Carter Newell LAWYERS

Insurance Newsletter

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A triumph for clear drafting – Court of Appeal refuses to imply a reasonable care standard to an absolute compliance condition

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Introduction

It is often argued that, where an insurance policy requires an insured to comply with a statute or Australian Standard, an insured need do no more than take '*reasonable care*' to comply. Our previous newsletter[1] discussed *WFI Insurance Ltd v Manitowoq Platinum Pty Ltd* [2018] WADC 89 where the implication of such a term was accepted. However earlier this year the Court of Appeal in *WFI Insurance Ltd v Manitowoq Platinum Pty Ltd* [2018] WASCA 89 overturned that decision finding that, in the context of the policy in question, absent express words, it was not reasonable or appropriate to imply a reasonableness standard.

Background

Manitowoq Platinum Pty Ltd (**Manitowoq**) contracted with Boss Shop Fitting Pty Ltd (**Boss**) for the fit-out of Manitowoq's restaurant. Shortly after the restaurant began operating, Manitowoq noticed water damage to various parts of the premises. Boss carried out repairs, however it was unable to determine the cause and extent of the problem.

A building inspector subsequently determined the water damage arose from plumbing work undertaken by Boss during the fit-out which was performed negligently and in breach of various Australian Standards.

Manitowoq rectified the plumbing works and commenced proceedings against Boss to recover the cost of those works. Boss subsequently went into liquidation and was deregistered, and Manitowoq commenced proceedings against Boss' insurer, WFI Insurance Limited (**insurer**), pursuant to s 601AG of the *Corporations Act 2001* (Cth).

The insurer did not contest Boss' liability, but denied the policy responded on the basis that Boss had breached a condition which required it to '*comply with legislation and Australian Standards*' (**condition**). The same section of the policy noted that '*[I]f you do not do what you are obliged to do under the policy, [the insurer] may refuse to pay a claim or any part of it*'.

At first instance, the trial judge construed the condition as being limited to an obligation to take reasonable care to comply with legislation and Australian Standards, and would only be breached if the failure to comply was reckless. It was also held that a failure to comply with the condition would not entitle the insurer to refuse indemnity under the policy. The insurer appealed.

Court of Appeal's decision

In reversing the decision at first instance, the Court of Appeal critically considered the various decisions relied on by the trial judge in support of her decision. We consider each of those briefly below.

Casino Show Society v Norris (1984) 3 ANZ Ins Cas 60-580

In *Casino*, the relevant condition required the insured to '*take all reasonable precautions to ... comply ... with all statutory obligations ... or regulations imposed by any Public Authority in respect thereof for the safety of persons or property*'. The insured claimed indemnity for liability incurred when an entertainment ride, which had not been properly erected in accordance with relevant regulations, tipped over while operating, causing injury.

The New South Wales Court of Appeal rejected the insured's assertion that the condition was repugnant to the commercial purpose of the insurance contract, and held that the insurer was entitled to deny indemnity because the insured had failed to take all reasonable precautions to comply with the relevant regulations.

Kim v Cole [2002] QCA 176

In *Kim v Cole*, the relevant condition required the insured to '*comply ... with all statutory obligations, By-laws and Regulations imposed by any Public Authority*'. The insured claimed indemnity for liability incurred when an explosion resulting from the insured's failure to install a valve for an oven as required by regulation caused property damage.

The Queensland Court of Appeal unanimously held that the insurer was entitled to deny indemnity because the relevant condition was not qualified by the obligation to '*take all reasonable precautions*' or to '*take all reasonable measures*', being qualifications expressly applied to other conditions within the relevant clause. The Court of Appeal was not prepared to construe the obligation to comply '*with all statutory obligations ...*' as imposing only an obligation to take reasonable steps to comply with such obligations.

Buckley v Metal Mart Pty Ltd [2008] ACTSC 79

In *Buckley,* the policy contained a clause headed '*Reasonable Care*'. The clause contained five separate obligations, only one of which was qualified by the requirement that the insured '*take all reasonable precautions*'. One of those obligations not expressly qualified (other than by the heading to the clause) was the obligation to '*comply with ... all laws, by-laws, regulations and recognised standards for the safety of persons or property*'.

The insured claimed indemnity for liability incurred when an employee was injured. The insurer denied indemnity on the basis that the injury was caused by the failure of the insured to ensure that its employees held the required certificate of competency to operate the forklift involved in the accident.

The insurer submitted that the principle of repugnancy did not apply because the obligation to comply with all relevant regulations was unqualified by the obligation to take reasonable precautions and was therefore absolute in nature.

The court rejected the insurer's position, concluding that all of the obligations within the clause, including the obligation to '*comply with all laws, by-laws, regulations and recognised standards ...*', should be construed as being qualified by an obligation to '*take all reasonable precautions*' followed by the application of the principle of repugnancy where liability is only established in the event of recklessness.

Victorian WorkCover Authority v Concept Hire Ltd [2009] VSC 194

In *Concept Hire*, the Victorian WorkCover Authority (**VWA**) denied that it was liable to indemnify an employer insured under a liability insurance policy because of the employer's breach of a policy condition requiring it to comply at all times with the provisions of the *Occupational Health and Safety Act 1985* (Vic). Section 21(1) of that Act imposes an obligation upon all employers to:

> *'... provide and maintain so far as is practicable for employees a working environment that is safe and without risks to health.'*

The court rejected VWA's position observing it is almost inevitable that in any case in which an employee succeeds in a claim in negligence against their employer, s 21(1) of the Act will have been breached. As such, construing the policy condition as requiring compliance with that provision would defeat the purpose of the policy.

The court expressed the view that the condition should be construed as qualified by the obligation to take '*reasonable precautions*' and that the condition, so qualified, should be construed in the same manner as conditions qualified by such an obligation - that is, as only applying to reckless conduct.

Barrie Toepfer Earthmoving and Land Management Pty Ltd v CGU Insurance Ltd [2016] NSWCA 67

In *Barrie Toepfer Earthmoving,* the relevant condition, headed '*reasonable care*', required that:

> '*You and any person acting on Your behalf must exercise reasonable care and precautions to prevent loss or damage to the Motor Vehicle, and to comply with all statutory obligations and by-laws or regulations imposed by any public authority for the safety of the Motor Vehicle ...*'

The insurer contended that the qualification relating to the exercise of '*reasonable care and precautions*' only applied to the obligation of preventing loss or damage to the motor vehicle and did not apply to the obligation to comply with all statutory obligations and by-laws or regulations.

The New South Wales Court of Appeal rejected that contention on the basis of the wording of the clause. Meagher JA observed that the heading formed part of the policy and should be taken into account as a general description of the provision which followed.

Court of Appeal's explanation

To the extent that the decisions relied on by the trial judge were relevant, the Court of Appeal indicated that *Casino* and *Kim v Cole* supported the insurer's arguments; the clause in the former case being expressly qualified by a '*reasonable precautions*' standard, whereas the clause in the latter containing an unqualified absolute obligation. As the balance of the cases considered clauses which were variously although differently qualified by a reasonableness obligation, those cases did not assist in construing the clause in question.

The Court of Appeal then turned to the express words of the condition, noting that the obligation to comply with legislation and Australian Standards was unqualified, in the context of a clause where two other obligations were expressly qualified by an obligation to take reasonable care. The Court of Appeal indicated that factor strongly suggested a construction that was not qualified by those words. It was therefore prepared to adopt that construction unless to do so would negate the commercial purpose of the policy.

In relation to the commercial purpose, the court noted that, while the policy provided cover for the insured's liability for personal injury or property damage, it expressly excluded the cost of doing, re-doing, completing correcting or improving any work done for or on behalf of the insured. Therefore construing the policy as a whole, the Court of Appeal considered excluding liability which fell below the relevant standards was consistent with the exclusion relating the quality of workmanship. In reaching that conclusion, the Court of Appeal rejected an argument that the construction would deprive the policy of a commercial meaning, providing various examples where cover would be available for negligent acts other than failures to comply with quality of workmanship.

Accordingly, the Court of Appeal rejected the trial judge's construction, finding that there was no basis to limit the operation of the condition to an obligation to take reasonable care to comply with legislation or Australian Standards.

As it was not disputed that the work did not meet the relevant standard, the subsequent question was whether breach of the condition entitled the insurer to decline cover. This issue was dealt with in short order. Having found that the relevant breach was causally related to the loss (and therefore subject to s 54(2) of the *Insurance Contracts Act 1984* (Cth)), the Court of Appeal held that, as the relevant section of the policy provided that '*[i]f you don't meet these conditions we may be able to reduce any claim or cancel your policy*', such terminology was entirely consistent with a construction where a failure to comply with the condition entitled the insurer to deny cover. In so doing, the Appeal Court expressly rejected the trial judge's apparent distinction between '*serious*' and '*less serious*' breaches.

Conclusion

The Court of Appeal's decision is a positive one for insurers. It follows a recognised approach which considers the express terms of a policy wording against the policy as a whole. It emphasises that where the words used impose an absolute obligation, then provided that obligation is not wholly repugnant to the commercial purpose of the policy, the parties should be held to their bargain without fear that it might be watered down by implied standards of '*reasonable*' compliance. The decision also highlights the importance of the role the precise wording plays in any subsequent indemnity disputes between insurers and insureds, and that except in the most clear cases, decisions on similar but not the same wording must be approached carefully.

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[1] '*Due diligence condition not strong enough*' Carter Newell Insurance Newsletter, April 2017.

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Two new appointments for Sydney

Carter Newell Lawyers is pleased to announce the recent appointment of two lawyers to its Sydney Insurance team. **Julie Bowker**, Special Counsel and **Matthew Algie**, Associate have joined the firm.

Julie is an experienced insurance lawyer having practiced in England prior to moving to Australia six years ago. With a focus on professional indemnity, Julie's experience also extends to property damage, construction and public and product liability claims. She has acted in number of significant property and fire losses.

Matthew also brings some international experience to the firm and is focused on general liability disputes and professional negligence claims involving the health profession.

Carter Newell Sydney Partner, Michael Bath stated, '*It is with great pleasure we welcome Julie and Matthew to the Sydney team. As the firm's eastern seaboard practice grows, the addition of these experienced lawyers enables us to continue to deliver strong results for our clients*.'

The new appointments for Carter Newell's Insurance division highlight the firm's growth in this specialty area.

Carter Newell welcomes Julie and Matthew to the team.