Indemnity interpretation & enforcement following settlement with a third party

Action Workforce Pty Ltd v DHL Exel Supply Chain (Australia) Pty Ltd; DHL Exel Supply Chain (Australia) Pty Ltd v Action Workforce Pty Ltd [2017] NSWCA 321

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Summary

The recent decision of the NSW Court of Appeal in *Action Workforce Pty Ltd v DHL Exel Supply Chain (Australia) Pty Ltd* involved a dispute about the construction and enforcement of a contractual indemnity in connection with the prosecution of a cross-claim by a warehouse operator against a labour hire company. This was in the context of a labour-hire employee causing damage to goods and followed the pre-trial settlement of the claims made by the owner of the goods against each party to the cross-claim.

Background

In October 2013, an employee of a labour hire company, Action Workforce Pty Ltd (Action), was driving a forklift in a warehouse operated by DHL Exel Supply Chain (Australia) Pty Ltd (DHL) when it struck and damaged a fire sprinkler pipe. The consequent escape of water damaged some goods owned by Sony, resulting in a damage bill of around $550,000.

Sony alleged that DHL was liable under its contract with Sony, relying on the terms of a warehousing agreement made in 2008. In particular, Sony alleged breaches of terms requiring DHL to safely and securely store the goods and a risk clause under which DHL incurred liability for loss or damage caused by any act or omission of DHL, its employees, agents or subcontractors. Sony also sued Action and DHL in negligence.

Before trial, DHL settled with Sony for $270,000 inclusive of interest and costs. Separately, Action settled with Sony for the further sum of $300,000 inclusive of interest and costs.

The trial proceeded because DHL had sued Action on a cross-claim alleging that Action was liable to indemnify it under the terms of their 2013 labour hire agreement. The cross-claim succeeded when the indemnity clause in that agreement (clause 11.1) was held to apply and to entitle DHL to recover from Action the $270,000, together with incidental costs.

At the trial in the District Court, Action unsuccessfully sought to defend the cross-claim on several grounds, including that the indemnity clause did not extend to loss or damage caused by the negligence of DHL and that DHL's settlement with Sony had not been reasonable – this was put on the basis that DHL had failed to mitigate its loss in that DHL had settled with Sony in circumstances where it had no liability to Sony.

On 12 December 2017, Action's appeal was dismissed.

Trial

At trial, the parties annexed to an agreed statement of facts the written advice DHL had received concerning Sony's demands and its liability to Sony. In particular, this advice identified the risk of Sony succeeding against DHL for breach of the warehousing agreement independently of any finding of negligence on the part of DHL.

In its defence, Action in essence contended that:

(a) the forklift driver was not negligent;

(b) DHL had no liability to Sony either and had failed to mitigate in that it had not run a defence that was available to it on the terms of clause 8.2 of the warehousing agreement; and

(c) alternatively, that DHL was indeed negligent and that the indemnity clause (clause 11.1 of the labour hire agreement) did not operate to require Action to indemnify DHL to the extent that DHL's own negligence had caused Sony's loss.

It was held by the trial judge, and not challenged in submissions made at the hearing of the appeal, that the forklift driver was negligent and that Action was therefore liable (vicariously) in negligence to Sony.

The trial judge also found that there had been no breach of duty of care by DHL. The trial judge added that even if she was wrong in this regard, the indemnity in clause 11.1 would still have operated in favour of DHL, because its language did not permit a construction that allowed Action to escape its obligation to indemnify DHL by reason of any negligence on the part of DHL.

That part of Action's defence in which it contended that DHL had failed to mitigate its loss was associated with the argument that DHL had available to it the option of defending the Sony claim by reference to clause 8.2 and clause 9.4 of the warehousing agreement.

Appeal

The relevant clauses from the warehousing agreement were set out in the reasons given by Justice Basten as follows:

> Clause 9 of the Warehousing Agreement was headed "Product losses and damage". Relevantly for present purposes, it read:
>
> "9.4 Subject to clauses 8.2 …, DHL will be liable to Sony for any losses of, or damage to, the Products caused by any act or omission (including a negligent act or omission or breach of contract) of DHL, its employees, agents or sub-contractors …."
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> Clause 8 was headed "Insurance"; cl 8.1 required Sony to take out insurance in respect of destruction or loss of or damage to its products "to their full value on an all risks basis whilst in the custody of DHL or its agents or sub-contractors." Clause 8.2 relevantly provided:
>
> "8.2 If any damage to or loss or destruction of Products occurs and the same falls within the terms of such policy or policies then Sony shall, if able, claim indemnity from the insurer(s) concerned … and, in the event that full indemnity is received from the insurers, Sony shall not bring any claim against DHL in respect of any such loss, damage, cost or expense except to the extent that any loss, damage, cost or expense is *caused by the negligence*, wilful misconduct, or unlawful act [or] omission of DHL, its employees, agents *or sub-contractors*. Nothing in this clause shall be construed as a waiver of any subrogation rights of Sony's insurers." (Emphasis added.)

The indemnity provision was contained in Clause 11.1 of the labour hire agreement, which relevantly provided:

> 11. LIABILITY AND INDEMNITY
>
> 11.1 [Action Workforce] shall indemnify DHL in full against all liability, loss, damages, costs and expenses (including legal expenses) awarded against or incurred or paid by DHL as a result of or in connection with:
>
> (a) …
>
> (b) Any negligent act or omission of [Action Workforce] or its employees, agents or sub-contractors in connection with the performance of the Services.

The NSW Court of Appeal in dismissing the appeal rejected the construction asserted by Action in respect of the indemnity clause and rejected the attempts by Action to distinguish, in the context of clause 8.2, between the vicarious liability incurred by Action in respect of its driver and a direct liability of Action.

The Court of Appeal was also satisfied that the trial judge had correctly found that the DHL settlement with Sony was reasonable.

Other interesting arguments were raised unsuccessfully in the appeal, including that a paragraph of the insurance clause (clause 12) in the labour hire agreement that required that DHL 'provide coverage for the indemnities given in this Agreement', extended to require DHL to obtain cover for the indemnity Action had given DHL in clause 11.1.

Implications

This case provides a good example of the challenges that can arise in disputes over the interpretation and enforcement of insuring clauses, indemnity clauses and risk clauses, which in commercial contracts are the main mechanisms for allocating and controlling exposures to the risk of injury, loss and damage.

The case demonstrates that in some circumstances the settlement of a perceived exposure to a third party's claim need not preclude recovery in full under an applicable indemnity clause.

A party seeking to enforce an indemnity need not establish its liability to the third party, merely that a settlement was reasonable. A reasonable settlement may be claimed as damages for the indemnifier's breach of the obligation to indemnify.

The assessment of the reasonableness of the settlement is undertaken by a court on objective grounds with regard to whether it was reasonable to settle at all and whether the settlement sum was itself reasonable. Reliance on legal advice alone is not enough, but such advice is considered relevant in the court's assessment.

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