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INSOLVENT INSURED NO BARRIER TO SUING ITS INSURERS – CIVIL LIABILITY (THIRD PARTY CLAIMS AGAINST INSURERS) ACT 2017 (NSW) STRIKES AGAIN

9 MARCH 2018 | DIRECTORS' & OFFICERS' LIABILITY

IN ISSUE

Whether the *Civil Liability (Third Party Claims Against Insurers) Act 2017* (NSW) (Act) could be invoked to join the insurers of an insolvent company to a representative proceeding.

THE BACKGROUND

In December 2014, Rushleigh Services Pty Ltd (Rushleigh) issued group proceedings in the Federal Court against Forge Group Limited (in liquidation) (receivers and managers appointed) (Forge) and two of its former directors. Rushleigh was a shareholder in Forge and commenced the proceedings on its own behalf, and on behalf of other shareholders. Rushleigh alleged failure by Forge to comply with continuous disclosure requirements, along with related misleading conduct. Leave to proceed against Forge under s 500(2) of the *Corporations Act* was refused, so Rushleigh applied under s 5 of the Act to join its D&O insurers (Chubb, Allianz and Axis) as parties to the proceeding.

THE DECISION AT TRIAL

Justice Markovic confirmed the position that cases dealing with the former s 6 of the *Law Reform (Miscellaneous Provisions) Act 1946* (NSW) applied equally to s 5 of the Act. There were three elements required to be established under the Act:

1. An arguable case against Forge.
2. An arguable case that the policies responded to the claim against Forge.
3. A real possibility that, if judgment was obtained, Forge would not be able to meet it.

Her Honour held that all of these elements were satisfied and did not accept the insurers' arguments that leave should not be granted on other grounds, including that:

- They would suffer irreparable prejudice by reason of them not being as familiar with the subject matter of the proceedings as Forge and by incurring defence cost estimated at $5.7 million (more than they would incur if just funding Forge's defence costs).

- As insurers had already agreed to indemnify Forge and its directors, there would be no utility joining them as parties.
- The joinder of insurers to overcome the consequences of the failed leave application against Forge was not a proper basis for the exercise of the discretion.

Her Honour held these were not factors that should be given significant weight. Insurers will inevitably suffer some forensic disadvantage (and additional cost) when joined under the Act as they will always be a stranger to a proceeding. The policies required Forge to provide all necessary assistance to insurers and that is one reason why reasonable assistance clauses are included in insurance contracts. The intention of the Act should not be undermined. Further, a failed leave application does not affect the substantive question of whether Forge is liable to shareholders. As the Act provides that an insurer stands in the place of an insured as if it was the insured, the refusal of a leave to proceed application under the *Corporations Act* against a liquidated company does not mean that the company cannot be found liable to plaintiffs. A finding of liability against insurers standing in Forge's place would still comprise a 'loss' that the policies may respond to. Therefore, it could not be said that there was no utility in the grant of leave.

Her Honour also noted that there is no requirement that an application for leave to proceed against a company in liquidation and an application for a grant of leave under s 5 of the Act against an insurer to be made at the same time. They are alternative procedures and a litigant has a choice as to which application to make and when.

IMPLICATIONS FOR YOU

The Act is now in full swing since its commencement on 1 June 2017. As more applications for joinder of insurers as parties to proceedings under the Act are made and determined, the scope and impact of the new regime is being tested and providing clarification to both insurers and plaintiff lawyers. Where leave applications under the *Corporations Act* to sue insolvent companies fail, it is clear that this does not preclude a subsequent successful application against an insurer under the Act. It is timely for insurers to check that Policy terms requiring provision of reasonable assistance and cooperation by insureds are clear, as watertight as possible and adequately deal with circumstances where an insured becomes insolvent. The scope and enforceability of reasonable assistance provisions may become very significant in the event insurers find themselves as defendants to proceedings in lieu of insolvent insureds.

It remains to be seen if this decision will encourage plaintiff lawyers to seek leave to join insurers under the Act (where it applies) as a first port of call, instead of pursuing s 500(2) *Corporations Act* leave applications in circumstances where a defendant company is in liquidation. It will also be interesting to see if there is any impact on corporate and D&O premiums as a result of the continued application of the Act to securities (and other) litigation in NSW.

Rushleigh Services Pty Ltd v Forge Group Limited (In Liquidation) (Receivers and Managers Appointed) [2018]

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