IN THE HIGH COURT OF NEW ZEALAND
CHRISTCHURCH REGISTRY

CIV-2012-409-2259
[2013] NZHC 690

	BETWEEN	NEW ZEALAND LOCAL GOVERNMENT INSURANCE CORPORATION LIMITED Plaintiff
	AND	R+V VERSICHERUNG AG Defendant

Hearing: 18-19 March 2013
(Heard at Wellington)

Counsel: M G Ring QC, D J Heaney QC and S H Macky for Plaintiff
M D O'Brien, F J Tregonning and E M Greig for Defendant

Judgment: 9 April 2013

In accordance with r 11.5 I direct that the delivery time of this judgment is 3pm on the 9th day of April 2013.

RESERVED JUDGMENT OF MACKENZIE J

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Introduction

[1] The plaintiff, which uses the trading name Civic Assurance (Civic), provides insurance to local authorities in New Zealand. It has reinsurance for part of the cover which it provides. The defendant (R+V) is a reinsurer under one of Civic's reinsurance contracts. The Christchurch earthquakes resulted in large claims under Civic's policies to its insureds. Civic has claimed under its reinsurance contracts. Other reinsurers have paid the claims. R+V has not. Civic seeks summary judgment for some $35m against R+V. R+V applies for a stay, on the basis that the reinsurance contract contains an arbitration clause. Both applications are before me.

[2] That raises the question: which comes first? If I address the summary judgment application first, then, if it is allowed, the stay application becomes redundant. If I address the stay application first, then, if it is allowed, the summary judgment application cannot proceed.

[3] A stay must be granted unless there is not in fact any dispute between the parties.[1] What is the test to be applied in deciding whether there is a dispute? The possibilities, on the authorities, are conveniently set out by Associate Judge Bell in *Cognition Education Ltd v Zurich Australian Insurance Ltd T/A Zurich New Zealand*.[2] On one test, the threshold as to whether there is a dispute is essentially the inverse of the test to be applied on a summary judgment application. On another test, the threshold for a stay is lower, and might require a stay before a summary judgment application is considered. An appeal in that case has recently been argued in the Court of Appeal. Judgment is awaited.

[4] I have found it convenient to consider first the summary judgment application. I have reached the conclusion, for the reasons which follow, that it must fail. That means that the higher threshold test for the grant of a stay, the inverse of the summary judgment test, is met. A stay must be granted. I need not wait for further guidance from the Court of Appeal as to the correct test.

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1 Arbitration Act 1996 sch 1 cl 8(1).

2 *Cognition Education Ltd v Zurich Australian Insurance Ltd T/A Zurich New Zealand* [2012] NZHC 3257 at [18]-[20].

[5] The principles to be applied in deciding a summary judgment application are well established and not in dispute. The onus is on the plaintiff to satisfy the Court that the defendant has no defence.[3] Where the only arguable defence is a question of law which is clear-cut and does not require further factual investigation, it should normally be decided on the summary judgment application.[4] There is a need for judicial caution, which must be balanced with the appropriateness of a robust and realistic judicial attitude when that is called for.[5]

[6] To a great extent, the issues here involve questions of interpretation of the reinsurance contract. Sometimes, such interpretation issues are clear-cut and can be resolved on a summary judgment application. Sometimes, they may require an examination of evidence external to the contract. The evidence may have to be tested before the true meaning of the contract can be ascertained. In such cases, summary judgment will be inappropriate.

[7] In the course of the reasoning which follows, there are instances of both of these types of interpretation issue. This gives rise to a dilemma, particularly for those in the first category; that is, interpretation questions which are clear-cut and could be decided on the summary judgment application. If I reach a decision on them which is adverse to Civic, summary judgment must be refused. The interpretation of the contract would, in that event, not be an issue for this Court at trial. It would be an issue for the arbitration which must follow. The dilemma which I face is how to explain my reasons for refusing summary judgment without trespassing on the field reserved to the arbitral tribunal. The Court should not, in determining the summary judgment application, fetter the ability of the arbitral panel to decide necessary questions of contract interpretation.

[8] Because of that dilemma, I have tried, in the reasoning which follows, not to go beyond expressing the conclusion that the interpretations for which Civic contends are not so clear-cut that summary judgment is appropriate. I have avoided, so far as possible, making findings as to the correct interpretation of the contract. I make these remarks to make it clear that, in limiting my reasoning in this way, I have

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3 *Pemberton v Chappell* [1987] 1 NZLR 1 (CA) at 3.
4 At 4.
5 *Bilbie Dymock Corporation Ltd v Patel* (1987) 1 PRNZ 84 (CA at 85-86.

been mindful of the general principle that difficult questions of law, including questions of contract interpretation, may be decided on a summary judgment application. The need to ensure that the field is left clear for the arbitral tribunal means that this is not a case for the rigid application of that general principle.

The reinsurance

[9] Civic is an insurance company formed to provide insurance for local authorities. It purchases reinsurance cover to reduce its exposure to claims under the policies it underwrites. The details of that reinsurance have varied over the years. I describe the cover in force for the 2010/2011 reinsurance period, from 30 June 2010 to 30 June 2011. The claims arising from the Canterbury earthquakes, between September 2010 and June 2011, fall within that period. There are two main components of Civic's reinsurance cover for that period.

[10] First, there is a quota share reinsurance contract. Under that contract, the reinsurers are liable to indemnify Civic for a fixed proportion of all claims payable by Civic under policies issued to its insureds. For the 2010/11 period, the quota share reinsurer's proportion was 32.5 per cent, with Civic retaining 67.5 per cent of the claims under its policies.

[11] Second, Civic has excess of loss (XL) reinsurance which covers part of its liability under the 67.5 per cent of its business which is not covered by the quota share reinsurance. That cover is placed with a number of reinsurers. R+V is one of these reinsurers, providing 40 per cent of the cover. That is the cover which is in issue in this proceeding. I describe the relevant terms of that reinsurance contract for the 2010/11 period.

[12] The reinsurance is described in the contract details as "per risk excess of loss". The class of business is described as:

> Covering all business written by the Reinsured including, but not limited to, Material Damage, Business Interruption, Personal Accident, Contract Works, Electronic Equipment, Machinery Breakdown, Boiler explosion, Marine Hull and Miscellaneous Accident.

[13] The "Limit & Deductible" in the contract details is described as:

> To indemnify the Reinsured for the amount of liability in respect of each layer, as set out under "LIMITS & DEDUCTIBLES" within the attached Reinsurer Signing Schedule(s).

[14] The reinsurance signing schedule for R+V describes the limit and deductible in these terms:

> NZD 39,600,000 any one loss, any one risk
>
> in excess of
>
> NZD 5,400,000 any one loss, any one risk.
>
> The Reinsured retains NZD 5,400,000 any one loss and any one risk.
>
> The Reinsured's share of all retained losses arising from one event is limited to NZD 10,800,000.

[15] There are other relevant provisions, in both the Contract Details and the Contract Wording. I describe those provisions as necessary in the course of my discussion of the issues.

The issues

[16] Civic has paid claims, and has sought recovery from the XL reinsurers. It has issued four Interim Payment Requests (IPRs) to reinsurers, including R+V, between September 2011 and August 2012. R+V's share of these totals $35,622,127.27. R+V has raised a number of issues about the claims.

[17] Counsel for Civic addressed these issues under six headings:

(a) Does R+V have an arguable case that Civic has not complied with art 20 of the reinsurance contract wording, which deals with loss settlements?

(b) Does the reinsurance contract provide unlimited reinstatements of the limit of indemnity for each loss occurrence?

(c) Does the reinsurance cover risks with an insured value in excess of $100 million?

(d) Does the reinsurance cover apply to schools and utilities?

(e) Does Civic's claim include "below ground assets"?

(f) Are Civic and LAPP to be treated as one entity for the purpose of the reinsurance contract?

Article 20

[18] The XL reinsurance contract contains a provision which addresses the extent to which settlements made by Civic under its policies with its insureds will be binding on the reinsurers for the purpose of calculating the amount payable under the reinsurance contract. Article 20 provides:

> All loss settlements made by the Reinsured, provided that they are within the terms and conditions of the original policies in respect of the business covered hereunder and of this Reinsurance, shall be binding upon the Reinsurers, and amounts falling to the share of the Reinsurers shall be payable by them upon reasonable evidence of the amount paid being given by the Reinsured.

[19] Civic asserts that all of the claims paid by it which form part of the claim on reinsurers have been properly assessed and paid by it under the terms of its policies, and that R+V is bound, by art 20, to accept Civic's assessment. It asserts that R+V's requests for further information to enable R+V to check that the amount claimed is properly payable by it are not in accordance with art 20. It submits that, on this summary judgment application, it is not sufficient for R+V to raise an objection that it has insufficient information.

[20] Article 20 is a common form of loss settlement provision in the reinsurance context. Its interpretation and application in an excess of loss reinsurance context has been authoritatively ruled on by the House of Lords in *Hill v Mercantile &*

General Reinsurance Co Plc.[6] Lord Mustill divided the "follow settlements" clause in that case into three lettered paragraphs:[7]

> "[a] All loss settlements by the reassured including compromise settlements and the establishment of funds for the settlement of losses shall be binding upon the reinsurers, [b] providing such settlements are within the terms and conditions of the original policies and/or contracts [c] and within the terms and conditions of this reinsurance."

[21] His Lordship's reasoning is of such importance, and of such clarity, that it is useful to quote it at some length. His Lordship said, of the approach to the interpretation of the clauses:[8]

> … There are only two rules, both obvious. First, that the reinsurer cannot be held liable unless the loss falls within the cover of the policy reinsured and the [sic] within the cover created by the reinsurance. Second, that the parties are free to agree on ways of proving whether these requirements are satisfied. Beyond this, all the problems come from the efforts of those in the market to strike a workable balance between conflicting practical demands and then to express the balance in words.
>
> These practical demands can be seen most easily in the context of traditional reinsurance, where the party reinsured is the insurer under a contract made directly with the person whose property or other interest is at risk. Two impulses act in opposite directions. The first is to avoid the investigation of the same issues twice; and, moreover, an investigation on the second occasion by a reinsurer whose knowledge of what happened when the risk was written, and whose facilities for investigating the claim, are inferior to those of the direct insurer. The second impulse, acting in the other direction, is to ensure that the integrity of the reinsurer's bargain is not eroded by an agreement over which he has had no control.

[22] Turning then to the wording of the clause his Lordship said:[9]

> I start with the two provisos: paragraphs [b] and [c] of the follow settlements clause. The intent of these seems clear in broad outline, although it may be difficult to apply on the margins. The crucial words are "within the terms and conditions" of the original policies and of the reinsurance. To my mind these draw a distinction between the facts which generate claims under the two contracts, and the legal extent of the respective covers: the purpose of the distinction being to ensure that the reinsurer's original assessment and rating of the risks assumed are not falsified by a settlement which, even if soundly based on the facts, transfers into the inward or outward policies, or both, risks which properly lie outside them. This restriction is perhaps more clearly visualised in relation to the second proviso. Here, the reinsurers are

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6 *Hill v Mercantile & General Reinsurance Co Plc* [1996] 1 WLR 1239 (HL).
7 At 1247.
8 At 1251.
9 At 1252-1253.

> entitled to say that they rated the policy by reference to its chronological and geographical extent, to the types of casualty insured, to the boundaries of the insured layer, the mode of calculating the loss, and so forth. These variables, defined by the terms of the policy, founded the bargain between reinsurers and reinsured on the basis of which the premium and other terms were set. The purpose of the second proviso is in my view to keep this foundation intact, and it would be undermined if an honest attempt by those further down the chain to ascertain the legal consequences of the facts could impose on the reinsurers responsibilities beyond those expressed in the policies. So also with the first proviso. The reinsurers undertake to protect the reinsured against risks which they have written, not risks which they have not written. To allow even an honest and conscientious appraisal of the legal implications of the facts embodied in an agreement between parties down the chain to impose on the reinsurers risks beyond those which they have undertaken and those which the reinsured have undertaken would effectively rewrite the outward contract: and it is this, in my opinion, which the provisos are designed to forestall.

[23] Applying those principles, the House of Lords concluded that the Judge at first instance had been right to refuse summary judgment to the reinsured.

[24] The essence of the decision in *Hill* is that the "follow settlements" clause did not relieve the reinsured of the need to establish that both provisos in the clause were satisfied. Summary judgment was refused because the reinsured had not done so.

[25] *Hill* was considered in *Equitas Ltd v R & Q Reinsurance Co (UK) Ltd*.[10] In that case, the reinsurance claim involved a chain of reinsurances in the LMX (London market excess of loss) spiral.[11] There was a chain of reinsurance arrangements between the original insurance with which proviso (b) of the "follow settlements" clause was concerned, and the reinsurance under which the claim was made, the subject of proviso (c). The issue was whether the reinsured, Equitas, was required to prove that the losses under the original policies of insurance had been correctly aggregated upwards through the LMX spiral. Gross J held that it was not. What it was required to prove was that the settlements under the original policies were within the cover of the policies as a matter of law. Gross J said:[12]

> Necessarily, *Hill v Mercantile* (*supra*) must be taken as my starting point. If the scope of that decision binds me to conclude that Equitas cannot succeed unless it can re-present correctly aggregated losses upwards through the

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10 *Equitas Ltd v R & Q Reinsurance Co (UK) Ltd* [2009] EWHC 2787 (Comm), [2009] 2 CLC 706.

11 For a description of the LMX spiral and its complexities, see *Deeny v Gooda Walker Ltd* [1994] CLC 1224 (QB), as set out in *Equitas Ltd v R & Q Reinsurance Co (UK) Ltd* at [26].

12 *Equitas Ltd v R & Q Reinsurance Co (UK) Ltd*, above n 10, at [64]-[65].

> spiral, then that is indeed an end of the matter – as Equitas neither attempts nor is able to satisfy that burden.
>
> But does *Hill v Mercantile* decide that or is it persuasive authority of the highest order for such a conclusion? Obviously, *Hill v Mercantile* did decide that the syndicates (the respondents on the appeal) were not entitled to summary judgment in respect of their particular claims. Plainly, however, it would be wrong and unreal to treat the authority of that decision (whether of a binding or persuasive nature) as thus confined. In considering the true ambit of the *ratio* and persuasive authority of *Hill v Mercantile*, here, as ever, regard must be had to the context. It will be recollected that the context in which this decision came to be given concerned the stark and key (if not the sole) issue as to the discontinuity between periods of cover. For the follow the settlements clause to 'trump' the principal potential defences, would have involved the conclusion that both the syndicates and Mercantile incurred liability notwithstanding that the loss (arguably) did not occur during the currency of the inward and outward contracts (i.e. contracts no. 3 and 4) – thus (arguably) not within the cover of the policy reinsured or the cover created by the reinsurance as a matter of law. Against this background, as it seems to me, *Hill v Mercantile* essentially stands as authority for the proposition, that the Settlements Clause requires the insurer/reinsured to satisfy both provisos (i.e. [b] and [c], adopting Lord Mustill's lettering) or, in other words, to satisfy Lord Mustill's 'first rule'. The burden is on the insurer/reinsured to do so, to a standard of a balance of probabilities. This issue is one of law, so that if the insurer/ reinsured fails to satisfy either or both provisos [b] and/or [c], the reinsurer/retrocessionnaire will not be liable.

[26] In this case, there is no intermediate chain of reinsurance as there was in *Equitas*. Both *Hill* and *Equitas* stand as authority for the proposition, relevant to this case, that Civic must prove that the settlements under its policies of insurance were within the cover of those policies as a matter of law. To do that, it must adduce sufficient evidence to establish that proposition to the summary judgment standard. Neither the IPRs which are sued on, nor the affidavit evidence adduced in support of the application, meet that burden. This is not a case where it is sufficient to file an affidavit verifying the allegations in the statement of claim and deposing to a belief that there is no defence. The statement of claim does not plead the facts in sufficient detail to meet the *Hill* and *Equitas* standard.

[27] The submission of counsel for Civic is to the effect that in seeking further information as to the basis of settlement of the losses, R+V is seeking to raise speculative defences, of which the Court should be sceptical. I do not accept that submission. For the reasons I have given, I consider that submission reverses the onus of proof. The onus is not on R+V to prove that a particular loss has not been properly settled within the terms of the policy, it is on Civic to prove that it has.

[28] The evidential burden on Civic to prove losses under art 20 would, even in a summary judgment context, be a very substantial burden. But this is a very substantial claim. Lord Mustill in *Hill* expressly rejected the proposition that requiring the reinsured to prove its claim would emasculate the follow settlements clause.[13]

The limit of indemnity

[29] This issue relates to the level of cover available under the reinsurance policy for any one loss or risk for which Civic pays a claim under its policy with an insured.

[30] I have set out, at [13] and [14], the relevant policy provisions as to the limits and deductibles under the reinsurance policy. There is a limit of indemnity of $39.6m "any one loss, any one risk". Those words make it clear that the limit of indemnity is not a single sum. It applies separately to every loss or risk for which a claim is paid by Civic. Civic has paid multiple claims to its insureds arising from the Canterbury earthquakes. Each claim is covered with, on the face of the limits and deductibles clause, an upper limit of $39.6m. The issue is whether that upper limit does in fact apply. Civic contends that, in the circumstances which have arisen, it does not.

[31] Some more detailed background to the structure of the reinsurances is required for a full understanding of this issue. As I have noted at [10], Civic bears 67.5 per cent of the claims under its policies, after its quota share reinsurance which pays to Civic the remaining 32.5 per cent. The XL reinsurance covers Civic's exposure to that remaining 67.5 per cent. As described in the "limits and deductibles" provision in the signing schedule, Civic pays the first $5.4m of that 67.5 per cent exposure for each loss. It is then insured for the loss to the extent of $39.6m. The consequence is that, if Civic's 67.5 per cent exposure on any one loss or risk is $45m or less, the whole of the excess above Civic's $5.4m retention will be covered. That means that, taking into account both the quota share reinsurance and the XL reinsurance, Civic's exposure to a single loss or risk with an insured value of $66.67m is fully covered by the two reinsurance policies, with a retention by Civic

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[13] *Hill v Mercantile & General Reinsurance Co Plc*, above n 6, at 1253.

of $5.4m. Of the balance, $21.67m is payable by the quota share reinsurers and $39.6m is payable by the XL reinsurers.

[32] The present issue potentially arises where the insured value of a risk insured by Civic exceeds $66.67m. There is no express restriction in the XL reinsurance on the value of risks which are covered by the reinsurance. The only reference to that figure is in the contact details which provide:

> Any original Property Risk with a limit in excess of NZD 66,666,667 can be ceded automatically to this reinsurance (up to NZD 100,000,000), however reinsurers are to be notified of such cessions within 30 days of attachment.

[33] That provision is relevant to both this issue and the following issue. I return to it later.

[34] There is no limit on the number of claims from any one event for which the XL reinsurers may be liable. Every claim which exceeds Civic's deductible of $5.4m is payable by the reinsurers. That is to say, there is no horizontal limit on the liability of the reinsurers for multiple claims during the policy period.

[35] There is, however, a horizontal limit on Civic's liability for its $5.4m retention for each claim. That is expressed in the final sentence in the quotation at [14]. If there are multiple losses from one event, Civic's share of "all retained losses" from that event is limited to $10.8m.

[36] Assuming, for the moment, that there may be risks with an insured value in excess of $66.67m, it is apparent that, if the $39.6m limit on the indemnity under the XL reinsurance applies, there are two levels at which Civic might face an exposure to losses on its 67.5 per cent not covered by the quota share reinsurance. First, it will be liable for the first $5.4m under its retained layer in the XL reinsurance. Second, it will be liable for the excess over $45m, because the $39.6m limit on the reinsurance will have been exceeded.

[37] Civic's contention is that, in that eventuality, its total liability for all claims arising from one event cannot exceed $10.8m, whether that liability arises from the

operation of the $5.4m deductible for each claim, or from the excess over the $39.6m limit on the XL reinsurers liability.

[38] The way in which Civic's submissions on this issue were presented by Mr Ring QC and Mr Heaney QC means that it is convenient to address Civic's arguments in support of this contention in two ways:

(a) as an exercise in contract interpretation, having regard only to the terms of the contract itself; and

(b) as an exercise in ascertaining the true meaning of the contract, having regard to the relevant factual matrix as to the making of the contract.

[39] As to the first, Mr Ring places particular reliance on the limitation to $10.8m of Civic's share of "*all* retained losses". He submits that precludes any gap in cover above the $39.6m XL layer. He submits that art 7 in the contract wording achieves that outcome. Article 7 provides:

> **Reinstatement**
>
> If so provided in the Contract Details, in the event of the whole or any part of the indemnity given hereunder being exhausted by a loss occurrence, the amount so exhausted shall be automatically reinstated from the time of commencement of the loss occurrence concerned, subject to payment of such pro-rata additional premium as may be specified in the Contract Details, calculated on the premium due hereunder, such additional premium, where applicable, to be paid at the same time as the loss settlement is made.
>
> The term "pro-rata" shall mean pro rata only as to the fraction of the limit of indemnity reinstated, regardless of the date of loss within the period of this Reinsurance.
>
> If the loss settlement is made prior to any applicable adjustment of premium, any reinstatement premium as may be provided for shall be calculated provisionally on the deposit premium, and adjusted once the final premium is known.
>
> Nevertheless, the liability of the Reinsurers hereunder shall never be more than the limit of indemnity as specified in the Contract Details in respect of any one loss occurrence, nor more than that amount plus the multiple of such limit derived from the maximum number of permitted reinstatements, as specified in the Contract Details, in all during the period of this Reinsurance.
>
> Losses shall be considered in chronological loss date order of their occurrence, but this shall not preclude the Reinsured from making

> provisional collections in respect of claims which may ultimately not be recoverable hereunder, provided that such collections are reimbursed or offset as soon as the definitive position is known.

[40] Mr Ring submits that, once the $10.8m total deductible has been reached, the reference to that being the limit on all retained losses constitutes a provision in the contract details which, in terms of the initial words in art 7, renders art 7 applicable. The provision that the amount exhausted by a loss occurrence "shall be automatically reinstated from the time of commencement of the loss occurrence concerned" means, Mr Ring submits, that the amount exhausted is reinstated for that same loss occurrence, so that there is unlimited vertical reinstatement of the sum insured for that loss.

[41] I am not persuaded that this interpretation is correct, to the extent that would justify summary judgment. The first question is whether the words relied on in the contract details are a provision in the contract details activating art 7. I have some difficulty with this first step. But, assuming this first question was answered in favour of Civic, Civic faces the difficulty that art 7 makes it clear, in the fourth paragraph commencing "Nevertheless …", that the reinsurers' liability shall never exceed the limit of indemnity in respect of any one loss occurrence. On its face that paragraph precludes a vertical reinstatement as submitted by Mr Ring.

[42] That preclusion of a vertical reinstatement is reinforced by art 5 which provides:

> **Indemnity**
>
> The Reinsurers hereby agree to indemnify the Reinsured for that part of its ultimate net loss which exceeds the deductible specified in the Contract Details on account of each and every loss occurrence, as defined in Article 9 hereof, and the sum recoverable under this Reinsurance shall be *up to but not exceeding the limit of indemnity specified in the Contract Details*, ultimate net loss on account of each and every loss occurrence, subject to the provisions of Article 7 hereunder.
>
> The deductible shall be retained net by the Reinsured and not reinsured in any way, other than under the underlying excess of loss layers, if any, on an each and every loss occurrence basis, recoveries under which shall be disregarded in calculating the ultimate net loss hereunder.
>
> However, the placement of this Reinsurance or any part thereof on a "per Risk" basis, shall not preclude the Reinsured from effecting excess of loss

> catastrophe reinsurance for its net account as part of the same reinsurance arrangement or under any other such arrangement in respect of the subject business.
>
> (Emphasis added)

[43] Mr Ring meets that difficulty, namely that vertical reinstatement is contrary to the plain words of art 7 and art 5, with the submission that those contrary provisions must be read down, to give full effect to the limitation to $10.8m on "all retained losses". He submits that "all" means "all", and this must prevail over the contrary wording.

[44] The full phrase on which Mr Ring relies is "all retained losses". The question is not what is meant by "all", but what is meant by "retained losses". On Mr Ring's submission, that phrase refers to any losses which Civic may incur either within its retained layer of $5.4m for any one loss or risk, or within the excess over the limit of indemnity of $39.6m. That is one possible interpretation. Another is that the final two sentences in [14], which both deal with the reinsured's retained layer, are to be read together. On that interpretation, the phrase "retained losses" means losses retained under the immediately preceding sentence.

[45] A factor which might favour that interpretation of the phrase "retained losses" is that, to know the extent of "retained losses", it is necessary to refer only to the terms of this reinsurance contract. On Civic's interpretation, it would be necessary to have regard to Civic's other reinsurance arrangements to know what losses it had retained. The third paragraph of art 5, as set out at [42], expressly recognises that Civic may take out reinsurance which may cover all or part of the layer above the $39.6m layer in this insurance.

[46] For the reasons given at [8], I do not propose to take this question of interpretation further, even though it is one which could be answered on a summary judgment application. I confine my conclusion to finding that Civic has not established, to the level necessary for summary judgment, that the wording of the contract leads to the interpretation for which Civic contends.

[47] The second question, set out in [38](b), is whether, when the contract is read in the light of the admissible evidence as to the pre-contractual situation and the commercial context, a different interpretation of the contract is required.[14]

[48] Civic contends that the background to its dealings with reinsurers of the XL cover in earlier years makes it clear that the indemnity for any one loss or risk is not limited to the $39.6m stated in the policy, once Civic's $10.8m total retention for any one event has been reached.

[49] Civic relies in particular upon exchanges with R+V following a review of its cover which Civic commissioned from a specialist reinsurance broker, Guy Carpenter, in 2007. In that review, Guy Carpenter raised "some concerns as to whether the per event coverage will indeed respond as you believe it will by capping your 'any one event' exposure to NZD 3 million". The figure of $3 million was the limit then in place equivalent to the 2010/11 limit of $10.8m. Mr Sole, the Chief Executive of Civic, said that he was satisfied that the cover was what Civic had intended to obtain, but that he adopted Guy Carpenter's suggestion that he clarify the position with reinsurers. He relies upon R+V's reply as confirming that the cover operates as Civic contends.

[50] There are difficulties with this evidence. First, Mr Sole's subjective view of the effect of the cover is not a permissible aid to the interpretation of the contract. Second, there have been changes in the policy wording since the review was conducted and R+V's confirmation sought. I need not examine these difficulties. I have formed the view that, putting the evidence at its highest for Civic, it does not support, to the level necessary for summary judgment, the contention that cover is unlimited once the $10.8m cap is reached. I explain my reasons for that conclusion.

[51] In its report, Guy Carpenter addressed the equivalent clause to that under consideration, that the reinsured's share of all retained losses arising from one event is limited to (now) $10.8m. It gave an example of how that clause would respond to a series of losses below Civic's per risk deductible. It also said:

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[14] *Vector Gas Ltd v Bay of Plenty Energy Ltd* [2010] NZSC5, [2010] 2 NZLR 444 at [22]-[24].

> We would also note that the current placement is vague as to what Limit of Loss is to apply were the reinsurance contract to respond on the basis you believe. That is, your net retained loss from one event is capped at NZD3,000,000 with reinsurers picking up an unlimited amount vertically. We believe, however, that reinsurers may seek to impose a limit on their liability vertically …

[52] Civic contacted R+V and other reinsurers through its broker Aon. Aon raised two scenarios. In neither of these was there a claim which exceeded the limit of indemnity. Aon's email to reinsurers said of these scenarios:

> … The point here is that there could be an earthquake that generated many small claims within the retention of the reinsurance, however the total of these small claims is also capped at $4.8m for Civic before the reinsurance becomes "ground up".
>
> …
>
> As a result of these observations, LGIC have asked me to seek confirmation from the markets that:
>
> 1. The reinsurance drops down to be ground up after $4,800,000 of retained claims regardless of whether these claims have affected the reinsurance or not …

[53] R+V responded to that email in these terms:

> Referring to your kind email dated March 29, 2007 we herewith confirm that our understanding regarding the captioned treaty is as follows:
>
> The reinsurance drops down to be ground up after $4,800,000 of retained claims regardless of whether these claims have affected the reinsurance or not.

[54] It is clear that this inquiry and the response were directed to a different situation than that now in issue. Aon's email did not expressly raise the point made in the Guy Carpenter report that "reinsurers may seek to impose a limit on their liability vertically". The question addressed was whether claims which fell entirely within the layer of Civic's deductible (now $5.4m) count towards the total retained losses (now $10.8m). The confirmation which was received was that they do, and that once there have been (now) $10.8m of such claims, the cover for further claims drops down to be "ground up", that is, the reinsured layer of (now) $5.4m will not apply to further claims. The present situation, namely that a claim may exceed the limit of indemnity, was not raised.

[55] Civic has interpreted the reference to reinsurance becoming "ground up" as meaning that the reinsurance cover is unlimited. That is not a necessary incident of the cover dropping down to become "ground up". The present issue is not where the reinsurance cover starts, but where it ends. It is not in issue that, once the $10.8m deductible is reached, the reinsurance layer starts at zero for each loss. That is, it is "ground up". The issue is, from "ground up" to where? The phrase "ground up" does not address the upper limit.

[56] Again, I do not propose to take this question further than is necessary to determine the summary judgment application. I find that Civic has not established, to the level required for summary judgment, that any claims which exceed the limit of indemnity of $39.6m are covered, to the extent of that excess.

[57] In reaching that conclusion, I have not found it necessary to address a submission made by Mr Ring, in which he gave examples of how the policy would respond to certain combinations of claim. He submitted that the interpretation for which Civic contends would remove possible anomalies which might otherwise arise from the order in which claims were presented. I note that art 5 (set out at [39]) provides for the order in which losses are to be considered. That provision may not fully address this situation, where there may be many claims occurring on the same date. It is not appropriate, for the reasons given at [8], to deal with this issue here. It is sufficient to observe that the submission as to the possible order in which claims are processed does not cause me to depart from the conclusion expressed at [56].

Risks with an insured value in excess of $100m

[58] This issue arises from the provision in the contract details of the XL reinsurance contract which I have set out at [32]. That permits Civic to obtain cover for risks with an insured value in excess of $66.67m, "up to $100m". The issue, as counsel for Civic expresses it, relates to a risk with a value over $100m. Can such a risk be ceded to the reinsurance (that is, covered by it) for an amount of $100m, provided Civic makes other reinsurance arrangements for the excess over that sum, or can it not be ceded at all?

[59] I consider that the clause must be considered in relation to all risks exceeding $66.67m, not just those exceeding $100m. As I have explained, the XL reinsurance has been structured so that the limit of indemnity of $39.6m will provide full cover (subject to Civic's retained layer) for risks with a value up to $66.67m. My conclusion on the previous issue is that Civic has not established, to the summary judgment standard, that there is cover above the $39.6m limit of indemnity. I need to consider whether that conclusion is affected by the provision for automatic cession of risks over $66.67m. Is the limit for these risks $39.6m, or is it higher so they are covered in full?

[60] The ability to obtain cover automatically for risks exceeding $66.67m does not necessarily mean that the $39.6m limit of indemnity has no application to such risks. If risks exceeding $66.67m were intended to be covered for the full amount insured, not limited by the policy limit, clear words or a clear indication of contractual intention would be needed. For the reasons I have given in dealing with the previous issue, I have found no such clear words or clear intention. The ability to obtain cover for risks exceeding $66.67m is meaningful, even when the $39.6m is applied, because Civic has cover to that level, and need only arrange reinsurance for the excess. The requirement to notify large risks to reinsurers is also meaningful, since large risks may affect the reinsurer's risk profile, as R+V submits. The requirement to notify reinsurers of large risks does not necessarily mean that the limit of indemnity for these risks is different from that on risks within the $66.67m limit.

[61] For these reasons, the automatic cession clause does not cause me to reconsider the findings that I have made as to the limit of indemnity in dealing with the previous issue.

[62] I turn then to risks with a value over $100m. Civic contends that there are at least two risks in that category which are covered by the reinsurance: Christchurch City Council AMI Stadium and Bromley Wastewater Treatment Plant, both of which are insured by Civic. Civic has obtained facultative reinsurance for the excess over $100m in each case. It contends that the value up to $100m is fully covered under the automatic cession clause.

[63] Counsel for Civic place emphasis on the placement of the words in brackets in the automatic cession clause. It is convenient to repeat the relevant part of the clause here:

> Any original Property Risk with a limit in excess of NZD 66,666,667 can be ceded automatically to this reinsurance (up to NZD 100,000,000), however reinsurers are to be notified of such cessions within 30 days of attachment.

[64] The submission is that if it was intended that the figure of $100m was intended to relate, as the figure of $66.67m is clearly intended to relate, to the limit of Civic's policy with its insured, the words in brackets would more logically follow immediately after the $66.67m figure. The essence of Civic's submission is that the separation of the reference to $100m from the reference to $66.67m means that those two figures apply to different limits. The $66.67m figure applies to the limit of the insured risk under Civic's policy with its insured. The $100m figure applies to the limit of Civic's retained liability in respect of that insured risk; that is, Civic's facultative reinsurance of the excess over $100m is to be taken into account.

[65] I do not find that submission persuasive. The more natural meaning of the clause is that both figures apply to the same limit. That follows from the lack of any words in the clause to indicate that the two figures are being applied to different bases. The lack of any such indication is, in my view, a stronger indicator of meaning than is the order of the words in the clause.

[66] The issue is whether Civic's contention is correct, or, more precisely, that there is no sufficiently tenable argument to the contrary that summary judgment should be refused. On this issue, too, I should limit my conclusions to that latter issue. I should not, for the reasons given at [8], resolve the question of interpretation.

[67] Having regard only to the words of the contract, I do not find Civic's interpretation so persuasive that it should result in summary judgment.

[68] Civic further submits that its policy schedules have been presented to reinsurers in a way which discloses that these assets have been included, and that a premium has been paid for them. That submission involves a factual inquiry which

goes beyond the limits of what can appropriately be addressed on a summary judgment application. In these circumstances, it is better that I say nothing more about it. Civic's case on this issue is not so strong that summary judgment should be granted on it.

Does this reinsurance cover apply to schools and utilities?

[69] The property information pack given to reinsurers by Civic's broker Aon said "schools and utilities are not included". The policy wording contains no express exclusion of schools and utilities.

[70] There is one risk included in the claims which R+V contends is a "school". That is the Christchurch Music Centre. R+V has raised a number of issues about that risk, including whether the claim payment properly falls within the scope of the Christchurch City Council's cover with Civic. That involves issues under art 20, which I have dealt with as the first issue. For the reasons given there, I consider that the evidence about the Christchurch Music Centre does not meet the standard required to meet the onus on Civic under art 20. I therefore need not address "schools" on the present issue.

[71] As to "utilities", the Bromley Wastewater Treatment Plant involves issues which are best addressed under the next issue, to which I now turn.

Does Civic's claim include "below ground assets"?

[72] This issue arises from the way in which local authority infrastructure assets are insured by the local authorities. For the most part, local authorities insure their assets in the commercial insurance market. Civic participates in that market. Some local authority assets are not insured in this way. Central and local government have, since 1991, shared responsibility for the restoration of essential infrastructure assets following a natural disaster. For assets in that category, central government is responsible for 60 per cent, and the local authority owner of the asset is responsible for 40 per cent.

[73] Local authorities formed a mutual fund, the Local Authority Protection Programme Disaster Fund (LAPP), to assist them in managing that 40 per cent responsibility. For participating local authorities, cover to the extent of the local authority's 40 per cent was provided by LAPP and the relevant assets were not insured in the commercial market. The LAPP cover is managed by Civic. Mr Sole, the Chief Executive of Civic, is also the Fund Administrator of LAPP.

[74] The formation of LAPP has also had an effect on the structure of the insurance provided by Civic in the commercial market. Mr Sole's evidence is that, as Civic manages LAPP, and as LAPP had a larger capital base than Civic, an arrangement was entered into under which LAPP "fronted" for Civic for some local authorities, including Christchurch City Council.

[75] The "policy" issued to Christchurch City Council for all of its insured assets was issued by LAPP, not Civic. I describe this document as a "policy", as LAPP is apparently not an insurance company. That "policy" appears to make no distinction as to coverage between ordinary assets which are to be insured in the commercial market and essential infrastructure assets which are covered by the agreement with central government (these assets are called "the 40 per cent assets"). All assets are covered.

[76] Under the fronting arrangement, Civic issued an insurance policy to LAPP to cover LAPP's liability under its "policies" issued, inter alia, to Christchurch City Council. Civic's policy covered only the assets which were to be insured in the commercial market. It did not cover the 40 per cent assets. As issued in June 2010 for the 2010/11 period, Civic's policy to LAPP was signed by Mr Sole as Chief Executive of Civic and dated 30 June 2010. It was very short. It provided:

> This is a policy of insurance in which Civic Assurance provides insurance to the New Zealand Local Authority Protection Programme Disaster Fund (LAPP).
>
> This Policy is limited to 'above-ground covers' such as damage to buildings, contents or vehicles and cover for business interruption and excludes cover for 'below-ground' assets such as damage to underground reticulation. Specifically, it includes everything covered by LAPP for the perils covered by LAPP except for the '40% assets' (assets for which the protection from

> LAPP is capped at 40% above a certain threshold). This Policy offers no cover for the '40% assets' in any circumstances.
>
> The cover is:
> - 55% of the first $8 million on any single loss and
> - 100% of any amount above $8 million on any single loss and
> - 55% of the first $16 million on any single event and
> - 100% of any amount above $16 million on any single event.
>
> EXCEPT THAT Civic Assurance will not meet any proportion of a claim where for any reason other than the presence of this clause Civic Assurance is unable to recover that proportion of the claim from Civic Assurance's reinsurers.
>
> The period of this insurance is 30 June 2010 to 30 June 2011, both days at 4:00 pm local standard time.
>
> The premium for This Policy is:
> - 55% of the corresponding contribution received by LAPP plus
> - 45% x 42% x 90% of the corresponding contribution received by LAPP plus
> - 45% of all facultative reinsurance premiums paid by Civic Assurance on individual assets that are protected by LAPP plus
> - GST.

[77] Because the XL reinsurance covered only Civic not LAPP, the Christchurch City Council assets "insured" by LAPP were not all covered by the reinsurance. Only those assets insured by the Civic policy issued to LAPP were covered. Following the earthquakes and the claims, R+V raised questions about which assets were included.

[78] In response to a query from R+V on this issue, Mr Sole issued a replacement policy for the policy from Civic to LAPP. He explained that in a letter to R+V dated 20 September 2012 as follows:

> R+V has raised some questions on Civic's insurance policy issued to LAPP. We agree that policy contained mistakes and so these have been rectified. A copy of the correction is attached for your information. Please confirm that these documents meet your understanding of Civic's intentions.

[79] The replacement policy, signed by Mr Sole as Chief Executive of Civic and dated 20 September 2012, is also very short. It provides:

> This document corrects drafting errors in the New Zealand Local Authority Protection Programme Disaster Fund (LAPP) policy from Civic Assurance dated 30 June 2010 (The Policy) and gives effect to the intentions of the

> parties, which were set out in the property information package provided to Civic's reinsurers.
>
> The Policy covers everything on LAPP's 'above-ground' schedules and any related loss adjusting costs or similar. The Policy does not cover LAPP for the assets that are on its members' 'below-ground' schedules.
>
> The Policy covers 100% of all amounts LAPP may pay to local authorities in connection with the above-ground covers referred to in the LAPP insurance policy from Civic Assurance dated 30 June 2012, EXCEPT THAT Civic will not meet any proportion of a claim where for any reason other than the presence of this clause Civic is unable to recover that proportion of the claim from Civic's reinsurers.
>
> The premium for The Policy is 100% of the corresponding contributions received by LAPP from its members in respect of 'above-ground' assets.
>
> To the extent that this document conflicts with the 30 June 2010 policy, the provisions of this document take precedence.

[80] The issue of what assets are covered by Civic under the LAPP policy is clearly of critical importance to the extent of cover under the XL reinsurance. A determination of the XL reinsurer's liability can only be made when it is properly determined what assets are covered by, and excluded from, Civic's policy to LAPP. That contract was entered into in June 2010. The terms of the original policy dated 30 June 2010 and the replacement policy dated 20 September 2012 are significantly different in ways which are clearly highly relevant to the present issue.

[81] The replacement policy asserts that there were errors in the original contract. There must be a proper and full inquiry into whether that is so. The reinsurer's liability depends on the interpretation of the original contract, not the replacement contract. The subjective views of the parties is not relevant to that interpretation. The test is objective, namely what a reasonable and properly informed third party would consider the parties intended their words to mean.[15] Ascertaining the objective intention of the parties is complicated by the fact that Mr Sole represented both parties. It is not appropriate to accept without examination Mr Sole's assertion that the intention was always as set out in the replacement policy. The crucial question of what the policy covers must be determined by the appropriate arbiter of the issues between Civic and R+V. It will require proper evidence and legal analysis,

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15 *Vector Gas Ltd v Bay of Plenty Energy Ltd*, above n 14, at [19].

beyond the scope of a summary judgment application. Civic's claim for summary judgment on this issue must also fail.

Are Civic and LAPP to be treated as one entity?

[82] This issue is important for determining the extent to which loss adjusting expenses are recoverable from the XL reinsurers, and whether Civic and LAPP collectively bear the retention of $5.4m per loss and $10.8m per event.

[83] In addition to the insurance policy from Civic to LAPP to which I referred in the previous issue, there is a reinsurance "policy" issued by LAPP to Civic. That is also a one-page policy, signed by Mr Sole as Fund Administrator for LAPP, and dated 30 June 2010. That policy was also replaced by a further document, also signed by Mr Sole, on 20 September 2012. The effect of those transactions is also an issue which must be decided after hearing full evidence, including an opportunity to cross-examine Mr Sole, and after full legal argument as to the effect of the arrangements. For similar reasons to those I have given on the previous issue, I am satisfied that this is not an appropriate issue for summary judgment.

Result

[84] The plaintiff's summary judgment application is refused.

[85] The defendant's application for a stay is granted.

Costs

[86] Counsel for the plaintiff made brief submissions as to costs. Counsel for the defendant did not.

[87] The general practice, on the dismissal of a plaintiff's summary judgment application, is that costs are reserved, to be determined following trial.[16] Counsel for the plaintiff seeks the reservation of costs in accordance with that practice. My

[16] *NZI Bank Ltd v Philpott* [1990] 2 NZLR 403 (CA).

tentative view is that this general practice is not appropriate here. The grant of the stay means that this proceeding is unlikely to proceed to trial. I incline to the preliminary view that the defendant should be awarded costs. The plaintiff has proposed category 3.

[88] If the parties are unable to agree in the light of that indication, memoranda may be submitted.

"A D MacKenzie J"

Solicitors: Heaney & Co, Auckland, for Plaintiff
Bell Gully, Wellington, for Defendant