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Proving arson and consequential loss — Worth v HDI Global Specialty SE

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In *Worth v HDI Global Specialty SE*,[1] the appellant had operated a childcare business from her home prior to it being burned down 5 years ago. The appellant was an insured under Home Based Business Property Insurance policy (the Policy) but the respondent insurer had denied indemnity on the basis that the appellant had deliberately lit the fire. The respondent insurer had initially granted the appellant conditional indemnity under the Policy pending the outcome of their investigations as to the cause of the fire but this was subsequently revoked. The appellant brought proceedings claiming:

1) the cost of reinstating her home rather than on an "indemnity basis", the agreed value of the contents and business interruption loss pursuant to the terms of the Policy, and
2) damages for consequential loss in the form of lost business revenue and damages for personal inconvenience suffered by the appellant

The basis of these two claims for damages was breach of the insurer's obligation to act with the utmost good faith pursuant to s 13 of the Insurance Contracts Act 1984 (Cth) or alternatively, for breach of its obligation to indemnify within a reasonable time.

The primary judge had found, on the basis of circumstantial evidence, that the appellant had deliberately lit the fire. For reasons that follow, the Court of Appeal, by majority allowed the appeal with indemnity under the Policy on an indemnity basis rather than a "reinstatement basis". The appellant was however unsuccessful in her claim for consequential loss and damages for personal inconvenience.

The issues on appeal

The New South Wales Court of Appeal had to determine the following issues:

- Whether the primary judge had erred in finding that the appellant had deliberately lit the kitchen fire.
- Whether, having made the primary finding, the primary judge erred in finding that the appellant had deliberately lit the living room fire.
- If yes, then the relief to which the appellant was entitled including whether the appellant was entitled to consequential loss and damages for personal inconvenience.

The process of reasoning of the primary judge

As alluded to above, the case of the respondent insurers was wholly based upon circumstantial evidence. There had been two fires at the house. One in the kitchen and the other in the living room ultimately caused the house to burn down. The primary judge had found that the appellant had deliberately started the kitchen fire and had used this finding to bolster his finding that the appellant had also started the living room fire.[2] McCallum JA found that the very serious allegation of deliberately lighting the kitchen fire could not form a part of the circumstantial case against the appellant unless it was separately proved.[3] The Court of Appeal, by majority did not consider that the evidence gave rise to "a reasonable and definite inference" within the meaning of *Bradshaw v McEwans Pty Ltd*,[4] that the appellant had deliberately lit the fires in the kitchen and the living room.[5]

The cause of the fire and the competing evidence

There had been a fire in the kitchen that had been started by a game guide that had been ripped in half and then partly left on an activated hotplate. The appellant could not explain how the game guide came to be ripped in half and then partially left upon the hotplate. The appellant's expert had put forward a hypothesis as to how the kitchen and the living room fires had both been started without human intervention. The game guide had fallen onto the hotplate as a result of turbulence and the fire in the living room had been started by a Tahiti wall screen. The primary judge had not accepted this "innocent" hypothesis. The primary judge said that the appellant was the only person who had the opportunity to deliberately light the fire.[6]

After a review of the competing hypothesis of the two experts, the Court of Appeal, by majority found that the innocent hypothesis had not been excluded as a reasonable possibility.[7] McCallum JA instead found that the

reasoning of the expert for the respondent as to the sequence of events that led to the fire in the kitchen rested upon "a level of impermissible speculation" and in particular, discounted the sequence of events that relied upon turbulence in the kitchen strong enough to knock the game guide from an unknown position onto the hotplate.[8]

The primary judge had therefore erred in finding that the appellant had deliberately lit the fire. Macfarlan and McCallum JJA said that the expert evidence of the respondent did not provide strong support for the case of the respondent. The remaining evidence also fell "well short of making out a case of arson".[9] It was accepted by all judges of appeal that the appellant had conducted "a happy and well-provisioned childcare business" from the home that she lived in with her 12-year-old son.[10] They did not find that the evidence of financial motive to be strong either. While her financial position was not "sound", neither was it dire.[11] Psychological considerations as to the likelihood that the appellant, as a single mother running a childcare business from her home, would have burned her house down also ought to have been taken into account. As McCallum JA said, the arson hypothesis made no "psychological sense" and was "quite bizarre".[12]

The relief to which the appellant was entitled

Basis of indemnity

The Court of Appeal said that the appellant was only entitled to be indemnified on an indemnity basis rather than on a reinstatement basis as the appellant had failed to commence the reinstatement with reasonable dispatch. This was conceded by the appellant in the Court of Appeal.[13] The proposition that the respondent was in breach of its duty of utmost good faith thereby entitling the appellant to indemnity on a reinstatement basis was not accepted. The court said that the respondent's refusal to indemnify the appellant was not so unreasonable as to be itself a breach of its obligation of good faith. The outcome of the dispute before the primary judge supported this proposition.[14]

Consequential loss — business interruption

There is a long-standing reluctance to award damages for a delay in the payment of money. A claim for a consequential loss is even more problematic. As a matter of construction, in the indemnity insurance context, the insurer's only promise is to pay an indemnity. There is no implied promise to act expeditiously. In *Globe Church Incorporated v Allianz Australia Insurance Ltd*[15] (*Globe Church*), the New South Wales Court of Appeal refused to imply such a term.[16] This is consistent with the approach of the English Courts.

Therefore, insureds founder on the fundamental rule that damages cannot be awarded for the late payment of damages. The position can be contrasted with *Hungerfords v Walker*.[17] In that case, there had been an overpayment of tax as a result of the negligence of the accountants. The tax office had refunded some of the overpayment of tax but had said that the recovery of the balance was time barred. The majority of the High Court in *Hungerfords v Walker* said that the client of the accountants was entitled to compound interest at a rate of 20% as compensation for the loss of use of the money.[18] This was on the basis that the funds would have either been used to repay loans bearing that rate of interest or invested in the business to earn profits at that rate. Nevertheless, the writer notes that there are several insurance decisions in Australia and New Zealand in which an insured has been awarded damages for consequential losses due to the insurer's failure to make timely payment.[19] However, these authorities cannot be followed unless the High court overrules *Globe Church.*

In *Globe Church*, the New South Wales Court of Appeal had also found that a cause of action under indemnity insurance accrues upon the happening of the insured event. The claim is for unliquidated damages calculated in accordance with the basis of settlement clause in the policy.[20] It is therefore unsurprising that the Court of Appeal was unanimous that the appellant is not entitled to damages for consequential loss on the basis of *Globe Church* and on the assumption that *Globe Church* is correct.[21]

It follows that the only available outcome for the appellant in the circumstances of this case is that she is only entitled to business interruption for the 12-month indemnity period calculated in accordance with the terms of the Policy.

Consequential loss — damages for personal inconvenience

The appellant sought to recover damages for personal inconvenience based upon the authority of *Baltic Shipping Co v Dillon*[22] on the basis that the appellant had suffered physical inconvenience as a result of the respondent's breach of contract and the mental suffering is directly related to that physical inconvenience. The appellant said that she had suffered physical inconvenience as a result of the respondent's refusal to indemnify. She and her son had to live with her parents for several years and she had lost her capacity to live independently.

It is not surprising that this claim was disallowed. Damages for mental distress, vexation and inconvenience are typically awarded in building cases where the

plaintiff has to live through the physical inconvenience of building work. It is difficult to see how living with one's parents which may be restrictive, can amount to physical inconvenience.[23]

Conclusion

This case illustrates the difficulties with proving arson where the insurer, as is invariably the case, is relying upon circumstantial evidence to prove fraud. Reasonable minds will differ as to the conclusions to be drawn from the circumstantial evidence. This is illustrated by the fact that four judicial minds have considered this issue and the polls are even.

While the appellant has been successful in obtaining indemnity under the policy, more than 5 years has passed since the fire. In that time, she has not operated her child care business which presumably meant that she was unable to obtain a loan to finance the rebuilding of her home. Given that the court found that she is not entitled to indemnity on a reinstatement basis, it seems unlikely that the appellant will be able to rebuild her home relying solely upon the proceeds of insurance as construction costs have risen markedly in the last 5 years.

While the duty of financial services licensees, to act efficiently, honestly and fairly pursuant to s 912A(1)(a) of the Corporations Act 2001 (Cth), did not apply to "claims handling and settling services" of insurers at the time that the cause of action crystallised in this case, an interesting point is whether the application of the duty might have given rise to another cause of action.[24]

It remains to be seen whether special leave to appeal is sought in this matter.

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Footnotes

1. *Worth v HDI Global Specialty SE* [2021] NSWCA 185.
2. Above, at [223] per McCallum JA.
3. Above.
4. *Bradshaw v McEwans Pty Ltd* (1951) 217 ALR 1 at 5.
5. Above n 1, at [5] per Macfarlan JA and at [205] per McCallum JA.
6. Above n 1, at [140] and [167] per Meagher JA.
7. Above n 1, at [3] per Macfarlan JA and at [275] and [277] per McCallum JA.
8. Above n 1, at [234]–[235].
9. Above n 1, at [2] per Macfarlan JA.
10. Above n 1, at [2] per Macfarlan JA and [139] per Meagher JA.
11. Above n 1, at [2] per Macfarlan JA, [135] per Meagher JA and [281] per McCallum JA.
12. Above n 1, at [206] and [272] per McCallum JA and at [3] per Macfarlan JA.
13. Above n 1, at [171]–[176] per Meagher JA, Marfarlan JA agreeing at [6] and McCallum JA agreeing at [207].
14. Above n 1, at [175] per Meagher JA, Macfarlan JA agreeing at [6] and McCallum JA agreeing at [207].
15. *Globe Church Inc v Allianz Australia Insurance Ltd* (2019) 99 NSWLR 470; 365 ALR 750; [2019] NSWCA 27; BC201901162.
16. Above n 1, at [179].
17. *Hungerfords v Walker* (1989) 171 CLR 125; 84 ALR 119; BC8908050.
18. Above.
19. W Courtney, *Contractual Indemnities*, Hart Publishing, 2014 at [5–53].
20. Above n 15, at [209].
21. See the L Chan "Globe Church Inc v Allianz Australia Insurance Ltd" (2019) 34(10) *ILB* 125 in which the author discusses whether the judgment of the minority ought to be preferred. Unfortunately, special leave was not sought in the case.
22. *Baltic Shipping Co v Dillon* (1993) 176 CLR 344 at 363–4 per Mason CJ, Toohey and Gaudron JJ agreeing, at 381 per Deane and Dawson JJ, at 405 per McHugh J.
23. Above n 1, at [203]
24. Section 912A(1)(a) of the Corporations Act 2001 (Cth) has not been tested within the context of a failure to act expeditiously by a claims handler or an insurer.