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Delta Pty Ltd v Mechanical and Construction Insurance Pty Ltd

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In *Delta Pty Ltd v Mechanical and Construction Insurance Pty Ltd*,[1] Queensland Investment Corp had contracted with Delta to undertake some excavation work in preparation for the construction of a high-rise building. Delta had subcontracted the installation of rock anchors for four retaining walls to Team Rock Anchors Pty Ltd (TRA). The work of TRA was "woeful" and the rock anchors did not perform as designed. TRA's defective work caused lateral movement of one of the retaining walls (SW1) and consequential damage. At issue was whether a contractor's all risks policy issued by the respondent (Mecon) responded to Delta's claim under the Mecon Policy.

Delta had sued TRA for damages for breach of contract and the claim had settled. However, pursuant to the terms of the settlement, TRA did not pay Delta the settlement amount but instead assigned its rights of indemnity under the Mecon Policy to Delta. Delta's right of recovery for the settlement amount depended wholly upon Delta successfully establishing that TRA had a right of indemnity for the settlement amount under the Mecon Policy. Delta therefore had to establish that TRA had a legal liability to pay Delta compensation for property loss within the meaning of the Mecon Policy.

The Mecon Policy

Clause 5 of the Mecon Policy provided that:[2]

> 5.00 … MECON will provide indemnity for all amounts which you become legally liable to pay in compensation of … Property Loss that happens within the Territorial Limits during the Period of Insurance as a result of an Occurrence which arises in connection with your Business.
>
> With MECON's prior written permission, and included within the applicable limits of Indemnity, MECON will also pay:
>
> …
>
> 5.03 costs incurred by you for temporary protective repairs undertaken to prevent any immediate threat of Property Loss or Personal Injury.

Property loss was defined to mean:[3]

> (a) physical loss, damage or destruction of tangible property including resultant loss of use of such property and/or,
>
> (b) loss of use of tangible property that arises from an Occurrence, provided that this loss of use does not result from:
>
> (i) delay or lack of performance of any contract or agreement by you or by others on your behalf, or
>
> (ii) a design defect or your failure to comply with a Project specification.

Occurrence was defined to mean an event, including the continued or repeated exposure of persons or party to conditions that are generally the same, which you could not have expected and did not intend to happen.

Event was defined to mean a single event of loss or damage.

Delta's case

Delta argued that:

- TRA's defective work impacted upon all four retaining walls in a way that amounted property loss within the meaning of the Mecon Policy.[4]
- The settlement deed rendered TRA "legally liable" to pay the settlement amount "in compensation of … Property Loss" that happened as a result of an occurrence.[5]

Delta is not entitled to indemnity under the Mecon Policy

The Court of Appeal[6] found that TRA was not entitled to indemnity under the Mecon Policy because the liability of TRA to pay Delta the settlement amount was not a legal liability to pay "in compensation of … Property Loss". The unchallenged finding of the trial judge was that only SW1 had moved excessively. The issue for the court was whether significant lateral movement to SW1 was capable of amounting to property loss within the meaning of the Mecon Policy. It was not. Movement of SW1 was not damage independently of damage to the wall or some other tangible property and was therefore not property loss. Further, any movement of SW1 was not by reason of any occurrence but was instead a result of TRA's breach of contract in installing rock anchors for all four retaining walls that were not in accordance with the specification and were therefore incapable of securing SW1.[7]

Delta's alternative claim under the Mecon Policy as an insured also failed as a matter of fact. Delta was not an insured under the Mecon Policy because it did not satisfy the condition precedent in the definition of "insured" that it was "not otherwise insured".[8]

The following issues were also determined and are worthwhile noting for their practical effect.

TRA was legally liable

The issue was whether the settlement deed rendered TRA legally liable for the settlement amount. The court held that as a matter of construction, it did. It is trite law that legal liability may be established by judgment, arbitral award or agreement, including an agreement of compromise. The issue of whether the settlement deed gave rise to legal liability on the part of TRA was a question of construction. The court noted and gave effect to the expressed objects of the deed, the repeated acknowledgments in it of TRA's liability to pay the settlement amount and the reference in cl 2.3 of TRA's represented lack of financial capacity to meet any substantial part of that liability as the explanation for Delta's agreement to cl 2.2. The deed rendered TRA unconditionally liable to Delta for the settlement amount and precluded Delta from enforcing that liability, except by and to the extent of any recovery by Delta as the assignee of TRA's right to an indemnity under the Mecon Policy.[9]

It is significant that a properly drafted settlement deed can render an insured legally liable to pay a sum of money for the purposes of a claim by the insured's assignee upon the liability insurance even though the liable is not directly enforceable against the insured.[10]

Is the settlement amount reasonable?

Delta was potentially entitled to recover the additional costs that it had incurred by reason of the breaches of subcontract as well as consequential loss claims arising from claims brought against Delta by another subcontractor. TRA's assumption of liability for the settlement amount was assessed upon the footing that it was reasonable for TRA to settle upon the basis that it inevitably would be found liable for serious and extensive breaches of subcontract which caused Delta substantial loss.[11]

In determining whether the settlement amount was reasonable, a thorough investigation or audit into Delta's claim for the additional costs incurred as a result of TRA's breach was unnecessary to prove reasonableness of the overall settlement amount. The amount that Delta had in fact incurred in additional costs indicated that the settlement sum was reasonable.[12] The settlement amount had involved a substantial compromise of this aspect of Delta's claim of more than a million dollars and it was relevant that the future costs of defending Delta's claims and Delta's costs of running the case would be very substantial.[13] This conclusion meant that Fraser JA did not strictly have to consider the viability of the consequential loss aspect of the settlement amount.[14] Nevertheless, a review of merits of the claim by the third party meant that the prospect of TRA being held liable for this claim was an additional ground for finding that the settlement amount was objectively reasonable even though the trial judge had been unable to estimate the quantum of this liability.[15]

No allowance should be made for any counterclaim

Mecon said that allowance should have been made for the value of the counterclaim that TRA had against Delta. Fraser JA said that TRA was entitled to an indemnity from Mecon for the reasonable amount which TRA became legally liable to pay Delta as compensation of property loss, whether or not TRA was entitled to payments from Delta for the subcontract price or under a contract for a different project.[16] This is undeniably correct. TRA's counterclaim was unrelated to its alleged liability for property loss in relation to which Delta claimed as assignee. The adequacy or otherwise of any available set-off in the counterclaim is therefore an irrelevant consideration as to whether the settlement is reasonable.[17]

Onus of proving a breach of the reasonable precautions clause

In accordance with the principle in *Wallaby Grip Ltd v QBE Insurance (Australia) Ltd; Stewart v QBE Insurance (Australia) Ltd*,[18] this issue is determined on a case-by-case basis and depends primarily upon the nature of the condition and the provisions of the policy. As a matter of construction, it was a matter for Mecon to prove a breach of the reasonable endeavours clause which had exposed TRA to a risk of incurring loss, damage or liability by a resulting danger that was recognised by TRA or its employee who knowingly did or omitted to do the act, such that the conduct of TRA or its employee should be characterised as reckless.[19]

Given the gross breaches of the subcontract, Fraser JA was satisfied that TRA was in breach of the reasonable endeavours clause.[20] This is not surprising in light of the "woeful" work of TRA which had involved "remarkably extensive and gross" breaches of contract. TRA had engaged in "extremely poor practice … which might have endangered the lives of workers within the excavation and in adjacent properties"[21] and had caused lateral wall movement and consequential damage. However, Fraser JA did not accept that the directors of TRA knew of the breaches of subcontract even though they were aware of the obvious risk of lateral wall movement

and consequential damage that would flow from an incorrect installation of ground anchors.[22]

Was Delta's claim time-barred?

Delta did not commence proceedings against Mecon until more than 6 years after the costs had been incurred. Fraser JA held that Mecon's obligation to pay Delta the "costs incurred by you for temporary protective repairs undertaken to prevent any immediate threat of Property Loss or Personal Injury"[23] arose when Delta incurred those costs. Compare this with the decision in *Globe Church Inc v Allianz Australia Insurance Ltd*[24] (*Globe Church*) where the court had determined that the cause of action under an Industrial Special Risks Insurance Policy accrued upon the happening of the insured event being property damage due to rainwater and flooding. The NSW Court of Appeal had not determined when the cause of action for additional costs arose as Globe Church had agreed that the question of principle was determinative of the issue.[25]

Conclusion

Delta's claim for indemnity failed because of the definition of property loss in the Mecon Policy. This is not surprising because in substance, Delta as assignee of TRA was effectively seeking indemnity for the costs of rectifying the defective work of TRA. The retaining wall was constructed defectively as a reason of the breaches of contract of TRA and therefore had to be rectified. It is loss of this nature that insurers typically ensure are not covered and such loss is therefore invariably expressly excluded from cover in contractor's all risks policies.

The case also provides useful insight into the approach of courts in relation to:

- the ascertainment of legal liability in circumstances where the claimant has taken an assignment of a named insured's entitlement to indemnity under a policy
- the relevant considerations in determining whether a settlement amount is reasonable
- the onus of proof in relation to an alleged breach of a reasonable endeavours clause and the requisite knowledge that has to be proved if it is alleged that a director of the insured is in breach of the reasonable endeavours clause
- when a cause of action accrues under an indemnity policy — given the possible tension between the approach of the Queensland Court of Appeal with the approach of the majority in the NSW Court of Appeal in *Globe Church*, this issue will ultimately have to be resolved by the High Court

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Footnotes

1. *Delta Pty Ltd v Mechanical and Construction Insurance Pty Ltd* [2019] QCA 062; BC201902880.
2. Above, at [8].
3. Above n 1, at [75].
4. Above n 1, at [4].
5. Above n 1, at [9].
6. Fraser JA with whom Flanagan J agreed, published the leading judgment. Except for one discrete issue, McMurdo JA at [161]–[162] also agreed with Fraser JA.
7. Above n 1, at [92].
8. Above n 1, at [103] per Fraser JA, [160] per McMurdo JA and [164] per Flanagan J.
9. Above n 1, at [32].
10. Above n 1, at [33]. See *CGU Insurance Ltd v One.Tel Ltd (in liq)* (2010) 242 CLR 174; 268 ALR 439; [2010] HCA 26; BC201005390 at [42]–[46]; and *Blakeley (as joint and several liquidators of Akron Roads Pty Ltd (in liq)) v CGU Insurance Ltd* (2017) 53 VR 733; 124 ACSR 1; [2017] VSCA 378; BC201711297 at [183]–[197] as authority.
11. Above n 1, at [40].
12. Above n 1, at [50].
13. Above n 1, at [64].
14. Above n 1, at [66].
15. Above n 1, at [74].
16. Above n 1, at [46].
17. Above n 1, at [46].
18. *Wallaby Grip Ltd v QBE Insurance (Australia) Ltd; Stewart v QBE Insurance (Australia) Ltd* (2010) 240 CLR 444; 264 ALR 425; [2010] HCA 9; BC201001702 at [28].
19. Above n 1, at [114] and [116].
20. See above n 1, at [122]–[128].
21. Above n 1, at [124].
22. Above n 1, at [130]–[132].
23. Above n 1, at [8].
24. *Globe Church Inc v Allianz Australia Insurance Ltd* [2019] NSWCA 27; BC201901162.
25. See case note for a discussion of the differing views of the majority and minority in that case: L Chan "Globe Church Inc v Allianz Australia Insurance Ltd" (2019) 34(10) *ILB* 125. The decision of Queensland Court of Appeal tends to indicate that they actually favour the minority view of Leeming JA rather than the approach of the courts in *Cigna Insurance Asia Pacific Ltd v Packer* (2000) 23 WAR 159; (2001) 11 ANZ Ins Cas 61-492; [2000] WASCA 415; BC200008007 and *Associated Forest Holdings Pty Ltd v Gordian Runoff Ltd* [2015] TASFC 6; BC201513471