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LIFE AFTER *CHUBB V MOORE*

The revival of Third Party Declaratory Relief Applications against Insurers

Introduction

In *Chubb v Moore*[1], the defendants were insured under various policies, for the liability of former directors and executives of companies in the Great Southern Group. The policies were claims made and notified contracts of insurance. The claimants notified the insurers of a charge in favour of the claimants, over the insurance money by operation of s6 of the *Law Reform (Miscellaneous Provisions) Act*[2] (the **LRMPA**). The insurers brought the proceedings before the Court in order to determine the rights of the parties.

Chubb v Moore dealt with a number of issues in connection with s6 of the LRMPA. One issue was whether s6 applies to claims made policies and if so, whether it creates a charge arising from an event that happened before the inception of the policy. The Court of Appeal held that s6 is not limited to occurrence based polices and prima facie, also applies to claims made policies. However, it held that a charge cannot attach in circumstances where the event giving rise to the claim occurred prior to inception of the policy.

Many professional indemnity insurers may have breathed a sigh of relief after *Chubb v Moore,* as in many circumstances of claims made policies, s6 will not be available to a third party claimant.

However, since *Chubb v Moore*, the Courts have positively endorsed third party declaratory relief applications as an alternative to s6, specifically in circumstances where s6 is not available. In *Belcastro v Gabriel Nakhal*[3], in September last year, Justice Campbell observed at [44(c)] that:

> '... the limited utility of s 6 [of the LRMPA] in many cases involving "claims made and notified" liability insurance policies as illustrated by Chubb v Moore, supports the adoption of another legally available path lest plaintiffs who have a strongly arguable claim for redress go without an effective remedy. That possibility is not in the interest of justice, or, I might add, the administration of justice ...'

Declaratory relief applications are not a new species. They are a common procedural mechanism by which insureds and insurers can proactively seek a determination regarding their respective rights and obligations under a policy as between themselves. Third party declaratory relief applications, however, seem to be on the rise, as an alternative avenue against insurers, since *Chubb v Moore*.

The necessary elements for a declaration

A declaration is an equitable discretionary remedy. It is a formal statement by a court, which may be of fact or law or mixed fact and law, pronouncing upon the existence or non-existence of a legal state of affairs. However, it does not create rights capable of enforcement without further order of the Court. This is in contrast to a coercive judgment which can be enforced.

In order for an applicant to be entitled to declaratory relief:

- there must be a justiciable controversy (ie, a controversy involving a real issue that can be settled by a court, involving a present claim made by one party and another party disputing it);

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[1] *Chubb Insurance Co of Australia Ltd v Moore* [2013] NSWCA 212; 302 ALR 101

[2] 1946 (NSW)

[3] [2014] NSWSC 1305

- the applicant must have a real interest in the matter (ie, they must be specially affected); and
- a declaration, if made, must have utility (ie, there must be foreseeable consequences in that a declaration, if made, must confer some recognisable advantage on the applicant).

In the decisions both before and after *Chubb v Moore*, the primary argument put forward by insurers is that because the third party and insurer are not in privity of contract there is:

- no justiciable controversy (ie, it is not the parties to the contract of insurance that are in dispute);
- the third party applicant does not have a real interest (ie, they lack standing to bring the claim, as only persons who are parties to a contract are entitled to enforce rights under the contract); and
- a declaration between a third party and an insurer would not be binding in subsequent proceedings (eg between insured and insurer) and therefore, would lack utility.

The case law discussed below, however, makes it clear that privity in contract is not a precondition to making an application for declaratory relief. Nor does it matter that the insured may not, for whatever reason, challenge the insurer's decision on indemnity. In relation to utility, it is this area where the law has developed as a cure to *Chubb v Moore,* when the policy is a claims made policy incepted after the event giving rise to the claim. As can be seen from the cases that came after *Chubb v Moore*, the Courts have concluded that so long as a declaration has the potential to have some practical effect then there is utility, even if it cannot legally bind an insurer and insured.

Before *Chubb v Moore*

FAI General Insurance Company Ltd v Interchase Corporation Ltd & Ors[4]

In this matter valuers, who had carried out valuation of a property for Interchase, were sued for negligence. The valuers' insurer initially conducted the defence of the claim but then declined indemnity under the policy. Although the insured was not insolvent, it did not have sufficient assets to justify Interchase proceeding to trial. Interchase sought to join the insurer as a defendant, to obtain a declaration that the insurer was liable to indemnify the valuers. This application succeeded at first instance, but was overturned on appeal. The main issue was whether a declaration, if made, would have utility. The majority said that a declaration, if made, would not produce foreseeable consequences, that is, it would not have utility. This was said to be so because:

- a declaration would not be legally binding between insured and insurer;
- res judicata, nor issue estoppel, would bind the insurer in future proceedings[5];
- if res judicata and issue estoppel do not apply, there is no appreciable prospect that in subsequent proceedings a defence by the insurer denying indemnity would be struck out as an abuse of process; and
- as it may be taken that the insurer would not accept a non-binding determination adverse to it in the present litigation, the declaration would be in the nature of an advisory opinion, without beneficial effects, and would therefore lack utility.

Justice Davies, however, dissented. In doing so, Justice Davies agreed that neither res judicata nor issue estoppel would operate to bind the insurer and insured, if the declaration was made. However, Justice Davies did not think there would be no utility simply because the declaration would not legally bind insurer and insured if, in its practical effect, it was binding. Justice Davies approached the matter somewhat differently and considered that abuse of process could afford the same protection as *Anshun* estoppel[6].

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[4] [1998] QCA 180

[5] Res judicata says a matter may not, generally, be relitigated once it has been judged on the merits and issue estoppel prevents an issue that has been litigated and decided from being raised in subsequent proceedings between the same parties in a different cause of action.

[6] *Anshun* estoppel is a wider concept of estoppel which prevents a party from bringing claims which should have been pursued in former proceedings.

Justice Davies said that if the insurer were joined as a co-defendant, the insurer and the insured would have full opportunity to litigate the question in respect of which the declaration was sought. Accordingly, it would be an abuse of process to permit either to litigate that question again in subsequent proceedings. The declaration would, in this way, have the practical effect of determining the question of the insurer's liability to indemnify the insured, as between those parties.

Examples of subsequent proceedings that might be contemplated and which, in Justice Davies' view, provide the necessary utility include:

- the insured could sue the insurer (with litigation funding from the third party who has obtained the declaration) and the third party could exercise priority rights under s562 of the *Corporations Act*[7] over the proceeds of that claim; or
- if the insured is subsequently deregistered the third party would be entitled to sue the insurer under s601AG of the *Corporations Act*.

Although Justice Davies was the minority in the *Interchase* decision, his Honour's dissenting judgment took on some significance in a number of subsequent cases.

Employers Reinsurance Corporation & Anor v Ashmere Cove Pty Ltd & Ors[8]

This decision is probably the most prominent in which Justice Davies' approach was adopted. The applicant investors sought leave to join the professional indemnity insurers of the entity responsible for an investment scheme gone wrong. The responsible entity, KMF, was in liquidation. The applicants were granted leave to sue KMF. The claim against the insurers was for a declaration that the policy responded to KMF's liability to them.

The applicants succeeded at first instance in their application to join the insurers for the purpose of seeking a declaration. In granting that leave, the Court acknowledged that an insurer joined as a co-defendant with the insured would not be bound as between itself and the insured by a declaration that it was liable to indemnify the insured, and that there would be no point in making an order for joinder if the declaration did not, in practice, effectively determine the insurer's liability to the insured. However, the Court went on to adopt Justice Davies' reasoning that there was utility if the declaration had the 'practical effect' of binding the insurer and insured, in that if the insurer had a full opportunity to contest the question the subject of the declaration, it would be an abuse of process for it to attempt to relitigate the issue in subsequent proceedings between insurer and insured.

The insurers appealed to the Full Court of the Federal Court on, inter alia, constitutional grounds. The basis of the constitutional challenge was that any declaration could not authoritatively determine the rights and duties of the parties to the contract of insurance and under the Constitution, the Court's jurisdiction did not extend to making non-binding decisions.

The insurers argued that central to the concept of judicial power was the power to make authoritative and binding determinations as to some immediate right, duty or obligation and as the declaration sought was non-binding, the Court was being asked to give nothing more than an advisory opinion on the meaning of the policy (this view is supported by the majority decision in *Interchase*, which was not followed at first instance). The insurers went on to argue that to avoid this conclusion, it was necessary to have an enforceable remedy against the insurers and no such remedy was available given the plaintiff was not party to the contract of insurance.

It is perhaps not surprising that this argument was rejected by the Full Court, which went on to affirm the decision at first instance that there does not need to be privity in contract. The Full Court observed, as did Justice Davies in *Interchase*, that any attempt by the insurers to relitigate their liability under the policy in subsequent proceedings would give rise to an issue concerning the application of the *Anshun* estoppel principle.

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[7] 2001 (Cth)

[8] [2008] FACFC 28

QBE Insurance (Australia) Ltd v Lois Nominees Pty Ltd[9]

In this matter, Mr Hill, a solicitor, ceased practice in 2006 but maintained run off professional indemnity insurance for claims made thereafter. In 2009 a claim was made by his former clients, Lois Nominees, who alleged Mr Hill misused trust monies given to him in 2004 and 2005. Mr Hill's insurer declined indemnity on the basis that the conduct of Mr Hill was not in connection with his legal practice and therefore, did not enliven the policy, and alternatively that certain exclusions applied.

In February 2010 Mr Hill was declared bankrupt and a trustee in bankruptcy was appointed. The trustee did not have the funds to litigate the indemnity question. Lois Nominees sued the trustee and also the insurer for a declaration that the policy indemnified Mr Hill. Initially, Lois Nominees made a failed application to join Mr Hill's insurer to the proceedings. That decision was not appealed but undeterred, Lois Nominees commenced a separate action against the insurer, which was joined to the proceedings against Mr Hill's trustee.

The insurer sought summary judgment in part on the basis that the proceedings against it were an abuse of process, as any declaration as between Lois Nominees and the insurer would not be binding on any future proceedings between the insurer and the trustee. In response, Lois Nominees relied on the principle in *Ashmere Cove*, that if a declaration was granted and Hill's trustee subsequently sought to challenge the denial of indemnity, any defence by the insurer would be struck out for an abuse of process because it would constitute an attempt to relitigate an issue already decided by the grant of the declaration.

The insurer argued that *Ashmere Cove* (and the cases that followed) were flawed and that the majority decision in *Interchase* should be followed. The Court, however, followed *Ashmere Cove* and dismissed the insurer's summary judgment application (at first instance and on appeal).

After *Chubb v Moore*

Sienkiewicz v Salisbury Group[10]

In this matter, a company of financial advisors had allegedly given negligent financial advice. The company went into liquidation and did not have any significant assets against which judgment could be enforced. Accordingly, the applicants sought to join the relevant insurers to the proceedings for the purpose of obtaining a declaration that the policy responded to the financial advisors' liability to them.

The matter dealt primarily with the issue that there must be a justiciable controversy, before there is an entitlement to bring an application for declaratory relief. The insurers argued that as the liquidators of the insured company did not intend to challenge the insurers' indemnity decision, there was no justiciable controversy. The insurers argued for the majority decision in *Interchase*, despite the *Ashmere Cove* and *Lois Nominees* decisions (which adopted Justice Davies' dissenting judgment). *Ashmere Cove*, however, was followed once again, and leave was granted to join the insurers for the purpose of seeking declaratory relief.

Austcorp Project v LM Investment Management[11]

This decision is possibly the first in which a Court openly acknowledged that a declaratory relief application provides an alternative avenue for third parties troubled by the decision in *Chubb v Moore*.

The proceedings were for equitable compensation, damages and other relief for the sale of land at a gross undervalue. The plaintiffs made an application to join the defendants' professional indemnity insurer. The applicants did not seek to invoke the provisions of s6 of the LRMPA, because although, in their view, *Chubb v Moore* was wrongly decided, they accepted that decision prevented them from invoking s6.

Ashmere Cove was followed and leave was granted to join the insurer.

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[9] [2012] WASCA 186

[10] [2013] FCA 977

[11] [2013] FCA 883

***Belcastro v Gabriel Nakhl*[12]**

This decision, handed down in September 2014, involved a third party application for leave to join an insurer pursuant to s6 of the LRMPA and in the alternative, for the purpose of seeking a declaration about policy response. However, in light of *Chubb v Moore*, the s6 application was not pressed. The Court observed at [33] that:

> '... given the decision in [*Chubb v Moore*] s6 may become redundant as a means of joining an insurer to proceedings which have their foundation in a claims made and notified policy like those in question here'.

On the alternative application to join the insurer for the purpose of seeking a declaration, the insurer argued that there was no justiciable controversy, as there was no evidence that indemnity had been denied (the insurer's counsel, however, had acknowledged it was very unlikely that indemnity would be extended).

Although the pleading against the insurer was struck out on the basis it was embarrassing[13], the Court agreed to allow the plaintiff an opportunity to re-plead and said (subject to the plaintiff re-pleading its case adequately) it was satisfied that the plaintiff had made a case for joining the insurer for the purpose of seeking a declaration on the basis that:

- although indemnity had not been formally declined, it likely would be;
- in circumstances where the liquidators of the insured were without funds to either actively defend the litigation, or bring a cross claim against the insurers, s562 of the *Corporations Act* provides an appropriate legal context to permit the plaintiffs to seek a declaration that the insurer is liable to indemnify the insured; and
- joinder of the insurer will avoid a multiplicity of proceedings, enabling all matters on controversy between the parties to be completely and finally determined, once and for all.

It was in this decision that Justice Campbell went on to offer words of encouragement to prospective applicants by saying at [44(a)] that *'the limited utility of s 6 of the LRMPA, as a result of Chubb v Moore, supports the adoption of another legally available path for plaintiffs'.*

***Akron Roads Pty Ltd & Ors v Crewe Sharp Pty Ltd & Ors*[14]**

The Victorian Supreme Court handed down this decision earlier this year, which involved an application to join the insurer of Crewe Sharp after Crewe Sharp went into liquidation, for the purpose of seeking a declaration that the insurer must indemnify Crewe Sharp. Indemnity had been declined. The insured had not applied to join the insurer, nor indicated any intention to challenge the denial of indemnity[15]. *Ashmere Cove* and *Lois Nominees*, among other cases, were relied on by the applicants as demonstrating a willingness by the Courts to permit the litigation of similar claims by a third party against an insurer.

Again, the insurer argued there was no privity of contract, as the applicants were not party to the contract of insurance. The insurer also argued that as no claim was made by the insured against the insurer, there was no justiciable controversy. The insurer submitted that there was a clear conflict of relevant authorities at an intermediate Appellate Court level, concerning the question of jurisdiction to grant declaratory relief in such cases. This conflict was said to arise from the majority decision in *Interchase* and the dissenting judgment in *Lois Nominees*. However, the Court was not persuaded that there was a clear conflict and ultimately, *Ashmere Cove* was followed.

Conclusion

Justice Davies' dissenting judgment in *Interchase* has been endorsed by at least six decisions dealing with third party declaratory relief applications against insurers since. Although insurers continue to actively oppose such applications based on arguments that there is no privity of

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[12] [2014] NSWSC 1305

[13] Primarily because the s6 cause of action, although not pressed, continued to be pleaded.

[14] [2015] VSC 34

[15] There is no equivalent provision to s6 of the LRMPA in Victoria.

contract, or no justiciable controversy[16], they appear to be fighting a losing battle. The legal landscape that has emerged since *Chubb v Moore* suggests that the law is now reasonably settled in this area, at least until the High Court shows an interest in the issues.

The cases make it clear that:

- third parties can make applications for declaratory relief against insurers;
- the absence of privity in contract is not a bar;
- the absence of a dispute between insured and insurer is also not a bar;
- such applications can be a way round *Chubb v Moore*, in circumstances of claims made policies incepted after the event giving rise to the claim[17]; and
- although a declaration is not a right enforceable directly by the third party against the insurer, it can still have practical utility.

The Courts have recognised that the necessary practical utility can manifest in one of the following ways:

- the third party can use a declaration to encourage the liquidator or trustee to commence proceedings against the insurer, challenging the denial of indemnity[18]; or
- the third party could wait for an insured in liquidation to become deregistered and then commence proceedings directly against the insurer[19].

Each case will ultimately turn on its own facts. However, if a declaration is made against an insurer, although of itself not enforceable, there is a significant prospect that a defence filed by that insurer in subsequent proceedings such as the above, will be struck out as an abuse of process. The end result is that the insurer then has no-where to turn, other than to agree to pay out the claim, consistent with the declaration obtained by the third party.

July 2015

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[16] If the insured has not challenged the denial of indemnity.

[17] Or in other circumstances where s 6 cannot be invoked, eg in jurisdictions outside NSW which do not have equivalent legislation.

[18] If there are no funds, the third party may fund this litigation given the level of comfort provided by the declaration it already obtained.

[19] Pursuant to s601AG of the *Corporations Act*.