IN THE HIGH COURT OF NEW ZEALAND
AUCKLAND REGISTRY

CIV-2012-404-7453
[2013] NZHC 1327

BETWEEN	NEW ZEALAND LOCAL AUTHORITY PROTECTION PROGRAMME DISASTER FUND Plaintiff
AND	THE NEW INDIA ASSURANCE COMPANY LIMITED Defendant

Hearing: 20 May 2013

Appearances: D Heaney QC and A Hough for Plaintiff
B Gray QC and K Deobhakta for Defendant

Judgment: 6 June 2013

JUDGMENT OF ASSOCIATE JUDGE J P DOOGUE

This judgment was delivered by me on
***06.06.13 at 4 pm**, pursuant to*
Rule 11.5 of the High Court Rules.

Registrar/Deputy Registrar

Date……

Background

[1] The plaintiff, New Zealand Local Authority Protection Programme Disaster Fund ("LAPP"), is a charitable trust that maintains a disaster fund to indemnify local authority members for part of the losses they may suffer in the event of catastrophes such as earthquakes. The trust was established pursuant to a trust deed executed in 1993. A replacement trust deed which made some changes to the terms of the trust was entered into in 2007.

[2] Protection is provided under the scheme for what were described as below the ground infrastructure assets. The scheme is confined to providing protection against damage to water mains, drainage pipes and the like. In other words it does not cover "above ground" assets such as roads, bridges and buildings.

[3] In or about 1991 the central Government introduced a scheme to cover 60% of the cost of repairing or replacing certain infrastructural assets damaged by natural disasters. Territorial authorities were expected to manage the other 40% of the loss themselves. LAPP was founded in order to provide a collective organisation which would receive contributions from the territorial authorities which decided to join its scheme. Part of the contributions would be used for the plaintiff to arrange the appropriate insurance. The objective of the trust throughout has been to provide 40% of the cost of reinstatement and response costs attributable to catastrophic damage to councils' essential infrastructure. The defendant, The New India Assurance Company Limited ("New India"), was one of the underwriters that participated, taking 10% of the reinsurance on offer.

[4] The events which gave rise to the present dispute were two earthquakes that occurred at the end of 2010 and February 2011 (Q1 and Q2) which caused substantial damage to relevant infrastructure assets located in the Waimakariri District Council ("WDC") and Christchurch City Council ("CCC"). These local authorities were participants in the LAPP scheme. The plaintiff alleges that combined losses sustained by CCC and WDC for Q1 and Q2 exceeded the total amount recoverable under the reinsurance programme which LAPP had funds to meet. LAPP accordingly made claims on its insurers as follows:

Date	Claim	New India's share
12 May 2011	Q2 - $5m	$250,000
11 April 2012	Q1 - $96m Q2 - $79m	Q1 - $9,473,931.60 Q2 - $7,900,000

[5] The reduced amount for Q2 was because $17 million had already been paid in March 2011, with New India paying its full share. New India has not paid the remainder and LAPP has commenced proceedings seeking the balance of its claim under the policies, $17,623,931.60, plus interest and costs.

[6] LAPP applies for summary judgment under r 12.2 High Court Rules and opposes the defendant's application for a stay on the basis that there is no dispute between the parties which could be referred to arbitration. LAPP argues that changes to the trust deed were disclosed to New India's broker and New India is deemed to have knowledge of this disclosure by operation of s 10 Insurance Law Reform Act 1977, or alternatively, non-disclosure was not material.

The Notice of Opposition

[7] The ground upon which the defendant opposes the entry of summary judgment is stated in the notice of opposition as follows:

> (a) The defendant has an arguable defence to the plaintiff's claim, in particular that the defendant is entitled to avoid and has avoided the insurance contracts due to the plaintiff's material non-disclosure of changes to the LAPP trust deed.

[8] The submissions that Mr Gray QC filed on behalf of the defendant reflected the notice of opposition but also said that the defendant disputed that "LAPP has complied with its obligations as an insured to provide evidence of modelling and bifurcation of the losses giving rise to the claim."

[9] Mr Heaney QC for the plaintiffs said that this last mentioned issue was irrelevant because it was not part of the defence set out in the notice of opposition. In addition to dealing with the material non-disclosure defence, I shall also examine

the question of whether the bifurcation issue is one that the Court would be justified in considering as part of its decision.

Application for Stay

[10] The defendant applied for a stay of the proceedings under r 15.1(3) HCR on the basis that the matter should be referred to arbitration as provided in the insurance contracts as there is a dispute between the parties. For reasons to be given, the outcome of the application for stay will be influenced by the Court's decision on the summary judgment application. Therefore consideration of the stay application will be deferred until later in this judgment.

The non-disclosure defence

[11] It was the submission of counsel for the defendant that any entity seeking insurance is obliged to disclose to a prospective insurer all facts which a reasonable insurer would consider material to the risk to be insured. It is a positive duty, cast on the prospective insured. The fact that an insurer does not specifically ask a question of the insured that would draw out the material information does not relieve the insured of compliance with the duty. The duty of disclosure arises pre-contractually, and before the inception of each contract of insurance. The duty arises fresh at the time of the renewal of each contract of insurance. Counsel made reference to the House of Lords decision in *Pan Atlantic Insurance Co Limited v Pinetop Insurance Co Limited* which considered the disclosure obligations of an insured.[1] *Pan Atlantic* has subsequently been applied in New Zealand.[2] In the *Pan Atlantic* case the test was described in the following terms:[3]

> Whenever an insurer seeks to avoid a contract of insurance or reinsurance on the ground of misrepresentation or non-disclosure, there will be two separate but closely related questions: (1) Did the misrepresentation or non-disclosure induce the actual insurer to enter into the contract on those terms? (2) Would the prudent insurer have entered into the contract on the same terms if he had known of the misrepresentation or non-disclosure immediately before the contract was concluded? If both questions are answered in favour of the insurer, he will be entitled to avoid the contract, but not otherwise.

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[1] *Pan Atlantic Insurance Co Ltd v Pinetop Insurance Co Ltd* [1995] 1 AC 501.

[2] *QBE Insurance (International) Limited v Jaggar* [2007] 2 NZLR 336 (CA); *Vero Insurance NZ Limited v Posa* [2008] 3 NZLR 701 (HC); *Bloor v IAG New Zealand Limited* (2010) 16 ANZ Insurance Cases 61-845 (HC).

[3] *Pan Atlantic*, above n 1, at 571.

[12] The further submission was made for the defendant that an undisclosed fact is material if disclosure of the information would have reasonably affected the mind of a prudent insurer in determining:

a) whether to accept the insurance, and if so;

b) at what premium; and

c) on what terms.

[13] The plaintiff did not disagree with the above submissions. I accept that they contain an accurate summary of the law in New Zealand.

[14] In the circumstances of the present case the plaintiff must establish for summary judgment purposes that there is no reasonably arguable defence available to the defendant that:

a) the failure to make complete disclosure concerning the trust deeds amounted to a material non-disclosure;

b) the non-disclosure induced the defendant to enter the contract of re-insurance; and

c) a prudent insurer would also have been so induced.

[15] The defendant takes the position that material changes occurred when the plaintiff adopted the 2007 trust deed in place of the earlier 1993 deed. In broad terms it was the contention of the defendant that the provisions of the later deed removed or reduced restrictions on the amounts which insurers such as the defendant might have to pay out pursuant to reinsurance contracts. Therefore the terms of the 2007 deed ought to have been disclosed to the defendant. The failure to do so, it was argued, was a material non-disclosure which voids the insurance policy.

[16] The plaintiff disputed that there was any material difference between the two trust deeds having the effect that the defendant complains of. In any event, the

plaintiff contends, the defendant is deemed to have had knowledge of the contents of the 2007 deed as a result of the operation of s 10(2) Insurance Law Reform Act 1977. A number of sub-issues arise under this general submission.

The Insurance Law Reform Act 1977

[17] The first basis upon which the plaintiff answers the claim that it did not make full disclosure is that pursuant to the provisions of s 10 of the Insurance Law Reform Act 1977 ("the Act") disclosure to the broker who was acting on behalf of the plaintiff, Aon Benfield ("Aon"), amounted to disclosure to the defendant itself.

[18] Section 10 of the Act prescribes as follows:

> **10 Salesman, etc, to be agents of insurer**
>
> (1) A representative of the insurer who acts for the insurer during the negotiation of any contract of insurance, and so acts within the scope of his actual or apparent authority, shall be deemed, as between the insured and the insurer and at all times during the negotiations until the contract comes into being, to be the agent of the insurer.
>
> (2) An insurer shall be deemed to have notice of all matters material to a contract of insurance known to a representative of the insurer concerned in the negotiation of the contract before the proposal of the insured is accepted by the insurer.
>
> (3) In this section the term **representative of the insurer** includes any servant or employee of the insurer and any person entitled to receive from the insurer commission or other valuable consideration in consideration for such person's arranging, negotiating, soliciting, or procuring the contract of insurance between a person other than himself and such insurer.

[19] Mr Gray for the defendant submitted that there is doubt whether the provisions of the Act applied because of doubt about the payment of commission to Aon. He refers to an exchange and e-mails that took place between Mr Sole on behalf of the plaintiff and Mr Gilbert of Aon which occurred on 16 December 2010. The point was made that while a payment was made to Aon for arranging the insurance, that could well have amounted to the equivalent of a gratuitous payment rather than the payment of commission and, further, it was self-evidently not a payment made by the defendant as the principal to Aon, but was made by the insured.

[20] The reason for enacting s 10 was to avoid difficulties that arose where an insured person was not dealing directly with the insurance company, but with an insurance agent or broker, which could give rise to insurance companies raising arguments that disclosures which were made to those persons were not to be equated with disclosure to the insurance company.[4] The result could be the vitiation of insurance cover. The section also makes it explicit that an employee of the insurer is to be regarded as its representative for the purposes of this section. Disclosure to a representative of the insurer as defined in s 10 is deemed to be a disclosure to the insurer itself.

[21] The argument for the plaintiff is that because there was disclosure to Aon, which was functioning as the broker representing the insurer, such disclosure would automatically be deemed to have been made to the insurer. It was argued that because there was evidence that the plaintiff had disclosed the 2007 trust deed to Aon, the defendant was deemed to have notice of it.

[22] The first issue is whether there is evidence of the kind which the plaintiff argues for because that point, too, was contested by the defendant. Mr Gray drew attention to the fact that it was the chairman of the trust who gave evidence that the copy of the trust deed had been provided to Aon. It was his submission that any evidence by the chairman to that effect could only be hearsay and therefore not evidence which the Court could rely upon.

The hearsay evidence point

[23] The plaintiff does not provide any evidence which establishes who from the plaintiff's organisation provided the 2007 trust deed to Aon. In my view, any lack of clarity on this issue should be resolved in favour of the defendant. The terms of the deposition that Mr Sampson made are consistent with the fact that some other person in the plaintiff's organisation sent the 2007 deed to AON rather than Mr Sampson himself sending it personally or witnessing another person in the organisation doing so. For the purposes of the present application his deposition ought to be viewed as hearsay.

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[4] *Body Corporate 398983 v Zurich Australian Insurance Limited* [2013] NZHC 1109 at [58].

[24] Mr Heaney responded by submitting that given that the Court was hearing a summary judgment application which was interlocutory in nature, hearsay evidence was admissible. It is therefore necessary to consider whether that contention is correct.

[25] Section 18 of the Evidence Act 2006 (EA) provides as follows:

> **18 General admissibility of hearsay**
>
> (1) A hearsay statement is admissible in any proceeding if—
>
> (a) the circumstances relating to the statement provide reasonable assurance that the statement is reliable; and
>
> (b) either—
>
> (i) the maker of the statement is unavailable as a witness; or
>
> (ii) the Judge considers that undue expense or delay would be caused if the maker of the statement were required to be a witness.
>
> (2) This section is subject to sections 20 and 22.

[26] The qualifying circumstances which the section refers to have not been established and therefore I would not accept that hearsay evidence could be admitted pursuant to the provisions of s 18.

[27] Section 20 of the EA provides that a hearsay statement contained in an affidavit may be admissible if and to the extent that the applicable rules of court require or permit a statement of that kind to be made in the affidavit. That in turn leads to a consideration of r 7.30 HCR which is to the following effect:

> (1) A Judge may accept statements of belief in an affidavit in which the grounds for the belief are given if—
>
> (a) the interests of no other party can be affected by the application; or
>
> (b) the application concerns a routine matter; or
>
> (c) it is in the interests of justice.

[28] The first two subparagraphs of the rule would not seem to apply. Nor would it seem to be in the interests of justice to allow hearsay evidence to be admitted for the purposes of summary judgment application. The summary judgment procedure already represents an inroad into the usual procedure in s 83 EA whereby witnesses are required to give evidence in oral form and be subjected to cross-examination. The compensatory mechanism that is built into the rules requires the plaintiff on oath

to negative the existence of a defence. That safeguard would be of diminished value if the evidence that was to be put forward did not represent the first hand knowledge of the deponent. *Ports of Auckland v The Ship "Raumanga"*, decided before the Evidence Act came into force, expressed the principle that in applications for summary judgment, the rules of evidence should be strictly adhered to.[5] This approach continues to apply under the Evidence Act 2006.[6]

[29] Mr Heaney for the plaintiff made the broad submission that in the case of corporations, the proof by one officer of what another did must be admissible in the form of hearsay evidence obtained from another person; otherwise there would be difficulty in the corporate entity carrying out its functions. He did not refer to any authority which would support acceptance of the above.

[30] To summarise, the evidence of the plaintiff does not carry matters to the point where the defendant is left without an arguable defence in relation to the application of the provisions of s 10 of the Insurance Law Reform Act. Even if Aon was a "representative of the insurer" so as to bring s 10(2) into operation, there is no admissible evidence of disclosure to Aon.

The assertion that the plaintiff made informal disclosure when the 2007 trust deed was adopted

[31] As an alternative route to establishing that the plaintiff in fact made disclosure of the replacement trust deed to Aon, Mr Sole gave evidence that at a breakfast meeting with Andrew Gilbert (LAPP's reinsurance broker) proposals that the plaintiff should offer cover for aboveground infrastructure were discussed.

[32] He said that the other person present at the meeting was Mr Bartle from Southern Cross. The latter company was engaged by Mr Sole's firm, Civic, to arrange the insurance for aboveground infrastructure.

[33] The significance of this evidence, I was told, was that the move to expanding the classes of insurance to include infrastructure above the ground was the trigger

[5] *Ports of Auckland v The Ship "Raumanga"* (1998) 12 PRNZ 84 (HC).
[6] *McArthur Ridge Investments Ltd v Schultz* [2012] NZHC 423.

event for the adoption of the 2007 trust deed. It was said that the deed had to be amended before such new classes of protection could be offered to members of the scheme. The assertion is that an inference arises that Mr Sole must have discussed the existence of the new trust deed in the presence of the executive from Aon at this meeting.

[34] In my view, that contention cannot succeed. I do not consider that the proposed inference can be drawn. Alternatively, it would not be of sufficient strength to negative the existence of an arguable defence relating to this issue.

[35] Mr Sole gave evidence that he also met socially with the same Aon executive who had been at the previous meeting, Mr Gilbert, and with Mr Bartle in both January 2008 and 2009. He said that he recalled on those occasions that he discussed the extension or proposed extensions of the LAPP scheme to aboveground infrastructure. He said that he also recalled discussing the changes to the LAPP trust deed. His evidence in summary is to the effect that this would have been of significance to both these men because of potential increase in the volume of business that could result. The fact that there was a link between the necessity for change to the 2007 deed and the initiative to add aboveground infrastructure to the cover arrangements was offered as a circumstance which would make his evidence more believable on this point.

[36] Mr Sole's recollection of what occurred in 2008 and 2009 is offered five and four years respectively after the event in an affidavit sworn in 2013. There is no independent support for his testimony. It may be correct. Even if it is, I agree with the submission that Mr Gray made to the effect that it is unlikely that an underwriter is fixed with knowledge of an employee for the purposes of s 10 ILRA when the knowledge is gained from discussions at what was at least partly a social occasion. Mr Sole's evidence of these social discussions is not enough to show that the defendant has no arguable defence to the application for summary judgment.

Did non-disclosure of the changes to the trust deeds induce New India to enter into the contract?

[37] The *Pan Atlantic* principle involves consideration of the effect that the non-disclosed matters would have had on the actual insurer and also the effect that they would have had upon a hypothetical prudent insurer. It is the former element that is now considered in this part of the judgment.

[38] For summary judgment purposes it must be accepted that unless the plaintiff was able to bring itself with in the ambit of s 10 of the Insurance Law Reform Act, the insurance company had not been informed of the changes that occurred through the substitution of the 2007 deed for the earlier 1993 one. This is important because the notice of opposition identifies the failure to disclose the changes wrought by the later deed as the basis upon which the policy is able to be avoided. New India's position, therefore, is that had it been told that the deeds had been changed it would not have entered into the relevant insurance contracts.

[39] Assuming that that is the correct approach, it would be necessary for the defendant to have been influenced to insure by the assumption that the 1993 deed was still in force, and to have been ignorant of the fact that there had been a change to the deed in 2007 and that providing insurance on the new basis would be more unfavourable to the insurer.

[40] The defendant's evidence was to the following effect:[7]

> 28. If I had been advised that there had been a change of or variation to the primary trust deed, I would certainly have asked Aon for a copy of the new trust deed.
>
> 29. I would have been concerned about the change in deed because any change to the terms of the trust deed was potentially significant to the risk. The terms of the 2010 policies meant that all loss settlements made by LAPP were unconditionally binding on new India provided that those settlements were within the terms of LAPP's trust deed and of the insurance contract. I would have wanted to satisfy myself that any change to the trust deed did not impact upon, or affect the trustees' obligations under the deed.

[7] Affidavit of Balachandra Balasubramanian, affirmed 5 February 2013.

[41] Mr Gray for the defendant submitted as follows:[8]

> 31 LAPP submits that the fact that New India never asked for, or received a copy of the 1993 Deed or the 2007 Deed until after the losses were suffered is "fatal" to its non-disclosure of argument. That is not the case. New India has been unable to locate a copy of the 1993 Deed on its underwriting files, and so cannot confirm whether it had the 1993 Deed when it first underwrote LAPP in 1994. Even assuming that it didn't see the 1993 Deed, this does not mean that the changes implemented by the 2007 Deed were not material. New India originally insured LAPP on a "subscription" basis. The lead insurer had negotiated the terms of the insurance. Once the terms of insurance were agreed, the risk was taken to the market for other insurers to sign on to underwrite a percentage of the risk on the understanding and agreement that they would follow the lead insurer in terms of its acceptance of the risk and its decision to pay claims.
>
> 32 New India (and presumably the other co-insurers) relied in part on the lead insurer assessing the risk before acceptance. Mr Balachandra [sic] says he would have expected that the lead insurer would have reviewed the 1993 Deed and satisfied itself that claims would be properly adjusted and assessed after each event giving rise to loss.[9] It is not clear whether or not the lead insurer actually did review the 1993 Deed in this case.

[42] There may be arguments about how far the obligations of LAPP extended in making disclosure. It might be an issue whether LAPP would have done enough if it simply sent a copy of the new trust deed to the insurer without further comment. Alternatively, it might be suggested that the obligation of LAPP was to go further and to expressly state that there had been a change to the trust arrangements. However, it is reasonably arguable on the basis of the evidence which Mr Balasubramanian has given that had he been told that there had been a change in the trust deed, he would have called for a copy of the original deed. It is not unreasonable to infer that had matters reached that point he would then have gone on to carry out a comparison of the two deeds, come to the realisation that the terms of the 2007 deed were comparatively disadvantageous, and either declined insurance or offered on different terms. Just whether Mr Balasubramanian would have taken all of these steps is not a matter that can be resolved short of trial.

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[8] Synopsis of submissions for the defendant, 25 March 2013.
[9] Affidavit of Mr Balasubramanian affirmed 19 March 2013 at paragraph [4]

[43] There may be some scepticism about whether Mr Balasubramanian would have followed up in this way had he been advised that the trust deed had been changed. After all, if he had not concerned himself with the provisions of the 1993 deed, why would he evidence a greater degree of interest in the 2007 deed? Possibly that is explained by the change in the structure of the underwriting arrangements. But stripped to their essentials, what Mr Balasubramanian seems to have said is that up until the point where the structure of the insurance arrangements changed (on a date which does not seem to be disclosed in the evidence) he was content to leave such matters to the lead insurer. I understand his evidence to say that he was prepared to trust another insurer's judgement on that issue because the particular structure adopted under the old arrangements had given him comfort in that regard. If that is so, then when the subscription basis for insurance ended, taking with it the protection or assurance that Mr Balasubramanian took from it, one might have expected to see some evidence of him actively attempting to make his own judgement about what was in the trust deed. He could not have done that without calling for a copy of the current trust deed.

[44] However, I accept that given the circumstance that Mr Balasubramanian has given a sworn deposition on the point, it is not possible for the Court to be certain at summary judgment stage that the actual underwriter would not have been influenced by any material changes to the trust deed.

[45] However, the test requires the Court to enquire whether material non-disclosure affected the decision of the insurer. It is not open to the insurer to claim that its opinion of whether the changes were material must prevail, even if the Court is of the view that the changes cannot be so described, and as it happens, I have concluded that the changes between the trust deeds in this case were not prejudicial to the insurer. The evidence of Mr Balasubramanian appears to assume that had he been advised of the changes that would have set in train a chain of events leading to the ultimate point which was that he would have appreciated that the 2007 deed made material changes which were prejudicial from the insurer's point of view. As discussed below, it is this last point that I do not accept. On the basis of the conclusions which I reach below, I do not consider that there is an arguable defence

that the actual underwriter, the defendant, was actually induced by material non-disclosure to enter into the policy.

Materiality of the changes to the trust deed

[46] Given that the plaintiff is not able to call in aid the provisions of s 10 of the ILRA, and because it is not able to prove that it actually provided a copy of the 2007 trust deed to the insurer, the only other way in which the summary judgment application could succeed is if the plaintiff is able to convince the Court that any change was not material. It would be fatal to the defendant because the actual underwriter could not have been misled by material change of circumstance if none had occurred. Secondly, the prudent underwriter contemplated by *Pan Atlantic* would not consider the changes as a material alteration in the circumstances. If it was material, it ought to have been disclosed to the insurer and the absence of disclosure would be fatal to the plaintiff's claim

[47] Elements of the materiality issue need to be considered. The first question is whether non-disclosure is capable of being material as a matter of law. Whether it is actually material is a matter of fact.[10]

[48] The submission which the plaintiff made concerning materiality of the nondisclosure was in the following terms:[11]

> There is a fatal flaw to New India's argument: it never requested/obtained a copy of either the 1993 or 2007 trust deeds until after the reinsurance claims were made in 2012. It is submitted Mr Stroud's affidavit evidence as a prudent insurer can be discounted because it is based on incorrect assumptions.
>
> Any changes between the deeds cannot have been material to New India and its ground of opposition is a recent obfuscation manufactured out of desperation to avoid its liability to pay LAPP's claims.
>
> Assuming, *arguendo*, New India had in fact received the 1993 trust deed prior to accepting LAPP's reinsurance proposals, it is submitted that the changes between the 1993 and 2007 LAPP trust deeds are not material.

[10] *Laws of New Zealand* Insurance at [326].
[11] Plaintiff's submissions. 18 March 2013 at paragraph 5.7 - 5.9.

[49] Whether a particular fact or circumstance is material is to be judged by asking whether it concerns a matter: [12]

> …which, if communicated, would affect the judgement of a rational underwriter in considering whether he would enter into the contract at all, or enter into it at one rate of premium or another.

[50] Whether a circumstance is capable of being material or not for the purposes under discussion is a question of law. The point was discussed in the judgment *Scottish Shire Line Limited v London and Provincial Marine and General Insurance Co Ltd*:[13]

> There has been a discussion as to how far concealment is a matter of law, and how far it is a matter of fact, but it is well settled now that evidence is admissible on the subject, and unless I can be satisfied, as a matter of law that the point in question could not be material, it is a matter upon which I must be guided by the evidence as to whether it was material to a reasonable underwriter, with a view either to his taking the risk, or to the premium he would charge for taking it, to be apprised of the fact in connection with this insurance that the Hobart apple contract specified at date about which the vessel had to arrive.

Is there evidence that could support a defence of material non-disclosure?

[51] The distinction between a determination that a particular change of circumstances could not have been material in the eyes of a rational underwriter, on the one hand, and the question of whether or not the fact or circumstance, on examination, is actually material, is an important one. At the summary judgment stage there should be no problem with the Court determining the first question. However, actually evaluating a dispute about how a reasonable underwriter would review the materiality of the non-disclosed circumstance is unlikely to be suitable.

[52] In the absence of special circumstances, any change to the description of the risk would, by definition, be capable of constituting a material circumstance which ought to be disclosed to the insurer. The issue is whether the trust deed, properly construed, makes any effective change to the re-insurer's risk.

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[12] *Rivaz v Gerussi* (1880) 6 QBD 222 (CA) at 229.

[13] *Scottish Shire Line Ltd v London and Provincial Marine and General Insurance Co Ltd* (1912) 3 KB 51, referred to in the judgment of *CTI - International Incorporated v The Oceanus Mutual Underwriting Association (Bermuda) Limited* 1984 WL 988816 (CA) Kerr LJ at 50.

[53] The next part of this judgment will consider the important issue of whether the insurer has grounds for arguing that the 2007 deed arguably increased the level of risk and so would have been therefore viewed by a prudent underwriter as material to the decision to insure.

[54] The complicating feature of the present case is that it is not entirely concerned with the non-disclosure of a factual matter known to the proposed insured. The fact that the existence of the 2007 deed was not disclosed can be disposed of as a simple issue of fact, once the non-application of the ILRA has been cleared away. But there is another layer to the issue. Whether there was a duty to disclose the 2007 deed depends upon what it means. Before the point can be reached where a definitive judgment can be made upon the question of whether or not there has been a material non-disclosure-the meaning of the 2007 deed has to be extracted from it. That involves a legal issue.

Features of the Insurance Scheme

[55] It is to be observed that a feature of the scheme was that the insurance company was liable to make very large payments in circumstances where it did not exercise the conventional degree of control over the claim. It was obliged to pay out such amount as the trust decided was the appropriate distribution for any particular claim that might be made. There was a large element of discretion reposed in the trust concerning the circumstances that it could take into account when deciding what if any distribution ought to be made. Under both deeds the trustee had to satisfy itself that the claim qualified under the LAPP scheme. In conformity with the trust deed, the trustee had to be satisfied that the claimant was a member of the scheme and that the event giving rise to loss was the qualifying event in that it resulted from a natural disaster or emergency.[14] A similar requirement was included in the 2007 deed.

[56] However, it is said that there were points of difference between the two deeds, the effect of which was that under the later deed the trustees were not required

[14] See definition of "coverage" clause 1.1 1993 deed.

to observe some of the restrictions and to see that the same preconditions to cover were established, when compared with the position under the earlier deed.

[57] Mr Gray reviewed the two trust deeds to contrast the provisions of each. It was his submission that the provisions of the 1993 deed established procedures that would have provided effective controls to ensure that only legitimate payments were made from the fund. He drew attention, for example, to clause 8 of the deed which required the trustees to determine whether any applicant was eligible to apply for a distribution, whether the events resulting in loss or damage to the applicant's infrastructure constituted a natural disaster or emergency for the purposes of coverage and noted that the provisions of clause 8.2 left the quantum of any distribution to the sole discretion of the trustees. In exercising that discretion in determining how much the distribution should be they were to have regard to matters such as the amount of the annual contributions that the affected local authority had made to the fund, the state of repair and maintenance of the infrastructure (before the event occurred which gave rise to the claim it would seem) and the amount reasonably required for reinstatement of the infrastructure.

[58] In the view of Mr Balasubramanian, expressed in his affidavit dated 5 February 2013, the differences between the two trust deeds were the following:

> (i) the 2007 deed removed the need for trustees to take any steps to obtain proper loss adjustment or assessment to ascertain the amount of the loss suffered by the LAPP member;[15]
>
> (ii) under the 2007 deed there was now no direction to the trustees to have any regard to the cost of reinstating the infrastructure when determining the quantum of the distribution;[16] and
>
> (iii) there was now effectively no control over the amount of the loss, or the requirement on the reinsured to ascertain the loss before seeking payment from reinsurers.[17]

[59] Mr Stroud's evidence was put forward as that of an expert in the area of reinsurance. No criticism was made of his credentials for giving evidence of that kind. In his opinion the most significant change "is the removal of the provision of

[15] Affidavit of Balachandra Balasubramanian at paragraph 31.
[16] Affidavit of Balachandra Balasubramanian at paragraph 32.
[17] Affidavit of Balachandra Balasubramanian at paragraph 35.

the 1993 deed under which a trustee is directed to have regard to 'the amount reasonably required for the reinstatement of the applicant's Infrastructure.'"[18] Mr Stroud was also of the opinion that "the 2007 Deed appears to place no obligation on the trustees to give any consideration to the amount of the loss actually suffered by the member before deciding the quantum of the distribution."

[60] The key passages from his evidence were to the following effect:

> 28. It is fundamental that the purpose of insurance is to indemnify the insured for loss that it has suffered (the Ultimate Net Loss, (Article 8)). The change in the 2007 Deed appears to run contrary to that principle by effectively making the quantum of the LAPP member's actual loss irrelevant to the trustee's assessment of the distribution to be granted to the member.

[61] The first point to note is that Mr Stroud's opinion about the difference between the trust deeds in the areas identified above depends upon whether his interpretation of the trust deeds is correct. The correct approach, in my view, when assessing the merits of the defendant's contentions is first to construe the provisions of the deed to ascertain their meaning and effect. Mr Stroud himself deposes that "upon seeing any changes to the trustee's powers of distribution in the 2007 Deed, I may well have sought advice or clarification on the effect of the changes."[19]

[62] Turning to the 1993 trust deed, the relevant provision was:[20]

> 8.2 *The quantum* of any distribution *shall be at the sole discretion* of the Trustees provided they shall in determining the quantum of any distribution nevertheless have regard *to all or any combination* of (*without any necessary obligation to make any allowance for*) the following factors:
>
> ...
>
> (f) the amount reasonably required for the reinstatement of the applicant's Infrastructure.

[63] It can be said that if the 2007 trust deed placed no obligation on the trustees to have regard to the amount of loss actually suffered by the member, then the same was also true of the 1993 deed. They could do so but were not required to. That is made clear by the passages from clause 8.2 which are set out above and marked with

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[18] Affidavit of Martin Stroud, sworn 5 February 2013 at paragraph 27.
[19] Affidavit of Martin Stroud at paragraph 32.
[20] Emphasis added.

emphasis. The trustees could either have regard to all of the factors, which would therefore include (f), or any combination thereof (which means that they could disregard (f)). That the reasonable cost of reinstatement was a factor which the trustees might at their option take into account is made clear by the reference to the fact that they were under no obligation to make any allowance for it.

[64] By comparison, the 2007 deed provided that the trustees had to first satisfy themselves that there had been damage to infrastructure caused by a "damaging event". A series of natural disasters are set out in clause 1 of the 2007 deed which are included in the definition of "damaging event". Once a decision had been made that the grounds existed for making a distribution to the member in question, the trustees could make a distribution "subject to" a number of matters that are set out in clause 8.3 to which I shall shortly make reference. However, the 2007 deed containing as it does the necessity for the trustees only to meet claims for damage caused by damaging events, directs the trustees to respond only to claims arising from the circumstances so described.

[65] The circumstances enumerated in clause 8.3 included:

> 8.3(b) the state of repair, maintenance and condition generally of the infrastructure or of any particular parts of the infrastructure *before and after the Damaging Event* for which the distribution is claimed

[66] The effect of 8.3 was that it was mandatory for the trustees to have regard to the factors set out in (b) of that clause.

[67] Although the provision does not explicitly say so, it seems reasonably clear that the objective of including (b) was to direct the trustees' minds to exactly the point which Mr Stroud expressed concern about, namely the loss that the member actually suffered. The requirement that the trustees advert to those factors presumably was intended to ensure that no element of betterment was paid for by the plaintiff fund. It would also direct their minds to ensuring that the trust met no more than the cost of repairing the damage attributable to the disaster. For that reason, it is not possible to agree with Mr Stroud's assessment of the comparative advantages and disadvantages of the two deeds.

[68] I also consider that the plaintiff was correct in submitting that Mr Stroud's evidence concerning the comparative meanings of the two deeds ought to be disregarded (see above at paragraph [48]). While Mr Stroud is no doubt qualified to give evidence about whether a prudent underwriter might be influenced by a non-disclosure, the question of whether there had been a non-disclosure or not is not, in the circumstances of this case, a matter that is within his province. The case comes within s 25(3) Evidence Act 2006:

> (3) If an opinion by an expert is based on a fact that is outside the general body of knowledge that makes up the expertise of the expert, the opinion may be relied on by the fact-finder only if that fact is or will be proved or judicially noticed in the proceeding.

[69] This is consistent with the position at common law as it was stated in *R v Turner*, where the Court said:[21]

> Before a court can assess the value of an opinion it must know the facts upon which it is based. If the expert has been misinformed about the facts or has taken irrelevant ones into consideration or has omitted to consider relevant ones, the opinion is likely to be valueless.

[70] To revert to the question of the comparative effect of the two deeds, in my view the only way the position could have been more advantageous to the defendant under the first deed was if it could be accepted in the defendant's favour that the inclusion of clause 8.2(f) - even as a discretionary factor - was better than nothing because of the limited assurance that it offered to the trust, and thereby the insurers, notwithstanding that the trustees could in their discretion choose to ignore it.

[71] The result of comparing the pivotal provisions of the two trust deeds can be summarised. The first deed more directly adverted to the need to focus on the reasonable cost of reinstatement of the applicant's infrastructure than the second did. However, any requirement in the first deed was discretionary and could be ignored. The second deed contains a requirement, which is perhaps more obliquely stated, that when deciding what should be paid out for repair costs, the trustees are to take account of the before and after state of the infrastructure. The requirement in the second deed is mandatory in its observance.

[72] If the consequences of the change between the two deeds are examined, the absence of any substantial change is made clear. There was nothing that the trustees

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[21] *R v Turner* [1975] QB 834.

could do pursuant to the powers under the 2007 trust deed that they could not have done under the earlier deed. There is no change of emphasis brought about, for example, by the inclusion in the later deed of directory or empowering provisions intended to bring about a more expansive approach to distributions under the scheme.

[73] There is evidence that the purpose of the re-drafting of the trust deed was to facilitate an objective that is unconnected with the present litigation and that was to empower the trustees to begin offering cover for aboveground infrastructure in addition to items that were below ground. It may be that in the course of redrafting the deed with that objective in mind the opportunity was taken to make purely textual changes that were thought to be an improvement on the existing wording of the trust deed.

[74] To summarise, the defendant claims that what occurred in this case was non-disclosure of aspects of the risk which an underwriter would regard as being influential. As a result, the insurance company contends that it has the right to refuse indemnity. But defining the way in which the changes to the deed brought about the alleged adverse changes to the risk remains elusive.

[75] For the foregoing reasons the second deed was not measurably less advantageous to the defendant than the first. That logically leads to the further conclusion that the failure to disclose the second deed and thereby to bring to the attention of the defendant the changed circumstances under which the plaintiff operated its disaster reinsurance scheme did not amount to material non-disclosure. That is to say, the changes contained in the second deed would not have influenced a prudent insurer to decline cover or to change the conditions upon which cover would be offered to the plaintiff.

[76] The defendant criticises the reinsurance scheme as not making any provision for a clearly defined loss-adjustment regime. That weakness, as the defendant would characterise it, was a feature of both schemes.

Proof of loss

[77] A matter that was raised in the submissions for the defendant was that LAPP has not obtained evidence of actual loss suffered by each of the CCC and WDC.

[78] Mr Gray emphasised that the way in which the defendant managed the claims which were submitted to it simply reflected business prudence. Before it paid out on the claims it was obviously concerned to ascertain that the claims were covered by the policy and that the payments that were sought were within their relevant limits of the policies. He noted that the approach that the plaintiff apparently took was that the extent of the damage was clearly so great that the assumption could be made that the damage exceeded the amounts insured and that therefore there was no reason for delaying in paying the claims.

[79] Counsel submitted that that the perspective of the plaintiff was quite different from that of the insurance company. There are many questions that needed to be asked to satisfy whether the claim in fact came within the policy. Examples of these reflected the "bifurcation" between the earthquake that occurred September 2010 and that which occurred in February 2011 - Q1 and Q2 respectively. There were questions about the justified extent of any payment on account of replacement of pressure mains. There were indications that claims were being submitted for replacement of major sections of pressure mains which had reached the end of their service life prior to the first of the earthquakes so that the Council would have had to replace them anyway had the earthquake not occurred. As well, many of the cost claims were estimates, and reports of consultants obtained provided good reason to suppose that there was a shortage of solid information backing up the estimates of what it was expected the repair costs would be.

[80] Such liability as the defendant has to the claimant has to be ascertained by considering the contract between the two parties and constraining that contract against the background circumstances that the defendant is essentially indemnifying the plaintiff in respect of the amounts that the plaintiff agrees to pay out under what can reasonably be described as an insurance scheme to its contributors. Against such a background, it can be taken to be the intention of the parties that the defendant has

not assumed liability to pay amounts other than those attributable to loss caused to the below ground infrastructure of the local authorities who are members of the scheme. Putting it another way, the defendant could not be expected to be liable for payment of amounts that the plaintiff accepted liability for under its scheme in cases where the plaintiff was accepting liability to make payments not referable to some identifiable loss. I consider that the defendant correctly identifies the situation in submitting that "New India is bound by what LAPP has done".[22] However, it does need to be recognised that there are limits to how far the insurer is so bound. The fact that under either trust deed the trustee was vested with considerable discretion does not negative this position.

[81] The issue is whether the plaintiff in this case has validly fixed the amounts that the trustees should pay to the affected members of the scheme, CCC and WDC.

[82] In the first place, the plaintiff has provided the usual affidavit negativing any defence and verifying the statement of claim. Secondly, the Court is entitled to give some weight to the fact that the trustees of the scheme are experienced and reputable people. In the third place, there is some evidence which would show that the amounts which the plaintiff has agreed to pay out are broadly justified.

[83] Evidence was produced for the plaintiff from Mr BV Whitefield, the director of a risk management firm from New South Wales Australia, who has examined the issue of loss caused by the Q1 and Q2 events. Information he obtained at an early stage from a manager of the CCC indicated that damage to the infrastructure in that city would exceed the total cover that LAPP was able to provide of $272.5 million together with the Central Government. That meant that the entire insurance cover together with excesses would be in excess of the $109 million that was the responsibility of LAPP. Further, he advised that the range of estimates for damage from Q1 which had been estimated by various expert advisers to CCC and WDC showed that losses to infrastructure assets would be in excess of $400 million.[23]

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[22] Synopsis of submissions for the defendant at paragraph 35.
[23] Affidavit of Mr BV Whitehead, sworn 7 December 2012, at paragraph 51(a).

[84] The loss would therefore exceed the total insured portion of the loss held by LAPP, $109 million, by at least $290 million, albeit undifferentiated between the two territorial authorities.

[85] In my view no criticism can be made of the plaintiff for not offering a breakdown of these amounts between the two territorial authorities. It is insured under the contract for "losses occurring during the period 12 months commencing 1 July 2010 to 30 June 2011, both days inclusive". From the perspective of LAPP, the loss is the amount that it concludes that it is required to pay out to its contributor members in accordance with the obligations it has under the trust deed. The fact that it has not waited until the claims were refined to the point where it had a figure available which could be stated as being a reasonably exact ceiling for the losses to infrastructure before agreeing to indemnify would not seem to be in breach of its obligations under the insurance contract. The circumstances and contingencies which the parties to the contract of insurance must have contemplated when they entered into the insurance, which is described as "catastrophe excess of loss reinsurance", tells against the precise and orderly approach to claims for which the defendant contends. The plaintiff is entitled to take a robust approach. As the trustee for a disaster relief insurance scheme, the plaintiff is under obligations to act promptly to fund recovery from a major disaster of the kind which struck Canterbury. Of course, such considerations would not absolve it if the evidence indicated that it was taking an unjustified approach to settling its members' claims and moving outside the ambit of what is permissible for a loss reinsurance scheme. But in my view the figures speak for themselves and confirm that the approach that LAPP has taken with respect to the Q1 event by accepting that the aggregate claims of its members exceed the insured amount and therefore that 100% payout is required seems wholly justifiable. I do not consider there is any arguable defence available to the defendant with regard to the Q1 claim.

[86] The circumstances if anything are stronger with regard to the Q2 event. Mr Whitefield has adopted a loss estimate of in excess of $700 million for infrastructure damage caused to the two territorial authorities covered by the LAPP scheme.[24]

[24] Affidavit of Mr BV Whitehead, sworn 7 December 2012, at paragraph 51(b).

Given that 100% of the indemnity provided by the LAPP scheme is $272.5 million[25] of which 40% has to be borne by the trust through its insurers, the claim up to the maximum amount under the policy is a fair and reasonable one in regard to which the defendant has no arguable defence.

The stay application

[87] New India has applied for a stay of proceedings on the basis that the matter should be referred to arbitration as provided in the insurance contracts as there is a dispute between the parties, which is whether New India is entitled to avoid the insurance contracts on the basis of material non-disclosure. The applicable law for the application for a stay of proceedings is Article 8 of the First Schedule of the Arbitration Act 1996, which sets out:

> A court before which proceedings are brought in a matter which is the subject of an arbitration agreement shall, if a party so requests not later than when submitting that party's first statement on the substance of the dispute, stay those proceedings and refer the parties to arbitration unless it finds that the agreement is null and void, inoperative, or incapable of being performed, or that there is not in fact any dispute between the parties with regard to the matters agreed to be referred.

[88] LAPP opposes the application for a stay on the basis that there is not in fact any dispute between the parties with regard to the matters agreed to be referred. This is because LAPP considers that New India has no defence to its application for summary judgment, which means that there is no dispute capable of reference to arbitration.

[89] New India had submitted that the test this Court should apply in assessing the application for a stay is a lower threshold than the test for raising an arguable defence for summary judgment purposes. However, the correct test to be applied where a stay of proceedings is applied for has recently been confirmed by the Court of Appeal in *Zurich Australian Insurance Limited T/A Zurich New Zealand v Cognition Education Limited*.[26] In the High Court, Associate Judge Bell had determined that the tests for determining whether a defendant has no defence to an application for summary judgment, and the test whether there is a dispute between

[25] Affidavit of Mr BV Whitehead, at paragraph 27.
[26] *Zurich Australian Insurance Limited T/A Zurich New Zealand v Cognition Education Limited* [2013] NZCA 180.

the parties to be referred to arbitration, are opposite sides of the same coin. In its appeal judgment from that decision, the Court of Appeal agreed that there was some merit to the lower threshold argument, however Parliament's intent was clear:[27]

> [76] All of that is not to say we consider Mr Galbraith's policy arguments are without merit. On the contrary, we consider that some of them do have merit. The point is that there are countervailing policy arguments and that Parliament has made its choice which we must uphold.
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> [77] We conclude that for the purposes of art 8(1) there will in fact be no dispute if the defendant has no arguable basis for disputing the plaintiff's claim. The court is thus empowered as a result of the added words to refuse to stay a proceeding if the claim is a proper one for summary judgment.
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> [78] The application for review is dismissed. We find that, by including the added words to art 8(1) of the First Schedule of the Arbitration Act 1996, Parliament intended that courts would apply the same arguable defence test to stay applications as is applied to summary judgment.

[90] It follows that the issue is whether New India has an arguable defence. As the Court's conclusion is that there is no arguable defence to LAPP's summary judgment application because non-disclosure was not material, there is no dispute between the parties capable of being referred to arbitration. The application for a stay of proceedings is dismissed.

Quantum

[91] The plaintiff alleges that the liability of the defendant under the first underwriting contract, 6207/2010, is the sum of $17,373,931.60. As well it claims interest pursuant to the Judicature Act from the date when payment was due to the date of judgment. It alleges that payment was due 26 April 2012. The defendant did not note any objection to the claim being calculated on this basis.

[92] In regard to Aon Benfield Contract 13627/2010 it claims the amount of $250,000 which it says fell due 27 May 2011. It also seeks interest on that amount from 27 May 2011 pursuant to the Judicature Act. Again no point was taken about the correctness of this calculation of the quantum.

[27] At [78].

Summary of conclusions

[93] The conclusions reached in this judgment can now be set out. First, the application for stay based on the submissions to arbitration is dismissed on the ground that the test applicable to a stay application based on article 8(1) involves the same arguable defence test as applies in summary judgment applications. The summary judgment application therefore ought to be permitted to proceed.[28]

[94] It is arguable that the defendant was not advised about the changes to the trust deed under which the LAPP scheme operated.

[95] The plaintiff is unable to establish the necessary facts to call in aid the provisions of s 10 ILRA. That is because the evidence that it has adduced that it sent a copy of the 2007 trust deed to Aon is hearsay and is not admissible because of the provisions of ss 18 and 20 of the Evidence Act and r 7.30 High Court Rules.

[96] The evidence that the plaintiff adduces that the changes to the trust deed in 2007 were communicated to Aon executives is not of sufficient strength to negative the existence of an arguable issue in relation to that point.

[97] However, the failure to disclose that there had been changes to the trust deeds between the 1993 iteration and that for 2007 were not material non-disclosures justifying the avoidance of the policy. A prudent insurer would have appreciated that the discretionary basis upon which the trustees were able to proceed when considering applications for relief under the fund were not essentially different between the two deeds so that the change to the 2007 version did not expose the insurer to greater risk.

[98] The defendant had not by its notice of opposition placed in issue the question of whether the plaintiff was able to prove the individual losses caused to each of the local authorities as a result of Q1 and Q2.

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[28] *Zurich Australian Insurance Limited v Cognition Education Limited*, above n 26, at [78].

[99] In any case, there was no need for the plaintiff to analyse the breakdown of the components of the aggregate loss which was suffered by the two territorial authorities as a result of Q1 and Q2. The plaintiff was entitled to claim as against the insurer that:

a) each event had caused loss which gave rise to an entitlement on the part of each local authority for indemnity under the LAPP scheme;

b) the amount of those entitlements in each case was going to involve calls on the fund which would exceed by a significant margin the limits of liability contained in the insurance contracts.

[100] The quantum of the plaintiff's claim against the defendant was correctly calculated.

[101] For the foregoing reasons I am satisfied that the defendant has no arguable defence to the plaintiff's claim. The defendant's application for a stay is dismissed.

Judgment

[102] There shall be judgment for the plaintiff as follows:

a) Judgment in the sum of $17,373,931.60 together with interest on that amount pursuant to the Judicature Act 1908 from 26 April 2012;

b) Judgment in the sum of $250,000 together with interest on that amount from 27 May 2011 pursuant to the Judicature Act 1908.

[103] The parties should confer on the issue of costs and if they are unable to agree are to file memoranda not exceeding five pages on each side within 15 working days of the date of this judgment being issued.

J.P. Doogue
Associate Judge