

A useful summary of the law of interpretation of insurance policies in Western Australia

Insurance & Risk Update

The below is an extract of the decision of Hall J in *Birla Nifty Pty Ltd v International Mining Industry Underwriters Ltd* [2013] WASC 386. It is a useful and succinct summary of how the Western Australian Supreme Court approaches the interpretation of insurance policies.

Principles of construction

[22] The ordinary principles relevant to the construction of commercial contracts are relevant to the construction of insurance policies. The principles to be applied are well established and can be summarised as follows:

1. The contract should be construed objectively. The subjective beliefs or understandings of the parties do not govern their contractual relations. The meaning of a term in the contract is to be determined by what a reasonable person would have understood it to mean: *Toll (FGCT) Pty Ltd v Alphapharm Pty Ltd* [2004] HCA 52; (2004) 219 CLR 165 [40].
2. The construction of a commercial agreement requires a reference to be made to the language used by the parties read in the context of the commercial transaction as a whole and the common intention of the parties as manifest in the text and explicit and implicit objects of the agreement: *Cape Lambert Resources Ltd v MCC Australia Sanjin Mining Pty Ltd* [2013] WASCA 66 (S) [52] (Martin CJ) and the authorities there referred to.
3. The starting point is the text of the agreement. It is to be construed in the context of the contractual document as a whole: *Australian Broadcasting Commission v Australasian Performing Right Association Ltd* (1973) 129 CLR 99; (1973) 47 ALJR 526, 109

Who does this affect?

- Insurers
- Insured persons
- Insurance Brokers

Article Highlights

- The Western Australian Supreme Court provides a succinct summary of the principles that the Court applies to the interpretation of insurance policies and how it seeks to give effect to the common intention of contracting parties.
- Insurance contracts are to be read objectively, commercially and contextually, as far as the text of the agreement will allow.
- The *contra proferentem* rule, where ambiguity is resolved in favour of the insured, will only be applied as a last resort where the language and logic of a document is not enough.

(Gibbs J); and *Royal Botanic Gardens and Domain Trust v South Sydney City Council* [2002] HCA 5; (2002) 240 CLR 45 [69], [71].

4. An absurd or manifestly unjust result will be avoided upon the hypothesis that such could not have been intended by the parties. A construction that accords with business common sense will usually be favoured over one that does not: *Magbury Pty Ltd v Hafele Australia Pty Ltd* [2001] HCA 70; (2001) 210 CLR 181 [43].
5. If the language of the agreement is ambiguous or susceptible of more than one meaning evidence of surrounding circumstances is admissible to assist in the interpretation of the contract: *Codelfa Construction Pty Ltd v State Rail Authority (NSW)* [1982] HCA 24; (1982) 149 CLR 337, 352 (Mason J); and *Western Export Services Inc v Jireh International Pty Ltd* [2011] HCA 45; (2011) 282 ALR 604 [2] - [6].

[23] In *Wilson v Anderson* [2002] HCA 29; (2002) 213 CLR 401, Gleeson CJ explained the objectivity principle in terms which are particularly relevant to this case:

The law of contract seeks to give effect to the common intention of the parties to a contract. But the test is objective and impersonal. The common intention is to be ascertained by reference to what a reasonable person would understand by the language used by the parties to express their agreement. If the contract is in the form of a document, then it is the meaning that the document would convey to a reasonable person that matters. The reason for this appears most clearly in the case of commercial contracts. Many such contracts pass through a succession of hands in the course of trade, and the rights and liabilities of parties other than the original contracting parties are governed by them. ... it is only the document that can speak to the third person [8].

[24] The requirement of ambiguity before there can be reference to surrounding circumstances has been considered in numerous cases. Whilst the reiteration of this requirement in *Jireh* leaves no doubt as to its existence, ambiguity is a broad concept. In any event it is enough if the instrument is susceptible of more than one meaning. A practical approach was suggested by Pullin JA in *McCourt v Cranston* [2012] WASCA 60 as follows:

If a trial judge decides that the contract under examination is not ambiguous or susceptible of more than one meaning, and rules that evidence of surrounding circumstances is not admissible, and an appeal court then decides that decision to be in error, then the case will have to be reheard, because relevant evidence will have been excluded. If, however, the trial judge receives evidence of surrounding circumstances and evidence of the object or aim of the transaction, and if the trial judge's construction is

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found to be in error, then the Court of Appeal will be able to remedy that on appeal without sending it back for retrial.

Until the High Court says more about the subject, it would be wise for trial judges, in cases where a party reasonably contends that the contract is ambiguous or susceptible of more than one meaning and there is relevant evidence of objective relevant surrounding circumstances known to both parties or objective evidence of the aim or object of the transaction, to allow that evidence in provisionally, even if the trial judge considers that his or her likely conclusion will be to reject the argument of the party contending that the agreement is ambiguous or susceptible of more than one meaning [25] - [26].

[25] Once the threshold for admissibility of evidence of surrounding circumstances has been met it is important to restrict the evidence to that which is relevant. The objective approach remains pertinent. Thus evidence of surrounding circumstances must be such as could assist a reasonable person to understand the language used in the contract. Clearly evidence of subjective opinions or of negotiations are not admissible; the surrounding circumstances must be objective facts and must be known to both parties: *McCourt v Cranston* [24] (Pullin JA).

[26] The plaintiff submitted that a liberal approach was to be adopted in the construction of insurance contracts and that in the case of ambiguity the *contra proferentem* rule should be applied against the insurer. It was said that this rule strongly applies to insurance contracts drafted by the companies who issue them. One of the authorities referred to in support of this submission was *Johnson v American Home Assurance Co* [1998] HCA 14; (1998) 192 CLR 266 [19] (Kirby J). Kirby J was in dissent in that case. In any event his statement that insurance policies containing words that are intractably ambiguous will be construed so as to strongly favour the resolution of the ambiguity in a way advantageous to the insured was based on *Western Australian Bank v Royal Insurance Co* [1908] HCA 11; (1908) 5 CLR 533, 559. His Honour accepted that this approach was now not so much in favour and that courts today accept the duty to endeavour to find the meaning from the language and logic of the document rather than by resort to maxims and other rules of thumb. His Honour also accepted that the *contra proferentem* principle was in any event a last resort in construction.

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