

How Much Does It Cost To Replace A Navy Patrol Boat? 31.5 Million!

DMS Maritime Pty Limited v Royal & Sun Alliance Insurance Plc [2018] QSC 303

Key Point

- When an insurer denies liability for a claim, or allows its insured to resolve a potentially insured loss against a third party, it loses control of the process. When this occurs, a Court will allow an insured significant discretion as to the terms on how it resolves the third party claim.

Background

The plaintiff was a ship builder that had a contract with the Commonwealth to design, manufacture and supply Navy patrol boats, plus provide the government with service support for a 15-year period. On 11 August 2014, one of the boats, the HMAS Bundaberg, was destroyed by fire.

Pursuant to the contract, the plaintiff became liable to indemnify the Commonwealth against "... any loss or damage to the [Bundaberg]" and also to "promptly replace or otherwise make good any loss of ... the [Bundaberg]". There was no dispute that the insurer had insured the plaintiff for the contractual liability assumed under the contract.

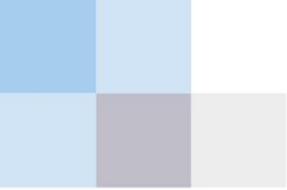
There had been a dispute between the plaintiff and the Commonwealth as to what "making good the loss" meant. Given the unique nature of the property, this was not an easy question to determine. However, in the course of negotiations between the plaintiff and the Commonwealth, the Commonwealth made a claim of \$51 million based on replacement costs which was significantly above the initial cost because the vessels were no longer in production.

For its part, the insurer had in fact argued at one stage that the vessel was valueless because there was no secondary market for it. Ultimately, and while informing the insurer of negotiations, the plaintiff settled the claim for \$31.5 million which was based on the cost of commissioning a new vessel with an alternative manufacturer. The plaintiff's evidence was that this was a good deal because the cost was based on the economies of scale of providing two vessels after hard-fought negotiations.

The Court agreed, finding that the insured had at all times acted prudently in negotiating with the Commonwealth including by conducting appropriate investigations and obtaining legal advice.

The Decision

In assessing the reasonableness of the settlement, the Court applied the leading case of *Unity Insurance Brokers Pty Ltd v Rocco Pezzano Pty Ltd* which summarised the following propositions:

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- (a) The test of reasonableness an objective one.
 - (b) Evidence of the advice which the insured received to induce it to enter into the settlement is not proof in itself of the reasonableness of the settlement.
 - (c) Evidence of the receipt of the advice is relevant but what will usually be much more important is the reasoning that supported that advice.
 - (d) The reasonableness of a settlement depends on the circumstances existing at the time, provided the plaintiff has acted reasonably in discovering the circumstances material to the settlement.
 - (e) Reasonableness is not to be judged according to whether material which was obtained later shows that a different result might have been obtained.
 - (f) Consideration will often be required of whether the party maintaining that the settlement was reasonable had made sufficient enquiries.
 - (g) In making that enquiry, attention may need to be given to whether the cost of seeking further information would outweigh the benefit.
 - (h) What is a reasonable compromise of the claim will almost always require consideration of the chances of the parties succeeding in their respective claims or defences.

In considering the above propositions, the Court had no difficulty in finding that the settlement was reasonable and therefore the insurer was liable to reimburse it.

Lessons Learnt

From time to time, insurers are faced with decisions as to whether to allow an insured to resolve a claim itself or to take over the conduct of a matter. We obviously do not know the commercial realities of this matter and whether this was possible.

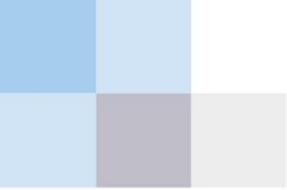
However, this case is a timely reminder that either pursuant to a request, or due to a denial of indemnity which is later reversed, if an insurer allows the insured to take conduct of a claim made by a third party, Courts will allow the insured significant leeway in what it considers a reasonable resolution of a claim.

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