IN THE COURT OF APPEAL OF NEW ZEALAND

I TE KŌTI PĪRA O AOTEAROA

CA97/2019
[2019] NZCA 444

	BETWEEN	LOCAL GOVERNMENT MUTUAL FUNDS TRUSTEE LIMITED Appellant
	AND	NAPIER CITY COUNCIL Respondent

Hearing:	3 September 2019
Court:	Kós P, Duffy and Woolford JJ
Counsel:	M G Ring QC and C J Hlavac for Appellant D H McLellan QC and N J Foster for Respondent
Judgment:	3 September 2019 at 2.50 pm
Reasons:	20 September 2019

JUDGMENT OF THE COURT

A The application by the appellant to adduce further evidence is granted.

B The Court file is not to be searched or accessed without leave of a Judge.

C The appeal is dismissed.

D The respondent is entitled to costs on a complex appeal on a band B basis together with usual disbursements.

REASONS OF THE COURT

(Given by Kós P)

[1] The respondent Council has sought a declaration of indemnity against its insurer, the appellant (known as Riskpool). Riskpool is a mutual trustee company established by the New Zealand Local Government Insurance Corporation Ltd, a local authority trading enterprise under the Local Government Act 1974. Riskpool is a mutual scheme, spreading certain insured risks across members.

[2] The declaration was sought because the Council faced a claim by owners of an apartment complex. The alleged defects concerned water ingress, fire protection and a defective wall structure. Riskpool says this claim is wholly excluded by its policy.

[3] The exclusion is contained in cl 13(a). It says that the policy does not cover "liability for Claims alleging or arising directly or indirectly out of, or in respect of … the failure of any building or structure to meet or conform to the requirements of the New Zealand Building Code … in relation to leaks, water penetration, weatherproofing, moisture, or any water exit or control system".

[4] What happens when a claim against the Council raises *both* water ingress and other building defect issues? Does exclusion cl 13(a) exclude the whole of that bundled claim or just that part of the claim asserting liability for damage caused by water ingress?

[5] Asserting the former position, Riskpool applied to strike out the Council's claim. Hinton J declined the application.[1] Riskpool appealed. On 3 September 2019 we dismissed the appeal.[2] These are our reasons for doing so.

A claim against the Council

[6] In 2013 the body corporate and individual freehold and leasehold interest holders in the Waterfront Apartment complex in Humber Street, Napier issued proceedings against the Council and a number of other defendants.[3] The latter

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1 *Napier City Council v Local Government Mutual Funds Trustee Ltd* [2018] NZHC 2269 [HC judgment].
2 *Local Government Mutual Funds Trustee Ltd v Napier City Council* [2019] NZCA 411.
3 Herein, the Waterfront proceedings.

included the developer, principal contractor, architect and various subcontractors involved in the development of the complex.

[7] The Waterfront plaintiffs' claim against the Council was cast in relatively simple terms: that the Council owed each of the plaintiffs a duty to exercise reasonable skill and care in performing certain functions under the Building Act 2004 — issuing building consents, inspecting the building work, and issuing code compliance certificates. The claim then alleged that, in breach of those duties, the Council: (1) issued consents where there were not reasonable grounds to be satisfied that the proposed work would comply with the building code; (2) failed to ensure a sufficient inspection regime was undertaken; and (3) issued code compliance certificates when it did not have reasonable grounds to be satisfied that the building work complied with the building code. It was claimed that these breaches caused or contributed to a number of scheduled defects. These are set out in a schedule to the statement of claim. The defects alleged number 22 in all. Defects 1 to 14 concern water ingress. Defects 15 to 21 concern fire protection. Defect 22 concerns an alleged structural defect in a wall. In consequence the Waterfront plaintiffs claimed costs for remediation, consequential losses, and an additional sum by way of general damages.

[8] In February 2019 the Waterfront proceedings were settled by agreement. The Council seeks indemnity for its contribution and costs from Riskpool.

Further evidence

[9] An application was made by Riskpool for the settlement agreement to be placed before this Court. Ultimately there was no objection to that course of action, and we will receive the evidence.

[10] The parties to the appeal are agreed that the content of the settlement agreement should remain confidential. The precise details of the settlement terms are immaterial to resolving the present appeal. We therefore make an order that the Court file of the proceeding is not to be searched without leave of a Judge. Counsel are to be given an opportunity to be heard in the event of such application.

A policy of insurance

[11] As noted earlier, the Council is a member of the Riskpool scheme. The insuring clause provides:

> Now The Fund hereby agrees ...
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> To indemnify the Member, up to but not exceeding the amount specified in the Schedule, against Claims first made against the Member and reported to the Fund during the period specified in the Schedule for breach of Professional Duty arising out of any negligent act, error or omission wherever or whenever the same was or may have been committed or alleged to have been committed on the part of the Member or on behalf of the Member including:
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> a) all costs and expenses incurred with the written consent of the Fund in the defence or settlement of any such Claim;
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> …

[12] The policy of course contains exclusions:

> Exclusions
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> This Section of the Protection Wording does not cover liability for:
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> 1) the first amount of any Claim shown as the Excess in the Schedule and for the avoidance of doubt, the "WHRS/WHT" Excess applies to any Claim directly or indirectly arising out of, resulting from, or in connection with Claims registered pursuant to the Weathertight Homes Resolution Service Act 2002 or the Weathertight Homes Resolution Services Act 2006, or any Act in substitution thereof, and applies to all Claims in connection with registrations lodged with the Weathertight Homes Resolution Service or the Weathertight Homes Tribunal pursuant to that legislation;
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> 2) any legal liability of whatsoever nature directly or indirectly occasioned by, happening through or in consequence of war, invasion, act of foreign enemy, hostilities …
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> 3) any legal liability of whatsoever nature directly or indirectly caused by or contributed to by or arising from ionising radiation …
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> 4) negligent acts, errors or omissions occurring within the United States of America or the Dominion of Canada …
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> 5) Claims made or actions instituted outside the Dominion of New Zealand or the Commonwealth of Australia;
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> 6) …
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> 7) any Claim:

a) for breach of contract; or

b) arising out of the Member's involvement in a tender or a tender process.

8) Claims caused by or arising from:

a) the approval of land for subdivision; or

b) the issue of a building permit or a building consent as the case may be;

…

9) …

10) any amount(s) awarded by any Court of law against the Member as exemplary and/or punitive damages or fines and/or penalties imposed by a Court and/or Tribunal;

11) …

12) This Section of the Protection Wording does not cover liability for any legal liability of whatsoever nature directly or indirectly, caused by, or contributed to, or arising from or in connection with asbestos or asbestos containing material.

13) This Section of the Protection Wording does not cover liability for Claims alleging or arising directly or indirectly out of, or in respect of:

a) the failure of any building or structure to meet or conform to the requirements of the New Zealand Building Code contained in the First Schedule to the Building Regulations 1992 or any applicable New Zealand Standard (or amended or substituted regulation or standard) in relation to leaks, water penetration, weatherproofing, moisture, or any water exit or control system; or

…

[13] "Claim" is defined to mean:

> … the demand for compensation made by a third party against the Member including the costs and expenses incurred in the defence of any such Claim but shall not include the Member's costs and expenses.

A claim against Riskpool

[14] In June 2017 the Council issued proceedings against Riskpool. The claim recorded that the Council had given notice of the Waterfront proceedings to Riskpool on 16 October 2014. It claims that the liabilities which the Council has or may have in respect of that proceeding fall within the scope of the cover in the protection wording. In particular, under the insuring clause which we have set out

at [11] above. It then records that Riskpool had denied liability to the Council, in reliance on exclusion cl 13(a). The Council claim goes on:

> If [the Council] is liable to the Waterfront Plaintiffs then its liabilities will or may include liabilities in respect of defects which arise from causes which are not excluded by Exclusion 13 (Non-Weathertightness defects).

[15] The Council then seeks a declaration of indemnity as follows:

> A declaration that the defendant is obliged to indemnify the plaintiff for any and all liabilities that it has or may have to the Waterfront Plaintiffs that arise from Non-Weathertightness Defects together with its own costs and expenses incurred in the Waterfront Proceedings.

[16] Riskpool's defence pleads that the claim against the Council in the Waterfront proceedings is a "claim … alleging or arising directly or indirectly out of, or in respect of" the failure of the Waterfront Apartments to meet the building code in relation to water ingress. Accordingly, the entire claim is excluded, Riskpool says, by exclusion cl 13(a).

A strike out application

[17] On 28 July 2017 Riskpool applied to strike out the Council's claim and dismiss the proceedings. It says the claim in the Waterfront proceedings falls entirely into the exclusion in cl 13(a). Riskpool therefore says the Council's statement of claim discloses no reasonably arguable cause of action.

Judgment appealed

[18] The Judge dismissed the application for strike out.[4]

[19] She held that exclusion cl 13(a) envisaged a number of claims arising out of the failure of a building. The Judge read exclusion cl 13(a) as "referring to claims in relation to different defects".[5] She continued:[6]

> It logically follows that the Protection Wording does cover liability for claims arising out of the failure of any building *not* in relation to [weathertightness defects], or, more precisely, that such liability is not excluded. At the least, on

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4 HC judgment, above n 1, at [36].
5 At [17].
6 At [17].

> the face of Exclusion 13, I cannot see that it is inconsistent with a proposition that there could be a number of claims arising out of the failure of any one building, some in relation to weathertightness defects, and others not in relation to weathertightness defects.

[20] The Judge did not consider that the use of the word "Claim" precluded there being a number of claims constituting a number of demands for compensation by a third party against a member. She declined to take a restrictive approach to the meaning of the word, noting that "Claim" was used in the contract in different ways and not with precision.[7] The Judge concluded:[8]

> … in my view, the intention of the parties must have been to exclude liability on the part of [Riskpool] in respect of weathertightness defects, and not to exclude liability in respect of other defects, whether these are pleaded in the one statement of claim or not.

[21] The Judge observed that Riskpool's interpretation was "not consistent with commercial reality".[9] She considered that if the protection wording were read in the way Riskpool contended for, there would be "little indemnity left to an insured". She noted:[10]

> The contract would deny them the entire benefit of an indemnity if the "Claim" made against them included even the most minor weathertightness defect, or worse, on Mr Ring's argument, even if that defect were wrongly alleged.

[22] Finally, the Judge noted that had that been the intention of the parties, she considered they would have chosen to express it in more unequivocal language, and that if the limits and effect of the clause were unclear, it should be interpreted against the party relying on it.[11]

Submissions

[23] For Riskpool, Mr Ring QC submitted that the error in the Judge's analysis is her conclusion that there were two "Claims" against the Council, one in respect of weathertightness and one in respect of non-weathertightness defects. Mr Ring

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7 At [18]–[20].
8 At [28].
9 At [29].
10 At [29].
11 At [30]–[31].

submitted that one has to start by asking what a "Claim" is for the purposes of both the insuring clause and the exclusion clause. A "Claim" is simply "the demand for compensation" — the claimant's formal assertion to the respondent that the respondent is liable to the claimant to pay compensation. At an abstract level, the claim here was the statement of claim. It superseded any prior letter before action. But that claim stands above its constituent causes of action, which themselves stand above constituent elements and then particulars of pleading. Here the "Claim" contemplated by the insuring clause (and exclusion clause) was the demand for compensation represented ultimately by the whole statement of claim. The Waterfront proceeding claim against the Council was simply expressed: breach of general duties was said to have caused defects, and the defects to have caused loss. The defects themselves and the loss caused were cast at the level of particulars of pleading further down the chain. As Mr Ring submitted:

> Once it is accepted that the "Claim" is even indirectly causally connected to weathertightness defects to a material extent, the whole (indivisible) "Claim" is excluded by exclusion 13(a).

[24] This is not a case, Mr Ring submitted, where the Waterfront plaintiffs had (or could ever have had) two "Claims" against the Council — one for weathertightness defects and the other for non-weathertightness defects. Instead, proper pleading would require a single statement. The result is one, albeit mixed, "Claim". Notwithstanding that the entirety of the claim was not based on the weathertightness, there could be no doubt that the claim filed was "alleging", was "arising directly or indirectly out of" or was "in respect of" weathertightness defects. The consequence was the entirety of the claim was therefore excluded.

[25] Mr Ring relied in particular on the decision of the Privy Council in *Haydon v Lo & Lo*, and of the English Court of Appeal in *Thorman v New Hampshire Insurance Co Ltd*.[12] In the former case a solicitor's clerk had committed 43 thefts from an estate. The solicitors were insured under a policy against "claims", that expression being undefined in the policy. The Privy Council held that, for the purposes of the policy excess, although there were 43 causes of action, there was only one "claim" under

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[12] *Haydon v Lo & Lo* [1997] 1 WLR 198 (PC); and *Thorman v New Hampshire Insurance Co (UK) Ltd* [1988] 1 Lloyd's Rep 7 (CA).

the policy because "[t]he reality is that there was only one demand, namely, the demand made by the … estate on [the solicitors]."[13] In *Thorman*, an issue arose as to which of two consecutive liability insurers were liable for professional negligence by an architect which resulted in structural failures in a number of houses. That depended on what "claim" meant in the insuring clause. Sir John Donaldson MR held that "[a] single complaint that they suffered from a wide range of unrelated defects and a demand for compensation would, I think, be regarded as a single claim."[14] Stocker LJ took the view that unless the separate breaches of duty could be brought as separate actions, they would constitute one claim.[15]

[26] For the Council, Mr McLellan QC submitted that the interpretation advanced by Riskpool confounds a fundamental purpose of liability indemnity insurance, which is to provide cover for liabilities that are within the scope of cover and are not excluded. And he said it confounds the reasons for including exclusion clauses in policies: to exclude certain perils because that is a peril one does not wish to indemnify against. Here the intended exclusion was of the risk of leaky building liability, a risk too great for Riskpool to cover. Mr McLellan continued:

> But [Riskpool] did not wish to exclude from the cover other construction defects that had no weathertightness cause, and it therefore agreed that it would indemnify in respect of those liabilities. If it had intended to exclude non-weathertightness liabilities, then it would have been expected to provide so explicitly. It did not.

[27] Mr McLellan submitted that Riskpool's interpretation would effectively exclude any cover for responsibilities for building defects. The policy wording was written in 2014. Most contemporaneous claims against councils based on building regulatory failure would then have included weathertightness defects. If a plaintiff sued the Council for loss caused by a wide range of non-excluded structural defects, costing say $5 million to remedy, and included in the particulars of loss a single defective window flashing letting water in, costing say $1,000 to remedy, on Riskpool's argument the entire $5,001,000 of loss would be excluded. Similarly, if the Council was sued for a claim based solely on non-excluded loss (no weathertightness defects alleged), Riskpool would of course be obliged to confirm

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13 *Haydon v Lo & Lo*, above n 12, at 205.
14 *Thorman v New Hampshire Insurance Co (UK) Ltd*, above n 12, at 11.
15 At 15–16.

indemnity. But if the plaintiffs later amended their statement of claim to include one little weathertightness defect, on Riskpool's argument the indemnity in relation to the entire claim (as amended) would be denied.

[28] Supporting the Judge's analysis, Mr McLellan submitted that "Claim" should not be directed at the form of demand, but instead at the substance of the assertion of a right to remedy for loss. It was directed at the object being claimed, so that one demand could have multiple claims within it. That argument was reinforced here because exclusion cl 13(a) is for "*liability* for Claims". Elsewhere wholesale exclusions are made for Claims simpliciter. So here, if the insured had a liability relating to weathertightness, that was excluded but the liability for non-excluded matters remain covered. The effect of following Riskpool's analysis would be to place control over whether cover was or was not extant into the hands of the third party plaintiff formulating its claim. Were it to advance a claim by separate proceedings, cover would exist. If however (and responsibly) the claim was advanced in a single statement of claim, it would not.

[29] Finally, Mr McLellan relied on the contra proferentem principle: the policy wording was ambiguous, and Riskpool had the burden of establishing the application of exclusion cl 13(a). The ambiguity should therefore be resolved against it as drafter of the policy.

Discussion

[30] We reach the same conclusion as Hinton J — that the Council's claim should not be struck out — but for slightly different reasons.

[31] It may first be observed that there are a number of curiosities about the drafting of the exclusion clauses, set out at [12] above. The insuring clause is an indemnity "*against Claims*" made for breach of professional duty arising out of negligence. The chapeau to the exclusion clauses provides that that section of the protection wording "does not cover *liability*" for certain items. So the clause immediately sets up a contest between cover for Claims, and certain defined liabilities which are excluded.

[32] It may also be observed that those excluded liabilities are set out in several varying fashions: (1) "amounts [of any claim]";[16] (2) "legal liability" for certain events;[17] (3) "negligent acts, errors or omissions" of certain kinds;[18] (4) "claims" in an undefined sense;[19] (5) "Claims" in a defined sense;[20] and then — critically for present purposes — (6) "liability for Claims".[21]

[33] If this is deliberately differentiated drafting, then the differentiation approaches fine art. The alternative view open is that it is all just a bit of a mess. Not art, and not fine at all.

[34] The essential question is what effect the parties intended this exclusion clause to have. Is the drafting deliberately intended to convey different outcomes according to whether one is dealing with an act, liability for an act, a "claim" or a "Claim" or "liability for [a] Claim"?

[35] Of particular interest are exclusion cls 12 and 13. They appear to be words added later. The drafter has overlooked the chapeau wording at the start of the exclusion clauses, to which those clauses do not respond. Exclusion cl 12 excludes "liability for any legal liability" (arising from asbestos). (The case for the drafting being a mess gains some traction at this point.) Exclusion cl 13(a) excludes "liability for Claims" alleging or arising directly or indirectly out of or in respect of water ingress.

[36] If one takes a very literal view of the drafting, Riskpool has a point. A "Claim" in its defined sense is a demand for compensation, and there is some serious authority to the effect that, in the world of insurers and insureds, you do not subdivide claims into their constituent parts — be they causes of action or something inferior again, such as a particular. Is that what the parties here intended by adopting the word "Claim" in exclusion cl 13(a)? If so, it has the rather heady consequence pointed out by Mr McLellan that a claim based upon structural defect (which would be covered)

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16 Exclusion cls 1 and 10.
17 Exclusion cls 2, 3 and 12.
18 Exclusion cl 4.
19 Exclusion cls 5 and 8.
20 Exclusion cl 7.
21 Exclusion cl 13.

suddenly becomes uncovered because the third party plaintiff tips a minor weathertightness complaint (to use a neutral term) into the Claim (to use a defined term).[22] Was that what the parties intended?

[37] The inquiry is then complicated by the fact that some exclusion clauses exclude "claims" (e.g. cls 5 and 8), some exclude "Claims" (e.g. cl 7), but cl 12 excludes "liability for any legal liability" and cl 13(a) excludes "liability for Claims". Assuming deliberately differentiated drafting, as opposed to the alternative available theory, is there an *intended* difference between these formulae? In particular, is there a difference between excluding "Claims" and "liability for Claims"? To place one's finger on the exact issue, was the latter formulation intended to exclude entirely bundled claims made which incorporate a weathertightness issue (even if merely minimally), or was it intended only to exclude the *liability* for that part of the claim asserting liability for damage caused by water ingress? Mr Ring says the former; Mr McLellan the latter.

[38] This is a question of broad significance for the insurance of local bodies. The stakes are high. The Court is being asked to decide the meaning of a highly variegated series of exclusion clauses in a contextual, factual vacuum. We are unwilling to do that. We consider extrinsic evidence may shed some light on intended meaning. In particular, contextual evidence on the circumstances in which exclusion cls 12 and 13 were added, on the implications for this mutual insurance scheme of weathertightness and other regulatory risk, and on the extent to which one, other or both were intended to be excluded from cover. The Council wishes to call that sort of evidence at trial, although the exact detail of that evidence is not known to us at this still-interlocutory stage of the proceeding.

[39] Against this general background, the question is whether it is inappropriate to strike out a claim where extrinsic evidence may yet be important to a fundamental contract interpretation issue on which the claim turns. In *Vero Liability Insurance Ltd v Symphony Group Ltd*, this Court made the following observation:[23]

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22 See the example given at [27] above.

23 *Vero Liability Insurance Ltd v Symphony Group Ltd* [2008] NZCA 419.

> [39] Both counsel addressed detailed argument on the second issue of the construction of the exclusion clause and the application of s 11 of the Insurance Law Reform Act 1977. However, it is unnecessary for us to consider these questions given our primary conclusion on the first issue of the third party notice. We would add, though, that we would have been reluctant to determine the scope and effect of the clause in the absence of primary evidence, such as might have been given if the Court had earlier ordered formulation of a question or questions for trial, informed by evidence of a limited nature: see r 418 of the High Court Rules. The reasons is that on one view of the provision (a view which Mr Hunter supported in oral argument) its scope is much wider than simply excluding liability for damage resulting from "leaky building syndrome", although presumably that syndrome was the reason for including the exclusion.

[40] The issue then was given closer consideration by this Court, albeit in a slightly different context, in *Trustees Executors Ltd v QBE Insurance (International) Ltd*:[24]

> [42] … We consider that the interpretation of the Policy should be undertaken at a full trial where the question can be considered other than in what is somewhat of a factual vacuum. This is particularly the case because we were urged to consider the background circumstances by both parties (with each asserting that the relevant background supported their interpretation).
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> …
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> [45] We do not consider that we have sufficient evidence to evaluate the different contentions properly. For example, we do not know the exact extent of the investment business of Trustees Executors and exactly how much QBE knew about that business and its extent. We have had no information on the pricing of the Policy as compared to other policies with similar alleged coverage or to those with more extensive coverage. We have limited information on market practice. We also have limited information on exactly how the losses eventuated and the link with the alleged breaches of contract. For example, merely having links between borrowers, valuers and lessees might increase the risks of default but by itself is not necessarily causative of loss. We also have no information on market trends during the relevant period and limited information on market practice. There may also be issues relating to subsequent conduct and possibly even prior negotiations.

[41] Here it is evident that there is room for extrinsic evidence as to context and purpose, in construing what the parties were seeking to achieve in the somewhat erratic drafting of the exclusion wording. The Council wishes to advance such evidence at trial. In our view the determination of the issue posed before us will be more

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[24] *Trustees Executors Ltd v QBE Insurance (International) Ltd* [2010] NZCA 608, 16 ANZ Insurance Cases 61-874 (footnotes omitted). See also *Fussell v Broadbase Christchurch Ltd* HC Christchurch CIV-2009-409-834, 29 June 2011 at [23], [53] and [64].

effectively resolved by a trial Judge in light of that evidence (and any extrinsic evidence called by Riskpool).

[42] Finally, we record our view, expressed at the hearing, that the argument for Riskpool might have been advanced more effectively on a preliminary question under r 10.15 of the High Court Rules 2016, with the benefit of evidence and cross-examination. But applications for strike out should generally proceed solely on the pleadings without reference to the evidence and particularly without reference to contested factual matters. The jurisdiction is one to be exercised sparingly, and only in a clear case where the Court is satisfied it has the requisite material.[25]

[43] For these reasons the appeal was dismissed.

Result

[44] The application by the appellant to adduce further evidence is granted.

[45] The Court file is not to be searched or accessed without leave of a Judge.

[46] The appeal is dismissed.

[47] The respondent is entitled to costs on a complex appeal on a band B basis together with usual disbursements.

Solicitors:
Young Hunter, Christchurch for Appellant
Wilson Harle, Auckland for Respondent

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[25] *Attorney-General v Prince* [1998] 1 NZLR 262 (CA) at 267, endorsed in *Couch v Attorney-General* [2008] NZSC 45, [2008] 3 NZLR 725 at [33].