

By Ray Giblett and Greg Moss

Courts lower the bar on insurance 'claims'



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A number of recent decisions have considered what constitutes a 'claim', both as against an insured and under a policy. The trend in these cases has been to lower the bar so as to allow claims against the insurer to proceed.

The recent decision of the NSW Supreme Court in *Eastern Creek Holdings Pty Ltd v Axis Speciality Europe Ltd* [2010] NSWSC 840 has highlighted the difficulties insurers face when resisting an application for leave to commence proceedings against them under s6(4) of the *Law Reform (Miscellaneous Provisions) Act 1946* (NSW) (the Act).

WHAT WENT WRONG?

In August 2006, Eastern Creek Holdings Pty Ltd as principal (the plaintiff) entered into a design and construction contract with Seana Constructions Pty Ltd (Seana) for development of the Chifley Hotel in Eastern Creek, NSW.

Seana was insured under a professional indemnity insurance policy, underwritten by Axis Speciality Europe

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(the defendant). The schedule to the policy described Seana's professional business as project/construction managers.

The policy period was from 11 September 2007 to 11 September 2008. The works were carried out during this time and were completed on or about April 2008. The policy provided:

'We agree to indemnify the insured against legal liability for any claim first made against the insured during the period of insurance and notified to us during the period of insurance for breach of professional duty arising from any act, error or omission ... committed or allegedly committed by the insured in the conduct of the professional business ...

[cl 1.1]

"Claim" shall mean:

the receipt by the insured of a demand for compensation made by a third party against the insured. It must take the form of:

...

(b) any other form of written or verbal notice.' [cl 6.1]

On 2 September 2008, the plaintiff gave the following written notice to Seana:

'This letter is to inform you that the principal (Eastern Creek Holdings) has become aware of significant design defects in respect of the Chifley Hotel, Eastern Creek.

These design defects may result in the principal suffering damages in the future, and as such the principal reserves its rights in respect of the contract, at equity and at law.'

In resisting the appeal, the insurer (QBE) argued that s34(1) had no application to a case where the insured did not make a claim under the applicable policy, and that s54(1) required the claim against the insurer to be made by the insured.

WHAT THE COURT SAID

With Seana in liquidation, the plaintiff sought leave under s6(4) of the Act (which creates a charge over insurance monies payable in respect of an insured's liability) to serve a statement¹ against the defendant. Section 6(4) of the Act provides:

'... no such action shall be commenced in any court except with the leave of that court. Leave shall not be granted

in any case where the court is satisfied that the insurer is entitled under the terms of the contract of insurance to disclaim liability ...'

What must the plaintiff establish?

The parties agreed that, to obtain leave, the plaintiff must show that there is:

- an arguable case against the insured;
- an arguable case that the policy responds; and
- a real possibility that if judgment is obtained, the insured would not be able to meet it.

The defendant accepted that the plaintiff had satisfied the first and third requirements, but argued that the plaintiff had not satisfied the second.

Hammerschlag J explained that the plaintiff merely needed to show it is 'arguable that the policy responds'. Whether in fact it does so is a matter for the final hearing.

The defendant argued that the policy would not respond because:

- the policy responded only to claims arising from acts, errors or omissions committed by Seana in the conduct of 'professional business' (as defined in the schedule), and the alleged failings of Seana as pleaded did not arise in this context; and
- no claim was made against Seana and no circumstances were notified during the policy period.

Hammerschlag J noted that it was inappropriate to determine finally whether the conduct complained of in the originating process amounted to activities of 'professional business' as described in the schedule. His Honour explained:

'For present purposes it is sufficient, as it clearly is, that the activities of the Insured out of which the claim against it arise, are capable of being viewed as part of the conduct of carrying on the business of project/construction managers.'

In relation to the defendant's second submission, his Honour found that it was arguable that the policy on its wording responded and, accordingly, found sufficient grounds for leave to be given. His Honour explained that the defendant's argument was not one that the policy did not respond, but rather that the plaintiff had no arguable reply to a defence that may be used by the defendant in the future.

By deferring this consideration, his Honour has set the bar for a grant of leave exceedingly low.

What is a 'claim' against the insured?

Even if the plaintiff was required to provide an arguable reply to any such defence, his Honour found that it had done so.

His Honour noted that the 2 September 2008 letter did not constitute notice of a 'claim' against Seana. This should be contrasted with the recent decision in *Cassidy v Leslie* [2010] NSWSC 742, where the court, in considering a very similar email, found that the email amounted to a 'claim' (constituting an assertion of a right to compensation, whether or not that right was contingent or conditional), with s54 of the *Insurance Contracts Act 1984* (Cth) (the ICA) remedying late notification.

It will be interesting to see whether Hammerschlag J's finding is challenged on the basis of *Cassidy v Leslie* although

subtle differences in the respective definitions and demands may be critical. The definition of 'claim' in *Cassidy v Leslie* also included the 'assertion of a right' to compensation, in addition to a demand, and the relevant email stated that a claim would be made if certain criteria were satisfied.

His Honour further commented that s40(3) of the ICA precluded the defendant from being relieved of liability under the policy if the 2 September 2008 letter constituted notice in writing 'of facts that might give rise to a claim' against the defendant. This finding may not withstand scrutiny, as s40 refers to notice given in writing 'to the insurer' by the insured, whereas the 2 September 2008 letter was from the plaintiff to the insured.

His Honour also considered s54 of the ICA, determining that it was sufficient to say that this section may operate to preclude the defendant from refusing to pay the claim as a result of the omission by the plaintiff to notify circumstances within the policy period. Again, this finding seemingly ignores the decision in *Gosford Council v GIO General Ltd* [2002] NSWSC 511 that s54 does not rectify a failure of an insured to exercise the statutory right provided by s40 of the ICA.

What is a 'claim' under the policy?

Staying with s54 for a moment, in *Gorzynski v W&FT Osmo Pty Ltd* [2010] NSWCA 163, the NSW Court of Appeal recently considered whether a third party claimant was entitled to the benefit of s54(1) of the ICA where the insured had not made a claim or notified circumstances under a 'claims made and notified' policy. This question also arose in the context of an application by a third party to join the insurer to proceedings under s6(4) of the Act.

In resisting the appeal, the insurer (QBE) argued that s54(1) had no application to a case where the insured did not make a claim under the applicable policy, and that s54(1) required the claim against the insurer to be made by the insured. The Court of Appeal noted that the 'claim' to which s54(1) was directed was the 'claim' against the insurer, not a claim by a third party against the insured. Accordingly, a third party 'claim' on the insurance is a 'claim' for the purposes of s54 of the ICA.

QBE further noted that in respect of a 'claims made and notified' policy, the third-party claim must be made (or circumstances notified) within the time limits provided in the policy. However, their Honours noted that there was no such sequential requirement for making a claim against the insurer under s54(1).

Therefore, the court held that a 'claim' for the purpose of s54 was not limited only to one made by the insured, but extended to claims by third parties, including in the context of s6 proceedings.

This expansive approach may have significant implications for the rights of third party claimants on insurance policies (and therefore the exposure of insurers) in the future.

AND THIS MEANS?

The decisions briefly touched upon above demonstrate the court's willingness to utilise the elasticity of language so as

to allow claims against insurers to proceed. In particular, the meaning of 'claim' in a variety of contexts has been clarified.

The low threshold that a plaintiff is required to meet in an application under s6 of the Act also renders resiting a claim at this initial stage rather difficult.

Further, the decision in *Gorzynski* has broad implications. Although the insured had never made a claim (or notified circumstances), a third party was afforded the benefit of s54 (although the insurer succeeded on other grounds).

Future developments in these areas will be viewed with interest as the implications of these decisions filter through to a new generation of cases. ■

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Note: 1 Amended Technology and Construction List Statement.

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