6. As a result, a $2.5 million excess applied in respect of each claim of ARTC's claims for indemnity. The Court interpreted the words:

- *"part of"* in General Condition 1 to mean that any claim under the policy was subject to an excess; and
- *"in respect of"* in Item 6 of the Schedule to mean that the relevant excess was determined by reference to whether the occurrence was in respect of one of the named entities in Item 6.

The Court was unable to identify any other provisions in the policy inconsistent with this construction. The primary judge's construction of the self-insured excess as applying to each occurrence was upheld and the appeal dismissed.

Comments

The case is a triumph for purposive over literal constructions of insurance contracts and provides a useful reminder of:

- the importance of considering the interaction between the various clauses in a policy;
- the need to take extra care to consider the adequacy and

limitations of cover provided under a policy that has been arranged by another party; and
- how a policy will be construed in accordance with the ordinary rules of contract interpretation, having regard to the context in which the words appear. ■

Suspicious fire claims – a hunch is not enough

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Introduction

If an insurer is seeking to rely on circumstantial evidence of an insured's misconduct to deny a claim for indemnity, the onus of proof is on the insurer to prove the alleged misconduct on the balance of probabilities. ***Mutual Community General Insurance Pty Ltd v Khatchmanian*** [2013] VSCA 144 demonstrates the difficulty insurers face in satisfying this burden, and the added risk of indemnity costs and adverse interest orders if an insurer fails to prove its case.

The facts

Mr Khatchmanian (**the Insured**) owned a house where he lived with his wife and children. On the night of Saturday 27 March 2010, while the Insured and his family were a considerable distance away for the weekend, the Insured's house was destroyed by fire. The expert forensic evidence suggested that the fire was deliberately lit.

The Insured had a home insurance policy (**the Policy**) with Mutual Community General Insurance Pty Ltd (**the Insurer**). The Insured made a claim under the Policy (**the Claim**) for losses caused by the fire. The Insurer declined the Claim alleging that the Insured had deliberately caused the fire. The Insured commenced proceedings against the Insurer in the County Court of Victoria.

The County Court decision

At the trial, the Insurer relied on circumstantial evidence to demonstrate that the Insured had deliberately caused the fire. The evidence included that the Insured was in financial difficulty and that no known arsonists were operating in the area at the time.

The trial judge found in favour of the Insured on the basis that the Insurer had failed to prove on the balance of probabilities that:

- the Insured was financially motivated to destroy the house; and
- no other person could have caused the fire.

The trial judge also considered the Insured's entitlement to interest under section 57 of the **Insurance Contracts Act 1984 (Cth)** (**the ICA**). Given the complexity of the Claim, the trial judge found that the Insurer had unreasonably withheld the insurance payment, and the Insured was entitled to interest commencing six months from the date of the loss.

On the issue of costs, the trial judge declined to award indemnity costs against the Insurer. The trial judge was of the view that a Calderbank offer made by the Insured prior to the hearing *"gave little consideration to the defendant's prospects"*.

The appeal

The Insurer appealed the trial judge's findings, and the Insured cross appealed the trial judge's findings based on interest and costs.

The Insurer submitted that because it had presented evidence that raised the prospect of the Insured's financial motive to destroy his home and lack of forced entry by an unrelated third party, the Court was bound to hold in the Insurer's favour unless satisfied on the balance of probabilities as to a lack of financial motive or evidence of a forced entry. This was, in effect, an attempt by the Insurer to shift the onus of proof to the Insured.

The Court rejected this submission and stated that it was not for the Insured to establish that he was without a financial motive or that there was forced entry by an unrelated third party intruder. It was for the Insurer to adduce evidence sufficient to persuade the judge on the balance of probabilities of each of those facts and the Insurer had failed to do so. The onus of proof remained with the Insurer.

The Court held that on the balance of probabilities:

- the Insured did not have a financial motive to destroy the house, as the Insured could have raised any necessary funds from the sale of other assets; and
- the evidence as presented left open a real and substantial possibility of the house having been forcibly entered by an intruder prior to the fire.

The Court therefore dismissed the Insurer's appeal and upheld the trial judge's findings that the Insurer had failed to prove its circumstantial case.

On the facts of the case, the Court allowed the Insured's cross appeal based on interest and costs. The Court found the Insurer should have completed its investigations into the Claim within three months from the date of the loss, and that interest under section 57 of the ICA should commence from that date.

In relation to costs, the Court found that the Insured's Calderbank offer was made at an appropriate time immediately prior to the hearing, and it was unreasonable for the Insurer to maintain its position on indemnity despite considerable objective evidence that the Insured was at his other property at the time the house burnt down. The Insured was therefore entitled to his costs on an indemnity basis from the date of the Calderbank offer.

Concluding comments

This case further illustrates the difficulty insurers face when the events surrounding a claim, especially in relation to a fire, apparently point to the Insured but there is no direct evidence to rely on. It is not enough for the Insurer to merely raise the suspicious circumstances and hope to shift the onus to the Insured; the Insurer must prove its case on the balance of probabilities. A hunch is not enough, and the age-old adage *"it is not what you think, but what you can prove"* should remain at the forefront of an insurer's mind in disputes of this nature.■

Dewatering explained

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The New South Wales Court of Appeal decision in ***Vero Insurance Ltd v Australian Prestressing Services Pty Ltd*** [2013] NSWCA 181 is instructive on questions of construction arising under a contract works and public liability insurance policy. It provides guidance on what constitutes *"dewatering"*; the construction of insurance contracts where terms are undefined; and the extent of an insured's obligation to mitigate further damage to property.

The facts

In January 2003, the respondents contracted to reconstruct a culvert that diverted water from Kensington Pond (in Centennial Park, Sydney) into a stormwater system. The works included a temporarily constructed wall (or cofferdam), which was required to hold back the water in Kensington Pond, where the remediation works were being carried out.

After the cofferdam was constructed, there was substantial rainfall that caused the water levels in the pond to rise. In an attempt to protect the cofferdam, the respondents pumped out (rather than drained) some of the water to prevent the cofferdam from breaching. In response to the respondent's claim for $470,000 in respect of the extra costs incurred in performing that work, the insurers denied cover primarily on the basis of a dewatering exclusion in the insurance policy.

At first instance

At first instance, the respondents successfully recovered over $360,000 for costs incurred in preventing the cofferdam from collapsing following the heavy rainfall. The primary judge found that the respondents were entitled to indemnity under the general insuring clause, which provided that:

> *"... the insurance by this Policy indemnifies the Insured against Loss, Destruction of or Damage to Property Insured occurring during the construction period arising from any cause not hereafter excluded."*

The primary judge concluded that the costs and expenses were incurred in preventing loss of or damage to the insured property, and were therefore within the scope of the insured risk. In doing so, the primary judge explained that Her Honour did not need to consider whether the costs were incurred in repairing the actual damage to – or restoring the damaged part of – the property insured, relying on the decision in ***Re Mining Technologies Australia Pty Ltd*** [1999] 1 Qd R 60 (***Mining Technologies***). The insurer appealed.

Issues arising on appeal

The issues arising on appeal included:

- Did a major part of the costs and expenses claimed fall within the dewatering exclusion?
- When interpreting the dewatering exclusion, did the primary judge err in having regard to the terms of the works contract and lay-expert evidence, regarding the meaning of dewatering?
- Did the respondent fail to establish that the claim fell within the terms of any insuring clauses under the policy?

- Was the insurer's liability to indemnify under the temporary protection extension limited to $250,000?

Was the insuring clause satisfied?

The Court found that the primary judge's reliance on ***Mining Technologies*** was not well founded. In that case, the issue was whether expenses incurred in retrieving mining equipment that had been incidentally buried could be recovered under a policy that insured equipment against *"loss, damage, or liability"*. McPherson J concluded that, as a matter of policy construction, there had been a partial loss of that machinery, and remedial measures amounted to repair and restoration of that partial loss.

In this case, expert evidence confirmed that the cofferdam was saturated and therefore damaged. If the work had not been carried out, the extent of the damage would have been magnified. The Court found that by the time the respondents had incurred the expense of removing or diverting water, there was physical damage to the cofferdam, which was insured under the general insuring clause. It was more than a mere loss of functionality or usefulness. Subject to the operation of the dewatering exclusion, the respondents were entitled to indemnity under the temporary protection extension in respect of costs and expenses incurred protecting the cofferdam. The insuring clause was therefore satisfied.

Dewatering

The next issue was whether the dewatering exclusion applied to exclude the claim. In construing the policy, the Court noted that the policy drew a distinction between *"dewatering"*, *"water diversion"* and *"flood mitigation"*. The primary judge had admitted and taken into account evidence from lay and expert witnesses on the meaning of *"dewatering"*.

In considering the exclusion, the Court summarised the relevant principles to be applied in construing insurance policies, namely that the language of a particular provision must be construed having regard to other terms, the commercial circumstances it addresses, and the objects the parties can be presumed to have intended to secure by making the contract (see ***McCann v Switzerland Insurance Australia*** [2000] HCA 65).

The Court indicated that it was possible to deal with issues that arose in relation to the exclusion, without having regard to the terms of the works contract or lay and expert evidence, through information provided by the insurance broker at the time the endorsement was negotiated and agreed. The Court applied ordinary and natural meaning of *"dewatering"*, concluding that it was the removal of water from a place or thing. The respondent had not used equipment for the purpose of removing water from the site to enable an activity or work to proceed in that place; it had done so to prevent the cofferdam from collapsing. *"Dewatering"* did not refer to a partial draining. The dewatering exclusion therefore did not apply.

Implying a term

The Court also considered whether the following term could be implied into section 2 of the policy:

> *"That where the loss, damage or liability which would otherwise have occurred was avoided by the exercise of reasonable care, the expenditure of money and/or the performance of work by APS and/or Bedi or any person acting on their behalf whether pursuant to the obligations referred to in paragraph 17AB or otherwise would indemnify APS and/or Bedi against such expenditure, costs or for the value of such work."*

The Court noted that an express policy term placed an obligation on the insured to take immediate action to minimise the extent of property damage, in the event of an occurrence that could give rise to a claim. In relation to terms implied by fact, the Court confirmed that the conditions summarised in ***BP Refinery (Westernport) Pty Ltd v Hastings Shire Council*** (177) 180 CLR 266 must be satisfied. As it was, the Court refused to imply the term because it was inconsistent with the express terms of the policy. ■

Causation: a case of "Elementary, my dear Watson"?

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Nulty v Milton Keynes Borough Council [2013] EWCA Civ 15 concerned the appeal against the English High Court decision of Edwards-Stuart J in ***Milton Keynes Borough Council v Michael Nulty (deceased) and others*** [2011] EWHC 2847 (TCC). In the appeal, the Court considered whether *"when you have eliminated the impossible, whatever remains, however improbable must be the truth"* (the so-called *"Sherlock Holmes causation dictum"*) is a sound test of causation when not all the relevant facts are known.

Applying ***Rhesa Shipping (The Popi M)*** [1985] 1 WLR 948 (***Rhesa Shipping***), the Court agreed that when not all relevant facts are known, the *"Sherlock Holmes causation dictum"* is an unsound test of causation. Instead, the Court must determine whether the party that bears the burden of proving causation has discharged that burden.

The background

The proceedings arose as a result of 2 fires at a recycling centre (**the centre**) owned by Milton Keynes Borough Council (**the Council**). On 2 April 2005, Mr Nulty attended the centre to urgently repair a fault with a machine. Mr Nulty had a cigarette break and 15 minutes later the centre's fire alarm was activated. The fire brigade attended the centre, extinguished the fire and left. Several hours later, a second fire broke out at the centre, causing around £4.5 million worth of damage to the centre and its contents.

The Council brought proceedings against Mr Nulty, alleging that he caused the first fire by discarding a cigarette, and that the first fire caused the second fire. Mr Nulty died before the claim came to trial; however, his professional liability insurers (**NIG**) defended the proceedings. NIG argued that the first fire was not caused by Mr Nulty but was caused either by the arcing of an electrical cable or by arson.

The High Court decision

In a detailed judgment, Edwards-Stuart J considered three potential causes of the first fire: a discarded cigarette, the arcing of an unsecured electrical cable or arson by an intruder.

Edwards-Stuart J concluded that none of the three suggested causes were *"inherently likely"* to have caused the fire, but nevertheless dismissed the notion that the first fire had been caused by an intruder or by a cigarette discarded by someone other than Mr Nulty. Edwards-Stuart J found that the arcing of an electrical cable was *"very unlikely"* to have caused the fire, whereas the

discarding of a cigarette by Mr Nulty was a feasible scenario. By eliminating the other possible causes, His Honour concluded that Mr Nulty's discarded cigarette must have been the cause of the first fire, and that the first fire caused the second fire.

The decision of the Court of Appeal

NIG appealed the decision on the basis that the trial judge had erred:

- in law, as his approach to the question of causation was contrary to the principles set out by the House of Lords in ***Rhesa Shipping***; and
- in fact, by finding that Mr Nulty's cigarette had caused the first fire.

Error of law

The Council, arguing in favour of the *"Sherlock Holmes causation dictum"*, submitted that the Court should allocate a probability factor to each individual cause and determine whether one factor had a probability greater than 50% of having caused the second fire. Toulson LJ of the Court of Appeal rejected this approach as *"intrinsically unsound"*.

In reaching that conclusion, the Court considered ***Rhesa Shipping***. In that case the Court rejected the *"Sherlock Holmes causation dictum"* on the basis that:

- it is open to the Court to conclude that the party bearing the burden of proof has failed to discharge that burden;
- the *"Sherlock Holmes causation dictum"* can only operate when all relevant facts are known; and
- it is contrary to common sense to conclude that the occurrence of an event is extremely improbable but nevertheless find that the balance of probabilities test has been satisfied.

Toulson LJ stated that the balance of probabilities test requires that:

> *"the Court must be satisfied on rational and objective grounds that the case for believing that the suggested means of causation occurred is stronger than the case for not so believing."*

Toulson LJ concluded that in cases where causation is based on circumstantial evidence, the court must consider:

- the whole picture, including the gaps in the evidence;
- whether factors that support an explanation are properly established;
- what factors detract from that explanation; and
- what other explanations might fit the circumstances.

While eliminating all other possibilities might lead to the conclusion that a particular explanation of events is more likely to be true than not, the Court confirmed that there is no rule of law to this effect.

Error of fact

The Court of Appeal refused to interfere with Edwards-Stuart J's findings of fact regarding the cause of the fire, as an appellate court can only re-examine factual conclusions when there is a serious ground to doubt the primary judge's overall conclusion. The Court of Appeal held that when the first instance judgment was read as a whole, it was implicit that the evidence indicating that Mr Nulty was responsible for the fire was stronger than the case that he was not.

Concluding comments

This case is a reminder that a party must not assume – especially

in complex cases or those where investigations are hampered by delay – that just because their explanation seems more plausible than the alternatives, a Court will accept that the burden of proof has been discharged. A defendant should challenge the claimant's evidence, identify factors that detract from the claimant's explanation, and remind the Court that it can find that the evidential burden has not been met. This case is also a reminder that if the defendant does not sufficiently challenge the evidence at first instance, appeals against findings of facts must overcome a high barrier if they are to succeed. ■

When flooding is not a flood – *LMT Surgical Pty Ltd v Allianz Australia Insurance Ltd* [2013] QSC 181

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The facts

During the 2011 Brisbane floods, the premises of LMT Surgical Pty Ltd (**LMT**) was inundated by the back-flow of floodwater from the Brisbane River. The water caused damage to the premises and interruption to LMT's business (**the Damage**).

The Damage was attributed to a back-flow of floodwater from two stormwater drainage pipes located near LMT's premises. LMT made a claim under its ISR policy (**the Policy**) issued by Allianz Australia Insurance Ltd (**the Insurer**). The Policy defined "flood" as:

> *the inundation of normally dry land by water overflowing from the normal confines of any natural watercourse or lake (whether or not altered or modified), reservoir, canal or dam."*

The Insurer declined the claim on the basis that the Damage triggered the flood exclusion clause in the Policy. LMT commenced proceedings in the Supreme Court of Queensland seeking a declaration that the Insurer was liable to indemnify it under the Policy.

The proceedings

The key issues in the proceedings were:

- whether the pipes *"altered"* or *"modified"* the natural watercourse and, if so, whether the inundation was *"by water overflowing from the normal confines"* of the natural watercourse;
- whether the pipes were a *"canal"* and, if so, whether there was an inundation by water overflowing from the normal confines of that canal; and
- whether the river was a relevant natural watercourse and, if so, whether there was an inundation *"by water overflowing from the normal confines"* of that natural watercourse.

The Court found the pipes were not an

"altered or modified" natural watercourse for the purposes of the flood exclusion clause. In doing so, the Court accepted that the pipes were installed to replace an original watercourse in the area and performed the same drainage function as the original watercourse. However, the Court considered the very act of installing the pipes and backfilling the original watercourse *"broke the link to the prior natural watercourse"*. The Court also did not consider the pipes to be a *"reservoir, canal or dam"* as they were *"underground storm water drainage pipe*[s]*"*.

The parties accepted that the Brisbane River was the *"natural watercourse"*. The Court found the *"normal confines"* of the Brisbane River were the banks (natural or altered) and did not include the stormwater drainage pipes or the original watercourse. The Court reasoned that *"the ordinary meaning of the words is directed to the place from where the overflowing occurred, not the place from where the water was sourced"*. Accordingly, the Court held the inundation of the premises was caused by the back-flow from the stormwater drainage pipes running from the riverbank, rather than by the floodwater overflowing from the natural confines of the Brisbane River. It followed that the flood exclusion was not triggered and LMT was entitled to indemnity.

Implications for Mark IV and Mark V ISR Policies and prescribed contracts

The decision could have potentially wide-ranging implications for all ISR insurers given the similarity between the wording in the Policy with the standard Mark IV and Mark V wordings, and the standard wording introduced for all prescribed contracts under section 37B of the **Insurance Contracts Act 1984 (Cth)**.

It is important to acknowledge that the Court expressly acknowledged that the outcome of this case turned on the language of the specific flood exclusion in the Policy. The Court did not make any reference to or put any reliance on any of the existing cases on floods. The Court said:

> *"The statement that a policy is intended to exclude damage caused by flood does not define the inquiry where the policy itself defines what is meant by flood. The surest approach is a close consideration of the contractual text in its context."*

The small but significant differences in the wording in each of the exclusion provisions – and a strict literal interpretation of any of them – may possibly lead to a different outcome. As there is no one definition of *"flood"*, we suggest that flood cases still have to be decided on a case-by-case basis. ■

Insurance Year in Review 2013
Trade + Transport

Arresting developments: existence of foreign proceedings no basis to resist ship arrest

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In ***Atlasnavios Navegacao, LDA v The Ship "Xin Tai Hai" (No 2)*** [2012] FCA 1497, the Federal Court was asked determine whether attempts to arrest a vessel in Australian waters could be prevented by the fact that proceedings had already been commenced in another jurisdiction.

The decision provides useful guidance on the factors Australian courts will take into account when applying the *"clearly inappropriate forum"* test to *in rem* proceedings commenced in Australia.

Background

A collision between the B Oceania, owned by Atlasnavios Navegacao LDA (**Atlas**), and the Xin Tai Hai, owned by China Earth Shipping Inc (**China Earth**), in the Straits of Malacca in July 2011 resulted in the sinking of the B Oceania. The vessel was loaded with iron ore owned by Hangzhou Cogeneration Import and Export Company Limited (**the cargo owner**).

On 4 November 2011, Atlas commenced *in rem* proceedings in the Federal Court of Australia seeking damages for the loss of B Oceania. On 1 May 2012, Atlas applied for a warrant to arrest the Xin Tai Hai in Australia. At the time of the application, Atlas, China Earth and the cargo owner were also involved in separate proceedings commenced in the Qingdao Maritime Court of the People's Republic of China (**the Maritime Court**). Atlas did not disclose the existence of the Maritime Court proceedings to the Federal Court when seeking the arrest warrant.

On 2 May 2012, Xin Tai Hai was arrested at Port Hedland, Western Australia. China Earth subsequently applied to have the Federal Court proceedings stayed in favour of the Maritime Court proceedings on the basis that:

- Atlas did not disclose the existence

of the Maritime Court proceedings when applying for the warrant; and
- Australia was clearly an inappropriate forum.

Disclosure of Chinese proceedings

In its judgment, the Federal Court held that Atlas was under no duty to disclose the existence of the Maritime Court proceedings when applying for the arrest warrant. Rares J found that a party seeking an arrest warrant was not analogous to a party seeking an *ex parte* injunction. In doing so, Rares J distinguished the English case of ***The Vasso*** [1984] QB 477, the Hong Kong case of ***Sin Hua Enterprise Co Ltd v The Owners of the Motor Ship "Harima"*** [1987] HKLR 770 and the Singapore Court of Appeal case of ***The "Rainbow Spring"*** [2003] 3 SLR(R) 362.

It was held that Atlas' disclosure obligations were limited to the express requirements under the **Admiralty Act 1988 (Cth)** and **Admiralty Rules 1988 (Cth)**, which had been complied with in this case.

Clearly inappropriate forum

The Court held that the existence of the Maritime Court proceedings did not necessarily mean that Australia was a *"clearly inappropriate forum"* (utilising the test from ***Voth v Manildra Flour Mills Pty Ltd*** (1990) 171 CLR 538 (***Voth***)).

In reaching that conclusion, Rares J considered the following propositions:

- An Australian court must exercise jurisdiction conferred on it, except where it is established to be a clearly inappropriate forum.
- The Court's discretionary powers involve a subjective balancing of different factors, including:
    - the nature and degree of connection between the proceedings;
    - which forum would provide a more effective resolution of the matters;
    - the order in which the proceedings were instituted; and
    - the stage each proceeding had reached.
- The rationale underpinning the *"clearly inappropriate forum"* test is the avoidance of injustice between parties in a particular case.

Applying Voth, Rares J held that the critical issue was the appropriateness of the local court, not the appropriateness (or comparative appropriateness) of a foreign forum. Rares J concluded that one court will not be an inappropriate forum merely because another may be more appropriate. In this instance:

- neither China nor Australia was a natural forum to resolve the liabilities arising out of the collision;
- no substantive progress had occurred in the Maritime Court proceedings prior to the arrest;
- China Earth would be an active litigant in the Maritime Court whether or not Atlas continued with its claim there;
- Atlas' right to arrest the Xin Tai Hai was not available in China;
- Atlas was seeking the benefit of legitimate advantages available in Australia, including:
    - greater security for its claim;
    - a larger limitation fund; and
    - exclusion from limitation of liability of wreck removal expenses.

Conclusions

Having regard to these factors, Rares J rejected China Earth's application and concluded that Atlas' purpose in filing the Federal Court proceedings and applying for arrest was a proper and legitimate use of the Court's process.

The decision suggests that Australian

Courts will be reluctant to let factors such as the prior commencement of proceedings in another jurisdiction prevent a party from commencing *in rem* proceedings in Australia or arresting a vessel, particularly where arrest of a vessel would not be possible in the other jurisdiction. ■

Federal Court packs a punch with interpretation of marine insurance cargo clauses

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Introduction

In ***Alstom Ltd v Liberty Mutual Insurance Company (and Others) (No 2)*** [2013] FCA 116, the Federal Court of Australia found that a deeming provision in the marine insurance policy applied so that the insurer could not rely on an exclusion clause to exclude cover for losses caused by *"insufficiency or unsuitability of packaging or preparation"*.

Background

Alstom entered into a contract with Crompton Greaves Ltd (**CG**) for the manufacture and supply of two transformers to be delivered by sea from Mumbai to Henderson Wharf, Fremantle, and then delivered by road transport to a new power station in Kwinana, Western Australia. Under the terms of the contract, the transformers were to be:

- factory tested; and
- packed and shipped in a seaworthy condition from Mumbai to Henderson Wharf, Fremantle.

During the voyage to Fremantle, the core coil assembly of each transformer moved within its steel container and was severely damaged.

Alstom brought a claim under its marine cargo insurance policy for indemnity in respect of the damaged transformers. The insurers argued that they were not obliged to provide cover because:

- the damage caused to the transformers arose through an inherent vice in the transformers, which was an excluded risk under the Institute Cargo Clauses (A) incorporated into the policy (inherent vice exclusion); and
- alternatively, the damage was caused by the absence of packing to ensure the core coil assembly did not move. The policy excluded cover for losses caused by *"insufficiency or unsuitability of packing or preparation"* (**packing exclusion**).

Alstom argued that the *"unsuitability of packaging"* clause in the policy applied

so that it should be covered for its losses because that clause operated as an exception to the packing exclusion. That clause stated that:

> "*Any packaging or external preparation of the interest insured is deemed to be sufficiently packed and prepared if:*
> *(a) the packing and external preparation is in accordance with usual custom or trade or the Insured's custom or*
> *(b) any insufficiency or unsuitability of packing or external preparation has not arisen through fault of or with the knowledge and consent of the Insured.*" (**the deeming provision**)

Alstom argued that the deeming provision applied because CG had packed the goods and therefore *"any insufficiency or unsuitability of packing or external preparation"* had not arisen through Alstom's fault or with its knowledge and consent.

Insurers argued that CG was also an insured under the policy for the purposes of the deeming provision, meaning Alstom did have knowledge of the packing, and the deeming provision did not apply.

Alstom also highlighted that the insurers could have utilised the *"surety warranty"* clause in the policy – under which the insurers had the right to "*approve and/or attend all packing, loading stowage ... arrangements and operations*" – but had not done so.

Federal Court decision

The Court found in favour of Alstom and held that Alstom should be granted indemnity for its losses.

Inherent Vice

Siopis J stated that the inherent vice exclusion was not triggered because the lack of internal bracing to secure the core coil assembly was not an inherent vice.

Packing exclusion v deeming provision

The Court held that the packing exclusion did apply because:

- the cause of the damage to the transformers was the impact of the top locating posts on the flanges, and resulted from the absence of internal bracing to secure the core coil assembly; and
- the absence of internal bracing constituted an insufficiency or unsuitability of *"packing"* rather than "*preparation*" as the transformer tank was designed to be a container for transport of the transformer component parts by sea and road, and any internal bracing applied was *"packing"*.

However, the Court held that the deeming provision applied because:

- on its proper construction, the policy is a composite policy (as opposed to a joint policy), meaning that each of the parties comprising *"the Insured"* (i.e. Alstom and CG) was to be treated as a party to a separate indemnity. The endorsement of the policy included clauses demonstrating a contractual intention to indemnify each of the parties in respect of that party's individual loss;
- the insufficiency in the packing of the transformers had not arisen through the *"fault of or with the knowledge and consent"* of Alstom; and
- the words *"knowledge and consent"* required Alstom to have actual knowledge that the packing of

the transformers was insufficient or unsuitable, and that it gave its consent for the transformers to be shipped in that state.

Siopis J held that Alstom:

- was not responsible for packing the core coil assemblies;
- had no actual knowledge of the insufficiency or unsuitability of the packing; and
- was not at fault and therefore was entitled to indemnity.

The decision also considered the extent of indemnity provided under section 61 of the **Marine Insurance Act 1909**, which provides that an insurer is liable for loss proximately caused by a peril insured against but not indirect or consequential loss. The court held that Alstom was not entitled to recover some items of expenditure incurred in respect of indirect and uninsured financial losses, including the cost of alternative power while the transformers were repaired, stored and transporting the repaired transformers to the power station site.

Comments

This case highlights the importance for insurers to consider carefully what they want to achieve from an exception to a standard form exclusion. In Alstom, it seems the insurer interpreted it to apply in circumstances where the insured played no role whatsoever in the cause of the damage, namely the insufficiency of the packing. However, in cases where an insured's agent is responsible for packing goods, insurers need to carefully consider whether the agent is included within the meaning of *"Insured"* for the purposes of the policy. Also, given that the policy included a surety warranty clause, insurers should have considered approval of the operating arrangements prior to the voyage (although in practice this may be difficult to achieve). ■

Federal Court provides guidance on procedures for charterparty termination

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In the ***Ships Hako***, the Full Court of the Federal Court heard an appeal against an interlocutory order to set aside writs issued under the **Admiralty Act 1988 (Cth)** (**Admiralty Act**). The decision, primarily of Rares J, provides useful guidance on the issues surrounding the termination of bareboat charters and the rights of entities to pursue actions *in rem* for the recovery of crew wages.

Facts

Programmed Total Marine Services Pty Ltd (**PTMS**) issued writs and applied for warrants for the arrest of four ships in April 2012: the Hako Endeavour, the Hako Excel, the Hako Esteem and the Hako Fortress. Each vessel was owned by a separate Singaporean company, each of which had demise chartered the ships to Hako Offshore Pte Ltd (**Hako**), which then time chartered the ships to Boskalis Australia Pty Ltd (**Boskalis**).

Boskalis used the ships to transport rocks as part of the Gorgon gas project off Western Australia. Hako failed to pay PTMS for the manning and crew services provided on the ships.

PTMS argued that Hako was the demise charterer or bareboat charterer of each ship (a leasing arrangement by which use of the entire vessel and all associated expenses pass from the ship owner to the charterer) and accordingly that sections 4(3)(m) and 18 of the Admiralty Act were enlivened.

PTMS argued that it had a maritime lien for each amount paid to the ship's master and crew pursuant to section 15(2)(c) of the Admiralty Act. The ships were arrested and subsequently released when sufficient security was provided.

First instance decision

At first instance, the primary judge refused the ship owners' application to set aside the writs under the **Federal Court of Australia Act 1976**. The arguments raised were that:

- with respect to the Hako Fortress, the owners had issued a notice of default and subsequently terminated the demise charter with Hako prior to the writ being issued by PTMS, such that section 18(b) of the Admiralty Act had no application and there was no right for PTMS to proceed in rem;
- Hako was not a demise charterer pursuant to section 18 of the Act because it was not

in possession and control of each ship in circumstances where it did not employ the master and crew (who were employed by PTMS);
- the goods and services claimed by PTMS were not supplied to the ship but instead were supplied to Hako, and therefore did not satisfy the jurisdictional issue required for section 4(3)(m) of the Admiralty Act that they be supplied to the ship;
- the debts claimed by PTMS were not owed to it but had been assigned under the deed to Boskalis pursuant to the terms of a deed entered into between those parties, which stated that Boskalis was required to purchase from PTMS the amount due at the time it became payable; and
- no maritime lien under section 15(2)(c) of the Admiralty Act could be asserted by PTMS because it had already paid the wages of the masters and crews it had employed.

Full Federal Court decision

On appeal, the Full Federal Court held that determining whether a demise charterparty has been terminated will be dependent on the terms of the specific charterparty agreement, not necessarily by the question of possession. His Honour held that the primary judge had erred in finding otherwise at first instance and concluded that the notice of default issued in respect of the Hako Fortress was sufficient to terminate the demise charterparty. The Federal Court therefore had no jurisdiction in respect of that ship.

In refusing the appeal with respect to the other 3 vessels, His Honour held that:

- a demise charter existed between Hako and the owners pursuant to the relevant charterparty agreements. Hako had the obligation to man the ships *"by its own procurement"*. Hako assumed the responsibilities and liabilities of the owner of the ship so far as third parties were concerned, including for any damage done or maritime liens created;
- there must be a direct connection between the supply of the relevant goods, materials or services and the ship to trigger section 4(3)(m). However, it was held that the provision of masters and crews, catering and other services to the Hako were services and goods provided to ships within the meaning of section 4(3)(m);
- any liability asserted against Hako had been assigned absolutely to Boskalis, and there was therefore no maritime lien in respect of the relevant crews' wages because they had been paid by PTMS – their legal employer;
- PTMS had not been paid by Boskalis or Hako any of the debts that were the subject of this claim. Therefore, Boskalis had not acquired, and PTMS had not assigned, any interest in those debts. PTMS still owed those debts when it commenced the proceedings;
- no maritime lien on any of the four ships was available to PTMS. Any maritime lien was extinguished once the relevant wages had been paid; and
- PTMS asserted it had an equitable right of subrogation that arose when it paid the masters and crews their wages. However, there was no assignment of the lien when the masters and crews were paid, and accordingly no right of equitable subrogation passed to PTMS.

Conclusion

This case provides useful guidance on the effective termination of charterparty agreements and the operation of crew's wages liens. It is clear from the decision that the payment of wages to a crew will extinguish any entitlement to enforce a maritime lien for such amounts, unless that lien is expressly assigned.

Australia makes an about turn on international arbitration position

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Introduction

Last year we reported on the Federal Court's landmark decision in ***Dampskibsselskabet Norden A/S v Beach Building and Civil Group Pty Ltd*** [2012] FCA 696, which dismissed a ship owner's application for enforcement of a UK arbitral award and held that:

- a voyage charterparty was a *"sea carriage document"* within the meaning of section 11(1)(a) of the **Carriage of Goods by Sea Act 1991 (Cth)** (**COGSA**); and
- a London arbitration clause in a voyage charterparty had no effect because, in accordance with section 11(2)(c) of COGSA, an agreement (such as the voyage charterparty) had:

> *"no effect so far as it purports to ... preclude or limit the jurisdiction of a court of the Commonwealth or of a State or Territory in respect of:*
> *(i) a sea carriage document relating to the carriage of goods from any place outside Australia to any place in Australia".*

The claimant ship owners appealed that decision because it undermined their ability to enforce the arbitral award made in London and were ultimately successful.

Background

By way of recap, ship owners Dampskibsselskabet Norden A/S (**DKN**) chartered a vessel from Beach Building and Civil Group Pty Ltd (**Beach Civil**) for the carriage of a cargo of coal from Australia to China. A demurrage dispute ensued between the parties.

In accordance with the arbitration clause in the voyage charterparty, DKN commenced arbitration in London, obtained an award against Beach Civil and applied to the Federal Court for enforcement of the award. Beach Civil contended that the London arbitration clause was invalid and the award was unenforceable because of section 11 of COGSA. The Federal Court found in Beach Civil's favour.

The appeal

It came as no great surprise that DKN appealed the first instance decision,

because it is widely understood internationally that:

- the meaning of *"sea carriage document"* does not encompass a charterparty;
- there is a distinct difference between a contract for the carriage of goods as evidenced by a bill of lading vis-à-vis a voyage charterparty;
- arbitration should be promoted as an alternative means of dispute resolution – arguably the first instance decision undermined that principle.

The Full Court's decision

The Full Court allowed the appeal in ***Dampskibsselskabet Norden A/S v Gladstone Civil Pty Ltd*** [2013] FCAFC 107 and held that the charterparty:

- was not a *"sea carriage document"* relating to the carriage of goods; and
- was not made ineffective by section 11(2) of COGSA.

That meant the provision in the charterparty specifying that any dispute be referred to arbitration in London remained valid.

The Full Court cited the following reasons for its decision:

- Traditionally, a clear line has been drawn between a charterparty, as a contract for the hire of a ship, and a *"sea carriage document"*.
- There has been a long-standing acceptance, under various international instruments given effect by domestic legislation, that international commercial disputes (including under voyage charterparties) may be settled by arbitration. The Full Court referred to the High Court's recent decision in ***TCL Air Conditioner (Zhongshan) Co Ltd v The Judges of the Federal Court of Australia*** [2013] 295 ALR 596.
- Although section 11 is open to interpretation, the Court should not too readily construe section 11 to limit the effect of arbitration clauses in respect of such disputes.
- Although *"sea carriage document"* is undefined in COGSA, the term was introduced into COGSA at the same time as that exact term was defined in the amended **Hague Rules** (which are annexed as a schedule to COGSA), so it is appropriate to apply the same meaning to both.
- The definition of *"sea carriage document"* in the amended Hague Rules does not include or specify *"charterparty"*, so it is clearly not encompassed within that definition.
- The Court held that this indicates *"that the amended Hague Rules preserve the distinction between a charterparty including a voyage charterparty and a sea carriage document"*.

Implications

The decision has been welcomed by the international shipping community because it recognises the difference between a "*sea carriage document"* and a *"charterparty"*. It also means that charterparty clauses referring disputes to foreign arbitration will most likely be valid (although similar clauses in sea carriage documents such as bills of lading will remain unrecognised in accordance with the provisions in COGSA). ■

Yu can't always get what Yu want

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In ***Yu v STX Pan Ocean Co Ltd (South Korea), in the matter of STX Pan Ocean Co Ltd (receivers appointed in South Korea)*** [2013] FCA 680, the Federal Court confirmed that a creditor's attempts to arrest an insolvent shipowner's vessel in Australian waters will not necessarily be prevented by operation of the **Cross-Border Insolvency Act 2008 (Cth)** (**the Act**), which incorporates the **United Nations Model Law on Cross-Border Insolvency** (**the Model Law**) into Australian law.

The Act allows Australian Courts to stay proceedings commenced in Australia in favour of a *"foreign main proceeding"* and to entrust the administration of all or part of a debtor's assets in Australia to a *"foreign representative"*, i.e. a foreign liquidator, receiver or administrator.

The ruling suggests that the Australian Courts will be very reluctant to make *"additional orders"* under the Act that would be likely to limit the rights creditors might otherwise have. For example, the right to commence in rem proceedings against a vessel.

Background

In June 2013, South Korean bulk shipping company STX Pan Ocean Co Ltd (**STX**) announced that it was on the brink of insolvency as a result of tough market conditions in that sector.

Corporate rehabilitation proceedings were commenced by STX in South Korea and STX was placed into court-ordered receivership. Mr Chun Il Yu (**Mr Yu**) was appointed as receiver of STX, a position analogous to a Court-appointed liquidator in Australia.

In light of STX's well publicised financial position, there was a very real prospect that creditors of STX worldwide would begin taking steps to arrest any of the ships comprising STX's fleet of over 300 vessels.

The Federal Court application

Against that background, and in circumstances where a considerable number of STX-owned vessels routinely dock in Australian ports, Mr Yu sought recognition from the Federal Court of Australia as a *"foreign representative"* and requested that the rehabilitation proceedings in South Korea be recognised as a *"foreign main proceeding"* for the purposes of the Act.

Mr Yu also sought an additional order pursuant to Article 21 of the Model Law, which allows a Court to grant additional relief where necessary to protect the assets of the debtor or interests of creditors. The additional order sought by Mr Yu was that secured creditors be restrained from enforcing charges against the property of STX (namely STX vessels in Australian waters) without first obtaining the leave of the Court or the consent of Mr Yu.

The practical effect of such an additional order would be to prevent STX's creditors from utilising the traditional international maritime law security regime by:

- arresting a ship owned by STX pursuant to

the **Admiralty Act 1988 (Cth)**; and/or
- exercising its rights pursuant to a maritime lien.

In seeking the additional order, Mr Yu argued that if ships owned by STX were allowed to be arrested, it would cause significant delays to STX's business operations and severely limit the prospects of STX being successfully rehabilitated in South Korea (to the detriment of STX's creditors globally).

The decision

The Federal Court had no hesitation in ordering that Mr Yu be recognised as a *"foreign representative"* or that the South Korean rehabilitation proceedings be recognised as a *"foreign main proceeding"* for the purposes of the Act. However, the Court did not agree to grant the additional order sought by Mr Yu. In dismissing Mr Yu's application for an additional order, Buchanan J held that:

- the wording of Article 20 of the Model Law makes it clear that it is not intended to override the operation of local insolvency laws (including, relevantly, sections 471(B) and 471(C) of the **Corporations Act 2001 (Cth)**;
- section 471(B) of the Corporations Act provides that leave of the Court would be required in any event if an arrest warrant was sought by a creditor;
- section 471(C) of the Corporations Act provides that nothing can limit a secured creditor's right to realise a security in circumstances where a company is being wound up or a liquidator has been appointed;
- an action *in rem* to enforce a maritime lien (such as a crew's wages or salvage costs) represents a security claim falling within the scope of section 471(C) of the Corporations Act; and
- any claimant seeking to enforce a maritime lien against a vessel owned by STX should be afforded the ordinary protection under section 471(C).

Conclusions

This decision goes some way to clarifying the interplay between the cross-border insolvency regime and the right of creditors to arrest ships in Australia once a ship's owner has gone into receivership (or a similar restructure). The position in Australia is currently that actions to enforce a maritime lien fall outside the cross-border insolvency regime, as they represent an existing security right enforceable by an action in rem and ship arrest.

What remains somewhat unclear is whether a party seeking to arrest a vessel other than on the basis of a maritime lien (for example, a claim for bunkers or for damage to cargo) remains subject to the restrictions of the cross-border insolvency regime.

In our view, it seems unlikely that such parties will be treated by the Courts as secured creditors entitled to the protection of section 471(C) of the Corporations Act. That said, bunker suppliers, cargo interests and their respective insurers might seek to circumnavigate this problem by ensuring their contractual arrangements incorporate a contractual right to a maritime law lien.

Navigating recent developments in Australian maritime law

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Over the past 12 months, a raft of maritime legislative amendments have been implemented in Australia, aimed at modernising the Australian law in this area and making the industry more competitive and attractive.

The centrepiece of these legislative reforms is the **Navigation Act 2012 (Cth)** (**2012 Act**), which replaces the century-old **Navigation Act 1912 (Cth)** (**1912 Act**), a piece of legislation which was being drafted the year RMS Titanic sank.

The 2012 Act

Coming into force on 1 July 2013, the 2012 Act now represents the primary legislative means by which the Australian Government regulates international shipping, seafarers' safety and employment conditions, and responses to marine pollution in Australian waters.

In the modern age of containerised shipping, many elements of the 1912 Act had long passed their use-by date.

The 2012 Act continues to give effect to a number of relevant international conventions to which Australia is a signatory, such as the **SOLAS Convention** (the **International Convention for the Safety of Life at Sea, 1974**), the **MARPOL Convention** (the **International Convention for the Prevention of Pollution From Ships, 1973**) and the **International Convention on Salvage, 1989**.

In addition, the 2012 Act incorporates and modernises the provisions of the **Lighthouses Act 1911 (Cth)**, ensuring that both Acts are now far more relevant to a world where navigation is aided by satellites and global positioning systems.

Specific criminal offences and civil penalty provisions

One of the more significant changes in the 2012 Act is the incorporation of new civil penalty provisions for offences committed by the owners and masters of foreign vessels while in Australian waters.

The definition of *"owner"* is particularly broad and extends to *"a person with overall general control and management of the vessel"* or *"a person who has assumed responsibility for the vessel"* from the owner. It remains to be seen whether the breadth of these definitions might even extend to a party who arrests a vessel.

Specific criminal offences and civil penalty provisions have been incorporated with respect to the inadequate training of crew members and taking unseaworthy vessels to sea. Both the owner and the master of a ship may be held to have committed an offence in allowing such events to occur.

The 2012 Act introduces a civil penalty regime

that expands the range of options available to the regulator, the Australian Maritime Safety Authority (**AMSA**), including the discretion to institute prosecutorial proceedings or civil penalty proceedings for contraventions.

The 2012 Act also addresses the important issue of maritime pollution and gives effect to Australia's international obligations in that area. Significantly, a master of a vessel who operates the vessel in a manner that fails to prevent pollution or damage to the marine environment outside of Australia can now be found guilty of an offence.

However, the real teeth in the 2012 Act are its civil penalty provisions. For example, the penalty for taking an unseaworthy vessel to sea is now 6,000 penalty units (currently A$1,020,000 or US$910,400).

Marine Safety (Domestic Commercial Vessel) National Law Act 2012 (Cth)

While the 2012 Act applies to international traffic, the new **Marine Safety (Domestic Commercial Vessel) National Law Act 2012 (Cth)** (**Marine Safety Act**), which came into force on 1 July 2013, applies to domestic commercial vessels that travel purely within Australia's exclusive economic zone (**EEZ**).

Again, AMSA is the single national regulator for domestic commercial vessel safety in Australia. In that capacity, it has responsibility for monitoring compliance with the Marine Safety Act and instituting proceedings against those who contravene it.

The Marine Safety Act imposes penalties for intentional, reckless or negligent conduct, as well as various strict liability offences. The penalties vary between the four types of offences but include imprisonment, fines and civil penalties.

Masters are obliged to reasonably ensure the safety of vessels, and their equipment and passengers. They are also under a duty to operate vessels in a reasonably safe manner. Duties are also imposed of the crew of domestic commercial vessels with respect to the safety of passengers.

The Marine Safety Act also imposes duties on those who design, build or supply domestic commercial vessels or marine safety equipment for such vessels. Such people and organisations have a duty to ensure that vessels and equipment are safe for the purposes for which they were designed, constructed or repaired.

Specific offences are also created in connection with certification of vessels – for example, operating a vessel without a certificate of operation or a certificate of competency – while extensive powers are given to marine safety inspectors to ensure compliance with the Marine Safety Act.

Neither the 2012 Act nor the Marine Safety Act apply to offshore industry vessels, as long as such vessels are considered to be *"facilities"* for the purposes of the **Offshore Oil and Gas Storage Act 2006 (Cth)**.

Other legislative developments

In addition to these two substantial pieces of legislation, a range of other more modest legislative reforms have been implemented in the past year, aimed primarily at increasing the opportunities for expansion of the Australian export market. These Acts include:

- the **Coastal Trading (Revitalising Australian Shipping) Act 2012 (Cth)**;
- the **Coastal Trading (Revitalising Australian Shipping) (Consequential Amendments) Act 2012 (Cth)**;
- the **Shipping Registration Amendment (Australian International Shipping Register) Act 2012 (Cth)**;
- the **Shipping Reform (Tax Incentives) Act 2012 (Cth)**; and
- the **Tax Laws Amendment (Shipping Reform) Act 2012 (Cth)**.

These Acts implement new licensing and tax regimes aimed at increasing the desirability of vessel registration and investment in Australia. Despite Australia's unique position in Asia and its significant shipping trade, the number of Australian-registered vessels remains very low. It remains to be seen whether the recent legislative reforms will result in an increase in Australian vessel registrations in coming years.

WA Court of Appeal provides useful guidance on the principles governing the incorporation of terms and conditions applied in commercial dealings

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Introduction

In ***La Rosa v Nudrill Pty Ltd*** [2013] WASCA 18, the Western Australian Court of Appeal held that an exclusion clause printed on the reverse of an invoice was not, by a previous course of dealings, incorporated into a cartage contract. As a result, the appellant could not rely on the exclusion clause to escape the consequences of his negligence.

Facts

Mr La Rosa had transported equipment for Nudrill Pty Ltd (**Nudrill**) for about 10 years. After each contract had been performed, La Rosa would send an invoice to Nudrill as proof of delivery and to request payment for the job.
In 2001, Mr La Rosa orally contracted with Nudrill to transport a drill rig from Perth to Kalgoorlie. The only specific terms discussed were price, destination, and pick-up location and time.
The drill rig was damaged in transit to Kalgoorlie, and Nudrill sued Mr La Rosa for damages for breach of contract, negligence and bailment.

Mr La Rosa sought to rely on an exclusion clause in the terms and conditions printed on the reverse of the invoice issued to Nudrill, which stated that:

"All goods are handled, lifted or carried at the owner's risk. The Contractor shall not be liable for any loss or damage of property and/or goods of the Client whether such damage was caused by any act, default or negligence on the part of the Contractor and/or his servants."

Mr La Rosa argued that even if he was found to be negligent or in breach of contract and bailment, he was excluded from liability pursuant to the exclusion clause.

First instance decision

At first instance, the trial judge found Mr La Rosa had breached his contractual and tortious duty to exercise reasonable care and skill by driving the prime mover at an excessive speed and causing damage to the drill rig.

The trial judge also found that the terms and conditions, in particular the exclusion clause, endorsed on the reverse of the invoices were not incorporated into the cartage contract such as to exclude Mr La Rosa's liability. Mr La Rosa appealed the first instance decision.

Court of Appeal decision

The Court of Appeal unanimously dismissed the appeal, and held that Mr La Rosa was liable for the damage caused to the drill rig because he had failed to discharge the onus of proving that the damage was not caused by want of care on his part.

Factors relevant to incorporation of terms

The Court of Appeal held that the exclusion clause had not been incorporated into the cartage contract by the previous course of dealings between the parties, so Mr La Rosa's liability was not excluded. The Court noted that there are several factors to be considered when determining whether a term has been incorporated into a contract as a result of prior dealings:

- Whether, from the prior conduct of the parties as a whole, an inference can be drawn of an acceptance of, and readiness to be bound by, the terms on the reverse of the invoices.
- It is not essential that the term in issue has been incorporated in a previous contract between the parties, whether by a contractual document or otherwise.
- There must have been sufficient notice to Nudrill of the terms on which Mr La Rosa would do business in the future.
- While actual knowledge of the content of the terms and conditions may be sufficient to justify an acceptance of, and readiness to be bound by, the conditions on the reverse of the invoice, it is not essential.

Having regard to these factors, the Court concluded that the facts did not support an inference that the exclusion clause was incorporated in the cartage contract as a result of the prior dealings between the parties because:

- each invoice was sent to Nudrill after delivery, i.e. after the contract had been performed. The purpose of the invoices was to secure payment for those services, and in the circumstances, a reasonable person in Nudrill's position would not have expected to find contractual terms in relation to the completed work in the invoice;
- the trial judge had not found that any of Nudrill's representatives had actual knowledge of the existence of the conditions or had read them, and Mr La Rosa had not challenged the absence of such a finding; and
- Mr La Rosa had given insufficient notice to Nudrill of the terms and conditions on the reverse of the invoices on which he would do business in the future. While the timing of notification was not necessarily the determinative factor, what Mr La Rosa needed to do was demonstrate that the exclusion clause had come to be accepted and treated as contractual by conduct. He did not successfully do so.

Buss JA held that the relevant course of conduct between Mr La Rosa and Nudrill had been to contract orally without the incorporation of written terms, and the parties never departed from that course of conduct.

As such, the receipt of the invoices by Nudrill was not sufficient to establish Nudrill's acceptance to be bound by the terms on the reverse of the invoices.

Implications

This case highlights the importance of making sure parties acknowledge and agree to terms and conditions before the contract has been performed, especially where those terms have only been provided on the back of an invoice. An invoice issued after delivery will likely only serve as a demand for payment and will not necessarily be deemed to include any contractual terms and conditions.■

Never let the truth get in the way of a valid claim – a little white device rings alarm bells to hull underwriters

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In the recent case of ***Versloot Dredging BV SO DC Merwestone BV v HDI Gerling Industrie Versicherung AG & Ors*** [2013] EWHC 1666 (Comm), the English Court held that a *"fraudulent device"* completely deprived the claimant owners of an otherwise valid marine insurance claim. The Court determined that the owners had told an untruth about why water ingress had resulted in a fairly significant incident which nearly led to the total loss of the vessel. That untruth ultimately forfeited the owners' claim for indemnity.

Facts

The DC Merwestone (**the vessel**), owned by Versloot Dredging (**the owners**), was damaged during a journey from Lithuania when water got into the engine. Water had frozen in the -35ºC temperatures within the emergency fire pump and displaced the filter cap. This expanded and created holes, allowing water to enter the bowthruster room and causing severe damage to the engine, which had to be replaced. The owners submitted a claim to their hull and machinery underwriters (**the underwriters**) for the cost of repairs and replacement of the engine, which amounted to EUR3.2 million (equivalent to approximately A$4.6 million). The policy was on the Institute Time Clauses – Hulls 1.10.83 with the Additional Perils Clause.

The claim

The underwriters declined indemnity for the following reasons:

- the damage to the engine was caused by unseaworthiness, an uninsured peril;
- the owners knew the vessel was unseaworthy when the vessel set sail; and

- even if the claim was valid, the owners forfeited their claim by reason of a fraudulent device used when making the claim.

The owners subsequently issued proceedings in the English Court for indemnity in relation to the claim.

The owners argued that the claim was valid and they should be indemnified because the following proximate causes of the loss were covered under the policy:

- perils of the sea – prior to the vessel leaving the load port, the crew failed to properly drain the emergency fire pump, resulting in the pump cracking and the eventual water ingress. This meant that the ingress was fortuitous;
- crew negligence under the Inchamaree Clause in the policy; and
- repairers' negligence – repairs carried out to the pump in 2001 were inadequate.

Despite the underwriters arguing to the contrary, the owners also maintained that they had met their due diligence requirements under the terms of the policy.

The decision

Popplewell J held that although the proximate causes of the loss relied on by the owners were valid, the claim was precluded by a *"fraudulent device"* implemented by the owners.

Meaning of a *"fraudulent device"*

The underwriters argued that the owners had falsified information during the claims process, which then tainted the claim as a whole. The owners stated that a bilge alarm had sounded to alert the crew to issues with the expulsion of water, but was ignored because the vessel was experiencing rough seas. It subsequently came to light that the alarm had not sounded, nor had the Vessel experienced rough seas.

The Court referred to the long line of authorities which established that an insured who makes a fraudulent claim forfeits any lesser claim it could have made, even if there is no express clause in the policy.

Popplewell J noted the definition of *"fraudulent device"* provided by Mance LJ in ***Agapitos v Agnew*** [2003] QB 556 whereby a frauduent device is used if the insured *"believes that he has suffered the loss claimed, but seeks to improve or embellish the facts surrounding the claim, by some lie"*.[1]

In the insurance context, a fraud relates to an intentionally dishonest act or omission by either the insured or the insurer seeking to obtain a material advantage. A fraud often relates to the entire claim, whereas a fraudulent device is a negligent or dishonest statement which is intended to support an arguable claim.

How is the fraudulent device proven?

Referring again to Mance LJ's dicta in ***Agapitos v Agnew***, Popplewell J noted that the fraudulent device must be *"directly related to and intended to promote the claim"*.[2] As with a deceit, it may never be discovered by the insurer, but *"*[i]*t may lead for the case to be fought on a false premise, or the lie may lead to favourable settlement"*.[3]

Although he relied on the principles in ***Agapitos v Agnew*** to ultimately find that the claim should be forfeited, Popplewell J discussed whether forfeiture of the claim as a whole was appropriate.

He commented that *"not all fraud attracts the same moral obloquy"* and that it may be unreasonable to apply a *"draconian"* approach that vitiates all claims involving a fraudulent device. Popplewell J suggested a *"scale of culpability"*[4], as an alternative to the current test, which would be *"capable of operating to visit disproportionately harsh and unjust consequences ... in favour of an undeserving insurer"*.[5]

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1 At [150].
2 ***Agapitos v Agnew*** [2002] All ER (D) 54 (Mar) at [37] as per Mance LJ.
3 *Ibid*.
4 At [165].
5 At [167].

Popplewell J justified his view in light of other areas of civil law, where a fraud or exaggeration does not forfeit the claim entirely, but enables it to be apportioned for reasonableness (for example in exaggerated personal injury claims).

Ultimately, Popplewell J found a fraudulent device was sufficient to forfeit the claim, deeming it a *"reckless untruth, not a carefully planned deceit"*. His opinion was that it was a *"disproportionately harsh sanction"* and that he favoured the introduction of a materiality test permitting the court to consider *"whether it was just and proportionate to deprive the assured of his substantive rights taking into account all the circumstances of the case"*.[6]

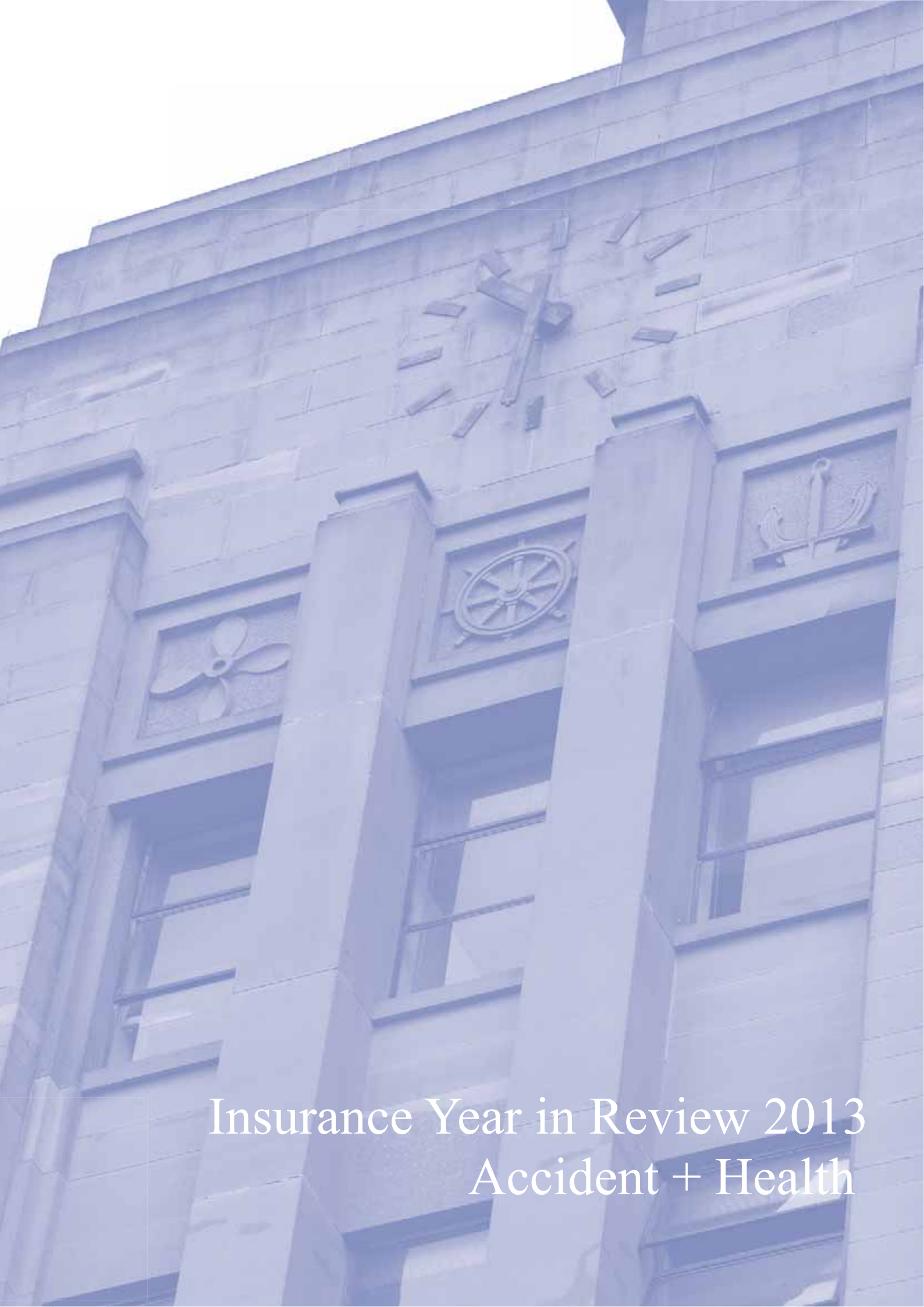
Commentary

In the Australian context, section 56 of the **Insurance Contracts Act 1984 (Cth)** (**ICA**) enables the court to apportion payments by insurers where forfeiture of part of a valid claim would be harsh and unfair. However, the ICA does not apply to marine insurance claims.

This decision is a warning to all insureds to carefully consider the reliability of information provided to insurers when reporting their claims, because even the most insignificant of untruths has the potential to forfeit the claim as a whole.

The decision has been referred to the Court of Appeal on the application of the fraudulent device rule. If the appeal is successful, it may result in the long-settled UK position on fraudulent devices being overturned. ■

6 At [171].



Insurance Year in Review 2013
Accident + Health

TPD or not TPD? That is the question

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On 20 March 2013, the New South Wales Court of Appeal delivered its decision in ***Hannover Life Re of Australasia Ltd v Dargan*** [2013] NSWCA (***Dargan***).

Background

Since leaving school in Year 11, Mr Dargan managed his parents' motel, and otherwise worked as a licensed truck driver and occasional labourer.

On 5 July 2007, Mr Dargan injured his lower back at work and was unable to continue in his occupation as a truck driver. At the time, he was working 40 hours per week. In June 2008, Mr Dargan obtained a certificate entitling him to drive a taxi, conditional upon him completing a training course. Mr Dargan completed the course and at the time of the proceedings was working as a self-employed taxi driver. It was common ground that he could only drive for 20 hours per week.

The insurance policy

This case revolved around a group life policy (**the policy**) held by Mr Dargan, of which United Super was the trustee and Hannover Life was the insurer.

The policy defined total and permanent disablement (**TPD**) as:

> *"*[TPD] *in respect of an Insured Person who is gainfully employed within the 6 months prior to the Date of Disablement and is where:*
>
> *The Insured Person is unable to follow their usual occupation by reason of an accident or illness for six consecutive months and in our opinion, after consideration of medical evidence satisfactory to us, is unlikely ever to be able to engage in any Regular Remuneration Work for which the Insured Person is reasonably fitted by education, training or experience."*

The next relevant definition is in respect of *"regular remuneration work"*, which the policy defined as follows:

> *"An Insured Person is engaged in regular remunerative work if they are doing work in any employment, business or occupation. They must be doing it for reward – or the hope of reward – of any type."*

At first instance

Gzell J concluded that as Mr Dargan had not been a taxi driver prior to his accident, and also given his need to obtain further training and a certificate in order to become qualified to work as a taxi driver, Mr Dargan did not have the education, training or experience required to be a taxi driver at the critical point in time.

Issues in the appeal

All parties had accepted that the relevant point in time to assess Mr Dargan's TPD was 6 months after the incident giving rise to the claim. It was also common ground that on that date, Mr Dargan was unable to work full time

and was capable of working as a part-time taxi driver. Lastly, it was common ground that the definition of TPD required the insurer to form an opinion as to whether Mr Dargan was unlikely to engage in *"regular remuneration work"* as defined in the policy.

The Court concluded that the need to undertake a training course to obtain a certificate does not preclude a person from being reasonably fitted for a particular occupation.

The Court observed that Mr Dargan was an experienced truck driver who was familiar with the rules of the road and the demands involved in driving commercial vehicles. It concluded that 6 months after the injury, Mr Dargan was capable of obtaining an ancillary certificate and completing the training course, which he ultimately undertook in 2008. It followed that at the time his capacity for employment was assessed, he was reasonably fitted to carry out the occupation of taxi driver, at least on a part-time basis.

The Court also observed that *"regular remuneration work"* only required that the insured person be capable of doing some form of part-time work for reward. It considered that approach consistent with the intent of the policy – namely, to provide benefits for TPD, not partial disablement.

Implications

This decision reminds us that when considering whether an insured person is reasonably fitted by education, training or experience, there is no strict obligation for the insured to have been specifically trained in that alternative employment. As always, the intent of the parties to the policy must be acknowledged and the Court has reminded us that TPD policies are designed to cover those with TPD rather than those who are partially disabled.

A subsequent decision

Chapman v United Super Pty Limited [2013] NSWSC 592 dealt with the same type of policy as was disputed in Dargan.

On 6 February 2007, Mr Chapman was working when he picked up a screwing machine weighing 50–60 kilograms. He injured his back. Mr Chapman then experienced 2 further injuries in the course of his employment, on 2 and 4 March 2007.

On 9 November 2009, the insurer rejected Mr Chapman's claim, which held medical evidence suggesting that Mr Chapman was capable of performing alternative employment as a spare-parts interpreter. There was also some suggestion that he could work as a check-out operator.

At trial, Mr Chapman gave evidence that he was not particularly successful in his former employment as a spare-parts interpreter and that there was little likelihood of him obtaining similar employment in the future.

Young ACJ indicated that ***Dargan*** makes it clear there is no bar to finding that work is within an insured person's education, training or experience, even if a short qualifying course, training or retraining may be required.

Notwithstanding that, His Honour agreed with Mr Chapman's evidence that he probably was not suited to working as a spare-parts interpreter, and was willing to accept that with some retraining, Mr Chapman could work as either a check-out operator or taxi driver.

Young ACJ noted that the onus was on Mr Chapman to show that he could not perform any part-time work. In His Honour's opinion, Mr Chapman had not demonstrated that there was no employment at all that he could reasonably undertake.

Comment

Young ACJ followed an almost identical line of reading as that set out by the NSW Court of Appeal in ***Dargan***. It is now clear that when examining a clause that requires an insurer to consider employment for which an insured person might be reasonably fitted by education, training or experience, it is permissible to consider employment options that require brief additional training or qualifications. ■

Insurance Year in Review 2013
Pro Bono

Community Footprint – a year in review

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In 2012, Wotton + Kearney (**W+K**) formally launched the firm's pro bono and corporate social responsibility (**CSR**) program, *"Community Footprint"*. Since then, the firm has dramatically increased its involvement in pro bono and CSR projects, and made a significant contribution to the work of charitable organisations in Australia and overseas. For example, in the 2012/13 financial year:

- 21 lawyers (25% of legal staff) worked on pro bono matters, almost twice as many as the previous year; and
- legal staff dedicated 882 hours to Community Footprint, compared to 487 hours the previous year.

Justice Connect

The firm's key pro bono partnership is with Justice Connect, previously known as the Public Interest Law Clearing House.

Offshore Asylum Seeker Project

One of the programs run by Justice Connect is its Offshore Asylum Seeker Project, providing assistance to people in immigration detention in Australia who have received a negative Independent Merits Review and are entitled to judicial review of that decision. W+K has played an integral role in the project since its inception.

Since 2011, the project has provided representation for 120 individuals. In the past year W+K has represented 13 individuals in their claims for judicial review. Without lawyers agreeing to act pro bono, these individuals would be without recourse to legal representation and proper protection of their human rights.

Working on these matters presents a number of challenges, particularly language barriers and the sensitive and highly charged nature of matters where an individual's safety and wellbeing may be at risk. One of the highlights of the firm's work with the project was the victory for *"Mr S"*, a Tamil man from the north of Sri Lanka who had fled his home due to political unrest and fear for his own life. W+K assisted Mr S with a successful judicial review application and successfully defended an appeal by the Minister of Immigration and Citizenship.

NGO Works Project

W+K also played an active role in Justice Connect's NGO Works Project, providing legal advice and assistance to not-for-profit organisations that offer important non-legal services to vulnerable, disadvantaged and marginalised people within the community. The project helps address issues of public interest and importance through awareness, advocacy and education.

Among other matters, the firm:

- provided advice on the extent of the liability faced by directors of not-for-profit organisations when discharging their duties as directors; and
- assisted a community organisation that provides medium-term accommodation for homeless women who have survived childhood sexual abuse, with its defence of a claim in the Consumer, Trader & Tenancy Tribunal.

MOSAIC Advice Clinic

Since July 2013, W+K has seconded a lawyer from the Sydney office to a Justice Connect–operated clinic that provides general legal assistance and advocacy to newly settled migrants.

Natural Justice Project

Through Justice Connect's Natural Justice Project, W+K is developing a step-by-step guide that assists Forgotten Australians and members of the Stolen Generation to access their government records in NSW, and their federal records where applicable. In addition to developing the guide, the firm is providing direct assistance to clients to help them obtain documents.

Other projects with Justice Connect

W+K has also partnered with Justice Connect by:

- participating in the annual *"Walk for Justice"*, which aims to increase public awareness of the unmet legal needs in our community, raise funds to support Justice Connect and boost the profile of pro bono legal services; and
- hosting a seminar entitled *"News from Nauru and Messages from Manus"*, with a panel consisting of the Senior Protection Officer at the United Nations High Commissioner for Refugees Regional Office in Canberra, the President of the Australian Human Rights Commission, and barristers and solicitors representing asylum seekers on Nauru.

Developing a pro bono program in Melbourne

On 1 July 2013, W+K's Melbourne office also became a member firm of Justice Connect. This exciting partnership will provide additional opportunities for staff to get involved in a wide range of pro bono projects.

The Melbourne office has already taken on its first project, aimed at helping eligible incorporated associations have their rules reviewed and updated to ensure compliance with the **Incorporated Associations Reform Act 2012 (Vic)**.

CSR Initiatives

Partnership with Royal Far West

Royal Far West is an independent charitable organisation that provides non-acute health and community development services for children living in rural and remote NSW. W+K has committed to a 12-month reciprocal partnership with Royal Far West, providing a range of opportunities for W+K staff to make a positive contribution to the organisation's work.

In March 2014, W+K will participate in a Ride for Country Kids – a 3-day bicycle ride from Dubbo to Wagga Wagga, travelling roughly 150 kilometres per day. Two teams of 4 W+K cyclists will join 4 other teams, with the aim of raising over $50,000 for Royal Far West. Royal Far West will use the funds raised from the ride to renovate and repair Drummond House. Drummond House provides secure home-style accommodation for families while their children attend medical appointments

at Royal Far West, enabling families to stay together and support each other during a difficult time.

Other CSR initiatives

Over the past year W+K supported a number of other organisations, including:

- **Lou's Place Women's Refuge**. Staff members from the Sydney office make regular donations of clothes, office supplies and toiletries;
- **The Smith Family Toy & Book Appeal**. For Christmas 2013, employees from our Melbourne and Brisbane offices donated gifts of toys and books to The Smith Family (the Sydney office donated gifts to Royal Far West);
- **Cancer Council and the Royal Society for Prevention of Cruelty to Animals (RSPCA)**. Employees participated in the Cancer Council's Biggest Morning Tea and the RSPCA's Cupcake Day, baking treats for their colleagues to enjoy in exchange for a donation to each charity; and
- **Planet Ark recycling**. W+K donates all used printer cartridges to Planet Ark for recycling and reuse in a range of products. ■

A lawyer's experience of a pro bono legal secondment

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Background

MOSAIC (Migrant Outreach Service Advice, Information and Community Education), is a new initiative of Justice Connect that provides free legal services to recently arrived migrants, asylum seekers and refugees. A free, weekly face-to-face legal clinic is at the heart of the MOSAIC project.

The legal clinic relies on pro bono legal assistance from the private legal profession, and Wotton + Kearney (**W+K**) is proud to have Heidi Nash-Smith, Special Counsel and Pro Bono Coordinator, and Amanda Cefai, Solicitor, volunteering their time and services as MOSAIC clinic lawyers.

Specialised legal training

Early in 2013, Heidi and Amanda received specialised legal training in areas that commonly affect MOSAIC's disadvantaged and vulnerable clients, and that are often complicated by the need to overcome language barriers. This training covered the legal aspects of acting in disputes involving Centrelink entitlements, debt relief, rental accommodation and traffic infringements. It also focused on the special allowances available to disadvantaged and vulnerable clients, and how to recognise the sensitive issues affecting clients who have survived torture, trauma and domestic violence.

The legal clinic opened its doors to clients on 9 July 2013, and Amanda was delighted to represent the W+K team on the opening day. It was inspiring to see the great reception the clinic received; a large group of people from a local migrant community dropped by – not necessarily because they needed legal advice but to share their excitement at hearing about the service, and to meet and thank the people who had made it possible.

A special case

During the MOSAIC clinic's short time in operation, the W+K team has already had the opportunity to see its unique ability to offer clients a high-quality, holistic service.

The team was especially touched by one client who came into the clinic in tears. She was an Ethiopian national staying in Australia on a tourist visa that would soon expire. She was living in crisis accommodation and had recently endured the unexpected death of her husband, who was an Australian citizen working for the United Nations. Her finances were tied up in a lengthy intestacy application (as her husband had died without a will) and she was unable to transfer her overseas assets to Australia until

her Australian visa status had been clarified. While she had been happy to live with her husband in Africa prior to his death, it was no longer possible for her to return there as a single women as she had been disowned and physically abused by her family for marrying a foreigner. Amanda, with assistance from Heidi and the MOSAIC staff, worked with the client over a number of days to:

- liaise with her case worker to ensure that her immediate accommodation needs and her son's education needs were being adequately attended to;
- research her entitlement to Centrelink benefits, which was limited because of her visa status;
- lodge an urgent Intent to Claim notification with Centrelink, so her entitlements would be back-dated to the date she first attended the MOSAIC legal clinic;
- attend Centrelink with her to ensure the correct claim was lodged and to assist her in filling out the lengthy forms and applications;
- liaise with MOSIAC partners – from the Metro Migrant Resource Centre and Refugee Advice & Casework Service – who arranged for a licensed migration solicitor to provide advice on her visa application; and
- act as a facilitator with her private regional solicitor, who – although he was acting in good faith on her behalf in the intestacy application – had corresponded with and sought his instructions from the husband's family because the client's English was limited. This had left the client confused about the status of the proceedings and suspicious that the lawyer or the family may have been taking advantage of the situation.

Although at first it seemed that the client would need extensive and ongoing legal assistance from the clinic, she was in fact able to walk away from the clinic confident about the direction of her visa application, her immediate accommodation needs, her short-term Centrelink entitlements and the expected finalisation of her intestacy application. That all this could be achieved by attending the MOSAIC clinic – and being provided with a lawyer who had the skills to navigate the different systems and the time to clarify the various issues on her behalf – is a testament to the value of the MOSAIC project.

Final thoughts

As lawyers who have spent the majority of their careers acting for corporate clients in complex civil proceedings, it is extremely rewarding for Heidi and Amanda to use that knowledge and skill to provide quality legal advice and assistance to the vulnerable members of the community who could not otherwise afford or access such assistance, and to witness the direct positive impact on their lives.

Wotton + Kearney's pro bono work in practice: *SZRZM v Minister for Immigration & Border Protection*

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Introduction

Since August 2011, Wotton + Kearney (**W+K**) has been involved in Justice Connect's Offshore Asylum Seeker Project, providing pro bono legal assistance to people in immigration detention in Australia who have received a negative Independent Merits Review (**IMR**) and are entitled to judicial review of that decision.

On 28 November 2013, Nicholls J delivered judgment in ***SZRZM v Minister for Immigration & Border Protection*** [2013] FCCA 2018 (***SZRZM***), one of the matters in which the firm has acted. The case raised interesting legal issues concerning the application of the *"complementary protection"* criterion in the **Migration Act 1958 (Cth)** (**the Act**).

What is complementary protection?

Complementary protection was introduced by the **Migration Amendment (Complementary Protection) Bill 2011 (Cth)** to give effect to certain of Australia's international obligations under the **Convention against Torture and Other Cruel, Inhuman or Degrading Treatment or Punishment**, the **International Covenant on Civil and Political Rights** and the **Convention on the Rights of the Child**. The relevant provision is contained in section 36(2)(aa) of the Act and reads:

> *"A criterion for a protection visa is that the applicant for the visa is: …*
>
> *(aa) a non-citizen in Australia ... in respect of whom the Minister is satisfied Australia has protection obligations because the Minister has substantial grounds for believing that, as a necessary and foreseeable consequence of the non-citizen being removed from Australia to a receiving country, there is a real risk that the non-citizen will suffer significant harm."*

"Significant harm" includes:

- the arbitrary deprivation of life;
- having the death penalty carried out;
- being subjected to torture;
- being subjected to cruel or inhuman treatment or punishment; or
- being subjected to degrading treatment or punishment.

Complementary protection allows asylum seekers processed in Australia on or after 24 March 2012 to claim protection on broader grounds than those contained in the **United Nations Convention Relating to the Status of Refugees** (**Refugees Convention**). Prior to

March 2012, Australia was unable to guarantee that people who did not meet the definition of *"refugee"* in the Refugees Convention[1] – but who would nonetheless face serious human rights abuses if returned to their country of origin – would be granted protection.

One of the issues considered in ***SZRZM*** was whether the Minister for Immigration, through his delegates, had adequately and correctly considered our client's claims for complementary protection.[2] Nicholls J found in our client's favour that:

- our client was denied procedural fairness because he had not been given any opportunity to be heard on the question of his complementary protection claims; and
- the process by which our client's complementary claims were considered was affected by legal error.

Factual background

Our client (**the applicant**) is an Iranian citizen who arrived in Australia in October 2010 as an *"irregular maritime arrival"*. He applied for a Refugee Status Assessment (**RSA**) soon after, on the basis that he could not return to Iran because:

- he would be detained and tortured because of his political opinion; and
- he might be subject to religious persecution due to his non-belief in Islam.

The applicant's RSA application was unsuccessful and in May 2011 he sought an IMR.[3]

On 10 October 2011, the IMR recommended that the applicant should not be recognised as a person to whom Australia has protection obligations under the Act. At that time the reviewer was tasked with considering the applicant's claims to protection only under the Refugees Convention, as the complementary protection regime was not yet in force.

In November 2011, the applicant's migration representative submitted further documents to the Minister's department and sought to have the IMR *"reconsidered"*.

The applicant was assessed in respect of the complementary protection provisions in August 2012. This assessment was conducted on the papers, and the outcome was reported in a departmental minute. Relevantly, the departmental assessment stated that *"no further claims and no new or additional information personal to* [the applicant] *has been provided"* and *"there have not been any changes to* [the applicant's] *circumstances ... since his IMR was finalised"*. Therefore, the departmental officers found that:

> *"… in the absence of any new evidence or information to indicate that he is of adverse interest to non-state actors or authorities in Iran, I find there is no real risk he would be subjected to significant harm, as a necessary and foreseeable consequence of his return to Iran."*

The applicant claimed that the Minister could not lawfully act on the basis of the departmental assessment because:

- it applied the wrong standard of proof when assessing whether the Minister could have *"substantial grounds for believing"* that the applicant would be arbitrarily deprived of his life;
- it was made by a process that denied the applicant procedural fairness as he was not given any opportunity to be heard on the questions relevant to the assessment of his

1 A refugee is someone with a well-founded fear of persecution for reasons of race, religion, nationality, membership of a particular social group or political opinion.

2 There were other grounds of judicial review in addition to our client's complementary protection claims. Those grounds are outside the scope of this article.

3 During the IMR process, the applicant raised additional claims for protection.

claims under complementary protection; and
- it was made by a process that applied the incorrect test at law to his claims for complementary protection.

The Minister did not deny the asserted legal error in relation to the first and third grounds above, but argued that the Court should not exercise its discretion to grant the relief sought.

Denial of procedural fairness

The applicant submitted that he was not given an opportunity, in person or in writing, to put his claim under complementary protection. Nicholls J agreed, finding that:

- the failure of the departmental officers to afford the applicant a specific interview or hearing did not necessarily of itself reveal some failure of procedural fairness. An oral hearing is not necessarily required in every case – it depends on the circumstances of each case and, in particular, the extent to which the assessment relies on an issue of credibility;
- the relevant procedural fairness obligation extended to the applicant being given the opportunity to present his case in relation to the subsequent departmental assessment affecting him. He had the right to be told the substance of the case to be answered and given the opportunity to respond to it;
- the submissions the applicant's migration representative provided in November 2011 did not address complementary protection; they preceded the date the complementary protection regime came into force by about five months; and
- in all the circumstances, the applicant was denied the opportunity to be heard (even in writing) in relation to his complementary protection claims.

Incorrect test at law and wrong standard of proof

In support of these grounds, the applicant relied on what was relevantly said by Lander and Gordon JJ in Minister for Immigration and ***Citizenship v SZQRB*** [2013] FCAFC 33 (***SZQRB***):

> *"In our opinion, the test is as for s36(2)(a) and as stated by SZQRB – is there a real chance that SZQRB will suffer significant harm (as that is defined in s 36(2A)) were he to be returned to Afghanistan"*

In other words, the applicant submitted that, following the Full Federal Court decision in ***SZQRB***, the test as to whether there is a real risk of *"significant harm"* (with reference to the complementary protection criterion) is the *"real chance test"*, as provided under the Refugees Convention.

The departmental assessment in ***SZRZM*** contained the following statement:

> *"The threshold for establishing a real risk of significant harm, as required by the Complementary Protection provisions of the Migration Act, is a higher threshold than the real chance test of the Refugees Convention."* (Emphasis added)

Nicholls J noted that the departmental officers applied a *"more likely than not"* test, which, as was found in ***SZQRB***, is the wrong test.

However, the Minister submitted that the Court should not exercise its discretion to grant relief in favour of the applicant because:

- no disadvantage or detriment flowed to the applicant in the failure to apply the ***SZQRB*** standard for assessing the *"real risk of significant harm"*; and
- the applicant had not identified any aspect of the findings to show that applying the correct test or standard could have led to a different outcome.

The applicant submitted, and Nicholls J agreed, that where there has been a failure to apply the correct legal test or standard required by law, the Court's decision to exercise or refuse to exercise its discretion must be held to a very high standard, given the public interest in requiring administrative decision makers to conform to the law. The question for the Court was whether, in relation to the error, the grant of relief would be *"futile"* in the circumstances – that is, if the correct legal test and standard had

been applied it could not have led to a different outcome. Ultimately, Nicholls J found that it could not be said in this case that a different outcome could not be achieved, such that to grant the relief would be an exercise in futility. Therefore, the ground of review was upheld.

Outcome

As a result of Nicholls J's findings regarding our client's grounds for complementary protection, the Court:

- declared that the departmental assessment was not made in accordance with the law; and
- ordered an injunction restraining the Minister, by himself or his delegates, from relying upon the departmental assessment.

Our client's claims for complementary protection will now be referred back to a decision maker to be considered in accordance with the law. The Court has not granted our client a protection visa – that is outside the scope of the judicial review process.

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