When does indemnity arise?

Accrual of a cause of action for breach of contract under a property damage insurance policy

Globe Church Incorporated v Allianz Australia Insurance Ltd [2019] NSWCA 27

Paul Angus & Jane Yoo | March 2019 | General Insurance

Summary

In a split decision delivered on 26 February 2019, the NSW Court of Appeal found that a cause of action for breach of a promise to indemnify under an insurance policy accrues at the time of the insurable event – even where a claim has not been made or has not been assessed.

The majority of the Court of Appeal held that the limitation period for property damage insureds under policies promising to 'indemnify' for loss begins to run from the date of damage rather than at some later time when indemnity is denied or taken to have been refused.

Background

Globe Church Incorporated (**Globe**) allegedly sustained property damage as a result of rainwater and flooding between 8 June 2007 and 31 March 2008.

Globe held an Industrial Special Risks insurance policy for the period 31 March 2007 to 31 March 2008 (**the 2008 Policy**) with Allianz Australian Insurance Ltd (**Allianz**) and Ansvar Insurance Ltd (**Ansvar**).

Globe first made a claim under the 2008 Policy in 2009. Both Allianz and Ansvar denied coverage in 2011.

Globe then commenced proceedings in the NSW Supreme Court in 2016 (almost 8 years after the last date on which the property damage is alleged to have occurred) against Allianz and Ansvar alleging breach of contract.

Globe's proceedings were the subject of a referral by the Supreme Court to the Court of Appeal with respect to the determination of the following separate questions:

1. In respect of any alleged damage to the properties that occurred between 8 June 2007 and 31 March 2008, which (if any) of Globe's claims in these proceedings in respect of the 2008 policy accrued at the time of the alleged damage, for the purpose of section 14(1) of the *Limitation Act* 1969 (NSW)?

2. In light of the answer to (a) which (if any) of Globe's claims in these proceedings in respect of the 2008 policy for that damage are maintainable?

Allianz argued that the insurer's promise is not to pay a specified sum but to indemnify; and that the obligation to do so arises immediately upon the indemnified event. This was based on a consideration of the insuring clause stating:

"…the Insurer will indemnify the Insured against Damage occurring to Property Insured during the Period of Insurance..."

Globe argued that the promise of indemnity was a promise to pay money subject to the terms of the policy 'within a reasonable time'. Globe relied upon general

principles of contract law and further contended that because the amount of indemnity could not be calculated at the time of the damage the obligation to indemnify could not arise at that time and not until it was quantified.

In reply, Allianz argued that, on the happening of property damage, Globe was immediately entitled to commence proceedings seeking damages for the insurer's failure to indemnify.

Decision

The NSW Court of Appeal (a 3:2 majority comprising Bathurst CJ, Beazley P and Ward JA) found that a claim for damages on an insurance policy for property damage accrues at the time of the property damage – and not at the time of any subsequent denial or refusal of the claim.

The majority expressly rejected Globe's argument that the 2008 Policy contained an implied term that the promise to indemnify was a promise to pay money within a reasonable time.

The majority decision is in line with the position adopted by UK courts and contrary to the apparent endorsement of the competing view by the NSW Court of Appeal in *CGU Insurance Ltd v Watson* [2007] NSWCA 301. The majority, in this case, concluded that Watson did not endorse the other view regarding the timing of the accrual of the cause of action for breach of a contract of indemnity insurance.

Noting the preference for the UK view in some other states, the majority considered that if the contrary view is to be adopted it would be for the High Court to make that determination.

The following passage from the majority highlights some issues with this decision at paragraphs [209] – [211], with our emphasis added in bold:

"2.09 Absent a provision in an indemnity insurance policy that makes lodgement of a claim a condition precedent to liability, ***the concept of a promise to indemnify*** *(to make good the loss or to hold harmless against loss)* ***in the context of a property damage insurance policy is such that the promise is enlivened when the property damage is suffered.*** *Unless it be necessary for there to be a claim made on the insurer to give rise to the liability,* ***it is at the point of property damage that the insured has not been held harmless against the loss and*** *(leaving aside any defences that might be raised on such a claim)* ***would be entitled to sue to enforce the promise to indemnify.*** *Such a claim is recognised as being a claim for unliquidated damages (albeit that the amount necessary to make good the loss is to be calculated in accordance with the basis of settlement clause in the policy).*

2.10 Thus, ***unless the making of a demand is a condition precedent to liability, all the essential facts required to be established by the insured to enforce the indemnity will by then have occurred and accordingly the cause of action for unliquidated damages will be complete.*** *It follows that the cause of action accrues on the happening of the property damage (the insured event).*

2.11 ***That it might seem "unfair" for the insurer to be in breach of contract at a time when it may have no notice of the occurrence of the insured event*** *(as was considered to be the position by the Law Commission in England); or that this* ***might seem a "surprising" result or commercially inconceivable,*** *as Professor Clarke suggests; or even that* ***it might stand on "shaky" reasoning,*** *as Professor Clarke also suggests,* ***does not seem to be the point.***"

Meagher and Leeming JJA (dissenting minority) found that there was no breach of an obligation to indemnify on the happening of an insured event and that the obligation was to be discharged within a reasonable time. They considered the majority's decision to be contrary to the position of the High Court in *CIC v Bankstown Football Club* (1997) 187 CLR 384. In their reasoning, the minority pointed out that neither the reasonable commercial expectations of the parties nor the language of the 2008 Policy suggested that the payment obligation was to be performed immediately upon the happening of the relevant damage. In a forceful, but ultimately unsuccessful minority opinion, Leeming JA noted at paragraph [302]:

> *"The defendant insurers invoke a limitation defence. That defence recognises that the plaintiff's claim is for breach of contract. The insurers accepted that their defence would fail if the cause of action of their insured*

did not accrue until a claim was made and a reasonable time had elapsed. The insurers submitted that it was a term of their contract that they indemnify their insured immediately upon the happening of Damage, before any claim was made and indeed before either the insured or insurer was aware of the Damage. On settled principles of construction, and with all respect to those taking a different view, I do not see how that can be so."

Implications

Insureds can issue as soon as an event arises and need not wait a reasonable time for an insurer to deal with a claim

The majority acknowledges that the insured could, on its reasoning, commence action for indemnity against the insurer as soon as the event arises and need not wait until a reasonable time has passed for its claim to be accepted. This is contrary to the standard commercial practice in the general insurance industry and potentially creates some problems for insurers.

The majority suggested that these concerns could be the subject of negotiation of terms between the insurer and the insured to ensure that their respective interests are protected if they wish them to be. This, again, seems to ignore a commercial reality of most insurance not being subject to negotiation by the insured.

Will the decision apply to all property damage policies?

The majority's reasoning suggests that if a policy, such as an agreed value policy, contains a promise to pay (rather than a promise to indemnify), this case would not apply as the 'promise' is one to pay and that has not been breached until such time that the payment has not been made.

For the time being, the application of this decision and the limitation period within which an insured can make a claim will depend on the terms of the insuring clause in the policy.

Does the decision affect liability policies?

The case of liability insurance was distinguished by the majority on the basis that the obligation to indemnify in a liability policy does not usually arise until the liability of the insured to a third party is established. This case will not affect the current position on liability policies.

This decision is a *'two-edged sword'* for insurers, given:

1. it provides a limitation defence for insurers to claims not brought by an insured within 6 years of the date of the loss in policies where the promise is to indemnify the insured; however, it suggests that insureds can bring actions for indemnity immediately against an insurer once a loss arises and even before a claim has been lodged or an insurer has had an opportunity to investigate or consider the claim; and
2. insurers may no longer have the benefit of a *'grace period'* that has, up until now, been considered a reasonable time to consider the issue of indemnity under a policy for property damage.

At this stage, it is unknown whether Globe will seek leave to appeal this decision. It appears that insurers will be left with a degree of uncertainty unless the High Court is given the opportunity to clarify the issues.

For more information, please contact:

Paul Angus
Partner
T: 02 8257 5780
M: 0408 188 808
paul.angus@turkslegal.com.au

Jane Yoo
Senior Associate
T: 02 8257 5736
M: 0403 094 602
jane.yoo@turkslegal.com.au