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Due diligence condition not strong enough

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Handed down in March 2017, the decision of M*anitowoq Platinum Pty Ltd & Ors v WFI Insurance Ltd*[1] (**Manitowoq Platinum**) is of particular interest as the District Court of Western Australia considered whether an insured's breach of statutory obligations could form the basis to refuse indemnity under a Commercial Risk Policy. The case also looks at whether the leading Queensland case and related authority around *Kim v Cole & Ors*,[2] should apply.

Kim v Cole

Briefly by way of refresher, in *Cole* Wesfarmers Federation Insurance Ltd (**WFI**) refused to indemnify its insured due to its breach of one of the general conditions of the policy, namely to *'comply … with all statutory obligations, by-laws and regulations imposed by any public authority'.*

WFI submitted the actions of its insured in fitting a temporary gas valve which did not have a fail safe breached the *Gas Act 1985* (Qld),[3] the Gas Regulation 1989 (Qld)[4] and the Australian Standards for gas fitting (AG 601-1989). The Court of Appeal agreed the insured had a statutory duty to fit a gas valve that *'automatically, unattended, or by remote control shall fail safe'* and this in turn, meant WFI was correct in declining cover for breach of the above general condition.

Manitowoq Platinum

In the present case, two restaurant owners (**plaintiffs**) contracted with Boss Shop Fitting Pty Ltd (**insured**) to provide a fit out of their restaurant. After opening, the plaintiffs noticed there was significant water damage throughout their restaurant.

The plaintiffs made a claim against the insured, who sought indemnity from WFI Insurance Ltd (**insurer**).

Of interest was whether the insurer was liable to indemnify the insured pursuant to its policy of insurance; the insurer sought to deny the claim on the basis the general conditions of the policy were not met due to (amongst other things) the failure of the insured to *'comply with legislation and Australian standards'*.

There was no dispute at trial the insured's plumbing work was *'very poor'* and fell well short in many respects of Australian plumbing standards. The insured's requirement to comply with relevant Australian Standards (including AS 3500.1:2003 and AS 3500.4:2003) were embodied in legislation, namely regulation 47 of the Water Services Licensing (Plumbers Licensing and Plumbing Standards Regulations 2000).

Policy

The insured held a Commercial Plan Insurance Policy with the insurer which consisted of 18 different policies covering a wide range of risks. Of importance, the policy contained a due diligence condition which stated:

> *'Conditions which you must meet whilst you have the policy (if you don't meet these conditions we may be able to refuse or reduce any claim or cancel your policy).*
>
> *What you must do when you have a policy … you must:*
>
> > *… comply with legislation and Australian Standards. Australian Standards means standards published by the Standards Association of Australia.'*

Decision

Judge David found the most appropriate test for assessing a condition precedent to the liability of the insurer was the *'repugnancy rule'*. He explained the aim of the rule was to view the clause in the context of the specific risks covered so as not to *'construe a condition as repugnant to the commercial purpose of the contract'*.[5]

Judge David pointed out that the decision in *Cole* makes no reference to the repugnancy rule or to any of the key cases on the point, including *Casino Show Society v Norris*.[6]

He noted that each case in the line of authorities was determined on a consideration of its own facts and policy terms and therefore, the current case must be decided as such.

Despite the similarities in the wording of the clauses, Judge David distinguished the case of *Cole* as he found that when considering the clause in the context of the entire policy, the circumstances were dissimilar, particularly that the breach of standards in *Cole* was a more serious one, relating to safety.

He held that having regard to the natural and ordinary meaning of the general condition in this instance, read in light of the contract as a whole and giving weight to the context in which the clause appears, he was not

satisfied that a breach of this condition entitled the insurer to refuse indemnity for the claim.

He also held that it had not been made clear the common intention of the parties was to deny liability for a claim unless this condition was complied with. He stated that if the general condition was to override the terms of the insuring clause then this had to be made clear and on his view, it had not been, nor was it stated that compliance with that specific general condition was a condition precedent to the insurer's liability to indemnify.

He considered the term should be read down and construed to imply that the insured must *'take reasonable care to comply with legislation and Australian standards'*. By that standard, Judge David found the insured's actions did not meet the standard of *'reckless'* and therefore the insurer could not refuse indemnity on the basis of a breach of the general condition.

Conclusion

The polarity of these decisions shows that although the wording of a particular clause may appear similar to that of another policy, when reading the clause in context of the policy and particularly by reference to the seriousness of an insured's actions in every given case, the due diligence clause will produce a different outcome. Judge David reinforces the importance of a detailed consideration of the intention of the parties and the clause in the context of the policy overall. Judge David also it seems takes much from a consequential assessment of an insured's actions by reference to the seriousness of the outcome from a safety and public policy perspective, to inform if an insured's breach is sufficient to support a declinature on lack of due diligence grounds.

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[1] [2017] WADC 32.
[2] [2002] QCA 176.
[3] Section 61(1) and s 61.
[4] Section 80(2B), s 81(1) and s 100(1)
[5] *Fraser v BN Furman (Productions) Ltd* [1967] 3 AII ER [57, 60, 61]; *Albion Insurance Co Ltd v Body Corporate Strata Plan No 4303* [1983] 2 VR339; *Legal & General Insurance Australia Ltd v Eather* (1986) 6 NSWLR [390, 393].
[6] (1984) Aust Torts Reports 80 - 664.

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