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Cover to Cover

Issue 31

Our publication for New Zealand insurance professionals

MinterEllisonRuddWatts.

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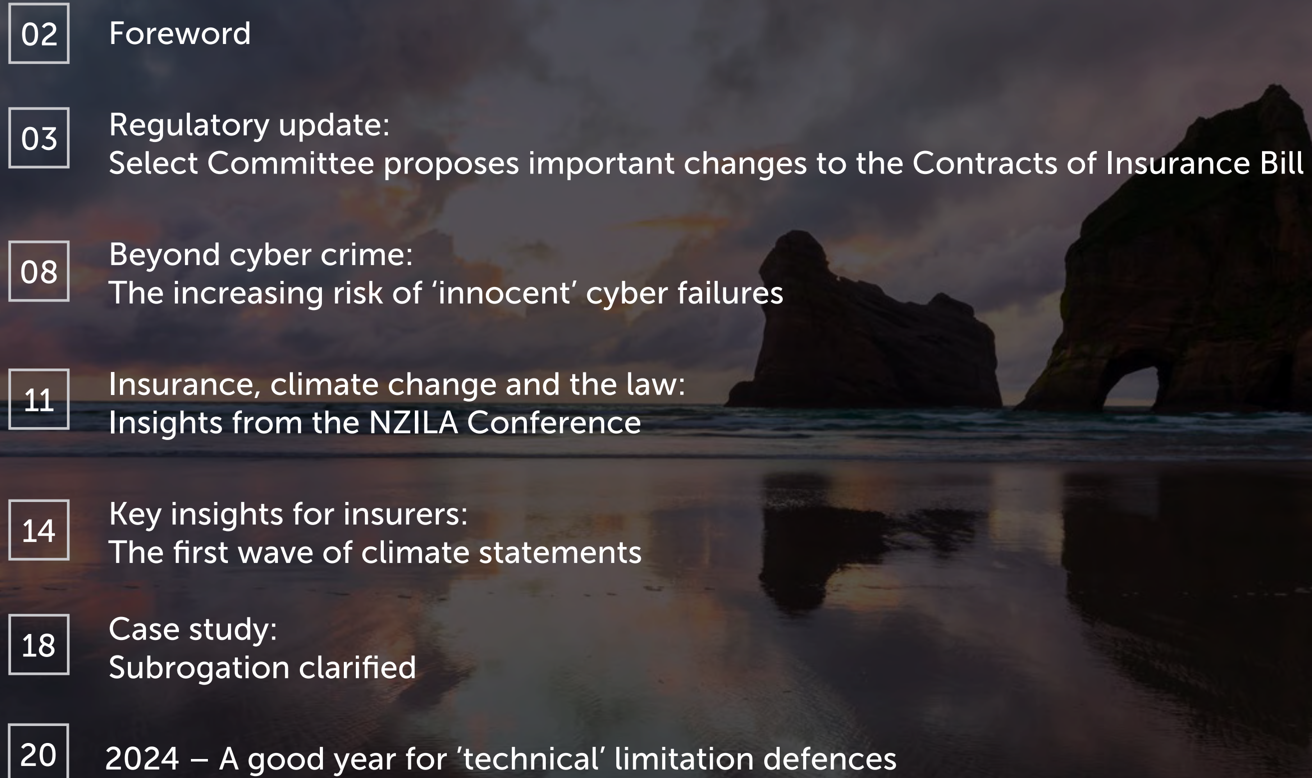

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Foreword

Welcome to the final issue of Cover to Cover for 2024 – our publication for New Zealand's insurance professionals.

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This issue finds New Zealand in difficult economic times. Business closures and collapses are daily news, especially in the construction and hospitality sectors. IRD liquidation applications are on the rise, as is unemployment, with over 47,000 newly unemployed in 2024 alone. As one politician put it, that is enough people to fill Eden Park.

The increasing level of business failures has seen a rise in claims against directors, with a corresponding uptick in claims on D&O insurance policies. Several issues emerge through these claims:

- The recent decision in *Boaden v Mahoney* thrust open the door to claims by creditors against directors, without the involvement of a liquidator. The Supreme Court left this particular door ajar in the *Mainzeal* case, finding that section 301 of the Companies Act 1993 permitted creditors to seek compensation from directors. We expect to see more claims of this nature, with creditors competing with liquidators for access to directors' (and their insurers') pockets.
- Claims against directors in a recession raise the spectre of insolvency exclusions. These clauses are often interpreted narrowly by the courts. However, the precise words of any exclusion (or any policy term, for that matter) need to be considered carefully. Suffice it to say that insurers cannot necessarily reject claims by liquidators and creditors following an insolvency in reliance upon an insolvency exclusion. Many such claims will have been caused by acts or omissions that would have caused loss regardless of insolvency e.g. because the company breached a contract. Simply because the board is later shown not to have had reasonable grounds to believe the company could meet that obligation does not mean that insolvency was the cause of the loss.
- Some claims are being brought long after the relevant act or omission and after policy periods have expired. Such claims test the sanctity of "claims made and notified" policies, which are intended to create certainty for insurers' annual financials. There is some authority in New Zealand to support the proposition that claims can be made after the policy period has expired, where the insured can show that the policy period allowed them to notify circumstances, and they knew of those circumstances and should have disclosed them. However, that is yet to be tested fully.

Another feature of recessions is redundancies and associated personal grievances. These can trigger claims under employment liability policies, which could be significant depending on the size of the workforce and the nature of the restructuring.

Against this backdrop, we have a variety of interesting topics to cover:

- We begin with an update on the Contracts of Insurance Bill. The Bill is aimed at modernising and consolidating New Zealand's insurance legislative regime and proposes significant changes to the existing law in important areas. We break down the recent report from the Finance and Expenditure Select Committee, which highlights important revisions following public consultation and explores what these changes could mean for insurers and brokers.
- Next, we turn our attention to the ever evolving cyber risk environment and the increasing risk of 'innocent' cyber failures. While cyber crime remains a priority for businesses, we explore this less obvious but equally critical threat, of which an example is the recent CrowdStrike failure.
- We then outline key insights from a keynote address that our firm sponsored on the intersection between climate change and insurance, delivered by Dr Franziska Arnold-Dwyer, a leading expert in sustainable insurance, at the New Zealand Insurance Law Association conference.
- We analyse New Zealand's first year of mandatory climate-related disclosures. Many licensed insurers were recently required to lodge climate statements under the new regime. We provide a snapshot of key trends and observations from the disclosures made to date.
- Finally, we look at a host of recent impactful cases, including a case on subrogation and the application of the "top down" principle to the allocation of recoveries, and a review of limitation cases that are noteworthy for both insurers and insureds.

We hope you find this issue informative and thought-provoking.

Regulatory update:

Select Committee proposes important changes to the Contracts of Insurance Bill

Authored by Andrew Horne, Partner and Hannah Jaques, Senior Associate

We have previously reported on the significant changes to New Zealand insurance law that will come into effect when the Contracts of Insurance Bill is passed into law.

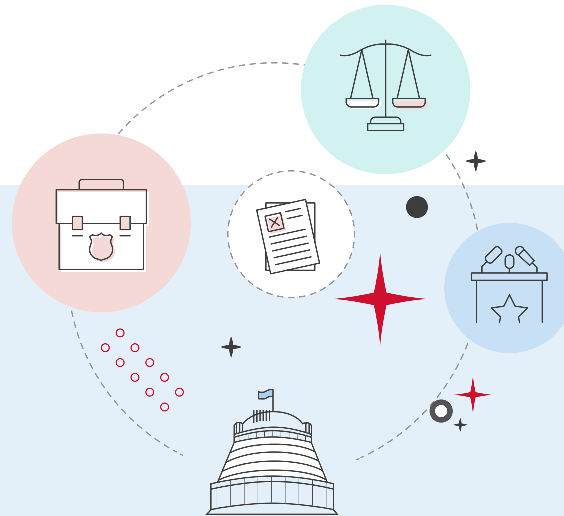
To recap, the Bill has been introduced to address longstanding issues with the law as it presently stands, and to modernise and consolidate existing insurance legislation and some common law principles. Among other things, it will make fundamental changes to insureds' duty of good faith and to the consequences of failures to comply with the duty of disclosure.

The Finance and Expenditure Committee has now released its report on the Bill, following receipt of over 50 submissions from the public sector, insurance market participants, law firms and individuals.

This article collates key insights from the Committee's report and highlights the implications of the proposed revisions to the Bill for insurers and brokers.

NOTE: As we went to print, the Bill passed its second reading adopting the Select Committee's recommendations set out below. It is now in the Committee of the Whole House stage, in line with the Government's intention for the Bill to pass its third ready and receive the Royal assent by the end of the year. Once passed, the Act is intended to come into force on a date or dates set by Order in Council with a longstop of three years from Royal assent.

Regulatory update: Select Committee proposes important changes to the Contracts of Insurance Bill



Key themes of the Bill

We discussed the changes proposed in the Bill in our previous article here. The key proposed changes are:

- Changes to a policyholder's duty of disclosure to remove the common law duty to disclose matters that a reasonable insurer would find material and replace it with new duties, with different standards applying to consumer and non-consumer policyholders.
- A limited extension of the application of the unfair contract regime in the Fair Trading Act to contracts of insurance.
- Proportionate remedies for non-disclosure rather than the singular remedy of 'avoidance' of the policy in its entirety.
- Replacement of the statutory charge upon insurance policy proceeds in favour of claimants under the Law Reform Act 1936 with direct third party claims against insurers.
- Introduction of an implied term in insurance contracts that an insurer will pay claims within a reasonable time.

Since our previous article, the Committee has received submissions on the Bill and reported back. While some submissions supported the reforms as a positive step towards increased transparency and consumer protection, others raised concerns about practical challenges, costs associated with compliance and implications on operational efficiency. A number of submissions pointed out that additional costs would likely be borne by policyholders through increased premiums or reduced scope of cover.

Key takeaways from the Select Committee's report

The Committee has recommended that the Bill is passed with amendments. Most of the amendments were unanimously agreed by the Committee. However, three were not:

- An amendment of the standard by which an insured will be judged to have lacked reasonable care not to engage in misrepresentations from "fraudulently" to "dishonestly". This amendment was made following submissions from the industry and to better align with the equivalent UK provision. Some committee members did not agree with this amendment on the basis that "dishonestly" was too broad, weak and vague.
- Extending the requirement for insurers to pay any sums due in respect of a claim within a reasonable time to acknowledge that this includes a reasonable time to gather information for the investigation and assessment of claims. Some committee members opposed this amendment as a significant step back from the consumer protection focus of the Bill.
- Introduction of a provision that allows for regulations to prohibit or regulate insurers' use of genetic information when underwriting life and health insurance. This was an issue raised in submissions but had not been included in the Bill at its first reading. It is intended to allow a flexible response to issues of genetic discrimination. Some Committee members opposed this amendment and submitted an amendment paper with proscriptive requirements for the provision and use of genetic testing.

Other key amendments at the Committee stage include:

- Extension of the definition of "specified intermediaries" to include financial advisers who indirectly receive commission from insurers through their financial advice provider. These specified intermediaries must comply with duties introduced by the Bill.
- Clarification of what knowledge will be imputed to an insurer from a specified intermediary. Knowledge of specified intermediaries' employees will not be imputed to the insurer where the relevant employee's work is unrelated to the insurance contract at issue.
- Modification of brokers' obligations to pass on money to insurers and policyholders.
- Identification of certain terms relating to life and health insurance that may be excluded from the unfair contract terms regime under the Fair Trading Act.
- Exclusion of reinsurance contracts from the ambit of the Bill – reinsurance contracts will not now be "contracts of insurance" as defined.

Changes relevant to all insurers

Consumers must take reasonable care not to make a misrepresentation

- The Bill would impose a duty on consumer policyholders to take reasonable care to not make a misrepresentation to an insurer when entering into an insurance contract. At its first reading the Bill provided that misrepresentations made fraudulently would be taken as showing a lack of reasonable care. The Committee has replaced "fraudulent" with "dishonest" in response to submissions, to more closely align with the equivalent provision in the UK Consumer Insurance (Disclosure and Representations) Act 2012 and to avoid associations with criminal fraudulent misrepresentations.
- To address concerns that the term "dishonestly" is less clear and could arguably cover any kind of misrepresentation, the onus will be on the insurer to undertake further steps if a consumer provides an answer to a question which is unsatisfactory or incomplete. When determining whether a consumer has taken reasonable care not to make a misrepresentation, the Bill now proposes to take into account any steps the insurer took in responding to a consumer who failed to answer a question or gave an obviously incomplete or irrelevant answer.

Insurers have a "reasonable time" to pay claims

- The revised Bill introduces an implied term to every insurance contract that an insurer must pay any sums due in respect of a claim within a "reasonable time". Previously, the Bill specified 12 months as the reasonableness period and provided that if a claim was not paid out within that period, interest would become payable by the insurer for unreasonably withholding payment.
- The submissions supported removal of the specified reasonableness period, as it would place undue operational pressures on insurers. The Committee has recommended a clarification that "reasonable time" includes time to gather information to investigate and assess the claim. This is intended to ensure that, while delays in claims handling are minimised, insurers do not face undue pressure to expedite claims handling to comply with a reasonableness period. The amendment recognises the reality often faced by insurers seeking to obtain information from policyholders and does not unduly punish insurers for delays outside their control.
- Some committee members disagreed with this change and submitted an amendment paper which proposes that insurers be required to pay interest, calculated in accordance with the Interest on Money Claims Act 2016, from the date on which it becomes unreasonable for an insurer to withhold payment. They would specify that it will become unreasonable 12 months after the date on which the claim was made, unless, in the circumstances, it is reasonable for the insurer to withhold payment until a later date. The proposed amendment is aimed at enhancing consumer protection but introduces a rebuttable presumption and an element of subjectivity and uncertainty.

Imputed knowledge of specified intermediaries

- The Bill proposed a new duty on non-consumer policyholders to make a "fair presentation of the risk" prior to entering into insurance contracts. However, policyholders are not expected to disclose what an insurer knows, or ought to know, including something that is known to any individual who is, or who works for, a specified intermediary in relation to the insurance contract.
- Some submissions proposed that insurers should only be deemed to know what the policyholder or specified intermediary actually disclosed to them. The Committee disagreed, and while it did not think the presumption should be removed, recommended making it clear that the presumption only applies to those who are or who work for a specified intermediary, not employees whose work is unrelated to the relevant insurance contract.
- The Bill provides for remedies for insurers in circumstances where a non-consumer policyholder breaches the duty of fair presentation (or any other misrepresentation qualifying a remedy). The Committee proposed amendments to these remedies so that an insurer may charge a higher premium for the remainder of the contract but be prohibited from also disproportionately reducing the amount to be paid on a claim.

Reinsurance contracts are not "contracts of insurance"

Previously, the Bill included reinsurance contracts as contracts of insurance, but they were excluded from specific parts of the Bill. Many submitters expressed the view that the Bill should not apply to reinsurance contracts at all. The Committee agreed, proposing that reinsurance contracts should generally be excluded from New Zealand insurance law as they are typically arrangements between insurers and large overseas based reinsurers. For this reason, they narrowed the definition of "contract of insurance" in the Bill by excluding contracts of reinsurance.

Changes relevant to brokers and other intermediaries

Wider definition of "specified intermediary"

- Some submitters were concerned that the definition of a "specified intermediary" under the Bill was limited to intermediaries who received commission or other consideration directly from insurers. The Committee has broadened the definition to intermediaries who receive commission indirectly from insurers. The change is intended to capture financial advisers who structure payments through financial advice providers. These specified intermediaries are then subject to certain duties introduced by the Bill, including the duty to take reasonable steps to pass on a consumer's representation to the insurer before the insurer enters into or varies the contract of insurance.

Competing obligations addressed

- Submissions by insurance brokers opposed the duties and penalties introduced by the Bill, particularly disclosure requirements. They feared that the Bill exposed them to excessive risk and could conflict with duties to their clients. In response to these arguments, the Committee proposed amendments which would ensure that specified intermediaries complying with the Bill's duties would not be in breach of any contract, including their contract with the policyholder. Additionally, the Committee recommended that any compensation a court orders for breaches of duties be subject to any position agreed between the insurer and the specified intermediary, such as agreed limitations of liability.

Duty to pass on premiums to insurers and payments to policyholders

- The Bill will introduce a duty on brokers to pass on to the insurer any premiums they receive from policyholders within a specified "relevant period" of time. The Bill does not prevent an insurer and broker varying the "relevant period". Submitters queried whether existing variation agreements will continue to apply, as it would be costly and inconvenient for parties to renegotiate. The Committee accepts that they should and proposed a "grandfathering provision" which would allow this.

- Previously, the Bill would have made it an offence for a broker to fail to pass on premium to an insurer within a reasonable time with a fine not exceeding $5,000 for individuals and $10,000 for companies. The Committee has removed the offence provision from the Bill and introduced a new provision that would allow insurers to recover amounts payable by the broker as a debt.
- The Bill would also have introduced a duty on brokers to pass on money to, or on behalf of, the policyholder within 7 days after receiving payment. Following receipt of submissions, the Committee acknowledged that many complex insurance arrangements mean that it will take longer than 7 days to forward payments to the policyholder. They accordingly recommended that brokers be required to pay the money to policyholders of non-consumer insurance contracts as soon as reasonably practicable. The 7-day period still applies where payments are to consumer policyholders.

Changes relevant to health and life insurers

Terms relating to life and health insurance may be excluded from being unfair contract terms

The Bill now provides for a new provision to be inserted into the Fair Trading Act providing that specified terms that define the main subject matter of an insurance contract cannot be declared unfair contract terms. The Committee proposed to include in that list a term that relates to the amount of premium payable under a life policy or health insurance contract. This is to align life and health insurers, who adjust their premiums on annual policy anniversaries, with general insurers who renew and reprice contracts on an annual basis.

No prohibition (yet) on insurers using genetic data

- In perhaps the most significant amendment to the Bill, it now provides for regulations to control life and health insurers' ability to use genetic data. A number of submitters raised concerns about the use of genetic information by insurers in life and health insurance and the potential for genetic discrimination. The law is currently silent on this issue. The Committee acknowledged the value of such data for insurers in assessing risk but also recognised the need to protect consumers from potential misuse. While several submissions sought an outright ban, the Committee ultimately preferred a flexible regulatory approach to manage the use of genetic data.
- Under the revised Bill, the Government will be empowered to prohibit or regulate insurers' use of genetic information through regulations. This could result in transparency and disclosure requirements on insurers to ensure that genetic data is used in a non-discriminatory manner. Insurers will need to keep abreast of any developments in this area and ensure that their use of genetic data complies with any regulations.
- Some Committee members disagreed with the Committee's approach. They have submitted an Amendment Paper that would proscribe insurers from requiring genetic testing and bar most uses of genetic testing, unless the use is beneficial to a policyholder.

What next?

The Bill is now at its second reading, meaning the House will debate and vote on any changes to the Bill, including the Committee's recommended amendments.

Government officials expect the Bill to be passed by the end of 2024. Once passed, the Bill is likely to impact various aspects of the insurance market, including pricing, underwriting, claims management and competition. Insurers should closely monitor the Bill's progress through the legislative process and prepare to align their practices and policies with new requirtements. In particular, insurers should review existing contracts and procedures and implement more rigorous documentation and communication practices to ensure compliance with new consumer protection measures, including any potential regulations on the use of genetic data and the new "reasonable time" requirement for claims.

Beyond cyber crime:

The increasing risk of 'innocent' cyber failures

Authored by Andrew Horne, Partner and Oliver Sutton, Senior Solicitor

Businesses and other organisations are rightly focused on safeguarding against cyber crime. News headlines frequently highlight the consequences of data breaches, ransomware attacks and the exposure of sensitive information by cyber criminals. These incidents can result in significant losses and liabilities for organisations and their cyber insurers, as well as damaging reputations.

A typical example is the recent attack upon Lehigh Valley Health Network in the US, whose refusal to pay a ransom led to a data breach in February 2023 and the release of cancer patients' sensitive medical information, including photographs. Unsurprisingly, a class action was filed on behalf of the affected patients, and a settlement has recently been agreed resulting in payments totalling USD65 million. More recently, in August 2024, Microsoft systems in New Zealand including Outlook and Teams faced disruptions and were unable to operate due to a distributed denial-of-service or DDoS cyberattack.

While cyber crimes such as these make headlines, IT systems are also susceptible to less dramatic but sometimes equally damaging failures that do not involve any criminal intent. Like cyber attacks, these failures can have significant effects, in some cases resulting in a total halt of business operations. However, whilst businesses may have safeguarded against the fallout of cyber crime, they may find themselves unexpectedly uninsured for non-malicious cyber failures. Understanding these risks and how best to comprehensively protect – and insure – against them is vital for businesses that rely on technology to function.

The CrowdStrike failure

One of the largest IT outages in history was caused by an innocent cyber failure. On 19 July 2024, the global cybersecurity company CrowdStrike released a faulty software update. The update, intended to enhance security, instead caused widespread IT system outages by rendering approximately 8.5 million devices running Microsoft software unusable.

The problem stemmed from a compatibility issue between CrowdStrike's update and the Microsoft operating system. Although a fix was quickly provided, the effect of the fault was to render computers unavailable, so the fix typically required IT professionals to intervene. This prolonged the resulting downtime for many companies. Although the issue affected only about 1% of Microsoft customers, the impact was severe because many of those affected were critical service providers. Banks lost access to payment systems, airlines were forced to ground flights, and hospitals had to revert to manual processes, which caused flow-on losses to many other businesses and organisations.

Risks and losses

When systems fail, businesses suffer losses in many ways. Production of goods or services may be reduced or brought to a halt. Without the ability to process payments or deliver services, businesses miss out on potential sales. Remedying system failures often requires the IT specialists or additional resources to restore systems. Extended downtime may mean further loss of revenue or overtime pay for employees working to restore systems and clear backlogs.

There may also be additional losses from liabilities to third parties. System failures may have legal consequences, such as claims for breach of contract from customers whose goods or services are not delivered and who in turn suffer loss. One example of this is that Delta Airlines is reportedly seeking to recover losses from CrowdStrike in the vicinity of USD550 million. An affected business may also lose custom because of damage to its reputation, as customers see the issue as a sign of unreliability, resulting in reputational damage, market share erosion and long-term loss of business.

There may also be shareholder claims against an affected company and possibly its directors. CrowdStrike's shareholders have reportedly launched a class action alleging misleading statements about its software testing.

Insurance response

The resulting business losses from the CrowdStrike outage have been estimated to cost US Fortune 500 companies around USD5.4 billion. However, the insured losses will likely be around only 10% to 20% of that figure. One reason for is that the non-malicious nature of the attack typically reduces or limits the standard cyber insurance coverage.

Insurance policies that may provide coverage in the event of an IT outage, and that should be reviewed to ensure adequate coverage is in place, are as follows:

1. Cyber insurance

Cyber insurance typically covers losses resulting from malicious cyberattacks. Importantly, many New Zealand cyber insurance policies do not extend coverage to losses resulting from non-malicious outages or actions by authorised users. Even if there is some cover, it may be limited to direct losses such as the cost of data recovery and system restoration, but exclude consequential losses, lost profits or reputational damage. Depending on the cause and consequences, businesses may find themselves unprotected for losses resulting from an infrastructure or software failure.

2. Fidelity / crime insurance

Fidelity or crime insurance protects businesses from losses due to dishonest acts such as fraud or theft, including, under some policies, cyber crime perpetrated by employees or third parties. Again, however, it typically does not cover losses caused by non-malicious cyber failures.

3. Business interruption insurance

Traditionally, this coverage applies to revenue loss arising from events causing physical damage such as from a fire or natural disaster. Whilst software-related issues are typically excluded, other than in dedicated cyber insurance, some policies are able to be expanded to cover losses due to cyber failures. However, many of these policies have "deferment periods," meaning coverage for loss only applies after a specified period of downtime.

4. Professional indemnity insurance

This type of insurance covers the legal and financial consequences of a failure to deliver services due to an outage, or a data breach. Businesses should ensure that their professional indemnity insurance includes cover for cyber failures to an appropriate level of cover.

5. Statutory liability insurance

While this type of insurance does not directly cover operational or financial losses from cyber failures, it can be relevant if a business is found to have breached specific regulatory obligations such as privacy laws as a result of system downtime or data loss. Statutory liability insurance can help cover legal costs and penalties associated with a breach.

6. Technology liability insurance (including errors and omissions)

For companies in the technology sector, this insurance typically covers financial losses caused by errors in software or technology services. In cases like the CrowdStrike update failure, this type of policy would likely be triggered, providing coverage for the financial impact of the defective software. However, the CrowdStrike event illustrates the special risk that providers of software services face when they release a software update to large numbers of customers, in effect multiplying the potential liability.

Key considerations for insurers and their customers

Businesses and their brokers and insurers should ensure that they understand the scope of their coverage for non-malicious cyber events and be aware of any limitations. They should consider whether their policies cover losses resulting from non-malicious cyber failures such as software defects or infrastructure downtime. It is also important to review policy triggers, excesses or limits, deferment periods, and any exclusions related to third-party service providers or software issues.

Companies should also consider whether the most relevant policies provide sufficient cover for the range of possible losses. Insurers may in time consider whether cyber policies should extend cover to non-malicious cyber events.

Preventing and mitigating future risk

Insurers expect businesses to take proactive measures to reduce their exposure to cyber failures. This includes implementing robust backup systems, testing updates before deployment, updating systems where required, and having a clear incident response plan. Businesses should ensure they comply with any such requirements. The following are some key strategies to ensure that businesses who heavily rely on technology can mitigate the risk of system downtime:

1. System testing and phased rollouts

Businesses should ensure that updates and changes to critical systems are rigorously tested before they are widely deployed. Phased rollouts can also help prevent widespread disruption in the event of a failure.

2. Back-up plan and incident response plan

Businesses should maintain robust data backup systems. They should ensure they have alternative methods for key operations, such as communication and payment processing, in the event of an outage, and should ensure they have plans in place for technical troubleshooting and legal and insurance notifications.

3. Supplier resilience

Businesses should evaluate the resilience of their key suppliers and ensure that service agreements include provisions for system failures, including remedies and compensation.

4. Insurance reviews

Regularly reviewing insurance policies is essential to ensure that coverage aligns with a business's evolving risk profile. Working with an insurance broker can help businesses assess gaps in coverage and make necessary adjustments.

5. Contract reviews

Review the terms and conditions of the contract held with the relevant technology provider. Understanding any relevant contractual limitations (such as limitation of liability) is crucial to assessing risk exposure and the ability to recover losses from the provider.

Concluding remarks

The recent CrowdStrike outage highlights that, whilst businesses may be well prepared for – and insured for – cyber crime, they must also be prepared for the less glamorous but equally damaging risk of non-malicious system failures. With the right insurance coverage, proactive risk management and comprehensive recovery plans, businesses can protect themselves from the financial and operational impacts of these unexpected events.

The outage also highlights the risk to IT service providers who are in the business of providing software updates to large numbers of customers. While the potential loss to each customer may be small, many small claims can add up to very significant liabilities, as CrowdStrike is discovering.

Insights from the NZILA Conference:

Insurance, climate change and the law

Authored by Olivia de Pont, Senior Associate

MinterEllisonRuddWatts was pleased to sponsor the international keynote speaker session at the New Zealand Insurance Law Association's annual conference in September.

Dr Franziska Arnold-Dwyer appeared by audio-visual link from London to speak on issues arising from the intersection of insurance, climate change and the law. Dr Arnold-Dwyer, an Associate Professor of Law at University College London, frequently speaks on sustainable insurance topics, and her book *Insurance, Climate Change and the Law* was published earlier this year. She has published widely on insurance law and is one of the editors of the next edition of MacGillivray on Insurance Law.

Our experts discuss and reflect on the themes raised by Dr Arnold-Dwyer in her keynote presentation.

Climate litigation is increasingly being used as an "enforcement strategy" to force climate action"

Dr Franziska Arnold-Dwyer

Insurers as climate risk carriers

The insurance sector is at the front line of climate change, as it meets the challenges of paying the insured costs of increasingly severe climate-related loss events and making provision for future claims. Dr Arnold-Dwyer spoke about the complex range of risks that climate change poses for insurers. She has broadly classified these risks into three groups: physical risks, transition risk, and liability and litigation risk.

Physical risk

Climate change poses obvious physical risks for insurers, with extreme weather events increasing both claims costs and claims risks for property / material damage, business interruption and life insurance policies. Recent, local illustrations of the physical risks posed by extreme weather events are, of course, the Auckland Anniversary floods and Cyclone Gabrielle, which together saw insurers pay out over more than NZD3 billion across more than 112,000 separate claims.

Extreme weather events may also pose a risk for insurers' investments if those investments are vulnerable to physical risks, placing further financial pressure on insurers at times when claims are high.

These risks have flow-on effects for premium costs and the availability of insurance. This is a live concern, with the Reserve Bank reporting in May 2024 that premium costs in New Zealand have outstripped inflation over the last decade. We have previously predicted that the pressures of climate change risks may result in a partial retreat by insurers from the market: see our article here.

Transition risk

Additional risks arise from the process of transitioning to a net zero or low carbon economy. The regulatory burden on insurers is continuing to increase, with all licensed insurers with more than NZD1 billion in total assets, or annual gross premium revenue of more than NZD250 million, now required to produce climate statements in accordance with the Financial Markets Conduct Act 2013. A failure to comply with this disclosure regime will carry significant financial penalties, and regulators are not the only party that will be keeping an eye on compliance with the climate-related disclosure regime. Australia has already seen proceedings issued by shareholders against companies who allegedly fail to disclose information about climate change-related business risks: see our discussion of *McVeigh v Retail Employees Superannuation Trust*.

Other examples of transition risk include:

- reductions in the value of insurers' investments if their owners and managers do not adapt;
- new technologies – while new technologies bring business opportunity, novel areas are also difficult to price accurately; and
- reputational risk arising from insufficient action.

Liability and litigation risk

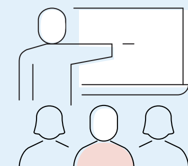
Litigation is also a significant area of risk. Insurers may face direct litigation and pecuniary penalties if they fail to comply with their climate-related disclosure obligations or make misleading statements about sustainability (that is, greenwashing). Climate litigation also poses risks to insureds, leading to claims under their liability policies or their director's and officers' insurance policies, all ultimately affecting risk pricing and potentially the availability of cover.

Climate litigation is increasingly being used as an "enforcement strategy" to force climate action and accordingly there is, as Dr Arnold-Dwyer highlighted, a need for climate litigation risk models to identify and evaluate these risks, particularly so that insurers continue to meet their solvency capital requirements.

Key themes

Insurers as climate risk carriers

Insurers as enablers



Public private partnerships

Dr Arnold-Dwyer also spoke to climate litigation in the UK and Europe, where there has been a measure of success for plaintiffs. For example, in *R (on the application of Finch on behalf of the Weald Action Group) (Appellant) v Surrey County Council,* in June 2024, the UK Supreme Court considered Surrey County Council's decision to grant planning permission to an oil company to produce hydrocarbons for a 25-year period. Ms Finch, on behalf of Weald Action Group, argued that it was unlawful for Surrey County Council not to require the applicant's environmental impact assessment to include an assessment of the impacts of greenhouse gas emissions arising from the eventual use of that oil as fuel (known as "scope 3" emissions). The Supreme Court agreed. While the case made clear that the production of scope 3 emissions does not preclude the granting of a permit, the Supreme Court's decision may impact the process for how approval is sought, and will incentivise litigants to challenge planning decisions where there are flaws in the process followed.

Dr Arnold-Dwyer also spoke to *ClientEarth v Shell plc*, a derivative action bought by ClientEarth, a shareholder of Shell plc, alleging that Shell's directors were in breach of their duty to act in the best interests of the company, including having regard to the company's impact on the community and environment, by failing to properly address the risks of climate change through its operations. While the claim was dismissed, demonstrating the courts' traditional reluctance to interfere with business decisions made by directors and management, this case demonstrates the potential risks of activist claims upon directors.

Climate change litigants have also enjoyed a measure of success in New Zealand, with our Supreme Court allowing claims brought by a climate change activist to proceed to trial in *Smith v Fonterra*. This judgment demonstrates a willingness of the courts to hear novel claims and a reluctance to strike out such claims even where the chances of success may remain low – which will impact on any insurer who may be on risk for defence costs. Our discussion of that case and the *ClientEarth* case may be found here.

Insurers as enablers

Having traversed the range of risks which climate change poses, Dr Arnold-Dwyer briefly introduced her vision for the insurance industry supporting others to take climate mitigation action. For example, she suggested that insurers may:

- Insure environmentally friendly infrastructure projects and invest in projects that allow the financing and development of "green" products. Dr Arnold-Dwyer has encouraged insurers to look for new opportunities to develop projects and invest in climate-friendly opportunities.
- Facilitate a managed withdrawal from greenhouse gas emitting activities. While there is no current requirement for insurers to withdraw cover for large emitters, Dr Arnold-Dwyer warned of the impact of a reactive and disorderly withdrawal and encouraged insurers to start planning for a managed withdrawal.
- Adapting existing insurance products in ways that allow policyholders to shift behaviours, take mitigation measures and assist in activities enhancing climate change preparedness. Dr Arnold-Dwyer suggested that insurers could use existing communication networks to develop green products, reward policyholders for adopting sustainable practices, and use policy wording to encourage and deter behaviours. At claims time, insurers can use claims as an opportunity to 'build back better' and invest in future climate change resilience.

These ideas warrant further examination, as the risks associated with climate change continue to compound.

Public private partnerships

Finally, Dr Arnold-Dwyer spoke to the partnerships which have arisen between the public and private sectors to address insurance gaps, with the Flood Re Scheme operating in the United Kingdom to provide subsidised reinsurance to insurers that cover high flood risks, and our own Toka Tū Ake Natural Hazards Commission. However, while there are benefits to these schemes in the form of high penetration of insurance that might otherwise not be available, it is not clear that Government-led partnerships are the best mechanism for creating incentives to mitigate risk or build resilience in a way that will be sustainable in the long term.

Dr Arnold-Dwyer's session was a useful reminder of the many ways in which the need to take action in response to climate change is affecting the insurance industry and is likely to affect it further in the near future. The good news is that climate change offers the insurance industry opportunities as well as risk.

Key insights for insurers:

The first wave of climate statements

Authored by Lloyd Kavanagh, Partner and Hannah Cross, Solicitor

We are now more than halfway through New Zealand's first year of mandatory climate statements, with the next round of climate statements due at the end of October as part of June reporting periods.

As at 25 September, seven licensed insurers have lodged – two being general insurers and the remainder life insurers. 15 banks have also lodged, though that includes dual registered banks lodging climate statements for both the overseas branch and a local subsidiary. Many other licensed insurers have June year-ends and will be lodging by 31 October.

We set out some key observations that are relevant to those 'large' licensed insurers with over NZD1 billion of assets or NZD250 million net written premiums who are required by the climate-related disclosures regime to prepare and lodge climate statements, complying with the Aotearoa New Zealand Climate Standards (**NZ CS**).

Particular insights for insurers

From the climate statements that have been lodged on the Climate-related Disclosures Register, it is clear that climate reporting entities (**CREs**) have put a great deal of time and effort into preparing these documents. As we are still in the early days of the climate-related disclosures regime, market practice is very much still evolving. But we are already seeing some key themes as to what entities are doing well, and not so well.

Style and approach

There has been a wide spectrum of approaches so far. The climate statements to date have ranged from 6 to 129 A4 pages – though those at the longer end have been fund managers whose documents cover multiple funds. The seven insurers'

statements so far have been between 20 and 28 pages. The banks' statements are typically twice as long. There is variety in the style of the document too, with some making greater use of images, diagrams, and tables.

While the great majority of CREs so far have published standalone climate statements, approximately 6% have integrated them within their annual report, and 12% within a broader sustainability report. Integrated disclosures are permitted under the NZ CS but when doing so you must include a detailed table of references identifying where primary users can find the location of the prescribed disclosures.

Some CREs have chosen not to follow the structure of the four pillars within NZ CS 1 (Governance, Strategy, Risk Management and Metrics & Targets), with Strategy often being at the front of the document. The logic we understand is that users are more interested in what CREs are doing than who is making the decision.

Though not strictly required by the NZ CS in a standalone climate statement, often a table of references or index of the prescribed disclosures in this case too can assist with readability.

We expect the reason for such variety in approach is because CREs have been making internal decisions that the level of detail, structure, or way in which the information is presented, is appropriate for their "primary users". Always having "primary users" front of mind during preparation of the climate statements is crucial, because that is the prescribed, intended audience by way of the materiality threshold in NZ CS 3.

For insurers, the largest group of primary users is most likely to be the CRE's investors and creditors. While policyholders are technically not primary users – at least until they make a claim – they will be some of the stakeholders who may also be interested in the climate statements.

Current and anticipated impacts of climate change

CREs are now well aware of the distinction between physical impacts (i.e. directly or indirectly attributable to the physical aspects of climate change) and transition impacts (e.g. directly or indirectly attributable to the actions taken by governments and markets to transition to a low-emissions, climate-resilient future).

Insurers are in the business of managing risk and general insurers tend to be highly focused on climate-related risks and adapting to weather events that can have large scale impacts on their policyholders and accordingly their business i.e. physical impacts. However, transition impacts that result from societal or regulatory change can have significant impacts on insurers too, so it is important for insurers to be thinking about how markets be, government and shifts in consumer preferences are affecting their business too – both positively and negatively.

An observation is that in relation to the requirement to disclose a CRE's current and anticipated climate-related impacts, it is important to disclose how the particular CRE has been impacted, as opposed to simply disclosing an event that occurred in the reporting period.

Targets

As part of the Metrics & Targets pillar in NZ CS 1, many CREs have been disclosing greenhouse gas (**GHG**) emission targets. Though everything in the climate statement must be substantiated, substantiating targets requires CREs to have a robust, clear action plan that it reasonably believes will lead to the achievement of that target. This is an area the Financial Markets Authority (**FMA**) has called out where some of the climate statements lodged to date have not had enough detail.

Coherent, effective disclosure

Both the External Reporting Board (**XRB**) and the FMA have publicly stated that at least some CREs are not focussing enough on the requirements of NZ CS 3. The NZ CS 3 principles complement the fair dealing provisions in Part 2 of the Financial Markets Conduct Act 2013; having regard to principles like Understandability, Balance, and Coherence will have flow on effects in terms of ensuring that the disclosure of targets or other statements made within the climate statement do not amount to inadvertent greenwashing by way of false or misleading representation. And NZ CS 3 contains some specific required disclosures that have been overlooked in some cases.

GHG assurance engagements

The requirement for CREs to obtain limited assurance of their GHG emissions does not come into force until next year (for reporting periods ending on or after 27 October 2024), however some CREs have chosen to obtain voluntary assurance. Many of those CREs getting voluntary assurance did not disclose the assurance report in the climate statement: This is key for providing full transparency to primary users as to whether the assurance had any qualifications, limitations or assumptions.

International reporting regimes

Many insurers have overseas parents or have a presence in another jurisdiction, such as Australia. Operating within an overseas group adds to the challenge of preparing climate statements, due to the misalignment of climate reporting regimes both in terms of a timing but also what is required to be disclosed. In September 2024, the Australian Parliament, Parliament passed the Treasury Laws Amendment (Financial Market Infrastructure and Other Measures) Bill 2024 (Cth) which paves the way for the implementation of a mandatory climate-related disclosures regime.

The XRB is closely following the international developments with the International Sustainability Standards Board (**ISSB**) Standards 1 and 2, and the still to be finalised Australian Accounting Standards Board's (**AASB**) standards (which have been issued in exposure draft form, will more closely follow the ISSB Standards, than the NZ CS did). The XRB published a report in 2023 comparing the NZ CS with the ISSB in 2023, and intends to undertake a review of the NZ CS in light of these international regimes in December 2025.

New Zealand has an estimated 200 CREs required to lodge climate statements, whereas Australia is estimated to have about 20,000 entities which will eventually be captured"

Generally, the Australian requirements will be much more granular than New Zealand's principles-based approach, and some have estimated the cost of compliance is roughly twice that for the NZ CS. But there are some elements e.g. the requirement to have three scenario narratives under NZ CS versus two under ISSB and AASB, which means that overseas documents will not automatically meet the New Zealand requirements.

The coverage in Australia will eventually be much broader too. NZ has an estimated 200 CREs required to lodge climate statements, whereas Australia is estimated to have about 20,000 entities which will eventually be captured in three phases: initially large public companies (500,000+ employees and NZD5 million+ revenue), then medium (250+ employees and NZD200 million+ revenue) and in 2026, smaller companies (100+ employees, NZD50million+ revenue).

FMA feedback

Having finished reviewing the December and January year-end climate statements lodged in April and May, the FMA is now in the midst of reviewing all of the climate statements that were lodged by 31 July in line with a March year-end.

Some CREs will be receiving individual feedback letters from the FMA where there are significant matters that need to be addressed. If there are more minor points that can be easily resolved, such as not including the required link in a CRE's annual report to its climate statement, or not having two directors sign the climate statement, the FMA may send an email for this to be addressed quickly. But the FMA has been clear that it has not and will not have time to write to everybody.

The FMA will be providing general feedback in a monitoring report they are intending to publish end of November or early December, based on what it has seen in a detailed review of as many of the statements as it can cover before then. This will be an important document to read as CREs get ready to prepare their second climate statements – those with December year-ends are already well underway with preparations.

The FMA has already been out and about speaking to their findings so far too. At a recent INFINZ seminar which MinterEllisonRuddWatts hosted, FMA's Jacco Moison's observations included:

1. They have seen limited disclosure in some cases of the underlying methods and assumptions, and data and estimation uncertainty used in the preparation of climate-related disclosures. This was particularly in relation to GHG emissions and scenario analysis disclosures. In future, they will be looking for more comprehensive disclosures for these NZ CS 3 prescribed requirements.

2. There had been some cases of insufficient disclosure of the nature of assurance obtained over GHG emissions and other verification or assurance services, where the CRE had chosen to refer to assurance ahead of the mandatory requirement to do so. Following the first climate statements, the FMA has engaged with all assurance providers to highlight areas to focus on for the mandatory assurance which applies from October 2024 onwards.

3. CREs also needed to ensure they disclose how they have actually been impacted by climate-related events rather just disclosing that an event happened. For example, disclosure that Cyclone Gabrielle happened without also disclosing what impact (if any) that had on the entity is not sufficient.

4. The language used in some climate statements to describe the link between climate-related risks and opportunities and capital deployment didn't always provide a clear picture. This was relevant in relation to how the short-, medium- and long-term time horizons for climate-related risks and opportunities are linked (if at all) to strategic planning horizons and capital deployment plans. Moison pointed out that if there was no link, then it was appropriate to say so, but general statements indicating a link – but not describing how they are connected – were not enough.

Overall, however, Moison indicated that the FMA was generally pleased by the proactive approach CREs had taken to the regime without much time to prepare. But that doesn't mean that the FMA will not have higher expectations in the years to come.

These various mediums by which the FMA is providing feedback aligns with the key message that the FMA has continued to reiterate – namely, is that they are taking a constructive and educative approach to monitoring in this first year, in line with their Climate-related Disclosures Monitoring Plan 2023–2026 published last year.

Get in touch with one of our experts if you would like to discuss any of our observations above, or your climate reporting obligations generally.

Case study

Subrogation clarified

Authored by Olivia de Pont, Senior Associate

In *Royal & Sun Alliance and Ors v Textainer Group Holdings and Ors* [2024] EWCA Civ 547, the UK Court of Appeal clarified and affirmed longstanding subrogation principles which determine what happens when insurers make payments to an insured who subsequently makes a recovery in respect of the same loss.

While the fundamental principles of subrogation rights are well established, their application is not necessarily straightforward where there are multiple excess layer insurers and the insured's total loss exceeds the level of indemnity – as was the case in *Textainer*.

A refresher on subrogation

Subrogation is the principle which allows an insurer which has indemnified its insured for a loss to step into the insured's shoes, and seek recovery from the third party who caused the loss.

The primary justification for the rule is that an insured should never recover more than an indemnity for their loss. In the absence of the insurer's right of subrogation, an insured could receive full payment of its loss under an insurance policy and then make a further recovery for the same loss by suing a liable third party. Under the principle of subrogation, any funds recovered from liable third parties are held in equity for the insurer.

Although parties to a contract of insurance are free to agree a different approach to the allocation of recoveries from third parties, the default position is the "top down" approach adopted by the House of Lords in *Lord Napier and Ettrick v Hunter* [1993] AC 713. Following this approach, also referred to as the "*Napier*" principles, recoveries from liable third parties are allocated:

- first, to any uninsured losses (excluding any excess) meaning that the insured benefits;
- secondly, to any insured losses, meaning that the insurer benefits; and
- lastly, to reimburse any excess paid by the insured, meaning that once again, the insured benefits.

Allocating recoveries can become complex where an insured loss is covered by multiple insurers who provide layers or tiers of cover. By way of example: isurer A insures the first $100,000 of any loss; insurer B insures the next $100,000 (i.e. the $100,000 in excess of $100,000); and insurer C insures a third $100,000 ($100,000 in excess of $200,000), so that total cover is $300,000. According to the *Napier* principles, recoveries are allocated top down, starting with insurer C. This is because C has agreed to pay only if A's and B's policies are insufficient to cover the loss. Similarly, B has agreed to pay only if A's policy is insufficient to cover the loss.

The application of the *Napier* principles in *Textainer*

The *Napier* principles were challenged, but ultimately affirmed, in an appeal brought by several insurers in the UK Court of Appeal against companies in the Textainer Group.

The Textainer Group is one of the largest container lessors in the world. In 2016, one of Textainer's lessees, Hanjin Shipping Co, entered into receivership while in possession of approximately 113,000 of Textainer's containers. This caused Textainer to suffer an agreed USD101,856,624 in losses, being the cost of retrieving and repairing its containers, along with the value of unrecovered containers and lease payments which remained unpaid.

Textainer had in place a container lessee default insurance programme with the following structure:

a. A USD5 million excess to be borne by Textainer.

b. A primary insurance policy of USD5 million above the excess.

c. Five excess layer insurance policies which together with the primary policy provided cover totalling USD80 million above the excess, comprising;

   (i) a first excess layer policy of USD5 million for losses above USD10 million;

   (ii) a second excess layer policy of USD5 million for losses above USD15 million;

   (iii) a third excess layer policy of USD25 million for losses above USD20 million;

   (iv) a fourth excess layer policy of USD10 million for losses above USD45 million; and

   (v) a fifth excess layer policy of USD30 million for losses above USD55 million.

Losses above USD85 million were uninsured.

Of the USD101,856,624 in losses, Textainer's insurers paid a total of USD75.1 million. The limits of the primary policy and the first to fourth excess layer policies were exhausted, and a discounted settlement was agreed in respect of the fifth excess layer policy, which comprised USD25.1 million, below the USD30 million fifth excess policy cap.

Accordingly, Textainer's uninsured losses were approximately USD21 million (excluding the USD5 million excess). However, to complicate matters, as part of the insurance settlement, Textainer was assigned the subrogation rights of the fourth and fifth excess layer insurers under the relevant settlement agreements.

Textainer subsequently recovered USD25,886,647.60 from Hanjin in partial settlement of Textainer's claims against it. The insurers of the primary and first to third excess layer policies then argued that they were entitled to a share of the Hanjin settlement proceeds. Textainer disagreed.

On appeal, the key question was whether the Hanjin settlement proceeds were to be applied in accordance with the top down approach, as Textainer argued, or whether the excess layer insurers who had not settled with Textainer were entitled to pro rata shares of the recovery.

Attempting to circumvent the *Napier* principles, the insurers argued that there is a distinction between a single or "unitary" loss, where recoveries should be allocated top down, and the circumstances of the Textainer case, which involved multiple losses of different items of property at different times. The insurers argued that recoveries in respect of each individual item must be allocated to the insurer that indemnified that loss.

The Court rejected this, commenting that it was an "overly formalistic and largely theoretical approach" which did not conform with the underlying rationale of subrogation and was not supported by the terms of the policies or the manner in which the claims were dealt with.

In dismissing the insurers' claim, the Court made two key observations:

- On the insurers' case, an insured's position would be worse if recoveries were made following insurance payouts than if the recoveries occurred first.
- If the Hanjin settlement proceeds were not applied top down, Textainer would not be fully indemnified to the extent of the policy limits.

As Textainer had been assigned the subrogation rights of the fifth excess layer insurer, applying the top down approach, it was entitled to retain the entirety of the Hanjin settlement sum.

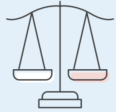
Conclusion

While the facts of this case were somewhat unusual, it is a helpful confirmation that the principles of subrogation where there are multiple insurers are straightforward and should not be overcomplicated. The case is also a cautionary tale for insurers and their lawyers who may be tempted to settle with insureds on terms in which they waive rights of subrogation, particularly where other insurers may not be doing the same.

2024 – A good year for 'technical' limitation defences

Authored by Nick Frith, Partner

Statutory time bars and contractual limitations of liability can be powerful weapons in a defendant's armoury. Recent decisions have highlighted the importance of keeping limitations defences front of mind for parties to potential claims. They also illustrate some of the nuances that may apply when determining whether a claim may be time-barred or limited by agreement.



Statutory limitation periods

Statutory limitation periods act as a complete bar to obtaining relief in civil proceedings, once the relevant statutory time period has expired. It is critical for defendants to consider limitation issues early when a dispute or a potential claim arise, to avoid:

- inadvertently taking steps which might re-set the limitations clock, such as an acknowledgement of liability or a part payment; or
- settling a claim for which a limitation period is about to expire, given the possibility that the claimant may not issue proceedings in time.

For almost all claims now, the Limitation Act 2010 is the statutory regime that imposes time-bars, with the express purpose of encouraging claimants to enforce their claims without undue delay. It applies to civil proceedings in courts, tribunals and arbitrations.

The most common limitation period that arises in the commercial context is the six-year time limit for "money claims", which encompasses claims for monetary relief at common law, in equity or under an enactment. However, the limitation period is shorter for some types of claims. For example, claimants have:

- 90 days to raise a personal grievance under the Employment Relations Act 2000 (same for claims relating to sexual harassment when the limitation period is 12 months).;
- two years to pursue a defamation claim; and
- three years from when the plaintiff knew or ought to have known of its loss or damage to bring a claim relating to contraventions of the Fair Trading Act 1986.

Parties to contracts may agree to alter the limitation period or contract out of the Limitation Act 2010 altogether. This is particularly important when considering claims under service contracts and sale and purchase agreements, which may contain terms that bar claims brought after very short periods of time, such as 18 months. It was once not unusual for insurance policies to bar claims where proceedings were not issued within as short a period as a year after the loss was suffered, although this is no longer common.

In some circumstances where the claimant has late knowledge of certain facts relevant to their claim, the statutory limitation period may be extended up to 15 years from the date of the act or to omission on which the claim is based. The limitations clock may also start to run again if the defendant has acknowledged liability or has made a part payment in respect of the liability. Construction claims have a 10-year long-stop for limitations purposes.

When deployed successfully, limitation defences are a complete answer to claims that would otherwise be meritorious. When considering a dispute resolution strategy, it is therefore vital to assess whether a limitation period is about to come into effect or whether a limitation defence is already available. Unnecessary legal costs may be avoided by bringing an enforceable limitation period to the attention of the plaintiff and persuading them not to commence proceedings, or by applying to dismiss claims that have been brought out of time.

Statutory time bar cases

We discuss below four cases from 2024 involving statutory time bars and contractual limitation defences, and highlight some of the nuances that may apply.

Case 1

Whangārei District Council v Daisley [2024] NZCA 161

In 2004, Mr Daisley purchased some land, including a long-established quarry. Shortly after he began working the quarry, the Whangārei District Council asserted that he did not have the necessary resource consent to do so. Mr Daisley maintained that the quarry enjoyed existing use rights, but over a period of five years, the Council sought to prevent him from quarrying the area by issuing abatement and enforcement notices and eventually seeking an enforcement order in the Environment Court.

The Council did not search certain hard copy records it held until asked to do so by Mr Daisley's solicitor in September 2009. These searches revealed that a land use consent had been issued for the quarry in 1988. The Council had, therefore, been wrong to prevent Mr Daisley from working the quarry. Preventing him from exploiting the quarry to its full potential had a detrimental impact on his finances, ultimately forcing him to sell the property to avoid a mortgagee sale. However, Mr Daisley waited until August 2015 to commence proceedings against the Council, alleging negligence and misfeasance in public office.

Limitation issues – extension of time for continuing breach and fraudulent concealment

The main issue in the case was whether Mr Daisley's claim was barred by the Limitation Act 1950, the predecessor to the Limitation Act 2010, which would ordinarily prevent claims being brought after six years following the accrual of the relevant cause of action (unless the default time period was extended).

The High Court held that the Council's limitation defence failed because Mr Daisley's cause of action accrued on a continuing basis or had been concealed by fraud within the relevant statutory meaning.

The Court of Appeal overturned the High Court's decision, in part on the basis that while there might have been a continuing breach of duty, there was no allegation of such a breach within the six-year limitation period. However, Mr Daisley's negligence claim was not time-barred, because of a narrow exception to limitation defences in cases of fraudulent concealment. This exception applied to the negligence claim because Council officers were provided with credible information that their records might contain evidence of existing use rights but had failed to search for that evidence. That failure was subjectively reckless and amounted to fraudulent concealment. This exception did not, however, apply to Mr Daisley's misfeasance claim, as there was no subjective recklessness by the Council officers as to the limits of their authority.

Although Mr Daisley was partially successful in defeating the Council's limitation defences, but for the exception for fraudulent concealment, his claim, which was substantial, may have been denied in its entirety.

The Supreme Court has granted leave to appeal the Court of Appeal's judgment, so the story of this claim may not be over yet.

Case 2

Tasman District Council v Buchanan & Ors [2024] NZCA 133 – The longstop statutory time bar under the Building Act 1991

In 2008, Ms Buchanan and Mr Marshall purchased an architecturally designed home oriented around a swimming pool which was built in accordance with a building consent in 2004. The property was issued a code compliance certificate in 2006, two years before the purchase. Unfortunately for the purchasers, despite no issues arising from Council inspections in 2009 and 2012, the pool fencing was found to be non-compliant when the property was again advertised for sale in 2019. The owners remedied the non-compliant fencing and issued proceedings against the Council in 2020 seeking compensation for the costs of doing so and the diminution in value caused by the loss of amenity and aesthetic value.

On appeal, the Court held that when the Council carried out inspections in 2009 and 2012, those inspections did not contribute to the existence of any defects in the property. Those defects had existed from 2006, and the Council did not owe any duty to take reasonable care to protect the property owners from the loss of litigation rights against it. The owners' claim was arguably a claim relating to the original building work in 2004–2006, and while the Court did not need to decide the point, it expressed a view that the 10-year longstop limitation applied from the date of the property's original construction so as to bar any such claim, not when the negligent inspections took place. This was because:

- there was no physical change in 2009 or 2012 – these were inspections of an already constructed pool; and
- if the limitation clock could be reset by subsequent failures to identify defects, time could run indefinitely in respect of these claims, which would be inconsistent with the purpose of the 10-year longstop.

This case illustrates the potentially harsh consequences that limitation defences can have for claimants. This claim was time-barred, even though the plaintiffs acted promptly once they become aware that they had a claim.

Case 3

Hobday v Selwyn District Council [2024] NZHC 550 – An unusual limitation issue – late service of a claim once filed

On 17 October 2022, Mr and Mrs Hobday filed proceedings against the Selwyn District Council and the vendors of a property they purchased in 2014, alleging that the property was not watertight. The Hobdays had filed proceedings within the 10-year longstop date under the Building Act 2004 (by one day). However, they subsequently failed to serve their claim within 12 months of filing.

Under r 5.72 of the High Court Rules, statements of claim must be served within 12 months of being filed. Failure to achieve service results in the proceeding being treated as discontinued unless an extension is granted.

In this case, by what appears to have been an oversight by the Hobdays' solicitor, the statement of claim was not served in time. This meant that the Court would need to grant an extension of time for service if the Hobdays were to have the ability to pursue a remedy against the Council. The High Court declined to grant the extension, finding that in the circumstances, the Council was the innocent party vis-a-vis the delay and there was not a good reason to grant an extension of time. In reaching this view, the Court stressed the importance of the 10-year longstop: *"Part of the reasoning for the long stop is that conducting litigation 10 years after the events in issue involves self-evident difficulties in respect of inter alia the availability of witnesses, the dimming of memories and the availability of records."*

Case 4
Beca Carter Hollings & Ferner Ltd v Wellington City Council [2024] NZSC 117 – Claims against third parties

In this case, the Supreme Court clarified that the 10-year longstop provision applicable to construction claims under the Building Act 2004 does not affect the right of defendants to claim contribution from joint tortfeasors. Contribution claims are subject to section 34 of the Limitation Act, which allows a defendant two years to pursue joint tortfeasors from the date on which their liability to the original plaintiff is quantified.

This case concerns the allegedly defective design of a building by Beca, who issued a producer statement for the building in March 2008. BNZ filed proceedings against Wellington City Council in August 2019, alleging that it was negligent in issuing consents and approvals for the building.

The next month, the Council filed a third party notice against Beca, seeking contribution in the event that it is liable to BNZ. Beca applied to strike out the claim against it on the basis that the Council's claim had been brought more than 10 years since its alleged negligent act or omission.

In a majority judgment, the Supreme Court noted that the purpose of the 10-year longstop period is to provide finality and certainty, while the contribution regime was intended to remedy the injustice that may occur if a defendant's ability to pursue contribution from responsible parties is at the whim of the plaintiff's choice of defendant. The Court considered that effect must be given to both of these regimes. Accordingly, the 10-year longstop period applies to the primary claim and, from the point that the defendant's liability is quantified, they have two years to issue proceedings against any joint tortfeasors.

Contractual limitations of liability

Tauranga City Council v Harrison Grierson Holdings Ltd & Anor [2024] NZHC 714

In a recent judgment, the High Court considered the effect of limitation of liability clauses in the ACENZ/IPENZ Conditions of Contract for Consultancy Services (**CCCS**) and Short Form Agreement (**SFA**), which are standard form consultant agreements in the construction industry.

This case concerned the design of a transport hub. The Tauranga City Council had engaged Harrison Grierson to produce the structural design for this hub, as well as PS1 and PS4 producer statements. The CSSS entered into with Harrison Grierson limited its liability to *"five times the fee, with a minimum amount of $500,000 and maximum liability of $2,000,000"*. The Council also engaged Constructure Auckland to peer review Harrison Grierson's design and provide a PS2 producer statement under an SFA. The SFA also limited Constructure's liability to *"five times the fee (exclusive of GST and disbursements) with a maximum limit of $500,000".* Standard limitation clauses were also included in Harrison Grierson's PS1s and Constructure's PS2s.

Substantial re-design work was required due to issues which arose during the delivery phase of the work. The Council ultimately abandoned construction and sold the site to the main contractor for $1. It then issued proceedings against Harrison Grierson and Constructure, seeking more than $26 million in damages. However, the Court held that the limitation of liability clauses in the CCCS and SFA operated to limit liability arising under the Building Act, the Fair Trading Act and for negligent misstatement. The limitation clauses in the producer statements, however, were not effective as the Court held that it was the contracts between the parties which determined the extent of liability – not the terms of the producer statements.

This case confirms that limitation clauses will be enforced on their own terms. It also cautions against relying on limitation clauses in producer statements, as these will be subordinate to the terms of the consultant agreement and any limitation clauses they contain.

We considered this case in more detail in a recent legal update by our Construction and Infrastructure team which can be accessed here.

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