Aspects of Australian Insurance & Reinsurance Law:

the Insurance Contracts Act 1984 (Cth)
the decision in HIH v Wallace

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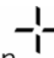


1. An introduction to this paper: a tale of two Acts

This paper is intended to provide a detailed introduction to two important areas that insurance professionals in the London market should be aware of when dealing with Australian insurance and reinsurance risks.

Part one of the paper deals with the federal *Insurance Contracts Act 1984* (Cth). This extremely consumer-friendly piece of legislation places very significant limitations on the way in which an insurer may exercise its rights to refuse or reduce a claim or to avoid, cancel or vary a policy.

The second part of this paper focuses on a recent reinsurance decision, *HIH Casualty & General Insurance Limited (in liquidation) v Wallac*e. This is an important case for reinsurers to be aware of since it enables reinsureds to commence proceedings in New South Wales to take advantage of previously overlooked, but highly favourable state legislation, the *Insurance Act 1902* (NSW). As a result, reinsurance law in New South Wales is currently out of step with the law in all other Australian states as well as England and Wales.

Part One: The Insurance Contracts Act 1984 (Cth)

2. Introduction to part one

The *Insurance Contracts Act (Cth)* 1984 (**Act**) is one of the fundamental pieces of Australian legislation dealing with the rights and obligations of insurers and insureds in relation to general contracts of insurance. It covers various issues ranging from the parties' pre-contractual negotiations, to the handling of claims and cancellation of policies. Certain provisions of the Act override the parties' rights and obligations which would otherwise exist under the contract and at common law.

The purpose of Part 1 of the paper is to provide a general introduction to the Act. As this task is extremely broad, this paper will focus on some key provisions that are likely to be of relevance to liability underwriters. In particular, it examines:

- the scope of the Act;
- insurers remedies for non-disclosure and misrepresentation;
- notification of circumstances;
- restriction on insurers' rights to deny claims;
- double insurance;
- the restrictions on parties' abilities to contract out of the provisions of the Act, in particular, the effect of choice of law and choice of jurisdiction clauses on the operation of the Act; and
- the recent Federal Government review of the Act .

3. History of the Act

Prior to the enactment of the Act, Australian insurance law comprised a mixture of common law principles and Imperial, Federal and State legislation. In 1976, the Australian Law Reform Commission (***ALRC***) was directed to review the adequacy of the law concerning insurance contracts (excluding marine insurance, workers' compensation and CTP insurance) having regard to the interests of insurers, insureds and the public. In particular, the ALRC was directed to consider whether:

(a) the terms and conditions presently found in contracts of insurance operate unfairly;

(b) certain, and if so what, terms and conditions should be mandatory in contracts of insurance;

(c) certain, and if so what, terms now found in contracts of insurance should be prohibited;

(d) the practice of incorporating statements made in proposal forms into contracts of insurance provides an equitable basis of contract between the insurer and the insured;

(e) it should be mandatory for an insurer to supply a person seeking insurance written information as to the person's rights and obligations under the proposed contract;

(f) arbitration clauses in contracts of insurance are operating unfairly to the parties or are otherwise undesirable;

(g) the principles of the law of agency in pre-contractual negotiations should be modified to provide greater fairness to the insured.

Six years later, the ALRC published its report, namely the Australian Law Reform Commission Report No. 20 (the ***Report***). Annexed to the Report was a draft Bill incorporating the recommendations made by the ALRC in the Report. The draft Bill largely formed the basis of today's Act.

4. Recent review of the Act

In 2003, the Commonwealth Department of Treasury commissioned a review (**Review**) of the operation of the Act with a focus on whether the rights and obligations of insurers and insureds (including persons seeking insurance) under the Act continue to be appropriate. The Review Panel were directed to first review the operation of s54 of the Act and then to consider the remaining provisions of the Act. The Review Panel issued its final report on s54 on 18 November 2003 and on the remaining provisions in January 2005.

Finally, in February 2007, Insurance Contracts Amendment Bill 2007 (**the Draft Bill**)was released for public consultation. The final form of the bill is currently being drawn up and is not expected to be introduced into Parliament before this year's federal election. Overall, the proposed reforms represent a refinement, rather than an overhaul, of the Act.

This paper comments on the provisions of the Draft Bill where appropriate.

5. Which insurance contracts are caught by the Act?

5.1 Commencement of the Act

The Act commenced operation on 1 January 1986 (ie approximately 4 years after the Report was published) and, subject to a minor exception[1], prima facie applies to all "contracts of insurance" entered into after that date.

5.2 Excluded contracts

Section 9 of the Act provides that the following types of insurance contracts and proposed insurance contracts are not caught by the Act (unless otherwise provided by the Act):

- reinsurance;
- health insurance (ie insurance offered by a registered health benefits organisation under the *National Health Act 1953*);
- insurance by a friendly society or the Australian Trade Commission;
- marine insurance (ie insurance subject to the *Marine Insurance Act 1909*) other than insurance for pleasure craft[2];
- workers' compensation;
- CTP insurance;
- State or Territory insurance.

For completeness, it is noted that s9 of the Act also provides that ss37, 41, 58, 59, 60, 63, 69 and 74 do not apply to insurance contracts in relation to loss of an aircraft, or damage to the hull of an aircraft, as a result of war.

5.3 Bundled Policies

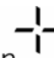
Some uncertainty exists in relation to how the Act should apply to contracts of insurance which combine 'excepted' insurance (ie insurance excluded from the operation of the Act under s9) and 'included' insurance (ie insurance which falls within the scope of the Act).

Moltoni Corporation Pty Ltd v QBE Insurance: In *Moltoni Corporation Pty Ltd v QBE Insurance Limited* (2001) 205 CLR 149*,* the High Court had to consider how the exception in s9(1)(e)(i) of the Act for workers' compensation insurance applied to a policy which insured an employer in respect to both its liability to indemnify an injured employee under the WA workers' compensation legislation and its liability at common law.

The Facts*:* The insured employer sought indemnity against its liability to the injured employee at common law. The insurer sought to decline indemnity on the basis of the insured employer's failure to provide the requisite notice of the employee's injury claim

[1] Section 4(2) of the Act extends ss32, 54 and 56 of the Act to certain type of superannuation contracts entered into prior to the commencement of the Act.

[2] Section 9A of the Act provides that contracts of insurance for pleasure craft are caught by the Act.



within the timeframe specified by the policy. The insured sought to rely upon s54 of the Act to overcome this failure[3].

At first instance, the trial judge held that the insurer was required to indemnify the insured employer because the insurer had not established that it had been prejudiced by the late notice for the purpose of s54(1). The insurer appealed to the Full Court of the Supreme Court of WA. The Full Court allowed the appeal on the basis that the trial judge had not sufficiently dealt with the evidence on prejudice in his reasons and directed that the matter be referred back to the lower court for a retrial.

The insured employer appealed to the High Court. The insurer cross-appealed relying on s9(1)(e)(i) of the Act to argue that the policy was a contract 'entered into …for the purposes of a law…that relates to …workers' compensation' and, therefore, was not a contract to which the Act applied.

Section 9(1)(e)(i) of the Act provides:

> Except as otherwise provided by this Act, this Act does not apply to or in relation to contracts and proposed contracts:
>
> (e) entered into or proposed to be entered into for the purposes of a law (including a law of a State or Territory) that relates to:
>
> (i) workers' compensation …

Unlike the workers' compensation legislation in some other jurisdictions which requires insurance against all forms of an employer's liability for personal injury to a worker[4], the WA scheme did not require an employer to insure against liability at common law.

The High Court's Decision: The High Court unanimously held that the exception in s9 of the Act only applied to that part of the policy relating to the statutory workers' compensation. Accordingly, the Act (including s54) applied in the usual way to the cover that was provided by the policy against the insured employer's liability arising under common law liability.

In reaching this decision, the High Court commented that:

> We do not accept that the criterion for the operation of s9(1)(e) is the form in which the particular arrangement between the parties was recorded….Account must be taken of the fact that there were, in this case, distinct insurances that were reflected in the two different insuring clauses…That both concerned an employer's liability to provide compensation to workers, one form of liability arising under a statutory scheme and the other stemming from the common law, is not to the point. What is important is that one form of the insurance was undertaken for the purposes of a relevant law; the other was not. The exception for which s9(1)(e)(i) provides is identified by reference to a contract being entered into for the

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[3] Essentially, s54 provides that if the act or omission of the insured relied on by the insurer is of a type which could reasonably be regarded as being capable of causing or contributing to a loss covered by the insurance, the insurer may only refuse to pay the claim if the insured can not show that the act or omission did not cause the loss. If the act or omission is not of that type, but in fact caused prejudice to the insurer, the insurer can reduce its liability to an extent which reasonably represents the prejudice suffered. This is dealt with more fully in section 9 below.

[4] *Workers Compensation Act 1987* (NSW) s155; *Accident Compensation (WorkCover Insurance) Act 1993* (Vic); *WorkCover Queensland Act 1996* (Qld) s 52

> purposes of a law relating to a particular subject matter. The exception is not identified by reference to the way in which the risk which is insured can be described.

For completeness, the High Court also unanimously held that the trial judge had not erred in his finding that, in the circumstances, the insurer failed to establish it had suffered any prejudice (for the purposes of s54 of the Act) by reason of the delayed notice given by the insured.

Recent Review of the Act: The Review Panel acknowledged that the decision in *Moltoni* gave rise to uncertainty about bundled contracts which it is desirable to resolve. The Draft Bill gives effect to the Review Panel's recommendation that the Act be amended so that insurance contracts that are entered into for the purposes of workers' compensation are excluded from the operation of the Act in their entirety, even if the contracts also contain cover for employers' common law liability to pay damages to workers for employment related personal injury. It appears that this recommendation was based upon the submissions by the Insurance Council of Australia Ltd that any potential disadvantages in this approach are manageable (in particular, the application of the State and Territory legislation to the additional cover does not create difficulties).

In relation to other cases of bundled insurance contracts, the Draft Bill follows the Review Panel's recommendation that the exceptions in s9(1) of the Act should apply to each aspect of the bundled cover as if they were included in separate insurance contracts (eg bundled policies covering CTP with third party property damage).

5.4 Section 10

Section 10 of the Act expands the operation of the Act by adopting a broad definition of a 'contract of insurance'.

Section 10 provides:

> (1) A reference in this Act to a contract of insurance includes a reference to a contract that would ordinarily be regarded as a contract of insurance although some of its provisions are not by way of insurance.
>
> (2) A reference in this Act to a contract of insurance includes a reference to a contract that includes provisions of insurance so far as those provisions are concerned, although the contract would not ordinarily be regarded as a contract of insurance.
>
> (3) Where a provision included in a contract that would not ordinarily be regarded as a contract of insurance affects the operation of a contract of insurance to which this Act applies, the provision shall, for the purposes of this Act, be regarded as a provision included in the contract of insurance.

Subsection 10(1) ensures that a contract remains a contract of insurance notwithstanding that it contains provisions which do not deal with insurance.

Examples of the application of ss10(2) is a contract under which an insurer agrees to sell certain property and also agrees to insure the property[5] or where there is a car rental

[5] Refer to the Notes to the Draft Insurance Contracts Bill 1982

agreement which includes provisions for collision indemnity for third party property damage[6].

Subsection 10(3) is directed at preventing insurers from circumventing the Act by requiring insureds to enter into collateral contracts that would not ordinarily be considered contracts of insurance[7].

6. Section 13 - duty of good faith

Each party to a contract of insurance is required to act towards the other party with the utmost good faith. Section 13 of the Act provides that the duty of utmost good faith is an implied term in contracts of insurance:

> "A contract of insurance is a contract based on the utmost good faith and there is implied in such a contract a provision requiring each party to it to act towards the other party, in respect of any matter arising under or in relation to it, with the utmost good faith.'

As an implied term in a contract of insurance a breach of the duty of utmost good faith by an insurer can give rise to a claim for damages to be assessed according to ordinary contractual principles. The meaning of utmost good faith is not defined in the Act and is best determined by reference to case law. An analysis of such case law falls outside the scope of this paper.

7. Section 21 – the insured's duty of disclosure

7.1 Section 21

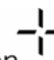
Section 21 of the Act sets out an insured's duty of disclosure and the statutory regime also provides for the remedies available to an insurer in the event of non-disclosure or misrepresentation (see section 7 below). An insurer cannot rely on common law principles if the Act applies to the contract of insurance.

Section 21 of the Act provides:

> (1) Subject to this Act, an insured has a duty to disclose to the insurer, before the relevant contract of insurance is entered into, every matter that is known to the insured, being a matter that:
>
> (a) the insured knows to be a matter relevant to the decision of the insurer whether to accept the risk and, if so, on what terms; or
>
> (b) a reasonable person in the circumstances could be expected to know to be a matter so relevant.
>
> (2) The duty of disclosure does not require the disclosure of a matter:
>
> (a) that diminishes the risk;
>
> (b) that is of common knowledge;

[6] See *Bayswater Car Rental Pty Ltd v Hannell* (1999) 10 ANZ Ins Cas 61-387

[7] Refer to the Notes to the Draft Insurance Contracts Bill 1982.



(c) that the insurer knows or in the ordinary course of the insurer's business as an insurer ought to know; or

(d) as to which compliance with the duty of disclosure is waived by the insurer.

(3) Where a person:

(a) failed to answer; or

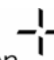
(b) gave an obviously incomplete or irrelevant answer to;

a question included in a proposal form about a matter, the insurer shall be deemed to have waived compliance with the duty of disclosure in relation to the matter.

7.2 The scope of section 21

Generally speaking , the following considerations apply when assessing the scope of an insured's duty of disclosure:

- the duty applies prior to entering into a contract of insurance, including the time between submitting a proposal form and acceptance of the risk by the insurer and therefore an insured is obliged to disclose any changes which should be reflected on the proposal form up until the risk is accepted by the insurer: *Prime Forme Cutting Pty Ltd v Baltica General Insurance Co Ltd* (1990) 6 ANZ Ins Cas 61-028;
- the duty of disclosure no longer applies once the contract is entered into: *Australian Associated Motor Insurers Ltd v Ellis* (1990) 6 ANZ Ins Cas 60-957;
- the duty of disclosure applies on each renewal of the contract of insurance: *Lumley General Insurance Ltd v Delphin* (1990) 6 ANZ Ins Cas 60-986;
- the insured's obligation to disclose matters that are relevant to the insurance risk does not include indirect factors, such as the commercial considerations of an insurer in accepting the risk: *Permanent Trustee Australia Limited & Anor v FAI General Insurance Company Limited (in Liq)* (2003) 214 CLR 514 (this case is looked at in detail below);
- the duty of disclosure is limited to facts actually known to the insured. A fact is "known" if the insured believes it to be true, as opposed to suspecting it may be true: *Australian Casualty of Life Ltd v Hall* (1999) 151 FLR 360;
- facts can be forgotten by an insured and if that is the case genuinely, the disclosure obligation will not be breached: *Hammer Waste Pty Ltd v QBE Mercantile Mutual Ltd* (2003) 12 ANZ Ins Cas 61-553;
- an insurer will be deemed to know all of the risks involved in the normal and lawful conduct of an insured's business: *AF & G Robinson v Evans Bros. Pty Ltd* [1969] VR 885; *Commercial Union Assurance Company of Australia Ltd v Beard* (1999) 47 NSWLR 735; *Carling v CGU Insurance Ltd* (2000) 11 ANZ Insurance Cases ¶61-643.
- generally, the knowledge of an agent (such as a broker) will be attributed to the insured principal where the agent is delegated the duty of disclosure as part of the process of effecting insurance. This means that a broker's knowledge will bind the



insured, and so will be required to be disclosed to the insurer if it is relevant, regardless of where the knowledge came from or whether it was known to the insured: *Blackburn Low & Co v Vigors* (1887) 12 App Cas 531; *Blackburn Low & Co v Haslam* (1888) 21 QBD 144; *Permanent Trustee Australia Limited & Anor v FAI General Insurance Company Limited (in Liq)* (2003) 214 CLR 514; and

7.3 Permanent Trustee Australia Limited & Anor v FAI General Insurance Company Limited

The scope of an insured's duty under s 21 was recently reviewed by the High Court in *Permanent Trustee Australia Limited & Anor v FAI General Insurance Company Limited (in Liq)* (2003) 214 CLR 514. The High Court held that an insured's duty of disclosure under section 21(1) of the Act is limited to disclosing matters that affect the insurer's assessment of the risk of the proposed insurance and does not extend to disclosing every matter relevant to the insurer's decision to enter into the contract of insurance.

The Facts: In 1991, Permanent Trustee Australia Limited and Permanent Trustee Company Limited (the ***appellants***) were looking to obtain insurance for the following year. Their existing insurance cover was provided by a number of insurers, one of which was FAI General Insurance Company Limited (***FAI***). The appellants had decided not to obtain any of their insurance from FAI in the following year, subject to obtaining satisfactory quotations from alternative insurers.

In the course of obtaining the new cover, the appellants were granted a short extension of their existing cover. All of the appellants' insurers agreed to the extension, including FAI, which was paid a standard commercial rate for the extension. When the appellants' broker obtained FAI's agreement to the extension of time, it did not disclose to FAI the intention of the appellants not to renew their insurance with FAI (subject to obtaining satisfactory quotations from other sources).

FAI claimed – and the trial judge found – that had FAI known that it might not be invited to participate in the renewal of the insurance, it would not have provided the extension of time (for commercial and emotional reasons unrelated to the risk of granting the extension). On this basis, FAI refused to indemnify the appellants for a claim notified during the period of the extension.

The appellants brought an action claiming that FAI was obliged to indemnify them. FAI argued, *inter alia,* that it was not obliged to indemnify the appellants because the latter, by failing to disclose their intention not to renew their insurance with FAI, had breached their duty of disclosure under s21 of the Act.

Section 21(2) lists certain matters that do not need to be disclosed, including matters that diminish the risk or are of common knowledge. FAI's argument was successful before the primary judge and the NSW Court of Appeal (ie these courts accepted that the appellants' intention not to renew their insurance with FAI was a 'matter relevant to the decision of [FAI] whether to accept the risk and, if so, on what terms').

The appellants appealed the matter to the High Court where Justices McHugh, Kirby and Callinan jointly delivered the majority judgment in favour of the appellants. Justices Gummow and Hayne delivered a joint dissenting judgment.

The decision: Justices McHugh, Kirby and Callinan held that the issue of whether the appellants did or did not intend to renew their policy was not a matter relevant to FAI's decision as to whether to accept the risk of the extension or the terms on which the decision to accept the risk would be made. Therefore, the appellants were not guilty of any relevant non-disclosure and were entitled to be indemnified for the claim notified during the period of the extension.

Their decision was based on the following two key findings:

- The wording of s21 (in particular, the use of the expression 'accept the risk' rather than, for example, 'enter the insurance contract' and the exception, in s21(2), for matters diminishing the risk), considered in light of relevant parliamentary materials, showed that the focus of the Act was on the particular risk of the proposed insurance rather the 'broader question of the commercial willingness of the insurer to accept the risk, still less emotional or individual reactions to that question'.
- If the duty of disclosure extended beyond matters material to the risk, the insured would be under an extraordinarily high burden, which could not have been intended by the legislature.

On the face if it, the majority judgment in *Permanent* has narrowed the scope of the duty of disclosure to the benefit of insureds by restricting the duty of disclosure to matters relevant to the particular insurance risk. The insured will have no obligation to disclose matters relating to the commercial considerations of an insurer in accepting a risk even if it knows these are relevant to that particular insurer. This may therefore, in certain cases, provide insureds with an argument with which to challenge a non-disclosure defence to a claim for indemnity.

The general consensus among Australian commentators is that the minority judgment of Justices Gummow and Hayne – that favoured maintaining the previously accepted scope of s21 - is to be preferred. It acknowledged that separating out those matters that are directly relevant to a risk, and those that are relevant only to whether a contract is entered into, is a distinction that cannot be drawn with any clarity – not least because an insurer only accepts a risk when a contract is entered into. In their view, the duty of disclosure should remain focused, as before, on matters relevant to the insurers' decision whether to accept the risk and on what terms.

However, in the meantime, the majority judgment represents the current state of the scope of the statutory duty of disclosure under Australian law.[8]

7.4 The Review

The Draft Bill implements the Review Panel's recommendation to ss21 and 21A of the Act.

[8] For more discussion of the effects of this decision on insureds and insurance brokers, as well as a general overview of brokers' duties in Australia, see the paper presented by Oscar Shub and Philip Hopley, Senior Associate, at Allens Arthur Robinson's Insurance & Reinsurance Forum on 4 July 2007, a copy of which is available at http://www.aar.com.au/pubs/insur/pap4jul07.htm

Section 21 is proposed to be amended to include the following non-exclusive factors that can be taken into account when determining the application of the duty of disclosure to resolve uncertainty in the application of the test.

(a) The nature and extent of the cover provided by the contract of insurance.

(b) The class of persons who would ordinarily be expected to apply for cover of that type.

(c) The circumstances in which the contract of insurance is entered into including the nature and extent of any questions asked by the insurer.

It is questionable whether these additional criteria will resolve any uncertainty associated with the application of the test. There is potential for the additional criteria to increase the level of uncertainty if the Courts are not provided with adequate guidance by Parliament concerning the application of these additional criteria.

Section 21A requires the insurer to provide the insured with specific questions that are relevant to it in making the decision whether to accept the risk. However, it only applies to 'eligible contracts of insurance', these being contracts of insurance for new business (not renewals) covering, *inter alia*, motor vehicles, home contents and travel insurance.

The Review Panel recommended section 21A be amended so subsection 21A(4)(b) is repealed, removing an insurer's right to ask a potential insured any general 'catch-all' type questions. This is likely to cause difficulties for insurers who will need to consider how to draft specific questions to capture all potential exceptional circumstances and is likely to lead to an increase in the number of specific questions insurers ask, which will make applying for and assessing applications for insurance more time consuming.

Further, the Review Panel recommended that section 21A apply to renewals. This is likely to result in substantial changes to insurer procedures and practices in effecting renewals.

The Review Panel also recommended that the Act be amended so that the insurer must provide to the insured, at the time when the insurance policy is issued, a reminder that the duty of disclosure obligations continue until the time the policy is entered into.

8. Section 28 – remedies for non-disclosure and misrepresentation

8.1 Section 28

At common law, as in England and Wales, an insurer is entitled to avoid a contract *ab initio* for any material non-disclosure or misrepresentation, whether or not the insured's breach was fraudulent or innocent. However, in Australia, the Act modifies the position.

Section 28 of the Act provides:

> (1) This section applies where the person who became the insured under a contract of general insurance upon the contract being entered into:
>
> (a) failed to comply with the duty of disclosure; or
>
> (b) made a misrepresentation to the insurer before the contract was entered into;

but does not apply where the insurer would have entered into the contract, for the same premium and on the same terms and conditions, even if the insured had not failed to comply with the duty of disclosure or had not made the misrepresentation before the contract was entered into.

(2) If the failure was fraudulent or the misrepresentation was made fraudulently, the insurer may avoid the contract.

(3) If the insurer is not entitled to avoid the contract or, being entitled to avoid the contract (whether under subsection (2) or otherwise) has not done so, the liability of the insurer in respect of a claim is reduced to the amount that would place the insurer in a position in which the insurer would have been if the failure had not occurred or the misrepresentation had not been made.

By virtue of s28 of the Act, an insurer is only entitled to avoid a contract of general insurance for fraudulent misrepresentation or non-disclosure.

The remedy for innocent misrepresentation or innocent non-disclosure is that the insurer may reduce its liability to the amount that would place it in the position it would have been in if the non-disclosure or misrepresentation had not occurred (s28(3)).

If the insurer would have entered into the contract for the same premium and on the same terms and conditions even with the non-disclosure or misrepresentation, it follows that the insurer has no remedy.

8.2 Section 28(2) – Fraudulent misrepresentation and non disclosure

As discussed above, s28(2) allows an insurer to avoid the contract of insurance in the event of a *fraudulent* non-disclosure or *fraudulent* misrepresentation.

The Act does not address the question as to what constitutes a fraudulent non-disclosure, but it has been the subject of debate in the Courts whether, for a non-disclosure to be fraudulent, the insured must have:

- deliberately failed to disclose; alternatively
- recklessly failed to disclose

The question of what the knowledge of the insured must be in relation to the material not disclosed and the insured's state of mind has been discussed in various cases.

8.3 NRG Victory Australia Limited v Hudson

In *NRG Victory Australia Limited v Hudson* (2004) 13 ANZ Ins Cas 90-121 the reinsurer appealed against the findings of a trial judge that an absence of a dishonest intent meant that the misrepresentations were not fraudulent within the meaning of s29 of the Act (s29 contains similar provisions to s28 but in the context of life insurance). The Supreme Court of Western Australia held that the existence of an honest and reasonable belief in the truth of a representation by an insured denied the insurer the ability to avoid a contract of insurance on the basis of fraudulent misrepresentation.

During his employment as a spray-painter, the respondent (***Hudson***) developed a rash and swelling over the exposed parts of his body, including his neck. Subsequently, Hudson was diagnosed with post-occupational dermatitis caused by exposure to epoxy-based products. He ceased his employment on the basis of this diagnosis. After 2 years of

unemployment as a result of his condition, Hudson commenced working as a fork-lift driver and loader.

In association with his new employment, Hudson completed an application form for membership of the Superannuation Trust of Australia. This application took the form of an insurance policy (the ***Policy***) to which the applicant (***NRG***) was the reinsurer. In completing the application form, Hudson incorrectly confirmed that statements to the following effect applied to him:

- "I have not received medical advice that I have a medical condition which is going to affect my ability to carry out the normal duties of my occupation"; and
- "I have never had a neck, back or shoulder injury or disease which has required more than 2 weeks off work; has recurred more than twice; which is still causing me trouble…"

The effect of these responses was to extend the basic cover (2 units) under the policy by an additional 2 units. In late 1993 Hudson developed a rash which subsequently spread all over his body and he has not worked since. Hudson was paid the first 2 units under the Policy, but NRG declined payment of the 2 additional units on the basis that Hudson had fraudulently misrepresented his condition on the application form.

At trial, it was accepted that Hudson, when completing the application form, believed that the first statement referred only to his capacity to work in his current occupation. Given that his condition only affected his ability to work with epoxy-based products, and not his ability to work as a loader / forklift driver, Hudson answered in the affirmative. Further, it was accepted that Hudson did not consider his condition to be a disease in the context of the second statement at the time that he answered that statement in the affirmative.

At first instance, Williams DCJ held that, whilst:

(a) incorrect completion of the application form amounted to a misrepresentation;

(b) Hudson had a duty to disclose his previous medical condition; and

(c) Hudson knew or could reasonably be expected to know that his previous medical condition was relevant to his application for increased cover,

an absence of fraudulent intent meant that the misrepresentations were not fraudulent within the meaning of s 29 of the Act.

In support of the appeal, NRG argued that Hudson, under a duty to disclose his skin condition, (which he knew, or should have known was relevant to the appellant's decision whether to extend the cover under the policy) failed to do so, and that this failure was made fraudulently.

Justice Parker, with whom Justices Steytler and Miller agreed, held that there was no need to turn to the question of whether the misrepresentations were made fraudulently because the facts were such that this was a case to which s 26 of the Act had application. Section 26 provides that:

> Where a statement that was made by a person in connection with a proposed contract of insurance was in fact untrue but was made on the basis of a belief that the person held,

being a belief that a reasonable person in the circumstances would have held, the statement shall not be taken to be a misrepresentation.

The Court held that it had been open, on the facts, for Williams DCJ to conclude that Hudson had given his answers on the basis of honest beliefs, and that each of those beliefs was a belief that a reasonable person would have held in the circumstances, given that the insured was not medically trained and felt able to work. Given such a finding, Justice Parker found in favour of Hudson and dismissed NRG's appeal.

Whilst Justice Parker was not required to consider the question of whether Hudson's answers were fraudulent within the meaning of s 29 of the Act, he noted that, for a statement to fall within the ambit of fraud, that statement must be made with an absence of an actual and honest belief in its truth. A fraudulent statement in the context of s 29, involves a deliberate decision to mislead or conceal something from the insurer, or recklessness amounting to indifference about whether this occurs.

8.4 Von Braun v AAMI

In *Von Braun v AAMI* [1999] 10 ANZ Ins Cas 61-419 the insured fraudulently stated to AAMI that he had paid $70,000 for a Mercedes and requested an insured sum of $65,000. Despite the fact that AAMI's dealer guide to car values valued the car at around $56,000, AAMI issued a cover note for the car, insuring it at $65,000. AAMI was also aware that NRMA had insured the car for a lower agreed value in the previous year. The car was stolen. AAMI refused the claim mainly on the ground that the insured had misrepresented the cost of the car.

Higgins J found that the insured had deliberately overstated the purchase price. The consequences of this were as follows:

- In the circumstances, there was no breach of the insured's duty of disclosure under section 21(1) of the Act. That was because there was nothing to suggest that a reasonable person in the position of the insured would have expected a hypothetical prudent insurer in the position of AAMI to agree to a particular value simply on the basis of an overstated purchase price. AAMI knew all the facts that were logically relevant to determine the agreed value.
- However, because the misrepresentation was fraudulent, s28(2) entitled the insurer to avoid the policy. Higgins J applied the definition of fraud as to "*dishonestly deprive a person of something he or she would be entitled to, but for the fraud*". The Court held that, for a misrepresentation to be fraudulent, the proponent needs to be aware only that the statement is false and intend the insurer to accept and act upon it as true. It did not matter that the insurer's representatives might well in fact have considered the option of offering a lower agreed value.

That decision of the Supreme Court of Australian Capital Territory should be compared to another 1999 case, that of *Australian Casualty and Life Ltd v Hall* (1999) 151 FLR 360 heard by the Queensland Court of Appeal. The Court held that there was no general rule that a deliberate intention to suppress information on the part of an insured will equate to fraud. That Court determined that fraud must involve an element of dishonesty or moral turpitude.

8.5 Tyndall Life Insurance Co Ltd v Chisholm

In the 2000 case of *Tyndall Life Insurance Co Ltd v Chisholm* (2000) 11 ANZ Ins Cas 90-104, the South Australia Supreme Court further considered what constitutes fraudulent misrepresentation.

In this case, the insurer offered life insurance whereby a benefit of $500,000 was paid if the insured suffered a "medical event", defined as meaning death and a number of major illnesses including cancer.

The insured submitted a proposal for the policy in early June 1991. The proposal was accepted and the policy issued with effect from 1 July 1991. In May 1992, the insured was diagnosed with cancer. On 1 June 1992, the insured gave notice of a claim under the policy. On 17 June 1992 he lodged his claim and the full $500,000 was paid out on 25 August 1992.

The insurer was prompted to investigate the insured's application. It discovered that in 1983 the insured had consulted a doctor concerning rectal bleeding. The doctor made a diagnosis that the bleeding was caused by haemorrhoids. Although the insured continued to experience episodes of bleeding from 1983 to June 1992, he did not consult another doctor about it.

In early June 1991 the insured participated in a Detectacol test, available to buy from pharmacies, designed to detect conditions, including cancer, which might cause bleeding of the colon. The test provided a means for individuals to submit samples for analysis without consulting a doctor. The insured gave a false name and birth date. He was subsequently informed that the test produced a positive result and advised to consult a doctor. As referred to above, the insured shortly thereafter submitted his insurance proposal.

As part of the application for the insurance, the insured completed a medical report. The allegations of fraudulent misrepresentation were based on his answers to two questions:

(a) during the last 5 years have you had any tests, including blood tests? *No*

(b) have you had any passage of blood from the bowel or in the urine? *Yes, past traces of blood from bowel.*

The insurer required a doctor to report in relation to life insurance applications, and therefore the insured consulted a doctor to complete the report. The doctor stated *"History of PR blood – but this appears to have been adequately investigated with no cause found."*

According to the judge, Debelle J, the requirements for fraudulent misrepresentation in relation to an insurance contract are:

- the insured makes a representation which is false;
- the representation is made
  - knowingly or without belief in its truth, or
  - recklessly, not caring whether be true or false, ("*consciously indifferent to the truth of his answers*")"

  and

- the intention of the insured is that the insurer will act on that representation,

He decided that the insured knew that the answer to question (b) was false. He considered that the answer painted a picture that the bleeding was a past and not a present condition, and would have deflected the insurer from making further enquiry. Given that an episode of bleeding had recently occurred, the insured could not have honestly believed that his answer was true.

In relation to question (a), the judge considered the insured's participation in the Detectacol test. He decided that by giving a false name and date of birth the insured took steps to conceal his participation in the test, and so concluded that he had acted fraudulently.

Whilst it was unnecessary for Debelle J to decide whether the insured had fraudulently failed to comply with the duty of disclosure, he nevertheless dealt with the issue. He considered that there will be a fraudulent non-disclosure if the insured knowingly or recklessly fails to disclose a matter which the insured knows to be relevant to the decision of the insurer whether to accept the risk, and if so, on what terms.

Debelle J held that the failure of the insured to disclose both the fact that he had had recurrent episodes of bleeding and the fact that he had participated in the Detectacol test constituted non-disclosure. The insured knew the answer to question (a) was false and therefore he fraudulently failed to comply with his duty of disclosure.

This case illustrates how fraud may apply both in respect of representations which are false, and in respect of representations which are true in a literal sense, but which paint a misleading picture.

8.6 Section 28(3) – Assessment of an insurer's loss

Under s 28(3) the assessment of the loss suffered by the insurer in relation to a non-disclosure or misrepresentation is carried out as follows[9]:

- Where the insurer would have accepted the risk but at a different premium, its loss is the difference between the two premiums.
- Where the insurer would have accepted the risk on different terms (whether at the same premium or not), the loss is the difference between its liabilities under the actual contract and the notional contract containing the different terms.
- Where the insurer would have excluded the risk which gave rise to the claim, the amount of its loss is equivalent to the full amount of the claim made against it. In that case, the insured would recover nothing in respect of the claim. However, the insured would generally be entitled to a refund of the premium.

If, the insurer would have entered into a contract on the same formal terms but the effect of the contract would have been different, the insurer may rely on s 28(3) to reduce the liability. Professional indemnity policies typically have a clause excluding circumstances notified prior to inception of the policy. If known circumstances are not notified, the insurer will be able to rely on s 28(3) to deny any claim arising out of them, although the claim may

[9] Australian Law Review Commission 20, para 192

be covered under an earlier policy in place at the time the insured became aware of the circumstances[10].

Bauer Tonkin Insurance Brokers v CIC & Ors (1996) 9 ANZ Ins Cas 61-298 reviewed the type of evidence that the Courts require from insurers. In addition to underwriting guidelines and a procedural manual, the South Australian Supreme Court ordered discovery of applications of similar cover that had been made to the insurer and documentary evidence whether such applications had been accepted, and if so, on what terms.

The insurer bears the onus of proving that, if the matters for disclosure had been disclosed, or if the misrepresentations had not been made, it would not have entered into the insurance contract for the same premium and on the same terms and conditions as it did[11].

To satisfy this burden of proof, the insurer should adduce evidence from someone within its organisation who has authority to approve or disapprove the relevant insurance applications, or produce underwriting guidelines touching upon the matter at issue[12]. In some cases, discharging the onus can be difficult where the insurer may have done a number of things at the insured's option eg. increase the premium or reduce the limit of cover. It then becomes necessary to investigate what the insured would have done.

The importance of evidence of what the insurer would have done is illustrated by the case of *McNeill & Ors t/a The Front Row & anor v O'Kane* [2002] QSC 144. In that case The Oriental Hotel in Mackay was damaged by fire which had been lit by arsonists. Prior to inception of the policy the insured had represented that the hotel was secured by a back to base alarm. The insurer claimed that, if it had known there was no back-to-base alarm, it would not have provided cover, and thus the misrepresentation of the alarm was a breach within the ambit of s28 of the Act. The insurer's underwriting guidelines stated that all metropolitan and regional capital hotels must have a monitored back to base alarm. It sought to demonstrate that its underwriting assessment criteria was "effectively practised and adhered to" and its practice was to impose a variety of exclusions and go off-risk for particular types of damage. It claimed, therefore, that had it known that these circumstances fell foul of that criteria, it would not have entered into the contract on the same terms and conditions. This was accepted by Holmes J who gave judgment in favour of the insurer. In doing so, he rejected an argument by the insured that it would have installed a back to base alarm had the insurer required it. The insured bore the onus in relation to such matters and the evidence was not sufficient to discharge the onus.

8.7 Refund of premium

At common law, an insurer avoiding a contract for innocent misrepresentation or innocent non disclosure is obliged to refund the premium.

Similarly under s 28, an insured is entitled to a premium refund when an insurer reduces its claim to nil under s 28(3) as a consequence of a misrepresentation or non disclosure. If

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[10] *Hendry Rae and Court v FAI General Insurance Co Ltd* (1991) 5 WAR 376

[11] *Commercial Union Assurance Company of Australia Ltd v Beard & Ors* [1999] NSW CA 422

[12] *Manchester Unity Total Care Building Society v MGICA Ltd* (1991) 6 ANZ Ins Cas 61-062

the insurer would not have entered into the contract, it would not have received that premium. A refund of premium may not apply where the misrepresentation or non-disclosure is fraudulent.

8.8 Section 31 - discretion to set aside avoidance

Section 31 of the Act provides:

> (1) In any proceedings by the insured in respect of a contract of insurance that has been avoided on the ground of fraudulent failure to comply with the duty of disclosure or fraudulent misrepresentation, the court may, if it would be harsh and unfair not to do so, but subject to this section, disregard the avoidance and, if it does so, shall allow the insured to recover the whole, or such part as the court thinks just and equitable in the circumstances, of the amount that would have been payable if the contract had not been avoided.
>
> (2) The power conferred by subsection (1) may be exercised only where the court is of the opinion that, in respect of the loss that is the subject of the proceedings before the court, the insurer has not been prejudiced by the failure or misrepresentation or, if the insurer has been so prejudiced, the prejudice is minimal or insignificant.
>
> (3) In exercising the power conferred by subsection (1), the court:
>
> (a) shall have regard to the need to deter fraudulent conduct in relation to insurance; and
>
> (b) shall weigh the extent of the culpability of the insured in the fraudulent conduct against the magnitude of the loss that would be suffered by the insured if the avoidance were not disregarded;
>
> but may also have regard to any other relevant matter.
>
> (4) The power conferred by subsection (1) applies only in relation to the loss that is the subject of the proceedings before the court, and any disregard by the court of the avoidance does not otherwise operate to reinstate the contract.

In cases of fraud, s 31 of the Act confers upon the Court a discretion to disregard the insurer's right to avoid, and to allow recovery of all or part of the claim.

The case of *Von Braun v AAMI* referred to above illustrates how s31 may be applied. In that case, Higgins J considered that the overstatement of the value of the car could have affected only the extent of the indemnity, not the acceptance or otherwise of the insurance proposal. He therefore allowed the claim as if the agreed value had been $56,000 (the figure in the insurer's 'dealer guide') rather than a figure closer to the $70,000 that the insured represented he had paid for the car.

8.9 Section 33 – the remedies contained in the Act are exclusive

Section 33 of the Act provides:

> The provisions of this Division are exclusive of any right that the insurer has otherwise than under this Act in respect of a failure by the insured to disclose a matter to the insurer before the contract was entered into and in respect of a misrepresentation or incorrect statement.

8.10 Cancellation of the contract

Notwithstanding that s28 does not allow an insurer to avoid a contract for innocent misrepresentation or non-disclosure, it may cancel the contract in such circumstances pursuant to s60 of the Act.

Section 60 provides:

> (1) Where, in relation to a contract of general insurance:
>
> (a) a person who is or was at any time the insured failed to comply with the duty of the utmost good faith;
>
> (b) the person who was the insured at the time when the contract was entered into failed to comply with the duty of disclosure;
>
> (c) the person who was the insured at the time when the contract was entered into made a misrepresentation to the insurer during the negotiations for the contract but before it was entered into;
>
> … … …
>
> the insurer may cancel the contract.

The insurer will, of course, remain on risk in respect of claims made prior to cancellation. If an insured makes a claim before the insurer has cancelled the contract, the insurer can then seek to invoke s28(3) and reduce its liability.

8.11 Co-insurance

Difficulties can arise when there is more than one insured and a material non-disclosure is made by only one insured.

The majority of the High Court held in *Advance (NSW) Insurance Agencies Pty Ltd v Matthews* (1989) 166 CLR 606 that there should not be a distinction between joint and composite contracts of insurance. It considered that s28 applies where one co-insured has failed to disclose a material fact, notwithstanding that the other did not know of the non disclosure.

However, the policy wording may suggest that the insurer has agreed to modify its right to deny cover to “innocent” insureds where there is a non-disclosure or misrepresentation by one co-insured. In *Sherry & Ors v FAI General Insurance Company Limited (in liq)* (2003) 12 ANZ Ins Cas 61-561, the policy defined the “Insured” as the partnership Mann Judd and a number of associated companies. It contained a clause which protected the Insured for claims arising by reason of fraud on the part of the Insured or its partners or its employees in which case cover extended in excess of the full extent of the fraudulent partner’s assets in the firm. The clause was expressed to apply notwithstanding that the fraud was not disclosed by the fraudulent partner. Where one partner dealt fraudulently with the estates of the plaintiffs, it was held that the policy was intended to cover innocent partners and each of the companies in which they had an interest. The insurer’s rights of avoidance were modified by the terms of the policy.

8.12 Affirmation and estoppel

An insurer with knowledge of a misrepresentation or non-disclosure may conduct itself in such a way as to indicate an election not to rely upon the breach or create an estoppel.

This will occur where the insurer is aware of the non-disclosure or misrepresentation prior to inception of the contract but nevertheless issues the policies and accepts the premium[13].

Where an insurer learns of a misrepresentation or non-disclosure after the contract is entered into, it will have a reasonable time to investigate the issue before its conduct will amount to an affirmation. However, in the meantime it is important to deal with the insured on a "without prejudice" basis.

8.13 Comment

In cases of innocent non-disclosure or misrepresentation, s28 of the Act limits the insurer's remedies to the actual loss resulting to the insurer. In many cases, this may be obvious. The matter not disclosed may be so material that any insurer would have denied cover. In such cases, the claim will be able to be denied. Problems arise where the matter would not necessarily have resulted in denial of coverage. Insurers seeking to rely on s28 in such circumstances need to be mindful of the sort of evidence required to discharge their onus. The insurer's underwriting guidelines and procedures, as well as its adherence in practice to those guidelines and procedures are all matters which can come under close scrutiny by the court when an insurer wishes to rely on s28. Evidence in the form of an affidavit from the underwriter concerned may also be required. Depending on the facts, the exposure to such an inquiry may discourage insurers that may be able to deny claims from doing so.

9. Section 40 – right to notify circumstances

Claims made and notified policies, as their name suggests, respond to claims actually made against the insured during the policy period. However, it often happens that, during the policy period, the insured becomes aware that a claim is likely to be made against them but no claim is actually made during that time. This puts the insured in a difficult position, as they will usually have to disclose the possibility of the claim to the insurers underwriting their subsequent policies. Those policies are likely to exclude cover for the claim, when it eventually arises.

The solution is for the insured to be able to inform the insurer of the possibility of a claim, when it first becomes aware of that possibility, with the effect that the claim will be covered even if it is eventually made outside the policy period. In Australia, this is achieved in one of two ways:

(i) either by an express clause to that effect in the policy wording (a notification of circumstances clause); or

(ii) by reliance on a statutory right to notify circumstances contained in s40 of the Act.

Section 40 provides:

[13] *Meyers & Paddington Motor Service Limited v Dalgety & Co. Limited* (1926) 26 SR (NSW) 195

> (1) This section applies in relation to a contract of liability insurance the effect of which is that the insurer's liability is excluded or limited by reason that notice of a claim against the insured in respect of a loss suffered by some other person is not given to the insurer before the expiration of the period of the insurance cover provided by the contract.
>
> …
>
> (3) Where the insured gave notice in writing to the insurer of facts that might give rise to a claim against the insured as soon as was reasonably practicable after the insured became aware of those facts but before the insurance cover provided by the contract expired, the insurer is not relieved of liability under the contract in respect of the claim, when made, by reason only that it was made after the expiration of the period of the insurance cover provided by the contract.

This provision allows an insured to notify circumstances that might give rise to a claim into the insured's current policy in the absence of a notification of circumstances clause.

Where there is an express notification of circumstances clause contained in the policy, the effect of s54 of the Act (see section 6 below) is that the insured can retrospectively notify the insurer of circumstances, even after the policy has expired, and still obtain cover for the claim, subject to any prejudice the insurer may be able to demonstrate.[14] However, the weight of current case law suggests that similar retrospective notification is not available where there is no express clause and the insured could only rely upon s40 of the Act.[15]

It should also be noted that provisions in the Draft Bill prevents an insured from retrospectively notifying circumstances, but allows a grace period of 28 days from policy expiration in which to notify, under s40, circumstances occurring during the policy .

10. Section 54 – insurers may not refuse to pay claims in certain circumstances

Section 54 of the Act restricts the circumstances in which an insurer may refuse to pay a claim in the event of a breach of a policy term.

Section 54 provides:

> (1) Subject to this section, where the effect of a contract of insurance would, but for this section, be that the insurer may refuse to pay a claim, either in whole or in part, by reason of some act of the insured or of some other person, being an act that occurred after the contract was entered into but not being an act in respect of which subsection (2) applies, the insurer may not refuse to pay the claim by reason only of that act but the insurer's liability in respect of the claim is reduced by the amount that fairly represents the extent to which the insurer's interests were prejudiced as a result of that act.

[14] See *FAI General Insurance Co Limited v Australian Hospital Care Pty Ltd* (2001) 11 ANZ Insurance Cases 61-497

[15] See *CA & MEC McInally Nominees Pty Ltd v HTW Valuers (Brisbane) Pty Ltd* (2001) 11 ANZ Insurance Cases 61-507 and *Gosford City Council v GIO General Limited* (2003) 12 ANZ Insurance Cases 61-566 but see the contrary dicta in *Einfeld v HIH Casualty and General Insurance Limited* (1999) 10 ANZ Insurance Cases 61-450 at 75,170

(2) Subject to the succeeding provisions of this section, where the act could reasonably be regarded as being capable of causing or contributing to a loss in respect of which insurance cover is provided by the contract, the insurer may refuse to pay the claim.

(3) Where the insured proves that no part of the loss that gave rise to the claim was caused by the act, the insurer may not refuse to pay the claim by reason only of the act.

The act (or omission) to which s54 applies is an act which would, but for s54, entitle the insurer to deny liability. Essentially, s54 provides that if the act or omission of the insured relied on by the insurer is of a type which could reasonably be regarded as being capable of causing or contributing to a loss covered by the insurance, the insurer may only refuse to pay the claim if the insured can not show that the act or omission did not cause the loss. If the act or omission is not of that type, but in fact caused prejudice to the insurer, the insurer can reduce its liability to an extent which reasonably represents the prejudice suffered.

The effect of s54(1) is to impose upon the insurer a prima facie liability to pay the insured's claim. The insurer may only reduce this liability to the extent that it establishes prejudice. Section 54 is relevant in a number of circumstances. We have already seen (see section 8 above) that it can permit late notification of circumstances where the contract of insurance contains an appropriate notification of circumstances clause. Other examples of its application include payment of defence costs and late notification of claims. These are looked at below:

Defence costs: It is usual for a professional indemnity insurance policy to require that the insurer's consent (perhaps in writing) be obtained prior to the incurring of defence costs.

Often, the insurer will engage legal representation for the insured directly and so issues regarding the payment of costs do not arise. However, if it is the insured who is primarily responsible for paying legal fees, the insurer's consent to the appointment of lawyers and the incurring of legal costs should, ideally, be obtained before such costs begin to accrue. However, the effect of s54 of the Act is that the insurer will usually nonetheless be obliged to pay the insured's defence costs, even if such consent has not been obtained, subject to any reasonableness requirement that may be contained in the policy and to the insurer being able to establish any prejudice as a result of being denied its opportunity to consent.[16]

Late notification of claims: On their face, claims made and notified policies appear to require the insured to inform the insurer of the fact that a claim has been made within the currency of the insurance policy. The effect of s54 of the Act is that the insured can notify the insurer of such claims even after the policy period has expired and be entitled to cover, subject to the insurer establishing prejudice[17] and assuming the claim occurred during the period of insurance.

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[16] See *Antico v Heath Fielding Australia Pty Ltd* (1997) 9 ANZ Insurance Cases 61-371

[17] *FAI v Australian Hospital Care, Supra*

11. Section 41 – settlement of claims

Professional indemnity policies (as with all liability policies) will often contain an express provision requiring the insured to obtain the insurer's consent to any settlement of a claim made by a third party against the insured. This can place the insured in a difficult position if it wants to settle a claim prior to the insurer confirming that it will provide indemnity to the insured under the policy.

Section 41 of the Act can assist the insured in these circumstances. It provides:

> (1) This section applies where it would constitute a breach of a contract of liability insurance if, without the consent of the insurer, the insured were to:
>
> (a) settle or compromise a claim made against the insured; or
>
> (b) make an admission or payment in respect of such a claim.
>
> (2) An insured who has made a claim under a contract of liability insurance may at any time, by notice in writing given to the insurer, require the insurer to inform the insured in writing:
>
> (a) whether the insurer admits that the contract applies to the claim; and
>
> (b) if the insurer so admits, whether the insurer proposes to conduct, on behalf of the insured, the negotiations and any legal proceedings in respect of the claim made against the insured.
>
> (3) Where the insurer does not, within a reasonable time after the notice was given, inform the insured that the insurer admits that the contract of liability insurance applies to the claim and that the insurer proposes to conduct, on behalf of the insured, the negotiations and any legal proceedings in respect of the claim made against the insured, the insurer may not refuse payment of the claim, and the amount payable in respect of the claim is not reduced, by reason only that the insured breached the contract as mentioned in subsection (1).

This allows the insured to give the insurer written notice requiring the insurer to inform the insured whether, in effect, it will indemnify the insured and take over conduct of the defence of the claim. If the insurer does not confirm it will do so within a reasonable time, it is then prevented from denying the insured's claim solely on the grounds that its consent was not obtained to a subsequent settlement. Section 41 does not define what constitutes a "reasonable time".

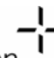
12. Section 45 – double insurance

12.1 Sections 45 and 76

The issue of double insurance is dealt with expressly by the Act. Two sections are relevant:

Section 45:

> (1) Where a provision included in a contract of general insurance has the effect of limiting or excluding the liability of the insurer under the contract by reason that the insured has entered into some other contract of insurance, not being a contract



required to be effected by or under a law, including a law of a State or Territory, the provision is void.

(2) Subsection (1) does not apply in relation to a contract that provides insurance cover in respect of some or all of so much of a loss as is not covered by a contract of insurance that is specified in the first-mentioned contract.

Section 45 should be read with section 76(1):

> When 2 or more insurers are liable under separate contracts of general insurance to the same insured in respect of the same loss, the insured is, subject to subsection (2), entitled immediately to recover from any one or more of those insurers such amount as will, or such amounts as will in the aggregate, indemnify the insured fully in respect of the loss.

The combination of these two sections gives an insured an unfettered discretion as to which insurer to target. Considerations are likely to include the terms of the insuring clause, excess provisions, the existence of aggregate retentions, policy conditions – particularly exclusions. Where there is a possibility that an exclusion may apply under one policy but not the other, the insured will target the policy without the exclusion (even perhaps if there is a higher excess) and leave the "other" insurer to struggle with the first insurer over the interpretation of the policy. As a result of the enactment of section 45 insurers now rely on the clauses requiring notice of other insurance.

12.2 HIH Casualty and General Insurance Limited v Pluim Constructions

Subsection 45(2) creates a significant exception to subsection 45(1) where "[another] *contract that provides insurance cover … is specified in the* [primary] *contract*". The extent to which the other policy must be specified has been considered by the New South Wales Court of Appeal in *HIH Casualty and General Insurance Limited v Pluim Constructions* (2000) 11 ANZ Ins Case 61 – 477.

Pluim Constructions (***Constructions***) was doing building work at a club. Related companies Pluim Detail Joinery Pty Ltd (***Joinery***) and Pluim Commercial Landscapes Pty Ltd (***Landscape***) were also involved with the job.

Mr Knight, a Landscape employee, was asked to assist Constructions by removing debris from the site using vehicles belonging to Landscapes, and in the course of doing so sustained a knee injury from glass shards.

Constructions had public liability insurance with the appellant (***HIH***). The club as Principal also had relevant public liability insurance with the Commercial Union Assurance company of Australia Ltd (***CU***) which responded to the claim.

Although HIH did not deny indemnity, it argued that a condition of the HIH policy (condition 7) allowed it to escape liability. Condition 7 provided that, in the event that the Principal agreed to provide a policy of insurance, then HIH would only indemnify the insured for such liability not covered by the policy of insurance provided by the Principal. The trial judge found condition 7 was rendered void by s45(1) and that the CU Policy was

not "*specified*" in the HIH policy for the purposes of the exception provided in subsection 45(2).

The issue was whether or not the words "*the policy of insurance provided by the Principal*" in condition 7 of the HIH policy were a sufficient description of the CU policies so as to bring the circumstances within the meaning of s45(2). The court held that the language of the condition was too general and not of sufficient specificity to satisfy s45(2). There was no identification of any particular policy with any particular insurer.

It followed that Constructions had double insurance. Significantly, the absence of formal claims for contribution between the two insurers did not prevent the court from making appropriate orders to finally dispose of the disputes in order to avoid further litigation.

13. Arbitration clauses

Section 43 of the Act provides:

(1) where a provision included in a contract of insurance has the effect of:

(a) requiring, authorising, or otherwise providing for differences or disputes in connection with the contract to be referred to arbitration; or

(b) limiting the rights of the otherwise confirmed by the contract on the insured by reference to an agreement to submit a difference or dispute to arbitration;

(c) the provision is void.

(2) Subsection (1) does not affect an agreement to submit a dispute or difference to arbitration if the agreement was made after the dispute or difference arose.

This provision prevents an insurer enforcing an arbitration clause against an insured. The parties are able to agree to arbitration after the dispute arose.

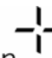
14. Restrictions on contracting out

14.1 Prohibition in s52 of the Act

Section 52 of the Act effectively prohibits the contracting out of the Act, where this would prejudice an insured or other interested third party. Section 52 provides:

(1) Where a provision of a contract of insurance (including a provision that is not set out in the contract but is incorporated in the contract by another provision of the contract) purports to exclude, restrict or modify, or would but for this subsection, have the effect of excluding, restricting or modifying, to the prejudice of a person other than the insurer, the operation of this Act, the provision is void.

(2) Subsection (1) does not apply to or in relation to a provision the inclusion of which in the contract is expressly authorised by this Act.



14.2 Impact on "prior circumstances" exclusions

An interesting issue is the impact of s52 on exclusions, frequently found in professional indemnity policies, which exclude liability for claims arising from circumstances known to the insured at the time the policy was taken out.

The question is whether an exclusion of that type can be said to have the effect of excluding, restricting or modifying to the prejudice of the insured the operation of the provisions of the Act dealing with misrepresentation and non-disclosure with the result that it is rendered void by section 52.

The only case which appears to have considered the question is *Pech v Tilgals* (1994) 28 ALJR 197. In that case, an accountant had given negligent tax advice. The policy contained an exclusion in respect of claims arising out of circumstances which the insured knew and which a reasonable person in the position of the insured would have considered may give rise to a claim. Dunford J found that the insured did know circumstances which would have alerted a reasonable person in the position of the insured of a possible claim. Consequently, he held the exclusion applied:

> "*But the Special Exclusion CL 3.2 is not concerned with non-disclosure; the claims specified are excluded from the cover whether the circumstances are disclosed or not, and accordingly the provisions of s 28 are not excluded or modified by the clause. The clause excluding claims notified to the insured before the commencement of the policy or arising out of anything done or omitted before such commencement would not have anything to do with non-disclosure, and similar considerations, in my view, apply to the clause here under consideration.*"

There are, however, difficulties with this analysis. Although the clause applies whether or not the circumstances are disclosed, it could be argued that the clause is clearly intended to protect the insurer against non-disclosure because anything which is disclosed could be made the subject of a specific exclusion or the insurer could, bearing that fact in mind, refuse to enter into the contract. It is true that the clause does not operate by reference to a non-disclosure. However, that is not the test under section 52. In any event, this is an issue for which we await further guidance from the courts.

14.3 Choice of law and jurisdiction clauses

Section 8 of the Act states:

> (1) Subject to section 9, the application of this Act extends to contracts of insurance and proposed contracts of insurance the proper law of which is or would be the law of a State or the law of a Territory in which this Act applies or to which this Act extends.
>
> (2) For the purposes of subsection (1), where the proper law of a contract or proposed contract would, but for an <u>express provision</u> to the contrary included or to be included in the contract or in some other contract, be the law of a State or of a Territory in which this Act applies or to which this Act extends, then, notwithstanding that provision, the proper law of the contract is the law of that State or Territory. [own underlining added for emphasis]

This provision calls into question the validity of choice of law and choice of jurisdiction clauses in insurance contracts. The leading authority on this issue is the High Court decision in *Akai Pty Limited v People's Insurance Co Ltd* (1996) 188 CLR 418.

14.4 Akai Pty Limited v People's Insurance Co Ltd

Background: Akai was a company incorporated in New South Wales and a wholly-owned subsidiary of a Japanese company. In 1991, Akai entered into a comprehensive credit insurance contract with The People's Insurance Co (***PIC***),a company incorporated in Singapore.

PIC did not carry on business in Australia. The policy was negotiated by Australian brokers directly with PIC's managers in Singapore. The policy was to cover Akai's business activities in Australia and New Zealand.

Under the policy, PIC agreed to indemnify Akai for loss suffered as a result for non-payment of goods supplied to Akai's customers on credit. The maximum liability under the policy was specified in Australian dollars (namely $2 million). Further, the Australian dollar was the currency in which the premium was payable.

Clause 9 of Art VI (***Clause 9***) of the policy provided:

> Governing Law
>
> This policy shall be governed by the laws of England. Any dispute arising from this policy shall be referred to the Courts of England.

Accordingly, the first part of this provision constituted a choice of law clause. The second aspect of the provision was a choice of jurisdiction clause.

It appears that Clause 9 was the result of negotiation between the parties. PIC's standard policy wording contained Singapore law and Singapore jurisdiction clauses. Akai had wanted the policy to be governed by Australian law. English law and the courts of England was the compromise finally reached by the parties. Both parties had recourse to legal advice on this issue before arriving at this compromise.

During the currency of the policy, one of Akai's largest debtors, Norman Ross Homeworks Pty Ltd (***Norman Ross***) went into receivership. Norman Ross operated approximately 36 retail stores, mostly in New South Wales. Subsequently, Akai made a claim under the policy for approximately AUD1.3 million. PIC alleged that breaches of the policy entitled it to refuse to indemnify Akai. Akai commenced proceedings in the New South Wales Supreme Court for a declaration that PIC was liable to indemnify it under the policy for loss it suffered in respect of moneys owed to it by Norman Ross. As part of its case, Akai sought to rely on s54 of the Act.

On the same day as it commenced proceedings in New South Wales, Akai also commenced proceedings in the English High Court of Justice (Queen's Bench Division – Commercial Court) seeking the same relief in effect as it sought in the New South Wales proceedings. It should be noted that there is no English equivalent to s54 of the Act. Therefore, it was in Akai's favour for proceedings to be determined according to Australian law.

In reliance on Clause 9, PIC resisted the claim in the New South Wales court by seeking a stay of the proceedings until further order or until the final determination of the English proceedings brought by Akai against it. It was necessary for the NSW court to determine whether the Act applied to the contract. In order for the Act to apply, it was necessary for Australian law to be the proper law of the contract. At first instance, O'Keefe CJ Comm D granted the stay of proceedings sought by PIC, holding that the Act did not apply to the contract.

The decision at first instance was affirmed by the majority of the New South Wales Court of Appeal. The Court of Appeal unanimously held that s8(2) of the Act required the express choice of law clause to be ignored in determining the proper law of the contract for the purposes of the Act. However in a split decision (2-1), the Court of Appeal found that the choice of jurisdiction clause was not an "express clause" within the meaning of s8(2) of the Act and, therefore, was a valid ground for determining that the proper law of the contract was the law of England. Accordingly, the Act was held not to apply.

High Court Decision: By a bare majority (3-2), this decision of the New South Wales' Court of Appeal was reversed in the High Court and PIC's application for a stay was dismissed. In reaching its decision, the majority (Toohey, Gaudron and Gummow JJ) addressed the following two issues:-

- What was the proper law of the insurance contract?
- Should a stay of proceedings be granted?

The Proper Law of the Contract: According to the majority, the Act applies to an insurance contract *if* the law of an Australian State or Territory is the proper law of the contract.

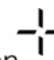
The traditional approach to determining the proper law of a contract involves a three tier approach, namely:

1. determine whether the contract contains an express choice of law by the parties;
2. if there is no express choice of law, assess whether the terms and context of the parties' bargain reveals an implied intention to select a proper law (for example, the existence of a choice of jurisdiction clause);
3. If no intention can be implied from the circumstances, identify the system of law that objectively has the closest and most real connection with the contract.[18]

The majority of the High Court in *Akai's case* modified the above traditional three tier approach to ascertaining the proper law of a contract by combining the first two issues to form a two tier approach.[19] According to the majority, the second step of the traditional approach was merely a species of the first step.

[18] Whilst the three tier approach has been adopted in some Australian decisions (see *John Kaldor Fabricmaker Pty Ltd v Mitchell Cotts Freight (Aust) Pty Ltd* (1989) 18 NSWLR 172) other cases suggest a two tier approach which combines the second and third step into one: see *Memdelson-Zeller Co Inc v T & C Providores Pty Ltd* [1981] 1 NSWLR 366.

[19] This two tier approach as annunciated by the majority in *Akai's case*, has subsequently been adopted in *KA & C Smith Pty Ltd (trading as Uticolour Australia) v Ward & Ors* Unreported, Supreme Court of New South Wales – Equity Division, 23 December 1998.



The majority construed the expression "express provision to the contrary" in s8 of the Act to extend to "those provisions of the contract from which, *or by recourse to which*, it would be determined that the parties to the contract had selected or chosen a proper law which was not the law of a State or a Territory [of Australia]"[20](*emphasis added*). In simple terms, the court held that the term "express" in s8(2) referred to the nature of the contractual term and not the nature of the choice of law.[21]

Therefore the first aspect of Clause 9, being a choice of law clause, clearly fell within the scope of an "express provision to the contrary" in s8(2) of the Act and was dismissed by the majority when determining the proper law of the contract.

Similarly, the majority held that the choice of jurisdiction clause in Clause 9 also had to be disregarded as it too fell within the exclusion in s8(2) of the Act as it was an express term of the contract which had the potential effect of changing the proper law of the contract.

Once the choice of law and jurisdiction provisions in Clause 9 were disregarded, the majority proceeded to ascertain the system of law with which the contract had its "closest and most real connection". In the circumstances, this was held to be New South Wales. In reaching this decision, the majority considered a number of factors, including:

- the places of residence or business of the parties;
- the place of contracting;
- the place of performance of the contract;
- the nature and subject matter of the contract.

On this approach, the majority found that the contract had no practical connection with Singapore apart from the fact that the insurer was incorporated in Singapore and had no factual connection at all to England. Whereas, the risk insured under the contract was very substantially situated in New South Wales, the debt the subject of the claim arose in New South Wales and the limit of liability and the policy currency was in Australian currency. Finally, the countries specified to be covered by the policy were identified as Australia and New Zealand.

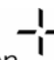
Unfortunately, the majority did not provide any indication as to the importance placed on each of these indicia in deciding the objective proper law of an insurance contract.

Stay of Proceedings: Where a plaintiff commences proceedings in jurisdiction in breach of a choice of jurisdiction clause, the court retains a discretion as to whether or not a stay of the proceedings should be granted. The guiding principle to the exercise of this discretion is that the discretion should be exercised by granting the stay of proceedings unless there is a strong cause for not doing so[22]. The burden of proving such a strong cause is on the plaintiff (that is, the party seeking to bring the proceedings in contravention

[20] Above n15 at 387.

[21] Greene J. "Party autonomy in choice of law in contract: Through the lens of Akai Pty Ltd v The People's Insurance Company ", (1997) 25 ABLR 330 at 332.

[22] *The Eleftheris* [1970] P.94 at 99 per Brandon J (as he then was).

of the jurisdiction agreement). In reaching its decision a court is required to take into account all the circumstances of the case[23].

Whilst the High Court unanimously agreed on the general principles applying to the exercise of its discretion to grant a stay of proceedings, the court was divided on the application of the general principles to the particular circumstances in this case.

As mentioned above, the majority agreed that if parties had agreed to a foreign jurisdiction clause, there exists a firm disposition in favour of maintaining that bargain unless strong reasons be adduced against the stay, it being an important principle of law that parties who have made a contract be kept to their bargain[24].

The majority proceeded on two assumptions:

1. that the Act applied to the contract of insurance in question; and
2. that an English court would apply English law which would not include as a component any relevant equivalent provisions of the Act (in particular s54 of the Act).

Relying on these assumptions the majority held that if a stay of the proceedings was granted, it would result in the preference of the private agreement of parties resulting in the circumvention of the Act. According to the majority, this would be in contravention of the policy of the Act and therefore was a strong reason against the exercise of the discretion in favour of the stay[25].

Further, the majority held that s52 of the Act precluded reliance on the foreign jurisdiction clause as the section operates to render void a provision of a contract of insurance which would, but for the effect of s52(1), have the effect of excluding, restricting or modifying to the prejudice of an insured (in this case, Akai) the operation of the Act. The foreign jurisdiction clause was held to be a provision which had such an effect. Accordingly, the application for stay had to be considered on the basis that there was no contractual obligation to refer disputes to any foreign court. Once the foreign jurisdiction clause was disregarded, the majority considered that there was an overwhelming number of circumstances favouring the matter proceeding in the New South Wales Supreme Court as opposed to the Commercial Court in London which combined to constitute a strong reason for refusing to stay the proceedings in New South Wales.[26]

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[23] Circumstances which need to be considered include:- (a) in what country the evidence on the issues of fact is situated, or more readily available, and the effect of that on the relative convenience and expense of trial; (b) whether the law of the foreign court applies and if so, whether it is different to the law of the desired forum in material respects; (c) with what country is either party connected, and how closely; (d) whether the defendants genuinely desire trial in a foreign country or are only seeking procedural advantages; (e) whether the plaintiff's would be prejudiced by having to sue in a foreign court because they would:- i) be deprived of security for their claim; ii)be unable to enforce any judgment obtained; iii) be faced with a time bar not applicable in the desired court; or iv)for political, racial, religious or other reasons be unlikely to get a fair trial: Id at 99 – 100.

[24] Above n15 at 394 in reliance on Dixon J's comments in *Huddart Parker Ltd v The Ship "Mill Hill"* (1950) 81 CLR 502 at 508-9.

[25] Id at 395.

[26] Id at 395-6.

Summary: The Act applies to contracts of insurance where the proper law of the contract is or would, if viewed objectively, be Australian law.

In determining the proper law of the contract, an Australian court must disregard any provision in the contract by which, or by recourse to which, it would be determined that the parties to the contract had selected a proper law which is not Australian law. Such provisions include choice of law clauses and choice of jurisdiction clauses selecting a non-Australian system of law and forum respectively[27].

In simple terms, an express choice of law or express choice of jurisdiction clause can not prevent the proper law of the contract from being Australian and the Act applying where Australian law would otherwise be applicable.

Akai – Practical Implications: There remains some doubt as to the effectiveness of choice of law and choice of jurisdiction clauses that refer to non-Australian law and courts in contracts of insurance.

Following the High Court's decision in *Akai*, it appears that the approach which will be taken by an Australian court is that if the proper law of an insurance contract is Australian law (when viewed objectively), then the Act will apply to the contract and Australian courts will have jurisdiction notwithstanding a choice of law and choice of jurisdiction clauses to the contrary. Essentially, *Akai's case* prevents parties from contracting out of the Act where the system of law with the closest and most real connection to the contract is Australian law.

However, at a practical level, it may still be possible for a party (most likely to be the insurer) to enforce the choice of law and choice of jurisdiction clause by recourse to proceedings in the forum selected by the parties in their contract to obtain an anti-suit injunction. The effectiveness of this injunction as a bar to the Australian proceedings will depend upon:

(a) whether the party intending to proceed in Australia is present in or has assets in the jurisdiction of the selected forum against which a judgment for contempt of court for breach of the injunction could be enforced;

(b) whether the jurisdiction in which the Australian judgment will be enforced will recognise the Australian judgment.

Therefore, there remains the possibility for parties to contracts of insurance to continue to be involved in costly and time consuming litigation aimed at resolving the issue of the jurisdiction applicable to the contract despite parties having stipulated the jurisdiction in their contract.

The Review of the Act: The Draft Bill reflects the Review Panel's recommendation that s8 of the Act should be amended to make it clear that it applies to all contracts issued by direct off-shore foreign insurers to Australian insureds for Australian risks.

The Review Panel noted that by providing a more direct statement about the intended scope of the Act, this may assist in circumstances where a foreign court is called upon to

[27] Sutton K. (ed.) "Australian & New Zealand Insurance Reporter" Volume 1 at 4-210

determine questions of the Act's applicability and therefore, go some way towards addressing the issue of practical enforcement by consumers.

However, there is still the potential risk that a foreign court may not apply the requirements of the Act in relation to the contract of insurance.

Part Two: HIH Casualty & General Insurance Limited (in liquidation) v Wallace

1. Introduction to part two

This decision of the New South Wales Supreme Court in November 2006 held that the *Insurance Act 1902* (NSW) (**Insurance Act**) applies to reinsurance contracts, and that as a result an arbitration clause in a reinsurance contract is not binding on a reinsured as a matter of New South Wales law.[28]

2. How does this decision affect you?

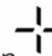
- The application of the Insurance Act to reinsurance policies which a Court has considered in this decision for the first time radically alters[29] the law of reinsurance as it is applied in New South Wales.
- The law of New South Wales is now out of step with the law in other states of Australia, although there is a somewhat similar old legislation in Victoria which now may also be interpreted to apply to reinsurance.
- New South Wales law and New South Wales Courts provide reinsureds with a significant juridical advantage.
- The decision suggests that this Act, at least insofar as it prevents reinsurers from enforcing an arbitration clause, has to be applied to any reinsurance matter heard in a New South Wales court no matter what the governing law of the contract is expressed to be by the parties.
- Together with the Australian High Court's recent decision in *Asset Insure v New Cap Re* it may mean that 'insurance' in other acts, such as s6 of the *Law Reform Miscellaneous Provisions Act* (1946) (NSW) and similar legislation in other states and territories also includes 'reinsurance'.

3. Background

The decision arises from a dispute in relation to various quota share reinsurance treaties under which Lloyd's Syndicate 683 (**reinsurers**) reinsured HIH Casualty & General Insurance Limited for professional indemnity insurance policies underwritten by HIH between 1993 and 1997.

[28] *HIH Casualty & General Insurance Ltd (in liquidation) v Wallace & others* [2006] NSWSC 1158. This section of the paper was originally presented by Michael Quinlan, Allens Arthur Robinson partner, in March 2007.

[29] Or confirms the views of some commentators as to the correct operation of the *Insurance Act* (see footnote 3, below).



The liquidator of HIH commenced proceedings against reinsurers in the Supreme Court of New South Wales (**proceedings**) when reinsurers sought to challenge the application to the reinsurance treaties of the decision of the House of Lords in *Charter Reinsurance Company Limited v Fagan* [1997] AC 313. Reinsurers have argued that their obligation to indemnify HIH under the reinsurance treaties did not arise until HIH actually paid the original insureds under the original policies. This decision did not resolve that issue.

Reinsurers sought a stay of the proceedings in reliance on an arbitration clause included in each of the reinsurance treaties. Justice Einstein refused the reinsurer's application for a stay, in part, on the grounds that the arbitration clause in each reinsurance treaty was not binding on HIH as a matter of New South Wales law under s19 of the Insurance Act.

4. Application of the Insurance Act to reinsurance contracts

In Australia at the federal level, the *Insurance Contracts Act 1984* (Cth)[30] **(Act)** varied many general principles of insurance law that were regarded as unfair to insureds. However the Insurance Contracts Act expressly does not apply to reinsurance.

Since the Act came into force there has been a tendency to overlook earlier state legislation, such as the Insurance Act 1902, which also varied some general principles of insurance law for similar consumer protection reasons.

Prior to the Act, the Insurance Act affected all classes of insurance in New South Wales other than maritime and life in the following key ways:

- the right of an insurer to rely on a failure by an insured to comply with a term of the insurance contract;
- the right of an insurer to rely on a misrepresentation or non-disclosure by an insured;
- the right of an insurer to rely on an exclusion clause; and
- the right of an insured to commence court proceedings notwithstanding an arbitration clause.

Each of these is considered in turn.

4.1 Breach of an insurance contract by an insured

Section 18(1) provides:

> In any proceedings taken in a court in respect of a difference or dispute arising out of a contract of insurance, if it appears to the Court that a failure by the insured to observe or perform a term or condition of the contract of insurance may reasonably be excused on the ground that the insurer was not prejudiced by the failure, the Court may order that the failure be excused.

An important difference between this section and s54 of the Act is that s18(1) only applies where "*the insurer was <u>not</u> prejudiced by the failure".* There is no provision in s18(1) to reduce the liability of an insurer to the extent that it was prejudiced. Therefore, if an insurer

is prejudiced by the breach of contract, then the insured is not entitled to relief from the consequences of that breach no matter how slight that prejudice.

Section 18(1) applies where there is a failure by the insured to observe or perform "*a term or condition of the contract of insurance"*. Before s18A was inserted, a few cases considered whether s18 applied to a failure by an insured to comply with its duty of disclosure. This in turn depended on whether or not the duty of utmost good faith and the corresponding duty of disclosure arose out of an implied term of the contract or were obligations independent of the contract.

This issue was resolved by the High Court in *Khoury v GIO (NSW)* (1994) 54 ALR 639, which held that the duty of disclosure was not an implied term of the contract. Mr Khoury could therefore not rely on s18 to excuse a breach of the duty of disclosure.

Section 18 is potentially very important for reinsurance contracts governed by New South Wales law. Reinsurance contracts frequently contain conditions obliging a reinsured to give notice of claims and to co-operate with reinsurers in the handing of claims[31]. A breach of such conditions might well be excused by s18 – see by analogy the decision of Yeldham J in *Panorama Plant Hire Pty Limited v Mercantile Mutual Insurance Company Limited* [1980] 2 NSWLR 618.

4.2 Misrepresentation and non-disclosure

Section 18A provides, in essence that a contract of insurance may not be avoided because of a misrepresentation or non-disclosure by an insured unless it was fraudulent or:

> The insured knew or a reasonable person in the insured's circumstances ought to have known that the statement was material to the insurer in relation to the contract of insurance.

The two most important consequences of this section are that:

(a) it negates the effect of "basis of contract clauses" and any scope for the doctrine of "constructive materiality"; and

(b) one looks at what a reasonable person in the insured's circumstances would regard as material, rather than what a prudent insurer would regard as material.

Basis of Contract Clauses

At common law a basis of contract clause entitles an insurer to avoid a contract for misrepresentation or non-disclosure in a proposal form whether or not the misrepresentation or non-disclosure was material to the decision of the insurer to provide cover. Section 18A prevents an insurer from relying on such a clause to avoid a contract where the relevant misrepresentation or non-disclosure was not material.

Constructive Materiality

It has also been suggested that, at common law, there is a doctrine of "constructive materiality" which provides that a matter is deemed to be material by the very fact that a

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[30] This part of the paper does not take into account the proposed reforms of the Act that are currently under consideration.

[31] A claims co-operation clause of that type was consider in *Gan Insurance Company Ltd v The Tai Ping Insurance Company Limited* [2002] EWCA Civ 248.

question relating to that matter is included in a proposal form. Section 18A overcomes any such doctrine.

Subjective Test of Materiality

At common law an insurer is entitled to avoid a contract for non-disclosure if an insured fails to disclose a matter which a prudent insurer would regard as material to its decision whether to not to provide cover and the terms on which cover should be provided (including the premium). Section 18A takes away this right and provides, instead, that an insurer can only avoid a contract if

> "a reasonable person in the insured's circumstances ought to have known that the statement was material to the insurer in relation to the contract of insurance".

There is an interesting comparison between this section and s21(1)(b) of the Act. The latter provides that an insured is obliged to disclose any matter which "a reasonable person in the circumstances could be expected to *know to be a matter so relevant"*. This section was based on draft legislation prepared by the Australian Law Reform Commission which referred to a person "*in the circumstances of the insured*". This is a subjective test requiring consideration of the circumstances of the particular insured. Before the Insurance Contracts Act came into force submissions were put to the government that the test should be an objective one – ie, an insured is obliged to disclose matters which a reasonable insured ought to know would be material to in insurer. Rather than resolve this issue, the section was drafted in an ambiguous manner, which has led to conflicting decisions as to whether and to what extent s21(1)(b) entitles a court to look at the circumstances of the particular insured.

By contrast with the ambiguity of the Act and to the position at English law[32], s18A clearly requires the court to consider the circumstances of the particular insured. This offers greater protection to insureds who are naive in insurance matters but arguably offers less protection to, for example, insurance lawyers.

4.3 Exclusion clauses

Section 18B restricts the right of an insurer to rely on an exclusion clause where the circumstance excluded did not in fact contribute to the particular loss. The following points arise from the wording of this section.

(a) The section is headed "limitation on exclusion clauses" but applies where

> "the circumstances in which the insurer is bound to indemnify the insured are so defined as to exclude or limit the liability of the insurer to indemnify the insured on the happening of particular events or at least existence of particular circumstances" (s18B(1)(a)).

It is therefore arguable that this section applies not only to exclusion clauses, but might also have some application to clauses defining the scope of cover. The section might therefore have a broad application similar to s54 of the Act which refers to "*the effect of a contract of insurance".*

[32] Where, according to *Pan Atlantic Insurance Co Ltd & Anor v Pine Top Insurance Limited* [1995] 1 AC 501, the test under section 18 of the Marine Insurance Act 1906 is whether the relevant non-disclosure was one that would have an effect on the mind of the prudent insurer in estimating the risk.

(b) Section 18B only applies where

> "the liability of the insurer has been so defined because the happening of those events or the existence of those circumstances was in the view of the insurer likely to increase the risk of loss occurring" (s18B(1)(b)).

This is an odd provision which denies an insured any entitlement to relief where the relevant exclusion clause was inserted for some other reason, or even for no particular reason. For example:

- an insured might be excused from an exclusion for claims for damage to a car while the driver is drunk, if that drunkenness did not contribute to the accident; but
- an insured cannot be excused if, for example, the policy excludes claims made between an insured changing address and informing the insurer of its new address.

This provision will also deny an insured any relief for failure to notify a claim under a claims made and notified policy.

Section 18B applies where "the circumstances in which the insurer is bound to indemnify the insured are so defined…". In this respect it is probably broader that section 54 of the Insurance Contracts Act, which in many ways covers the same ground as section 18B, but which only applies to "some act of the insured or of some other person".

A consequence of this difference is that s18B, but not s54, would apply to an exclusion for claims made while a state of war existed between the country of the insured and the country of the insurer. A further difference is that s18B, but not s54, would apply to latent defects, although these would generally be covered by s46 of the Act.

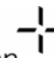
Section 18B only applies where the relevant loss "was not caused or contributed to by" the relevant circumstances. There is no provision enabling the liability of an insurer to be reduced to the extent that the relevant circumstances contributed to the loss. In this respect s18B provides less protection to an insured at s54.

5. Insurance Act not previously applied to reinsurance

The Insurance Act applies to all contracts of insurance except those set out in s21 and the regulations made under that section. The effect of those provisions is that the parts of the Insurance Act that reform general principles of insurance law do not apply to certain insurance contracts, including most relevantly:

- contracts of insurance that are subject to the Act;
- contracts of marine insurance; and
- contracts of life insurance.

As noted earlier following the introduction of the Act in 1984 most insurers and reinsurers gave the New South Wales Insurance Act no further thought.



Although some commentators and lawyers[33] have previously expressed the view that the Insurance Act would apply to a contract of reinsurance, because a contract of reinsurance is a type or variety of insurance contract and because contracts of reinsurance are expressly excluded from the operation of the Act, *HIH v Wallace* is the first case to ever address that issue.

Justice Einstein held that the Insurance Act does apply to reinsurance contracts. In reaching that conclusion, his Honour considered various English and Australian authorities. His Honour considered and distinguished the decision of the House of Lords in *Agnew v Lansforsakringsbolagens* [2000] Lloyd's Rep IR 317, and held that reinsurance contracts were insurance contracts.

However, it remains unclear whether the Insurance Act applies to contracts of reinsurance where the original insurance can be characterised as marine or life insurance. This issue would seem to depend on whether the subject matter of the reinsurance contract should be regarded as:

- the liability of the reinsured to pay claims under the original insurance policy; or
- the original risk.

If it is accepted that a reinsurance contract is an insurance of the original subject matter, the reinsured's liability under the original insurance merely serving to provide it with an insurable interest, then it should follow that reinsurance of original marine or life insurance policies should be similarly characterised. This may be important depending upon the type of treaty written.

6. The International Arbitration Act 1974 (Cth) & reinsurance contracts

Australia is a signatory to the Convention on the Recognition and Enforcement of Foreign Arbitral Awards 1958 (**Convention**). Article II(3) of the Convention provides that a court of a contracting state *'when seized of an action'* which is the subject of an arbitration agreement *'shall at the request of one of the parties refer the parties to arbitration, unless it finds that the said agreement is null and void, inoperative or incapable of being performed'*.

Australia's obligations under article II(3) of the Convention are implemented under s7 of the International Arbitration Act 1974 (Cth) which requires a court to stay proceedings commenced in breach of an 'arbitration agreement', unless that agreement is 'void, inoperative or incapable of being performed'. Reinsurers sought a stay under section 7. However Justice Einstein ruled that section 19 of the Insurance Act rendered the arbitration clause in each reinsurance treaty inoperative and refused to grant the stay.

Justice Einstein also decided that s19 of the Insurance Act constituted a mandatory rule of the forum, such that it must be applied by a New South Wales court, irrespective of the court's conclusion about the law governing the contract.

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[33] Including Allens Arthur Robinson Partner, Malcolm Stephens, in his prescient paper 'State Legislation Affecting General Insurance Law" that was presented on 13 June 2002 and from which parts of this paper have been sourced.

7. Arbitration clauses generally

In addition to an arbitration clause, each reinsurance treaty considered in *HIH v Wallace* contained the following service of suit clause:

> The Reinsurer hereon agrees that:
>
> (i) in the event of a dispute arising under this agreement, the Reinsurer, at the request of the Company will submit to the jurisdiction of any competent court in the Commonwealth of Australia. Such dispute shall be determined in accordance with the law in practice applicable in such Court.

Justice Einstein considered a number of English authorities on contracts containing apparently inconsistent jurisdiction and arbitration clauses. His Honour found that the combined effect in this case of the service of suit clause and the arbitration clause in each reinsurance treaty was to provide HIH with an option to litigate in any court of competent jurisdiction in Australia, or to require reinsurers to submit to arbitration. Once HIH elected to commence proceedings in New South Wales, the effect of the service of suit clause was to provide that the law of New South Wales would govern the contract[34]. As a result his Honour found that the International Arbitration Act had no application, the decision to arbitrate being contractually reserved to HIH.

Further, it is a requirement of both articles II(1) and (2) of the Convention and s3(1) the International Arbitration Act that arbitration agreements be in writing. Justice Einstein considered various international texts and authorities in relation to this requirement. He also considered evidence before him relating to the procedure for issuing insurance and reinsurance policies at Lloyd's. He found that a number of the reinsurance treaties failed to meet the requirements of article II(1) and (2) of the Convention, which were as follows:

- the arbitration agreement must be signed by both parties; or
- the arbitration agreement must be contained in an exchange of letters or telegrams.

Justice Einstein held that it was not sufficient for one party to stipulate that the contract was subject to an arbitration agreement and for both parties to continue to act on that basis. Where the arbitration agreement consisted of a clause in a treaty wording or other agreement, his Honour held that it must be signed by both parties, before article II of the Convention is enlivened. He ruled that proof by Reinsurers that the Reinsurance Treaties were processed in accordance with LPSO procedures did not discharge the burden that fell on them to establish the existence of the arbitration agreement in each case.

It will be interesting to see whether Courts in other common law jurisdictions might adopt some of the reasoning of this case in considering the law in their jurisdiction to govern policies of insurance with a jurisdiction election clause and indeed whether those clauses

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[34] It is interesting to contrast this case with the recent English decision in *425 Catlin Syndicate Ltd & Ors v Adam Land & Cattle Co* [2006] EWHC 2065 (Com) which considered the same clause and concluded that the insurance was governed by English law but the insured had a contractual right to elect for the jurisdiction of a Court in Nebraska. The judge concluded that the insurers plainly took the risk that the Nebraskan Court might not apply English law as the English Court might do. He stayed English proceedings so that the matter could proceed in Nebraska.

remain in policy wordings as the market considers the implications of this decision and English decisions on such clauses such as *Catlin v Adams*[35].

8. The Insurance Act and reinsurance contracts

Reinsurers have not appealed from the decision. The application of the Insurance Act to reinsurance policies in *HIH v Wallace* radically alters[36] the law of reinsurance as it is applied in New South Wales and has the potential to be the same in Victoria by reason of its potential application to the Victorian *Instruments Act 1958* (**Instruments Act**).

As noted above, the Insurance Act's provisions go far beyond the validity of arbitration clauses. The provisions which now apply to reinsurance contracts include, in addition to s19:

- s18(1) which empowers the court to excuse a failure by a reinsured to comply with a term of the contract where the reinsurer did not suffer prejudice as a result.
- s18A which operates, in essence to prevent a reinsurer from avoiding a contract of insurance for misrepresentation or non-disclosure by a reinsured unless the misrepresentation or non-disclosure was fraudulent, the reinsured knew, or a reasonable person in the reinsured's circumstances ought to have known, that the statement or matter was material to the reinsurer. In essence, s18A would replace the 'prudent reinsurer' test in relation to materiality with one that focuses on the circumstances of the reinsured and its state of mind as to materiality. (Arguably, this may not benefit a reinsured to the same extent as a more 'naive' consumer).
- s18B which limits the right of a reinsurer to rely upon an exclusion clause where the 'circumstances' excluded did not contribute to the loss in question.

Whilst the Court found that s19 had a mandatory application in a New South Wales Court it did not express any view as to whether that view extended to the other provisions of the Insurance Act.

8.1 The Instruments Act

As yet no case similar to *HIH v Wallace* has considered whether or not "insurance" includes "reinsurance" in the Victorian *Insurance Act 1958*. However, there seems to be no logical reason why it should not do so.

8.2 Application of the Instruments Act

The Instruments Act has a similar application, in very broad terms, to the Insurance Act. Although there do not appear to be any regulations expressly limiting its application, it would not apply to contracts of marine insurance or life insurance as Commonwealth legislation covers the field in this area. Furthermore, subject to one matter discussed below, there does not appear to be any room for the Instruments Act to operate on contracts governed by the Act.

[35] [2007] EWHC 2065 (see discussion above).

[36] Or confirms the view of some commentators as to the correct operation of the *Insurance Act (see 3 above).*

8.3 Misrepresentation and non-disclosure

Section 25 of the Act provides:

> No contract of insurance (other than a contract of life insurance) shall be avoided by reason only of any incorrect statement made by the proponent in any proposal or other document on the faith of which such contract was entered into revived or renewed by the insurer unless the statement so made was fraudulently untrue or material in relation to the risk of the insurer under the contract.

Unlike s18A of the Insurance Act, this section does not alter the common law rule that an insurer is entitled to avoid a contract if there is a non-disclosure of a matter which a prudent insurer would regard as material. The Act therefore repeats the common law test of materiality (this was confirmed by Pape J in *Babatsikos v Car Owners' Mutual Insurance Co Limited* [1970] VR 297).

Section 25 does change the common law, however, in that it prevents an insurer relying on a basis of contract clause or on any principle of "constructive materiality". These changes are the same as those discussed in relation to section 18A of the Insurance Act.

Like s18A of the Insurance Act, but unlike s28 of the Act, this section does not provide that the liability of an insurer shall be reduced to the extent it has been prejudiced by a material non-disclosure. Under s25 an insurer remains entitled to avoid a contract of insurance notwithstanding that a non-disclosure might be innocent and cause no prejudice to the insurer.

8.4 Failure to give notice or make a claim

Section 27 protects an insured against a failure "*to give any notice or make any claim in the manner and within the time required by the contract of insurance"* where:

(a) the failure was due to an "*accident mistake or other reasonable cause";* and

(b) the reinsurer has not "*been so prejudiced by such failure that it would be inequitable if such failure were not a bar to the maintenance of such proceedings".*

This section provides a fair amount of discretion to a court in determining what constitutes a "reasonable cause" in failing to comply with the insurance contract and determining the circumstances in which an insurer has been "so prejudiced" that it would be "inequitable" to allow the insured's claim to proceed.

Section 27 is rather awkwardly worded. It states that the relevant failure by the insured "*shall not be a bar to the maintenance of any proceedings…upon the contract by the insured".* It was argued in *GRE Insurance Limited v QBE Insurance Limited* [1985] VR 83 that the section could not be relied on to establish the liability of an insurer where the proceedings were brought by another insurer for contribution (rather than being brought by an insured for indemnity). The majority of the Full Court of the Supreme Court of Victoria rejected this argument on the basis that it would frustrate the clear intention of this section.

It was also argued in that case that the section did not operate where there was a failure by the insured to comply with a condition precedent to the insurance being "effected". It was argued that, as no insurance had been "effected", there was no "contract of insurance" on

which the section could operate. This argument was supported by Anderson J but was rejected by the majority of the Full Court.

Unlike s54 of the Act, s27 of the Instruments Act does not provide for the liability of an insurer to be reduced to the extent it was prejudiced by any such failure by an insured. This would generally work in favour of an insurer. If, however, a court held that the prejudice suffered by an insurer did not make it "inequitable" for the failure to be excused, then an insured might believe it could do better relying on s27 of the Instruments Act (which entitles the insured to full recovery) rather than s54 of the Act (which reduces the insured's recovery to the extent of any prejudice). This option is not open to an insured, however, as s54 would prevail over section 27 to the extent that there is a direct conflict. As s54(1) provides that, in the relevant circumstances, an insurer "may not" refuse to pay a claim but that its liability "is reduced" to the extent of the prejudice, one must assume that s54 "by necessary intendment" (see s7 of the Act) overrides s27 of the Instruments Act.

8.5 Arbitration

Section 28(2) entitles an insured to bring court proceedings notwithstanding any arbitration clause in the insurance contract.

9. Section 6, Law Reform Miscellaneous Provisions Act 1946 (NSW)

The decision in *HIH v Wallace* together with the High Court's decision in *Asset Insure v New Cap Re* also increases the likelihood that Courts will interpret the term "insurance" when it is used in other legislation as including "reinsurance". One such piece of legislation is s6 of the Act.

Relevantly, s6 of the *Law Reform Miscellaneous Provisions Act 1946 (NSW)* (**LRMP Act**) provides as follows:

(1) If any person (hereinafter in this Part referred to as the insured) has, whether before or after the commence of this Act, entered into a contract of insurance by which the person is indemnified against liability to pay any damages or compensation, the amount of the person's liability shall on the happening of the event giving rise to the claim for damages or compensation, and notwithstanding that the amount of such liability may not then have been determined, be a charge on all insurance moneys that are or may become payable in respect of that liability.

(4) Every such charge as aforesaid shall be enforceable by way of an action against the insurer in the same way and in the same court as if the action were an action to recover damages or compensation from the insured…

If s6 applied to reinsurance it would operate in this way:

- the direct insurer and the reinsured under a contract of reinsurance (**Insurer**)
- has entered into a contract of insurance (its contracts of reinsurance);
- by which the Insurer is indemnified by its reinsurer (**Reinsurer**) against liability to pay compensation (it is indemnified against its liability to indemnify those insured by it under the contracts of direct insurance) (**Direct Insureds**);

therefore, pursuant to s6:

- on the happening of the event giving rise to the claim for compensation (the notifications by the Direct Insureds under its contracts of insurance with the Insurer);
- a charge on all insurance moneys that are or may become payable in respect of that liability (the reinsurance proceeds due to the Insurer from the Reinsurer);
- is created in favour of the Direct Insureds and – subject to the Court granting leave - can be enforced pursuant to s6(4).

10. A liability to pay damages or compensation?

It might be argued that a contract of reinsurance does not indemnify the reinsured against its liability to "*pay any damages or compensation*" on the basis that arguably a payment pursuant to a contract of insurance does not meet the description of either "*damages*" or "*compensation*".

10.1 Damages

Whilst there is academic debate over whether an insurer's liability under a contract of insurance is a liability to pay damages[37], the better view is that absent a breach of contract by the insurer this is not the case. Windeyer J in the Supreme Court case of *Odyssey Re (Bermuda) Ltd v Reinsurance Australia Corp Ltd* (unreported 12/4/01) seems to have confirmed the position in New South Wales:

> But the plaintiff's cause of action was for unliquidated damages for breach of contract: see *Luckie v Bushby* (1853) 13 CB 864; 138 ER 1443; *E Pellas & Co v Neptune Marine Insurance Co* (1879) 5 CPD 34; *William Pickersgill & Sons Ltd v London and Provincial Marine and General Assurance Co Ltd* [1912] 3 KB 614 at 622; *Chandris v Argo Insurance Co Ltd* [1963] 2 Lloyd's Rep 65 at 74 and *Reynolds v Phoenix Assurance Co Ltd* [1978] 2 Lloyd's Rep 440 at 462. It had to establish a contract (the policy) by the which the defendant promised to do something (indemnify it against Mitora's claim), and breach of that contract (failure to indemnify it against Mitora's claim). It could then recover the loss suffered as a consequence of that breach. The plaintiff's cause of action accrued upon breach. Thus it must be asked what the defendant was required to do in performance of its promise, and when it failed to do what was required of it. Only when the defendant failed to do what was required of it could a cause of action for damages for breach of contract accrue to the plaintiff. There was no cause of action simply because Mitora made its claim or the claim was notified to the defendant – the defendant could have thereafter fully performed its promise.

[37] For example, it is has been argued that a promise to indemnify is a promise to keep a party from harm, which when infringed would give rise to a right to damages: on this basis when an insured suffers loss the insurer would have breached its promise to indemnify giving rise to a liability in damages. See for example Rafal Zakrzewski, *"The Nature of a Claim on an Indemnity"* (2006) 22 JCL 54; Robert Cameron, *"Reinsurance and the Australian Context: A two part discussion of aspects of the interaction of federal, NSW and common law in the context of reinsurance" (2001) 12 ILJ 199;* cases referred to in *Re Motor Group Australia Pty Ltd (administrators appointed) (ACN 101 051 101):Marsden & Anor (as voluntary administrators of Motor Group Australia Pty Ltd (administrators appointed)* (2005) 54 ACSR 389).

On this basis, in New South Wales an insurer's liability is not technically a liability for damages unless the insurer breaks its promise to indemnify the insured against its loss by refusing to pay the claim as required pursuant to policy terms and conditions.[38]

However, whilst it may be true that reinsurers do not reinsure their reinsured for damages claims but rather for claims on insurance policies, the reality is that reinsurers in practical terms do not refuse to pay claims simply because their reinsured (by failing to pay within its contractual obligations) has converted a claim on an insurance policy into a claim for breach of contract.

10.2 Compensation

The better view appears to be that an obligation to indemnify against a liability is an obligation to pay compensation. "To indemnify" and "to compensate" have a similar if not identical meaning:

(a) the authoritative Australian dictionary, the Macquarie Dictionary, defines compensation as "something given or received as an equivalent for services, debt, loss, suffering etc; indemnity";

(b) the Macquarie Dictionary defines an indemnity as "*compensation for*" *damages or loss sustained*";

(c) the Lexis Nexis Australian Encyclopaedic Legal Dictionary defines an indemnity as "a sum of money paid to compensate a person for liability, loss or expense incurred by the person".

(d) The Oxford Companion to Law defines an indemnity as "*an undertaking to compensate for loss, damage, or expense*".

Whilst there does not appear to be any Australian case law directly on point, Stoughton LJ in *Total Transport v Arcadia Petroleum (The Eurus)* [1998] 1 Lloyd's Rep 351 at 358 (CA) when referring to an indemnity clause in a bill of lading commented that: "*there the word 'indemnify' is used in what might be regarded as its primary meaning, to compensate one person in respect of his liability to another.*"

The LRMP Act speaks of liability to pay "compensation" only, not liability to make payment in "compensation for a wrong". On this basis, it appears that an obligation to compensate does include an obligation to indemnify within s6 of the LRMP Act.

Whilst in light of the decisions in *HIH v Wallace* and *Asset Insure v New Cap Re* there seems to be a solid argument for s6 of the LRMP Act extending to reinsurance we will need to await a judicial determination to clarify the question.

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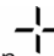
[38] The common law position in England was considered by the House of Lords in *The Fanti* (*Firma C-Trade SA v Newcastle Protection and Indemnity Association; The Fanti; Socony Mobil Oil Co Inc and ors v West of England Ship Owners Mutual Insurance Association (London) Ltd; The Padre Island* [1990 2 All ER 705) in which Lord Goff of Chieveley accepted that: "*...at common law, a contract of indemnity gives rise to an action for unliquidated damages, arising from the failure of the indemnifier to prevent the indemnified person from suffering damage, for example, by having to pay a third party. I also accept that, at common law, the cause of action does not (unless the contract provides otherwise) arise until the indemnified person can show actual loss:* see *Collinge v Heywood* (1839) 9 Ad & El 633, 112 ER 1352"



11. Comment

Many aspects of the decision in *HIH v Wallace* will be troubling for reinsurers. The decision means that so far as reinsurance contracts are concerned, the law of New South Wales is out of step with the law in other states (though the courts in Victoria may take the same approach in relation to similar legislation enacted in that state) and comparable jurisdictions outside Australia. New South Wales law now provides reinsureds with a significant juridical advantage.

Equally troubling from a policy perspective is the main issue to be heard, ie the contention advanced by reinsurers regarding their liability for claims as yet unpaid by the cedent. When that issue is heard, consideration will need to be given to its prudential implications. If reinsurers' contention prevails, no doubt regulators will focus on the issue in future in the context of capital regulation. This will in all likelihood operate to the detriment of both insurers and reinsurers.

The courts have decided within the space of 12 months, that 'insurance' includes 'reinsurance' for the purposes of both the *Corporations Act 2001* (Cth) (**Corporations Act**)[39], and the Insurance Act, leaving unanswered for the time being the question of whether the same result will be obtained in relation to the Instruments Act in relation to s6 of the LRMP Act and to legislation that is similar to s6 in other states and territories.

If the result of the decision is that a significant number of HIH's reinsurance contracts are subject to New South Wales law and jurisdiction, and that as a result judgments can be obtained by the liquidator in New South Wales (such that any judgment debt becomes payable in New south Wales), it may result in a significant benefit to HIH's insureds if the judgment can be enforced against the reinsurer (eg if the reinsurer has assets in New South Wales). It may increase reinsurance proceeds available to the Australian liquidator for distribution in accordance with s562A of the Corporations Act (or s6 of the LRMP Act if it applies) rather than under less favourable English law[40].

We await the judicial, legislative, regulatory and industry response.

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[39] *AssetInsure Pty Ltd v New Cap Reinsurance Corporation Ltd* [2006] HCA 13, see case analysis at http://www.aar.com.au/pubs/insol/foinsolapr06.htm.

[40] See the Court of Appeal's decision in *HIH Casualty & General Insurance Limited* [2006] EWCA Civ 732 see case analysis at http://www.aar.com.au/pubs/insol/foinsoljun06.htm.

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