Cover to Cover

Issue 27

Our publication for New Zealand insurance professionals

MinterEllisonRuddWatts.

Contents

David Ballew / Unsplash

Foreword

New Zealand's insurance sector is experiencing unprecedented demand from repeated extreme weather events less than two months into the year. At the same time, new developments in other areas also challenge the industry.

The unprecedented Auckland Anniversary weekend floods, and further damage caused almost immediately afterwards by Cyclone Gabrielle, have had a significant effect on the insurance market. The Minister of Finance, Grant Robertson, told reporters that, in terms of insurance, the floods alone would be the biggest non-earthquake event that New Zealand had ever experienced. In this edition of *Cover to Cover*, we discuss the extent of the damage inflicted throughout communities and the subsequent impact on the insurance industry.

Retail insurers and banks are busy preparing for the upcoming Financial Markets (Conduct of Institutions) Amendment Act 2022 (CoFI Act) regime. We outline the principal requirement of the conduct regime – the fair conduct programme – and what financial institutions should be doing to prepare for the regime, which comes into full force in early 2025.

Forbes magazine recently reported a prediction by Cybersecurity Ventures that the global cost of cyber-crime will reach USD8 trillion in 2023 and will grow to USD10.5 trillion by 2025. The same article also reported that cyber-crime would be the world's third-largest economy after the United States and China, if it was measured as a country. Our experts continue to reinforce the importance of protecting your organisation against cyber attacks. We discuss key risks and strategies to respond to an attack, as well as developing themes in this space locally and globally.

The Rules Committee (Te Komiti mō ngā Tikanga) has released its *Improving Access to Civil Justice* report. If implemented, the report's recommendations will create widespread changes in litigation procedure in the High Court, District Court, and Disputes Tribunal for most civil cases. We consider some of the anticipated impacts of the report on insurance disputes in Aotearoa New Zealand.

The insurance industry should prepare for increased regulator enforcement this year. The Financial Markets Authority has indicated that it intends to take a harder line on regulatory compliance, particularly where customer outcomes are poor. We outline an example of the best approach to take when faced with a breach, as well as an approach to avoid.

We also provide insight into two case studies: a recent ruling by the England and Wales Court of Appeal on exclusion for losses caused by *"pollution or contamination"*; and a judgment from the High Court of Australia providing guidance on insurers' rights of election.

We hope you find this issue insightful and useful.

Floods, landslips, cyclones and locusts

Co-authored by Andrew Horne and Nick Frith

When asked about the magnitude 6.3 earthquake that rocked the central North Island on 15 February this year, the Prime Minister, Chris Hipkins, said that he was looking out the window for a plague of locusts.

Hipkins' reaction was understandable. The earthquake followed unprecedented rainfall that caused substantial damage in the Auckland region, followed by Cyclone Gabrielle shortly afterwards, which itself caused extensive flooding and other damage in a widespread area including the Hawke's Bay, Northland, Gisborne, Bay of Plenty and Waikato regions. Geonet, in reporting the earthquake, offered a more restrained observation, saying that it was *"a difficult time for the North Island"*.

It was also a difficult time for insurers, who calculate reserves and arrange reinsurance based on assumptions that do not factor in multiple major loss events in quick succession.

Auckland Anniversary floods

The Auckland Anniversary weekend floods were unprecedented. A reported 24.5 centimetres of rain – nearly a quarter of a metre – fell in the 24 hours between the Friday and Saturday. This was well above Auckland's previous record for rainfall in one day, which was 16.1 centimetres of rain recorded on a day in 1985. 24.5 centimetres exceeded the normal rainfall that would be expected in a typical three-month summer.

The resulting flooding caused substantial damage. The Minister of Finance, Grant Robertson, told reporters that, in terms of insurance, it would be the biggest non-earthquake event that New Zealand had ever experienced. The Guardian newspaper in the UK reported that some insurers were describing it as the biggest climate event in the city's history. Tim Grafton, head of the Insurance Council, was reported as saying that the insurance industry expected the cost to insurers to exceed NZD1 billion.

As well as losses covered by private insurance, Toka Tū Ake EQC (EQC) will receive claims for land damage where landslips were caused by the flooding. EQC provides limited cover for damage to

Casey Horner / Unsplash

residential land. This extends to the land under an insured home and outbuildings, within eight metres of the home and outbuildings, and under or supporting the main accessway (but not the driveway surfacing), up to 60 metres from the home.

Some owners of clifftop houses suffered high-profile losses of land which collapsed many metres below, in many cases robbing the owners of lawns and other features, but in some cases undermining the foundations of the houses and making them unsafe. Claims for damage to land through landslip may be made to EQC, provided the land is in the covered areas. In many cases, the land lost will not be within the areas that are covered under the Act, so the owner will be uninsured. Even where there is cover, it will be limited to the market value of the land that has been lost (and indemnity value of land structures, such as bridges and retaining walls), and will not likely take account of the much-reduced desirability of the property as a whole, once a part has been lost to landslip.

In addition to private insured losses, Waka Kotahi NZ Transport Agency estimated that the damage to roads from the Anniversary weekend flooding may cost NZD1 billion to repair.

Cyclone Gabrielle

These costs do not include the cost of claims from Cyclone Gabrielle, which Grafton said included around 30,000 claims so far. Grant Robertson has suggested that the total cost of the cyclone damage could be around NZD13 billion, although much of that would not be insured.

The total losses to insurers from both events may be comparable to those that resulted from the Kaikoura earthquake in 2016, which gave rise to more than NZD1.8 billion in insurance claims, including around NZD1 billion for building claims in Wellington. They will be less, however, than the losses from claims arising from the Canterbury earthquakes, which cost private insurers around NZD21 billion and EQC around NZD10 billion.

Legal claims that may result from the flooding and cyclone damage

Those affected by the Auckland floods and Cyclone Gabrielle, including insurers, are beginning to consider the civil liability claims that could arise from these events. Our firm recently spoke to the NZ Herald about the types of claims that could potentially be made.

News articles have raised the possibility of claims arising from the damage caused by forestry slash (i.e. detritus such as branches) when it impacted bridges and other structures in the flooding, which has resulted in the Government's announcement of a Ministerial inquiry. We discuss slash claims below, but they are by no means the only liability claims that could have an impact on the insurance industry. Other possibilities include:

- Claims against councils, possibly asserting that they negligently failed to provide or maintain appropriate drainage, or that they negligently approved earthworks and other works that exacerbated natural flooding problems.
- Claims against professional service providers, such as architects, engineers and geotechnical engineers.
- Claims against neighbouring landowners for failing to resolve hazards or making changes that exacerbated flooding.
- Claims against EQC for land damage.
- Claims against private insurers for flood and related damage.

Forestry slash

The prospect of forestry slash claims is attracting increasing media attention.

In principle, claims in negligence or nuisance may be available to property owners who have suffered slash damage. Claimants would need to establish, among other things, that:

- The relevant damage was caused by slash from an identifiable source, or at least a finite number of identifiable sources (i.e. forestry companies).
- The owner of the slash had a duty of care to downstream property owners to prevent the escape of slash in a severe weather event and that the resulting damage was foreseeable (for negligence) or that the build up of slash and its escape was caused by a non-natural use of the land (for nuisance).

There may be difficulties in identifying the source of damage-causing slash. However, that is not necessarily a barrier to claims. The High Court Rules allow plaintiffs to sue several defendants on the basis that they do not know which caused the relevant damage. One of the issues in the proceeding will be the identification of the correct defendant.

Potential plaintiffs may band together to create a representative (class) action if a sufficient number suffered damage likely caused by the same landowner's slash, or an identifiable group of landowners' slash. A variation on that theme might be a staged class action where multiple potential defendants are sued, first for a declaration as to the cause of damage and other preliminary issues, and second for individual claimants to prove loss. A similar model was to be adopted in the *Ross v Southern Response* litigation. Yet further variation might well be insurers collating subrogated claims covered under their policies and prosecuting those claims in group form.

These claims will likely engage landowners' public liability insurance (if held) and may also result in shareholder claims if slash was not managed as required.

Aside from civil claims, there may also be prosecutions for breach of consent requirements to clear slash. Those claims may engage landowners' statutory liability policies.

Claims against councils

Councils may be sued for a failure to act when forestry companies breach their obligations to manage slash. Councils may also be subject to claims arising from consenting decisions. Properties built in flood-prone areas may be subject to scrutiny in terms of the steps required to mitigate flood risk.

Litigation may also flow from any council decisions around 'red zones' prohibiting rebuilding in certain flood-prone areas.

Claims against professional service providers and others

Catastrophic events tend to increase the risk of claims against professional service providers. This is primarily because the magnitude and extent of the loss unearths potential defects that would not have been identified if the event had not occurred.

Insureds who find that they are not covered to the extent they expected (or now expect) may look to their insurance brokers for answers.

Claims could also arise against builders, architects, engineers and geotechnical engineers who designed or approved buildings that were susceptible to flooding or cliff collapses.

Claims may also be made against neighbouring landowners for failing to resolve hazards or making changes that exacerbated flooding.

Where buildings have sold recently, claims could be made against vendors or estate agents if relevant misrepresentations were made.

Solicitors may be found liable for failing to identify relevant details such as flood risk warnings in LIMs. Property owners could take action, as could lenders who relied upon solicitors.

"Unsurprisingly, these events are having an effect upon the New Zealand insurance market. That impact is likely to deepen if the claims discussed above eventuate."

Effects upon insurers

Unsurprisingly, these events are having an effect upon the New Zealand insurance market. That impact is likely to deepen if the claims discussed eventuate.

Insurance premiums are tipped to rise. One reason for this is that insurers' apprehension of a risk often increases once that risk has eventuated. Mel Gorham, Chief Executive of the Insurance Brokers Association, is reported as saying that insurance rates could be in for a re-think as the extent of the damage from the flooding is revealed, and that even before this event, insurers were looking with greater scrutiny at flood risk.

Another reason is that multiple, large claims in quick succession drain insurers' reserves, and insurers may have to replenish them. This may be achieved by seeking funding from shareholders or external funders or, in the case of large group insurers, by transferring funds from other parts of the business. In the longer term, premiums will likely rise to fund the replenishment of reserves, but that does not solve the immediate need.

Furthermore, some insurers may take the view that it is prudent to obtain additional or amended reinsurance with a lower deductible. This will likely increase the demand for reinsurance with relatively low deductibles, at least for a time. It will also increase insurer's costs, as the lower deductibles will come with higher reinsurance premiums which are likely to flow through to customers.

It is also likely that there will be wider flow-on effects which will affect insurers along with others. The cost of labour and materials in the construction industry is likely to rise as a large stream of work becomes available for the repairs of flood and cyclone damage. Subject to policy limits, this will increase costs for insurers as they fund repair and replacement works. It may also increase business interruption insurance payments, where insureds are unable to arrange repairs to business premises in a timely manner because of the shortage of skills and materials.

The significance to insurers of the Auckland Anniversary weekend floods and the further damage caused by Cyclone Gabrielle is therefore potentially broader than the immediate cost in terms of reductions in reserves and increased premiums. Longer term reinsurance costs will likely rise, as will costs, and the risk of a wave of liability claims that engage defence costs cover.

Preparing for the CoFI regime:

Fair conduct programmes

Co-authored by Lloyd Kavanagh, Maria Collett-Bevan and Sarah Jones

Retail insurers and banks are busy preparing for the incoming Financial Markets (Conduct of Institutions) Amendment Act 2022 (CoFI Act) regime.

This article outlines the principal requirement of the upcoming conduct regime – the fair conduct programme (FCP) – and what financial institutions should be doing now to prepare for the regime coming into full force in early 2025. In short, there is an enormous amount to do before then.

In particular, financial institutions should be preparing and implementing their FCP (a requirement of the regime), in order to obtain a conduct licence after applications open on 25 July 2023.

CoFI is in fact relatively simple and boils down to this:
Are your customers getting the financial products and services they need, when they need them, and do they do what the customer reasonably expects them to do?

Samantha Barrass, Chief Executive of the Financial Markets Authority (FMA)

The CoFI regime

The CoFI regime (now contained in new Subpart 6A of Part 6 of the Financial Markets Conduct Act 2013 (FMCA) inserted by the CoFI Act) introduces a legal framework requiring financial institutions to:

- be licensed by the FMA in respect of their conduct towards consumers;
- comply with a "fair conduct principle" to treat consumers fairly, through the requirement for financial institutions to establish, maintain and implement an FCP;
- take all reasonable steps to comply with the programme; and
- comply with regulations that ban target-based sales incentives and regulate other types of incentives.

The CoFI regime builds on the recommendations from the FMA and RBNZ's thematic reviews on conduct and culture in banking and insurance (which were in turn triggered by the Australian report on misconduct in the banking, superannuation and financial services industry). But it translates those expectations into specific legal obligations that can be enforced either by FMA or by customers (for example, through class action claims).

The fair conduct principle

The CoFI regime centres around the fair conduct principle. The fair conduct principle is now defined in the FMCA and requires financial institutions to treat consumers fairly. This means:

- Paying due regard to consumers' interests.
- Acting ethically, transparently and in good faith.
- Assisting consumers to make informed decisions.
- Ensuring that relevant services and products are likely to meet the requirements and objectives of consumers.
- Not subjecting consumers to unfair pressure or undue influence.

The FMCA also specifies when the financial institution must apply the fair conduct principle. This includes when it is:

- designing any relevant service or associated product;
- offering to provide and providing a relevant service or associated product to a consumer; and
- has any dealings or interactions with a consumer in connection with any relevant service or associated product (for example, responding to a complaint or handling a claim under an insurance contract).

The FCP: Putting the fair conduct principle into practice

An FCP means effective policies, processes, systems and controls are designed to ensure the financial institution's compliance with the fair conduct principle.

As the FMA has emphasised, this is not to be regarded as a separate compliance exercise. Because of its broad scope it must be reflected in everyday business processes and culture in order to be successful.

Key considerations of the FCP

1. It must be suitable for the business

Some financial institutions, particularly those with large and/or complex operations, may choose to create an overarching policy or framework document that explains the structure of the FCP and outlines the different policies, processes, systems and controls that comprise the FCP. Other financial institutions may determine that a single document is sufficient to capture their FCP.

2. It must have at least the minimum requirements of an FCP

The minimum requirements for the content of an FCP are set out in section 446J of the CoFI Act. These are minimum requirements, and financial institutions may choose to implement additional policies, processes, systems and controls to ensure that consumers are treated fairly.

The FMA expects financial institutions to be able to demonstrate how they have considered all of these factors. This may be achieved by including commentary about this in the FCP itself.

3. It must be implemented and maintained

A key component of implementing an effective FCP is ensuring it is understood by those financial institution employees whose actions and outputs may have an impact on how consumers are treated. The CoFI Act requires an FCP to include initial and regular ongoing training for the financial institution's employees, including training on:

- the relevant services or associated products that are provided to consumers; and
- the FCP and the processes and procedures that the employee must follow to support the institution's compliance with the fair conduct principle.

Financial institutions will need to determine the frequency, delivery methods and content of initial and regular ongoing training for employees and ensure this is appropriate for the employees' work in providing the relevant services or associated products to consumers.

Financial institutions are required to maintain an effective FCP. The FMA expects financial institutions to have assurance processes to assess the effectiveness of their FCP.

4. It must be approved and have the support of the Board

To be effective, an FCP must have the support of the financial institution's governing body, which would generally be the board of directors. The FMA expects the governing body to have oversight and take accountability for the financial institution's compliance with its licence obligations and the CoFI Act requirements.

The governing body should review the FCP to consider its adequacy and effectiveness and recommend changes where appropriate. The final approval of the FCP should be provided by the governing body.

Prepare the FCP now

Applications for licences open in July this year. While the CoFI regime won't come into force until early 2025, timing is still tight. Financial institutions are already on their CoFI journey because applicants need to have an established FCP before they can apply for a licence.

The FMA doesn't expect the FCP to be fully implemented by the time of applying for the license, they "*do expect the FCP to have been approved by the applicant's board of directors*" before the application is lodged.

And, of course, the FCP will need to be fully operational by the time the regime goes live. That means, amongst other things, any new technology solutions to support the FCP will need to be in place, and relevant staff will need to have been trained as to what the FCP requires of them, by the start date in early 2025.

Cyber risk and cyber insurance:

Themes and predictions

Authored by Andrew Horne

There has been no let-up in the threat posed by cyber criminals to private sector and Government entities. CERT NZ reported at the end of 2022 that the number of reported unauthorised access incidents had risen by just under 30% in the third quarter of that year, having been relatively stable for the previous four reporting quarters. Forbes magazine recently reported a prediction by Cybersecurity Ventures that the global cost of cybercrime will reach USD8 trillion in 2023 and will grow to USD10.5 trillion by 2025.

The scale of the risk to insurers was brought home in November last year, when Australia's largest health insurer, Medibank, reported that it had suffered a large data breach in October that involved personal medical information of around 9.7 million customers, although it was reported that the data did not link customers' names with medical details. This cyber breach caused its share price to fall significantly and resulted in a class action lawsuit on behalf of affected customers, which Medibank has said it will defend.

Insurance companies, along with banks, investment funds and other financial institutions, are particularly attractive targets because of the rich rewards on offer to cyber criminals. Because of this, the financial sector ranks second only to health organisations for damaging data breaches. The head of ANZ Bank's institutional bank, Mark Whelan, said recently that he saw cyber attacks as the single biggest issue or threat facing banking today. At the time, ANZ Bank was receiving 8 to 10 million attacks each month.

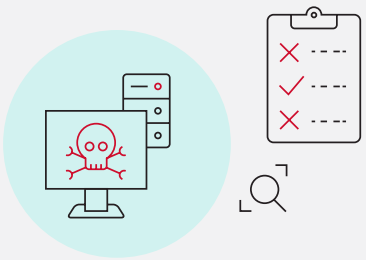
With cyber-crimes increasing in number, sophistication and severity, it is increasingly important for businesses to protect themselves as much as possible. Self-evidently, this involves putting appropriate IT systems and procedures in place to ensure that systems are secured to the greatest extent practicable and, crucially, ensuring that staff are appropriately trained.

Our associate firm in Australia, MinterEllison, recently issued its annual cyber risk report, in which it noted that the practice of testing data breach response plans at least once a year has increased from 34% to 55% of respondents. The increase is welcome, but it is not enough.

Increasingly, adequate protection will also involve taking out appropriate cyber insurance to protect against business losses and liabilities to third parties from cyber events. Cyber insurance, however, poses increasingly complex challenges for insurers, brokers and insureds. Insurers, who value predictability to inform them as to which risks to insure and to set premiums, are aiming at a moving target with cyber crime as they strive to assess risks accurately and set premiums appropriately. At the same time, insurers can afford to be selective, as demand for cyber cover increases while insurer capacity and appetite for cyber risk reduces.

Key risks and strategies to respond

MinterEllisonRuddWatts hosted a cyber risk breakfast at which leading professionals from the insurance (AIG), insurance broking (Aon) and IT security (Datacom) industries offered their thoughts and shared their experiences of the developing risks and the place of cyber insurance. We added our thoughts about the legal risks presented by cyber events and the appropriate legal responses.



The key take-outs from that event included the following:

- New Zealand is a soft target – our small size and geographical isolation lulls us into a false sense of security. This is wrong, as cyber crime may be committed from anywhere, so it does not matter where a victim is located geographically.
- Ransomware claims increased 150% from 2018-2020 (although there are indications that the number is beginning to plateau) and comprised one in every five claims. They are increasingly sophisticated, with bad actors now taking the time to identify the most crucial data to enable them to target their attacks for maximum damage and effect. Losses include ransom costs, event management costs such as IT costs, network interruption losses, regulatory actions and customer claims.
- There are two key ways to address cyber risk – mitigation and insurance.
- Good IT 'hygiene', doing the basics (such as prompt installation of patches) well and quick responses to cyber events are critical. Remote working increases risk.
- Many organisations run legacy systems with inadequate security. Insurers are asking increasingly detailed questions of insureds and will decline to offer cyber cover to insureds with inadequate security. Cyber insurance cover is becoming a mark of quality for organisations as insurers will only cover firms that have good security technology and practices.
- Losses from cyber crimes include the victim's own loss and damage (operations are halted, money may be stolen), liability to customers and third parties (whose data may be released or misused), and regulatory action and fines. Victims should make no admissions, take prompt steps to recover systems, involve insurers at the outset and take appropriate advice.

More recently, it appears that cyber criminals are viewing data breaches as the most attractive and rewarding form of attack upon insurers. Insurers hold sensitive and confidential information about their customers, so they may be tempted to pay large ransoms to prevent stolen customer information from being disclosed, although Medibank reported that it would not pay a ransom. Payment diversion scams, which often begin with data breaches that inform criminals about transactions that may be diverted, will also put insurers at risk, such as where large claim payments are to be made.

Developing themes

We are expecting to see the following developments in cyber-crime in 2023 and beyond:

Threats have been increasing, although the number and severity may be plateauing

Cyber insurance is increasingly challenging to obtain

Insurers' reliability and consistency is increasingly valued

Cyber insurance continues to offer real value

Threats have been increasing, although their number and severity may be plateauing

There has been no let-up in the onslaught of cyber-crime. In June 2022, Forbes magazine reported that a research company had found that there had been an increase of 50% per week in cyber-crime attempts on corporate networks globally in 2021 from 2020. The FBI's Internet Crime Complaint Center issued a public service announcement in May 2022, reporting a 65% recorded increase in identified global losses between July 2019 and December 2021. As outlined previously, CERT NZ is also receiving increasing numbers of reports.

The New Zealand Government's Budget for 2022 reflected an increasing concern about cyber-crime. It provided approximately NZD50 million in additional funding over four years for the GCSB to combat cyberattacks and engage in counter-terrorism activity, aiming to protect information services from the increasing frequency and severity of cyberattacks.

Cyber insurance is increasingly challenging to obtain

Insurers are responding to the rising risks and costs of cyber events with increasingly detailed assessments of insureds' IT systems, while in some cases also reducing cover limits and increasing premiums. One major New Zealand insurer has dealt with the additional complexity required by the assessments by introducing a 'smart' cyber questionnaire in which an insured's answers to the initial questions trigger different or additional questions, depending upon the responses. Other New Zealand insurers have reduced limits significantly or have withdrawn cover altogether. Large firms, such as those with revenue over NZD100 million, are facing particular scrutiny, as they present an increased perceived risk as more attractive targets to criminals.

The complexity of insurers' questionnaires and their importance means that IT departments must be well prepared and resourced to answer them. This should be done well in advance of the cyber insurance renewal date, as the time commitment is significant and answers often need to be drawn from different sources. IT departments may realise as they work through the questions that the answers they would give will not satisfy insurers, so it may be necessary to take remedial steps urgently so that a more satisfactory response can be given.

An additional challenge is that insurers are conducting their own security reports and scans of an insured's systems. Whereas previously, insurers might have accepted insureds' responses uncritically, many now test and challenge them. Insurers will often share reports with the insured, and sometimes insureds and their brokers will need to challenge aspects of an insurer's report that may not tell the full story.

A key lesson for brokers and insureds is that 'wrong' answers to questions asked by insurers may have significant effects upon their willingness to offer or renew cyber cover. It is crucial that insureds provide a full explanation of any responses that might not tell the full story. For instance, insurers expect to see multi-factor authentication as a core requirement for access to an insured's system. This means that any circumstances in which multi-factor authentication may not be used, such as where there are other security systems in effect, will need to be explained.

Brokers and insureds need to prepare for their renewals with a full appreciation of the time and work that is likely to be required to present a compelling proposition to a cyber insurer. Insureds will also need to be prepared to consider reductions in cover or moving to different insurers as capacity and limits change.

Insurers, for their part, will need to continue monitoring claims closely and adapting quickly as cyber criminals change their approaches and the threat landscape develops. Cyber insurers will increasingly need to provide a proactive, advisory service to assist brokers and insureds to understand what their requirements will be and enable insureds to satisfy their expectations, rather than confining their role to a reactive response.

Insurers' reliability and consistency is increasingly valued

The cyber insurance market has been relatively volatile until recently. Some cyber market leaders in New Zealand in 2020 had reduced capacity in 2021, while others offered new capacity to help meet the resulting demand. Brokers reported that many customers were obliged to place cover with new insurers. This further added to the burden faced by insureds' IT departments as they were asked to respond to multiple insurer questionnaires.

We expect that insureds will increasingly value stability and consistency in their cyber insurers and may prioritise those characteristics over price and cover limits.

Cyber insurance continues to offer real value

While cyber insurance is increasingly challenging to obtain, brokers report that it continues to benefit insureds. They report that, perhaps because of the care taken when it is arranged, it features a relatively high claim acceptance rate compared with other types of insurance, so notwithstanding the cost and time investment required, it is worthwhile and provides a real benefit.

Cyber insurance also remains one of the few insurance products that assists insureds to prevent claims. Insurance assessments are often valuable tools to identify security weaknesses and remedy them, as insurers often have up to date knowledge of the latest risks. Cyber insurance discussions can therefore benefit insureds by assisting them to improve their systems and remove vulnerabilities.

There is also the additional benefit that cyber insurance provides a badge of quality, as it demonstrates that an insurer has assessed the insured as a good risk. For professional services firms in particular, whose own customers are increasingly demanding reassurance as to their cyber defences, this is likely to be increasingly important.

"Cyber insurance provides a badge of quality, as it demonstrates that an insurer has assessed the insured as a good risk."

Increasing access to justice and streamlined civil litigation:

Considerations for insurers

Co-authored by Nick Frith, Hannah Jaques and Siobhan Pike

The Rules Committee (Te Komiti mō ngā Tikanga) released its *Improving Access to Civil Justice* report in November 2022. If implemented, the report's recommendations will create widespread changes in litigation procedure in the High Court, District Court, and Disputes Tribunal for most civil cases. In this article, we consider some of the anticipated impacts of the report on insurance disputes in Aotearoa New Zealand.

The Committee's recommendations

The proposed recommendations are wide-sweeping and are likely to have significant impacts on the conduct of insurance-related litigation. Below, we summarise the thrust of the proposed changes in the High Court, District Court and the Disputes Tribunal.

High Court

The recommendations propose significant changes to the High Court Rules. If implemented, proportionality will be included as a guiding principle. Other changes include narrowing the scope of witness evidence and document discovery, requiring the exchange of more limited written evidence at an earlier stage and increased focus of genuinely disputed facts in the proceeding.

District Court

The recommendations aim to reinvigorate the District Court's civil jurisdiction. The proposed appointment of a Principal Civil District Court Judge and part-time deputy judges from the bar aim to strengthen the expertise of the court's civil registry and improve case management.

Disputes Tribunal

The recommendations propose substantially increasing the jurisdiction of the Disputes Tribunal from NZD30,000 to NZD70,000 (or NZD100,000 with the consent of the parties). The aim of this recommendation is to increase the efficiency and proportionality of justice for smaller disputes to improve access for litigants.

Changes to High Court Procedure

Due to the size and complexity of commercial insurance disputes, we consider that the procedural changes with the greatest impact in this practice area will be those made to the High Court Rules. The proposed changes reflect a desire to streamline evidence and discovery processes in the High Court, as it is these costs that are usually most costly for both plaintiffs and defendants.

Initial disclosure and discovery

The rules propose expanding initial disclosure to include adverse documents known to the parties. Parties will not have to search for adverse documents to provide initial disclosure. However, all known adverse documents will be required to be provided from the outset. This proposed change is expected to give parties a better understanding of the merits of the dispute at an earlier stage in the proceeding.

As a result of increased initial disclosure obligations, it is proposed that subsequent discovery will only be ordered at a judicial issues conference where it is considered necessary and proportionate.

Evidence

In connection with increased initial disclosure obligations, it is proposed to serve evidence at a much earlier stage in the proceeding. Importantly, evidence will be provided prior to any subsequent discovery orders. Additionally, briefs of evidence will be replaced by witness statements that are intended to be more limited in scope. Parties will also be limited to providing the evidence of one expert per speciality, with experts required to engage in joint conferral prior to trial.

Impact on insurance disputes

We expect that these proposed reforms, if implemented, will ensure greater access to justice by reducing the cost and increasing the speed of proceedings in complex insurance disputes. This is important because it is commonplace for insurance disputes to persist for many years, often long after the event causing loss occurred. This can unnecessarily leave insureds out of pocket or divert insurer resources.

However, it will be important to ensure that the proposed reforms enable parties to fully make their case and examine the evidence of other parties. Given the complexity of insurance disputes, reducing the scale and complexity of expert briefs may be impractical and undesirable as it may cause important evidence to go unheard. Additionally, streamlined disclosure requirements may result in important evidence remaining undiscovered by parties. As cases, which are typically covered by defence costs cover, often generate significant document volumes, a streamlined discovery process will only be effective if safeguards remain in place to ensure discovery is proportional to the size and complexity of the proceeding. This is especially so in the context of large insurance disputes, where parties often negotiate bespoke arrangements on the basis of commercial relationships dating back many years.

Disputes Tribunal

Proposed changes to the Disputes Tribunal rules are likely to make subrogated recovery claims easier, quicker and cheaper.

- The proposed increase to the Disputes Tribunal's jurisdictional cap to: (a) NZD70,000 as of right; and (b) NZD100,000 by consent will open up most motor claims to the Disputes Tribunal.
- There is no change to the current rules regarding representation in the Disputes Tribunal. So insurers can still be represented by their own personnel.
- Costs will continue to lie where they fall other than in exceptional circumstances. So there is no real costs burden to consider.
- Importantly, referees to be legally qualified. This is a major step in the right direction in terms of reliable outcomes.
- Consideration is be given by the District Court to more effective and straightforward enforcement. So more efficient and effective enforcement may be on the horizon.

> "Arbitration as a dispute resolution process has numerous benefits."

The role of arbitration and mediation

In light of the mentioned reforms, we anticipate that arbitration and mediation will serve a greater role in the resolution of insurance disputes and those covered by defence costs.

Arbitration as a dispute resolution process has numerous benefits. Subject to limited exceptions, arbitrations are private and confidential. They tend to result in quicker resolution than High Court proceedings, and some procedures can be adapted to suit the requirements and needs of the party. Importantly, appointed arbitrators are usually individuals with expertise or a particular knowledge within a specific field. In the insurance arena, the benefit of having an arbitrator specialising in insurance may mitigate any evidential deficits resulting from the truncated procedural requirements of the proposed High Court Rule changes.

Participating in mediations may also provide increased benefits in insurance disputes. For large commercial organisations, mediations are a cost and time-effective way to solve communication, evidentiary, and procedural issues between parties without incurring court expenses. In light of the streamlined discovery and evidentiary requirements proposed by the Rules Committee, mediation may become particularly useful to resolve common issues in insurances disputes (for example, the interpretation of policy wording) with the assistance of a neutral third-party facilitator.

Our view

Overall, we consider that the changes proposed by the Rules Committee are likely to improve access to justice and streamline defences work, by reducing the costs involved in lengthy Court proceedings. This will likely benefit insurers involved in disputes to secure speedier resolutions. Additionally, we commend the Rules Committee for their commitment to facilitating access to justice on a more equitable basis. Consideration will need to be given to the proposed discovery and evidential rules should they come into effect (to ensure that they do not impede justice by preventing consideration of the issues in light of all the evidence). In the meantime, we consider that arbitration and mediation proceedings will become more popular forums for the resolution of complex commercial insurance disputes.

Credible deterrence:

FMA enforcement to increase

Co-authored by Jane Standage, Maria Collett-Bevan and Sarah Jones

The insurance industry should prepare for increased regulator enforcement this year. The Financial Markets Authority (FMA) has indicated it intends to take a harder line on regulatory compliance, particularly where customer outcomes are poor. In this article, we outline the FMA's stated desire to exercise its powers *"broadly"*[1] and learnings from recent enforcement actions in the insurance industry including the continued focus on fair dealing and self-reporting.

The FMA's approach to "*credible deterrence*"

The FMA's statement of intent for 2020–2024 signals its intention to effect *"credible deterrence"*.[2] It has recently clarified that credible deterrence is about *"balance, proportion, precision and timeliness … we're clear it cannot always be hammer time"*.[3] Paul Gregory, the FMA Executive Director of Regulatory Response, has also acknowledged that credible deterrence may involve taking a course of action stronger than anticipated by the market. To support this focus on deterrence, the FMA has applied significant resource and capability to its enforcement function, and we can expect an uptick in enforcement generally.

The FMA has also signalled that there will be some changes in its enforcement approach. The key change is that the FMA says it will be thinking more broadly about what success looks like.[4] The FMA has indicated that it may be more willing to bring an action in order to clarify the law and provide certainty for markets and consumers. However, we expect that, for reputational reasons, the FMA will want to be on the winning side of any litigation more often than not, so this desire for legal clarity alone is unlikely to result in a significant up-tick in enforcement action.

Bill Fairs / Unsplash

1. *Regulatory Response Guidelines issued by the FMA in August 2016.*
2. *Samantha Barrass Keynote speech at Financial Services Council Outlook, 25 January 2023.*
3. *Paul Gregory speech at Financial Services Council Outlook, 25 January 2023.*
4. *Paul Gregory speech at Financial Services Council Outlook, 25 January 2023.*

The FMA has also said that it will take an outcomes-based approach (in its general supervision, but also regarding enforcement). The FMA's Chief Executive, Samantha Barrass, has recently noted that *"an outcomes-focused approach does not start at what the legislation says, or a rule book says, it starts with what is the right outcome for a strong sector that works well for all"*. Therefore, the insurance industry should take note that contraventions involving harm to customers, or of significant relevance to the market, are likely be subject to enforcement action.

The insurance industry can also expect the FMA to continue to use its full enforcement toolkit which includes enforcement in the Courts as well as public warnings and enforceable undertakings.

Recent learnings from the Vero and Cigna Life enforcement actions

Cigna Life

Cigna Life Insurance New Zealand (Cigna) admitted to breaches of the fair dealing provisions in Part 2 of the Financial Markets Conduct Act 2013 (FMCA) in August 2022.

The breach involved Cigna charging for inflation benefits (indexation) to customers holding 52,363 policies between April 2014 and early 2019. Until early 2019, Cigna used a flat rate of indexation (as opposed to a rate set by the Consumer Price Index (CPI)), which was not consistent with what was required under the relevant policies.

The flat rate exceeded the CPI. Cigna communicated these changes to customers on an opt out basis, through annual notification letters.

Cigna Life received an order to pay a pecuniary penalty of NZD3.575 million in January this year.

Vero Insurance

In 2022, the FMA filed proceedings against Vero Insurance New Zealand Limited (Vero) for failing to apply multi-policy discounts, which led to 47,000 customers being overcharged approximately NZD8.7 million in premiums.

The FMA considers that Vero made false and/or misleading statements, contravening the fair dealing provisions in Part 2 of the FMCA, regarding invoices stating that customers were entitled to discounts. Vero failed to apply the discounts due to errors and deficiencies in its systems (which were designed by Vero).

Vero self-reported the issue in December 2019, by which time remediation was underway. However, further affected customers were later discovered by Vero. Vero has reimbursed NZD10.259 million in overcharges to affected customers.

The recent enforcement actions taken against Cigna and Vero indicate the FMA's continued focus on compliance with the fair dealing provisions. However, the cause of the harm in the two cases differs. The Cigna case involved fair-dealing breaches stemming from decisions made by senior management, rather than systems and controls issues (as was the case in Vero).

Self-reporting

Both cases involved self-reporting of issues to the FMA through the conduct and culture review process. The FMA expects all regulated entities to self-report issues. Not doing so is an aggravating factor when setting pecuniary penalties.

The industry should be mindful that self-reporting does not cure the underlying breach. The FMA's then Head of Enforcement Karen Chang discussed the issue of self-reporting in a speech in November 2021, stating that the FMA expects those it supervises to self-report issues promptly to the FMA. However, self-reporting cannot provide immunity from litigation, especially if the issues are significant, systemic or have led to customer harm. That said, self-reporting entities can expect to receive some credit for genuine self-reporting in relation to penalties for contravention. In the Cigna case, the FMA submitted that a lower discount of 30% (as opposed to the 35% discount that was applied) was warranted given Cigna's level of cooperation was only that *"expected of a responsible company"*. However, the Court decided that Cigna's prompt self-reporting, although it was expected of a responsible organisation, was worthy of recognition to appropriately incentivise responsible behaviour. For this reason, Cigna received in total a 35% discount – a discount of 5% was applied for Cigna's self-reporting (a further 25% applied for cooperation and acceptance of responsibility, and 5% for this being Cigna's first contravention of the FMCA).

In short, getting self-reporting right is critical. The FMA distinguishes promptly answering FMA requests for information from self-reporting. Self-reporting needs to be unprompted – where the FMA specifically requests information, this is not self-reporting. Paul Gregory, in his speech to the FSC conference in January 2023, described self-reporting in some cases as *"the tip of a somewhat grimier iceberg"*. Self-reporting of issues can reveal significant carelessness and misconduct which goes on undetected, or unchecked for a long time before reporting. In this case, it will not demonstrate a regulated entity's responsible conduct – but rather, further conduct and culture issues in the organisation.

Remediation

While remediation is not a 'cure all' of the contravention, getting the remediation right is critical. Karen Chang, in her November 2021 speech, highlighted that remediation again demonstrates a regulated entity's conduct: *"Putting customers right is the bare minimum step we expect from entities – of course it wouldn't be acceptable to benefit from misconduct, however inadvertent. We also take notice of how the remediation has unfolded – whether it was timely, well organised and communicated or whether there were delays and mistakes. Where an entity seriously struggles with the exercise, it doesn't tend to reflect well on the robustness of their systems and governance."*

Both Cigna and Vero remediated the harm to customers. In the Cigna judgment, the Court found that Cigna's comprehensive approach to remediation, including keeping the FMA regularly informed about the remediation, was a mitigating factor. This factor contributed to a 25% discount on the pecuniary penalty, which reflected Cigna's full cooperation with the investigation, remediation and acceptance of responsibility. The judgment also stated that *"a 30 percent discount is at the bottom end of the available range for these factors and a little more would not be out of range"*. The penalty in Vero's case has not yet been decided, however, the FMA expressed concern at whether the investigation and remediation of the problem was sufficient, which led to further remediation of unidentified errors.

Navigating the new regulatory environment

Regulatory scrutiny on the insurance industry is increasing, and regulated entities should prepare for a more combative FMA going forward.

The recent enforcement cases demonstrate that responding to contraventions is critical. Insurers need to ensure that they have processes in place to identify and elevate issues through the appropriate governance channels. Further, in the event of a breach, insurers need to establish a coordinated response regarding investigation and self-reporting and remediation, that cements the insurer as a responsible entity, with strong systems and governance focused on conduct and consumer outcomes.

Further, with the introduction of the Financial Markets (Conduct of Institutions) Act 2022, the FMA will hold an insurer's licence to operate. Insurers should consider compliance as a critical risk, and adjust their risk tolerance accordingly.

Case study

Court of Appeal rules on exclusion for losses caused by *"pollution or contamination"*

Co-authored by Zoë Bowden, Sam Nicholson and Isabella Denholm

Brian Leighton (Garages) Ltd (BLG) operated a workshop and 24-hour petrol station in East Yorkshire.

In June 2014, a sharp object pierced a section of pipe which connected an underground fuel tank to six of BLG's forecourt fuel pumps. The resulting fuel leak caused such extensive damage to BLG's premises that it was at risk of catching fire or exploding and the business had to be closed.

Allianz insured BLG under a Motor Trade policy. Allianz declined cover on the basis that the policy excluded damage *"caused by pollution or contamination"*. Allianz sought to have the question of cover determined via summary judgment. The High Court agreed that the damage was excluded. BLG appealed, arguing that, while the effect of the leak was pollution or contamination, the cause of the damage was the sharp object which punctured the pipe.

The policy

The policy wording covered Damage to Property Insured by any cause not excluded. Damage was defined as *"accidental loss, destruction or damage to Property Insured"*. It was common ground that Property Insured was damaged by the leak.

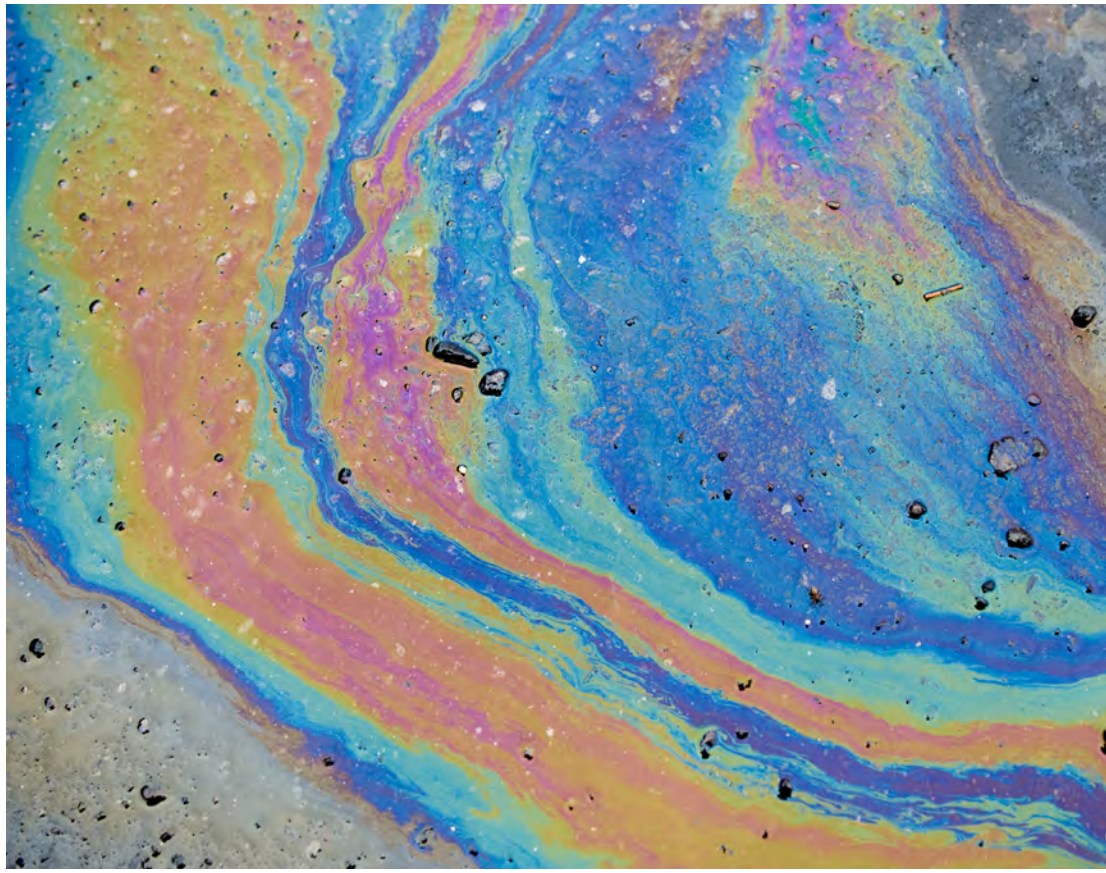
The policy excluded:

"Damage caused by pollution or contamination, but we will pay for Damage to the Property Insured not otherwise excluded, caused by:

a) *pollution or contamination which itself results from a Specified Event*

b) *any Specified Event which itself results from pollution or contamination."*

The definition of Specified Event included fire, explosion, flood and the escape of water from a tank or pipe.



"The key issue was whether the words "caused by", as used in the exclusion, should be taken to refer to a proximate cause test."

The Court of Appeal's decision

The key issue was whether the words *"caused by"*, as used in the exclusion, should be taken to refer to a proximate cause test. By a 2-1 majority, the Court found that they did. The exclusion only operated where the pollution or contamination was the proximate cause of the damage.

BCL submitted that the exclusion ought to be narrowly interpreted, such that it would not bite where something other than the pollution or contamination was the proximate cause of the damage. Allianz argued that *"caused by"* meant something looser than proximate cause so that any claim where pollution or contamination formed part of the causative chain would be excluded, regardless of the immediacy or remoteness of the cause. Allianz contended that a wider interpretation was consistent with the write back in the exclusion's sub-clauses a. and b., which it said operated to provide cover for fuel leaks arising from Specified Events, but not otherwise.

A majority of the Court of Appeal agreed with BCL, finding that the exclusion's application turned on whether or not pollution or contamination was the proximate cause of the damage. The Court noted that the usual requirement to establish proximate cause is based on the parties' presumed intentions, which could be displaced if the policy provided otherwise. This would typically be achieved by using words such as *"directly or indirectly"* in policy wordings.

The Court found that this was not the case here – the parties' presumed common intention was that the exclusion applied to pollution or contamination where it was the proximate cause of the damage. The exclusion was not triggered where the pollution or contamination was merely the result of some other insured cause.

The dissent

Males LJ dissented from the majority and found that the wording of the exclusion, when read as a whole, displaced the presumption that the words *"caused by"* referred to damage proximately caused by pollution or contamination. In reaching this view, the Hon. Lord Justice focussed on the effect of the write back of cover in subclauses a. and b., as they formed part of the exclusion as a whole. He did not agree that the write back clauses were themselves concerned with proximate cause – rather they were there to ensure that any Specified Event which is caused by or causes pollution or contamination would be covered, regardless of whether the pollution or contamination or the Specified Event was the proximate cause of the damage.

Other observations

Across the three judgments, the Court made some other relevant findings and observations, including:

- **The parties' intentions in entering the contract** – in determining the question of indemnity, the Court had regard to the fact that a fuel leak from pipes would be *"amongst the most obvious risks"* for a business of BLG's size and kind to require and seek cover for.
- **The meaning of proximate cause** – the Court confirmed that the proximate cause of a loss is not necessarily the most recent or least remote cause, but rather that which is proximate to efficiency, being the dominant, effective, or efficient cause. The Court also affirmed the long-established principle applying to concurrent proximate causes that was established in *Wayne Tank*, whereby if one proximate cause is covered and the other is excluded, the exclusion prevails.

- **Brokers' understanding of insurance terms** – the Court held that brokers are to be taken to be familiar with the basic insurance principle of proximate cause, and the language used in policies which reflects or modifies it. The fact that many policies contained 'terms of art', shaped by consistent judicial authority, did not deter the Court from finding that the words *"caused by"* had *"historically and uniformly been interpreted in this context as importing the concept of proximate cause"*, and that this was the meaning that ought to be given to the words in this case.
- **Reconciling exclusions and write backs of cover** – Popplewell LJ held that the presumption that *"caused by"* denotes proximate cause would survive in this case, unless the wording of the write back could not be reconciled with it. However, Males LJ (dissenting) and Nugee LJ (majority) disagreed and found that the relevant question was whether the exclusion, when read as a whole *"would demonstrate to the reasonable reader to whom it is addressed an intention to displace the general rule. That intention may be demonstrated, even if it is possible to give some meaning to the write-back provisions which does not render them redundant"*. Males LJ considered that, as a matter of ordinary language, and despite a 'pedantic lawyer' reaching the view that the pollution or contamination was not the proximate cause of damage, the relevant damage was caused by pollution or contamination.
- **Using wording from other, optional, sections of the policy as an interpretative aid** – two of the three judges expressly warned against reading into the use of different wording, such as *"directly or indirectly caused by"*, elsewhere in the policy wording. While it is orthodox to have regard to contrasting wording to determine the meaning of that wording within the same contract, no reliance should be placed on wording used in other sections of the policy that are optional, and which may not have been reviewed by the relevant insured.
- **The application of the contra proferentem rule** – there was no room for an argument that the exclusion ought to be construed narrowly against the insurer. This was because the wording of the insuring clause as *"any cause not excluded"* meant that the exclusions defined part of the scope of cover and ought not to be interpreted as an exemption from liability for cover which would otherwise exist.

Our view

This case provides helpful guidance on the doctrine of proximate cause. Like the UK, the use of *"caused by"* in insurance policies governed by New Zealand law is generally held to require the identification of a single proximate cause of the relevant loss. The principle of proximate cause is also codified in marine insurance by section 55 of the Marine Insurance Act 1908 which provides *"an insurer is liable for any loss proximately caused by a peril insured against."*

However, the doctrine of proximate cause may be displaced or varied in New Zealand insurance contracts using clear wording to the contrary. It is critical that both insurers and brokers pay careful regard to the use of the precise wording of exclusions in determining the applicable standard of causation. As was the case here, imposing a proximate cause test could have the effect of introducing uncertainty and complexity in relation to exclusions.

Brokers should also be mindful of the risk of a court finding, as the majority did in this case, that they ought to be aware of the precise meaning of terms commonly used in insurance contracts that have had judicial consideration. The Court found that this would extend to language that both reflects, and modifies, the basic insurance principle of proximate causation.

Case study

Case study: High Court of Australia provides guidance on insurer election and duty of good faith

Authored by Hannah Jaques

Delor Vue Apartments in North Queensland suffered substantial damage during Tropical Cyclone Debbie in 2017. When its public liability and property policy was placed, it knew its apartment buildings had serious non-structural defects, but had failed to disclose their existence to its insurer, Allianz.

The facts

In March 2017, Tropical Cyclone Debbie made landfall in Queensland, Australia and caused approximately AUD2.5 billion in damage across areas in the south east of the state.

The cyclone caused substantial damage to the roof of the apartments at Delor Vue as well as to several individual units. Delor Vue notified a claim under its public liability and material damage policy. As part of that claim, Allianz, acting through its underwriting agent, SCI, became aware of Delor Vue's failure to disclose pre-existing non-structural defects. However, Allianz initially responded positively. On 9 May 2017, it sent the following email to Delor Vue:

"Despite the non-disclosure issue which is present, [SCI] is pleased to confirm that we will honour the claim and provide indemnity to [Delor Vue] in line with all other relevant policy terms, conditions and exclusions."

The email described the decision as one to *"grant indemnity"* but stated that there were two categories of damage: defective materials and construction of the roof and resultant damage. SCI said it would cover the second category but not the first. The High Court of Australia described the language used by SCI as *"imprecise"* and *"unclear"* and noted that the parties ultimately disagreed on the scope of application of the second category. It was uncertain whether Allianz contemplated that it would be necessary for Delor Vue and Allianz to reach agreement as to the roof repairs for which each party would pay before they were undertaken.

Following engagement of, and reports from, engineers and builders, Allianz discovered that there were more defects with the roof construction, including defects in the roof trusses and the manner in which they had been tied down. The result was that they were inadequate and could not be salvaged (although many remained undamaged by the cyclone).

On 3 May 2018, Delor Vue wrote to Allianz recording complaints, including an alleged failure by Allianz to state its position on indemnity *"with any clarity"* and allegations of breach of duty of good faith, among others.

That lead to a response from Allianz on 28 May 2018, in which Allianz set out its 2017 communication in full and proposed a *"settlement"* that required Delor Vue to pay for rectification of defects excluded under the policy, before Allianz would pay for the costs of repair or replacement arising from the cyclone damage.

Allianz's offer expired unaccepted. It notified Delor Vue that its liability had been reduced to nil in reliance on s 28(3) of the Insurance Contracts Act 1984 (*Cth*).

Australian statutory context

The statutory response to non-disclosure and misrepresentation in Australia is clearer yet more nuanced than it is in New Zealand.

In Australia, s 28(3) of the Insurance Contracts Act 1984 (Cth) provides insurers with a right to reduce any claim made under the policy where there has been material but non-fraudulent non-disclosure or misrepresentation:

If the insurer is not entitled to avoid the contract, or being entitled to avoid the contract (whether under subsection (2) or otherwise) has not done so, the liability of the insurer in respect of a claim is reduced to the amount that would place the insurer in a position in which the insurer would have been if the relevant failure had not occurred.

We are likely to see a similar approach if the Insurance Contracts Bill comes into force.

Lower Court decisions

The Federal Court found that Allianz was entitled to rely on the statutory remedies for non-disclosure, subject to any election, waiver or estoppel. It ultimately found in favour of Delor Vue because it held that there had been sufficient waiver and Allianz was estopped from resiling, and in breach of its duty if it was to resile, from its representation.

On appeal to the Full Court, Delor Vue was successful on all four grounds.

High Court decision

The High Court of Australia, by majority, allowed Allianz's appeal for the following reasons:

No waiver

Although the 9 May 2017 email contained a waiver of the s 28(3) defence, that waiver was conditional upon the acceptance of terms resolving ambiguity and was therefore revoked on 28 May 2018 when no resolution was reached. The majority held that a unilateral waiver could be revoked at any time on reasonable notice unless there were exceptional circumstances. According to the majority, to find otherwise would undermine other contractual rules including requiring variations of contracts to be for consideration.

No election

There was no election by affirmation. The majority confirmed that the modern approach applied where a party to a contract has two sets of rights that could not exist simultaneously: the choice between them should be irrevocable. However, in this case, Allianz's decision to exercise a remedy under s 28(3) of the Act did not involve alternative and inconsistent sets of rights because s 28(3) operates only as a defence to reduce the amount of the insurer's liability: "*[w]ith or without waiver, the insurance contract remains on foot and reliance on the defence under s 28(3) is not immediately inconsistent with any of the contractual rights*." It distinguished this position from the decision to avoid a policy under s 28(2) of the Act. A promise not to enforce a legal right can be revoked at any time with reasonable notice to the other party, absent a variation to a contract by way of entry into a deed or a fresh agreement for consideration or the expiry of a limitation period. Further, Allianz's early email amounted to taking steps that were inconsistent with an intention to rely on the s 28(3) defence, but it did not constitute full satisfaction of that alternative right i.e. payment of the indemnity.

No estoppel

Allianz was not estopped from resiling from its position in May 2017 because Delor Vue had not established that it had suffered any detriment (by way of adverse consequences, a source of detriment or even that it had lost an opportunity that was of real or substantial value) in reliance on Allianz' representation. This approach aligns with the New Zealand Court of Appeal's decision in *Doig v Tower.* Delor Vue alleged it was prejudiced because it lost the opportunity to obtain more in an early mediation than was offered by Allianz in May 2018 or that it lost the opportunity to carry out the repair work itself soon after the loss, rather than having a damaged building for over a year. Neither was made out on the evidence.

No breach of duty of utmost good faith

There is no free-standing obligation upon an insurer, independent of its contractual obligations, to act in a manner which is decent and fair so there was no basis to find that Allianz breached its duty of utmost good faith. The majority found that such a stand-alone duty would be inconsistent with the operation of existing legal doctrines and with the Act itself and would have "*radical consequences*" for an insured. The majority found that:

There is no free-standing general obligation upon an insurer, independent of its contractual rights, powers, and obligations, to act in a manner which is decent and fair. The obligation to act decently and with fairness is a condition on how existing rights, powers and duties are to be exercised or performed in the commercial world.

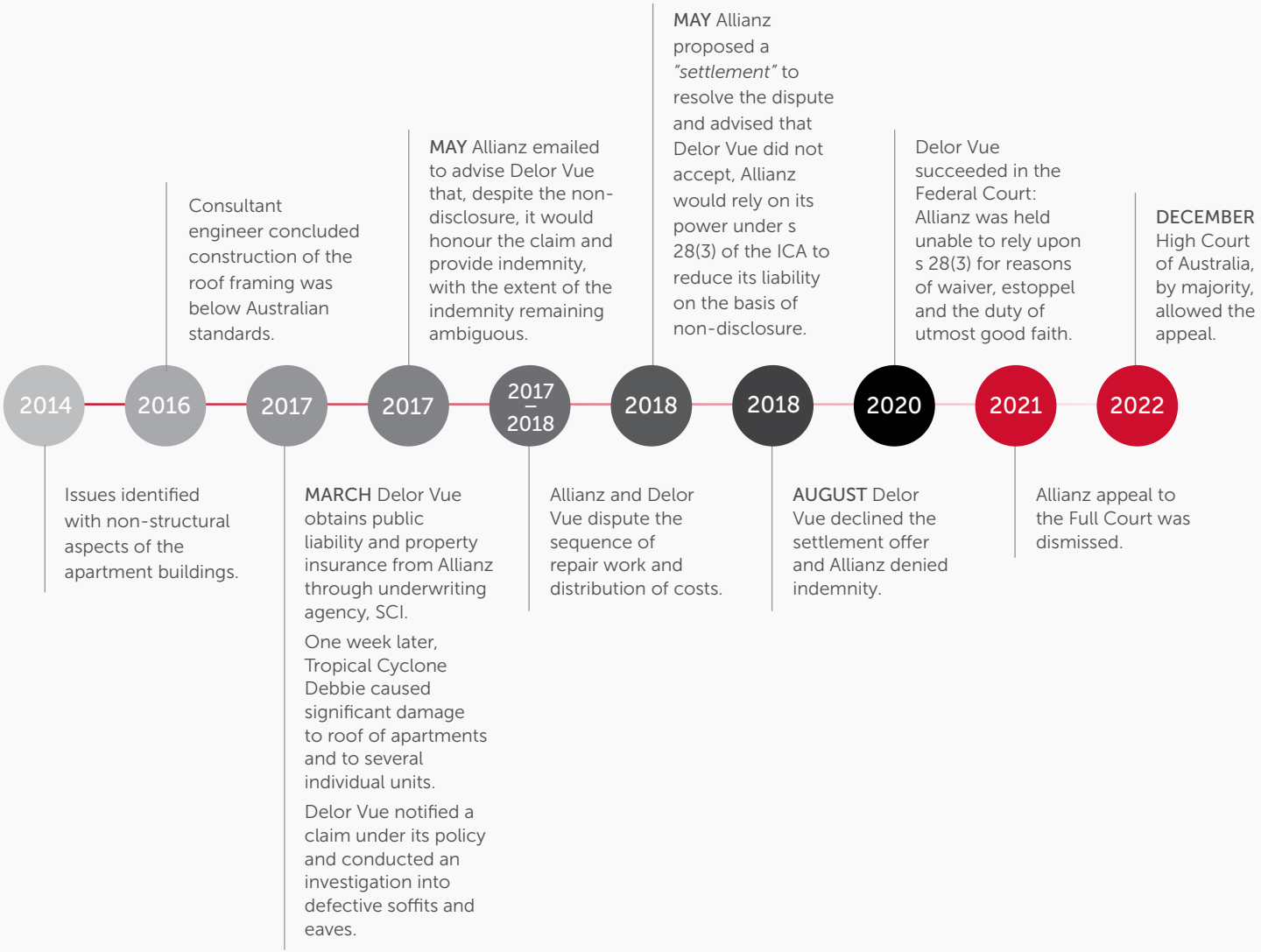
Although the duty is codified in s 13 of the Act, the majority noted that it is an *"instantiation of the centuries-old common law "duty of utmost good faith"".*

New Zealand position and takeaways for insurers

The High Court of Australia's finding that there was no extended or novel duty of good faith on Allianz not to resile, without a reasonable basis, from representations to an insured about a claim under its policy is relevant in New Zealand. The Court's treatment of general contractual principles such as waiver, election and estoppel serve as a good reminder of how New Zealand courts would likely approach the issue. The FMA's expectations might well differ where retail customers are involved.

The case also provides an insight into how the New Zealand statutory regime may well operate if the Insurance Contracts Bill is brought into law.

Timeline



Speak to our experts

Andrew Horne
Partner
P +64 9 353 9903
M +64 21 245 1545
andrew.horne@minterellison.co.nz

Nick Frith
Partner
P +64 9 353 9718
M +64 21 920 292
nick.frith@minterellison.co.nz

Jane Standage
Partner
P +64 9 353 9754
M +64 21 411 728
jane.standage@minterellison.co.nz

Lloyd Kavanagh
Partner
P +64 9 353 9976
M +64 21 786 172
lloyd.kavanagh@minterellison.co.nz

Jeremy Muir
Partner
P +64 9 353 9819
M +64 21 625 319
jeremy.muir@minterellison.co.nz

Olivia de Pont
Senior Associate
P +64 9 353 9738
M +64 27 202 1400
olivia.depont@minterellison.co.nz

Hannah Jaques
Senior Associate
P +64 9 353 9956
M +64 21 177 6340
hannah.jaques@minterellison.co.nz

Zoë Bowden
Senior Associate
P +64 9 353 9987
M +64 27 305 9346
zoe.bowden@minterellison.co.nz

Thomas Leggat
Senior Solicitor
P +64 9 353 9721
thomas.leggat@minterellison.co.nz

Sarah Jones
Solicitor
P +64 9 353 9837
sarah.jones@minterellison.co.nz

Siobhan Pike
Solicitor
P +64 9 353 9859
siobhan.pike@minterellison.co.nz

minterellison.co.nz

MinterEllisonRuddWatts.