HIGH COURT OF AUSTRALIA

FRENCH CJ,
GUMMOW, HEYDON, CRENNAN, KIEFEL AND BELL JJ

Matter No S110/2010

WESTPORT INSURANCE CORPORATION & ORS APPLICANTS

AND

GORDIAN RUNOFF LIMITED RESPONDENT

Matter No S219/2010

WESTPORT INSURANCE CORPORATION & ORS APPELLANTS

AND

GORDIAN RUNOFF LIMITED RESPONDENT

Westport Insurance Corporation v Gordian Runoff Limited [2011] HCA 37
5 October 2011
S110/2010 & S219/2010

ORDER

Matter No S110/2010

1. *Grant special leave to include, as a further ground of appeal in Matter No S219/2010, ground 5 of the applicants' draft notice of appeal.*

2. *The respondent pay the applicants' costs.*

Matter No S219/2010

1. *Appeal allowed.*

2. *Set aside orders 2, 3 and 4 of the orders of the Court of Appeal of the Supreme Court of New South Wales made on 1 April 2010 and, in place thereof, order that the appeal to that Court be dismissed with costs.*

3. *The respondent pay the appellants' costs of the appeal to this Court.*

On appeal from the Supreme Court of New South Wales

Representation

B W Walker SC with T M Mehigan for the applicants/appellants (instructed by Allens Arthur Robinson Lawyers)

I M Jackman SC with T M Faulkner for the respondent (instructed by Mallesons Stephen Jaques)

S J Gageler SC, Solicitor-General of the Commonwealth with M J O'Meara appearing as amicus curiae on behalf of the Attorney-General of the Commonwealth (instructed by Australian Government Solicitor)

D F Jackson QC with M F Holmes QC and J A Redwood appearing as amici curiae on behalf of the Australian Centre for International Commercial Arbitration Limited & Ors (instructed by Corrs Chambers Westgarth)

CATCHWORDS

Westport Insurance Corporation v Gordian Runoff Limited

Arbitration – Judicial review of awards – Section 38(5) of *Commercial Arbitration Act* 1984 (NSW) ("Arbitration Act") provided that the Supreme Court shall not grant leave to appeal on any question of law unless it considers that, having regard to all the circumstances, the determination of the question of law could substantially affect the rights of a party to the arbitration agreement (par (a)), and there is a "manifest error of law on the face of the award" (par (b)(i)) – Reinsurance treaties between respondent and appellants included arbitration agreement which required that any dispute arising thereunder be referred to arbitration to be held in accordance with and subject to Arbitration Act – Appellants appealed to Supreme Court on questions of law arising out of award – Whether leave to appeal should have been granted – Whether error of law manifest on face of award.

Arbitration – Reasons for award – Section 29(1)(c) of Arbitration Act required arbitrator to include in award a statement of reasons for making award, unless parties otherwise agreed in writing – Arbitrators delivered written award accompanied by "Reasons for Award" comprising 96 paragraphs – Nature and extent of reasons for award required by s 29(1)(c) of Arbitration Act – Whether reasons for award must be same standard as judicial reasons – Whether nature and extent of reasons for award depends upon circumstances of particular dispute.

Insurance – Statutory construction – Statutory limitation on exclusion clauses – Section 18B of *Insurance Act* 1902 (NSW) prevented insurer from avoiding liability by relying upon exclusion clause in contract of insurance where operation of exclusion clause was triggered by event with no relationship to cause of event giving rise to particular loss and claim, unless in all the circumstances it was not reasonable for insurer to be bound to indemnify insured – Respondent sought to rely on s 18B to overcome finding by arbitrators that reinsurance treaties between respondent and appellants did not respond to certain policies of insurance underwritten by respondent – Whether s 18B applicable to reinsurance treaties between respondent and appellants.

Words and phrases – "appeal", "arbitration agreement", "award", "considerations of general justice and fairness", "exclusion clause", "judicial standard", "manifest error of law on the face of the award", "question of law", "reasons", "reinsurance treaty".

Commercial Arbitration Act 1984 (NSW), ss 22, 29, 38-40.
Insurance Act 1902 (NSW), s 18B.

1 FRENCH CJ, GUMMOW, CRENNAN AND BELL JJ. This appeal and application for special leave reaches this Court from the decision of the New South Wales Court of Appeal (Spigelman CJ, Allsop P and Macfarlan JA)[1], allowing an appeal against the order of the primary judge (Einstein J) setting aside an arbitral award[2]. The essential narrative commences on 10 October 2008, when, in an arbitration conducted under the *Commercial Arbitration Act* 1984 (NSW) ("the Arbitration Act")[3], the arbitrators delivered their written award in favour of the respondent ("Gordian"). This comprised three paragraphs. It was accompanied by "Reasons for Award" comprising 96 paragraphs ("the Reasons"). Section 29(1)(c) of the Arbitration Act required the giving of reasons. One of the issues in this matter is whether the Reasons were inadequate.

The arbitration

2 The arbitrators found that at all material times Gordian underwrote professional indemnity ("PI") insurance and directors and officers liability ("D and O") insurance. Both categories of insurance customarily were written to cover the insured with respect to claims alleging prior wrongful acts, being claims made and notified to Gordian during the period of the policy. The Reasons identified a series of steps whereby Gordian (and a Lloyd's syndicate ("R E Brown")) wrote for FAI Insurance Limited ("FAI") a seven year D and O runoff policy ("the FAI policy"). Gordian's share of risk was 60 percent and R E Brown's 40 percent. The FAI policy applied to wrongful acts occurring before 31 May 1999 and allowed for claims to be made and notified for seven years thereafter. A number of claims in respect of alleged wrongful acts prior to 31 May 1999 were made and notified to Gordian under the FAI policy within seven years, that is to say, by 31 May 2006. All but one of these claims were made and notified within three years.

3 At all material times Gordian's PI portfolio and D and O portfolio were at least partially reinsured. The dispute between the parties to the arbitration turned upon the issue whether the liabilities of Gordian in respect of claims under the

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1 *Gordian Runoff Ltd v Westport Insurance Corporation* (2010) 267 ALR 74.

2 *Westport Insurance Corporation v Gordian Runoff Ltd* (2009) 15 ANZ Insurance Cases ¶61-798.

3 The Arbitration Act was repealed by s 42 of the *Commercial Arbitration Act* 2010 (NSW) with effect 1 October 2010, but still applies to this litigation: *Interpretation Act* 1987 (NSW), s 30.

FAI policy were reinsured under reinsurance treaties between Gordian and the appellants ("the reinsurers"). The primary question was whether any of the reinsurance treaties covered the FAI policy given that it covered claims made and notified to Gordian within an extended period of seven years from 31 May 1999 rather than a period of three years. The reinsurers had not been aware of the existence of the FAI policy until after 23 February 2001. On that date Gordian had been notified of circumstances which could give rise to a claim under the FAI policy and the reinsurers then were informed of this. The reinsurers contended that they had conducted their dealings with Gordian on the basis that Gordian would not change the classes of business to which the reinsurance applied without the prior approval of the reinsurers.

4 It was common ground that the reinsurance treaties required the dispute to be decided by arbitration. The reinsurance treaties appear to have selected the law in force in New South Wales as their proper law and required any arbitration thereunder to be held in accordance with and subject to the Arbitration Act. Further, in accordance with ordinary principles of statutory construction, the Arbitration Act applied to arbitration agreements which selected New South Wales as their governing law[4].

5 The arbitration proceeded before a panel of three arbitrators upon a set of detailed pleadings which extended to more than 60 pages. The hearing commenced on 14 July 2008 and continued until 22 July, with representation by senior counsel, witnesses being sworn and cross-examined on their written statements, many documents being in evidence and a full transcript provided. In many respects, therefore, the arbitration proceeded along the lines of the conduct of a commercial cause in a superior court. This complexity of the arbitration will be relevant when considering the content of the requirement in s 29(1)(c) of the Arbitration Act that the arbitrators provide a statement of the reasons for the making of the award.

6 The reinsurers resisted the claims made by Gordian on the grounds that the class of business they had agreed with Gordian to cover was limited to underlying policies with a term not exceeding three years, which excluded a seven year policy, so that the reinsurers had no liability to Gordian even upon

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4 *Wanganui-Rangitikei Electric Power Board v Australian Mutual Provident Society* (1934) 50 CLR 581 at 601; [1934] HCA 3; *Kay's Leasing Corporation Pty Ltd v Fletcher* (1964) 116 CLR 124 at 142-143; [1964] HCA 79; *Insight Vacations Pty Ltd v Young* (2011) 85 ALJR 629 at 635 [30]; 276 ALR 497 at 504-505; [2011] HCA 16.

claims made and notified within three years under a seven year policy. Gordian responded by relying upon s 18B of the *Insurance Act* 1902 (NSW) ("the Insurance Act"). The rejoinder pleaded by the reinsurers was that the effect of relief to Gordian under s 18B would be that they were obliged to indemnify Gordian without any additional premium for coverage of a seven year policy, which, in any event, they would have refused.

7 In the Reasons, the arbitrators noted that the reinsurers accepted that by the reinsurance treaties they agreed to cover D and O policies limited to claims made and notified to Gordian within a period of three years but not thereafter. But the arbitrators were not persuaded that the FAI policy, which extended to claims made and notified to Gordian within the seven year period from 31 May 1999, was covered by the reinsurance treaties.

Section 18B

8 However, as indicated above, Gordian had contended that, even if the reinsurance treaties did not cover the FAI policy, provisions of the Insurance Act applied to contracts of reinsurance[5] and saved the position of Gordian by producing the result that the reinsurance treaties did cover Gordian's liability under the seven year policy, if any, in respect of the claims made and notified to Gordian within the three year period. The arbitrators accepted that submission insofar as it relied upon s 18B of the Insurance Act.

9 Section 18B, titled "Limitation on exclusion clauses", provides:

> "(1) Where by or under the provisions of a contract of insurance entered into, reinstated or renewed after the commencement of this section:
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> (a) *the circumstances* in which the insurer is bound to indemnify the insured are so defined *as to exclude or limit the liability of the insurer* to indemnify the insured on the happening of particular events or *on the existence of particular circumstances*, and
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> (b) the liability of the insurer has been so defined because the happening of those events or the existence of those

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5 These provisions no longer apply to reinsurance: Insurance Regulation 2009, cl 4(b).

> circumstances was in the view of the insurer likely to increase the risk of loss occurring,
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> the insured shall not be disentitled to be indemnified by the insurer by reason only of those provisions of the contract of insurance *if*, on the balance of probability, *the loss in respect of which the insured seeks to be indemnified was not caused or contributed to by* the happening of those events or *the existence of those circumstances, unless in all the circumstances it is not reasonable for the insurer to be bound to indemnify the insured.*
>
> (2) The onus of proving for the purposes of subsection (1) that, on the balance of probability, loss in respect of which an insured seeks to be indemnified was not caused or contributed to by the happening of particular events or the existence of particular circumstances is on the insured." (emphasis added)

10 Section 18B was added to the Insurance Act by the *Insurance (Amendment) Act* 1983 (NSW). It appears to have been assumed by the parties that s 18B applies not only to contracts entered into in New South Wales (as the opening words of s 18B(1) suggest) but to contracts the governing law of which is that of New South Wales, so that it applied to the reinsurance treaties in question.

11 The perceived mischief which s 18B was designed to remedy was the avoidance by insurers of liability by reliance upon exclusions or terms contained in the contract of insurance, the operation of which was triggered by events with no relationship to the cause of the event giving rise to the particular loss and claim in question; no consideration, as Allsop P pointed out in giving the leading judgment in the Court of Appeal[6], appears to have been given by the legislature to the application of s 18B to contracts of reinsurance.

12 The reinsurers had submitted to the arbitrators that a provision which identifies the scope of coverage does not impose a term or condition which can attract the operation of s 18B. In the Court of Appeal, Allsop P went on to indicate a critical difficulty in the construction of s 18B which had been presented to the arbitrators, by asking whether, as Gordian contended (and the arbitrators accepted)[7]:

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6 (2010) 267 ALR 74 at 102 [150].

7 (2010) 267 ALR 74 at 104 [160].

> "s 18B can operate to extend beyond its effect on so-called exclusion and limitation clauses leaving the so-called true scope of cover to operate and to have an effect on clauses that truly reflect the so-called scope of cover, thereby extending the intended substantive reach of the policy".

13 Further consideration of the point made by Allsop P will be necessary later in these reasons and will be of decisive importance for the outcome of this matter.

The Reasons

14 In the Reasons the arbitrators extracted the text of s 18B(1), including the concluding words. The arbitrators said (par 88):

> "The reinsurers submitted that ss 18B(1) has no material operation. However, we see no reason to doubt that s 18B applies in relation to the 3-year claims if the requirements of ss 18B(1)(a) are met. In particular, we are comfortably satisfied that it would be reasonable within the meaning of s 18B(1), and entirely consistent with 'considerations of general justice and fairness' within the meaning of the reinsurance treaties, for the reinsurance treaties to apply in relation to the 3-year claims."

15 In pars 92, 93 and 94 the arbitrators then wrote:

> "The reinsurance treaties do not cover the 3-year claims under the FAI D&O run-off policy although they were made within 3 years from the inception of that policy because the policy covered claims which were made and notified to Gordian within 7 years from its inception and the reinsurance treaties were limited to policies which covered claims which were made and notified to Gordian within 3 years from inception and/or excluded policies which covered claims which were made and notified to Gordian more than 3 years from inception. Subsection 18B(1)(a) operates in relation to the 3-year claims if, but only if, that exclusion or limitation on the liability of the reinsurers to indemnify Gordian in respect of the 3-year claims under the FAI D&O run-off policy is an exclusion or limitation that is based '*on the existence of particular circumstances*'. The '*particular circumstance*' for this purpose can only be that the FAI D&O run-off policy covered claims which were made and notified to Gordian more than 3 years from the inception of the FAI D&O run-off policy. The '*loss in respect of which [Gordian] seeks to be indemnified*', namely, its liability on the 3-year claims, '*was not caused or contributed to by ... the existence of [that] circumstance*' because the 3-year claims were made and

notified to Gordian within 3 years of the inception of the FAI D&O run-off policy.

Consistently with the remedial character of ss 18B(1) and in compliance with the obligation to construe its language so as to give the most complete remedy which is consistent with the actual language employed and to which the words are fairly open, we have concluded that the exclusion and/or limitation on the '*liability of the [reinsurers] to indemnify [Gordian]*' in respect of the 3-year claims made under the FAI D&O run-off policy is based '*on the existence of [the] particular circumstance*' that the FAI D&O run-off policy covered claims which were made and notified to Gordian more than 3 years from the inception of the FAI D&O run-off policy. If at large, 'considerations of general justice and fairness' would produce the same result.

Accordingly, we have determined that reinsurance treaties cover Gordian's liability, if any, in respect of the 3-year claims."

16 The reference by the arbitrators to "considerations of general justice and fairness" repeats words in s 22(2) of the Arbitration Act. This sub-section states:

"If the parties to an arbitration agreement so agree in writing, the arbitrator or umpire may determine any question that arises for determination in the course of proceedings under the agreement by reference to considerations of general justice and fairness."

The arbitration clause in the reinsurance treaties provided that s 22(2) apply to the arbitration.

17 The reinsurers complain that in the Reasons the arbitrators did not explain why, by reason of the concluding words in the sub-section, s 18B(1) should still be held to apply; the reinsurers assert an absence of explanation as to why in all the circumstances it was reasonable for them to be bound to indemnify Gordian.

The Arbitration Act and the Supreme Court

18 An award, subject to the Arbitration Act and to any contrary criterion in the arbitration agreement, is final and binding on the parties to the agreement (s 28). The award may order specific performance of a contract if the Supreme Court would have power to decree specific performance (s 24). By leave of the Supreme Court, judgment may be entered in terms of an award and an award may be enforced in the same manner as a curial judgment or order to the same effect (s 33). The Supreme Court is empowered by s 44 to remove an arbitrator

who has misconducted the proceedings or who is incompetent or unsuitable to deal with the particular dispute.

19 These statutory provisions indicate that the making of an award in arbitration proceedings is more than the performance of private contractual arrangements between the parties which yields an outcome which rests purely in contract. They also suggest the importance which the provision of reasons by arbitrators has for the operation of the statutory regime. That statutory regime involves the exercise of public authority, whether by force of the statute itself or by enlistment of the jurisdiction of the Supreme Court. It also, as explained later in these reasons, displays a legislative concern that the jurisdiction of the courts to develop commercial law not be restricted by the complete insulation of private commercial arbitration.

20 No doubt it is true to say that the provision of an award under the Arbitration Act lacks distinctive hallmarks of the exercise of judicial power, namely the maintenance of public confidence in the manner of its exercise and in the cogency or rationality of its outcomes, and the operation of the appellate structure and of the case law system. However, it is going too far to conclude that performance of the arbitral function is purely a private matter of contract, in which the parties have given up their rights to engage judicial power[8], and is wholly divorced from the exercise of public authority.

The federal scheme

21 The Commonwealth Solicitor-General, who appeared for the Attorney-General as *amicus curiae*, sought to distinguish provisions of the Arbitration Act with respect to the giving of reasons from the state of affairs obtaining under Pt III (ss 15-30A) of the *International Arbitration Act* 1974 (Cth) ("the federal Act"), after amendment by the *International Arbitration Amendment Act* 2010 (Cth). The Attorney-General was moved to do so in the light of the treatment by the Court of Appeal of the Supreme Court of Victoria in *Oil Basins Ltd v BHP Billiton Ltd*[9] of the provision under the new federal scheme for the giving of reasons as *in pari materia* with the provision in the Victorian legislation equivalent to s 29(1)(c) of the Arbitration Act.

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8 Cf *Melbourne Harbour Trust Commissioners v Hancock* (1927) 39 CLR 570 at 585-586, 590-591; [1927] HCA 26.

9 (2007) 18 VR 346 at 364-365 [51].

22 Section 16 of the federal Act gives the force of law in Australia to the UNCITRAL Model Law on International Commercial Arbitration ("the Model Law"), the English text of which is set out in Sched 2 to the federal Act. If the Model Law applies to an arbitration, State or Territory law relating to arbitration does not apply to it (s 21). In exercising a power to recognise and enforce an arbitral award under the Model Law, a federal, State or Territory court must have regard to the objects of the federal Act and the circumstance that awards are intended to provide "certainty and finality" (ss 39(1)(a)(iii), 39(2)(b)(ii)). The federal Act in this way enlists the judicial power of the Commonwealth in aid of the operation of the arbitration system established by s 16 and the Model Law.

23 Article 31(2) of the Model Law requires that an award "shall state the reasons upon which it is based". However, the Solicitor-General submitted that this appears in a context where Art 5 provides that "no court shall intervene except where so provided in this Law", and there is no provision for appeal on a question of law. An award may be set aside only under Art 34 and relevantly only on the ground of a breach of the rules of natural justice. The Solicitor-General contended that here these rules require no more than a statement of reasons to demonstrate whether the arbitrators have addressed the dispute referred for determination. Whether this is the proper construction of the federal Act and the Model Law may be left for determination on another occasion. The provisions of the federal scheme may be put to one side in construing the Arbitration Act, upon which this litigation turns.

Statements of reasons and errors of law

24 Section 29(1) of the Arbitration Act required the arbitrators in the present case to:

> "(a) make the award in writing,
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> (b) sign the award, and
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> (c) include in the award a statement of the reasons for making the award."

25 Succeeding provisions of the Arbitration Act employ the term "award" to identify in some provisions the award in the strict sense of the outcome of the arbitration which then may be enforced by the Supreme Court, and in others to identify the inclusion of a statement of reasons in the written instrument containing the award which is the outcome of that reasoning.

26 The term "the Court" is relevantly defined by s 4(1) as meaning the Supreme Court of New South Wales. Part 5 (ss 38-49) is headed "Powers of the Court". In the circumstances detailed in ss 39 and 40, the Supreme Court may determine any question of law arising in the course of an arbitration. However, s 38(1) denies to the Supreme Court "jurisdiction to set aside or remit an award on the ground of error of fact or law on the face of the award"; the face of the award would include the statement of reasons. The denial of that jurisdiction by s 38(1) is qualified by s 38(2) and (4).

27 With the consent of the parties to the arbitration agreement (s 38(4)(a)) or (subject to s 40, which permits "exclusion agreements" but is not presently material) with the leave of the Supreme Court (s 38(4)(b)), a proceeding described in s 38(2) as "an appeal" lies to the Supreme Court "on any question of law arising out of an award". These provisions thus have a dual function. They both create a new head of justiciable subject matter and confer jurisdiction on the Supreme Court to determine whether to grant leave, and, if this is given, to entertain the "appeal". The subject matter of this "appeal" is confined to questions of law[10]; the scheme of the legislation is to hold the parties to their agreement to accept factual findings by arbitrators.

28 Leave of the Supreme Court is not to be granted pursuant to s 38(4) unless the Supreme Court considers that the applicant for leave has satisfied the criteria specified in pars (a) and (b) of s 38(5). These paragraphs state:

> "(a) having regard to all the circumstances, the determination of the question of law concerned could substantially affect the rights of one or more parties to the arbitration agreement, and
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> (b) there is:
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> (i) a manifest error of law on the face of the award, or
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> (ii) strong evidence that the arbitrator or umpire made an error of law and that the determination of the question may add, or may be likely to add, substantially to the certainty of commercial law."

29 Section 38(5) specifies conditions which must be satisfied before the power under s 38(4)(b) to grant leave is enlivened. The statute does not provide

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10 See the remarks of Brennan J in *Waterford v The Commonwealth* (1987) 163 CLR 54 at 77-78; [1987] HCA 25.

that if s 38(5) is satisfied, then leave must be given. The distinction was explained by Sheller JA in *Promenade Investments Pty Ltd v New South Wales*[11], and in *Qantas Airways Ltd v Joseland & Gilling*[12] McHugh JA, giving the judgment of himself, Glass and Priestley JJA, emphasised that the discretion to grant leave is "to be exercised after considering all the circumstances of the case".

30 The Arbitration Act[13] repealed the *Arbitration Act* 1902 (NSW) ("the 1902 Act"). However, the provisions of the Arbitration Act just described, in particular s 38(1), are best understood in the light of the system under the 1902 Act which they replaced.

31 A starting point for that understanding is provided by the following statement by Lord Diplock when delivering the reasons of the Privy Council in *Max Cooper & Sons Pty Ltd v University of New South Wales*[14]:

> "One of the principal attractions of arbitration as a means of resolving disputes arising out of business transactions is that finality can be obtained without publicity or unnecessary formality, by submitting the dispute to a decision maker of the parties' own choice. From the arbitrator's award there is no appeal as of right; it is only exceptionally that it does not put an end to the dispute. England and those other Commonwealth jurisdictions, including New South Wales, whose arbitration statutes have followed the English model are exceptional when compared with most other countries, in providing procedural means whereby the finality of an arbitrator's award may be upset, if it can be demonstrated to a court of law that his decision resulted from his applying faulty legal reasoning to the facts as he found them. Two of these procedural means, the statement by the arbitrator of his award or of a question of law in the form of a special case for the opinion of the court, are statutory in origin; the third, setting aside an arbitrator's award for error of law upon its face, originated in the common law. It is as the result of an anomaly of legal history that it still survives in New South Wales

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11 (1992) 26 NSWLR 203 at 225-226.

12 (1986) 6 NSWLR 327 at 333.

13 Section 3(1) and Sched 1.

14 [1979] 2 NSWLR 257 at 260-261.

> and, until the passing of the *Arbitration Act* 1979 [(UK) ('the 1979 UK Act')], survived in England."

32 The concept of an error of law appearing, or manifest, upon the face of an award, thus has a long history. His Lordship went on[15] to describe the jurisdiction exercised by the Court of King's Bench as analogous to that asserted over inferior tribunals by the writ of certiorari and as one whereby awards were set aside for errors of law apparent on their face, and added:

> "This jurisdiction operated haphazardly, because the ability of the court to exercise it depended upon whether or not the arbitrator had chosen to set out in the award itself the legal reasoning on which he had based it. If he had not, the court was powerless to intervene but, if he had and his legal reasoning so set out in the award itself was erroneous, the court could quash the award."

33 It is to the removal of this jurisdiction that s 38(1) is directed; it had persisted despite the provision of statutory means of review, in particular by ss 9 and 19 of the 1902 Act. These provisions had empowered arbitrators to state an award as to the whole or part thereof in the form of a special case for the opinion of the court, and also had empowered the court to compel an arbitrator to state a special case for its opinion on any question of law arising in the course of the arbitration[16]. The decisions of English courts on cases stated by arbitrators under this system was said by Lord Diplock in *The Nema*[17] to have made an important contribution to "the comprehensiveness and certainty" of English commercial law, which in turn makes it "a favoured choice as the 'proper law' of contracts ... and London arbitration as the favoured curial law for the resolution of disputes arising under them". That concern with the certainty of commercial law as enhanced by curial involvement in arbitration proceedings is apparent particularly from the terms of par (b)(ii) of s 38(5) of the Arbitration Act.

34 However, as Lord Diplock explained in *Max Cooper*[18], before the repeal of the 1902 Act:

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15 [1979] 2 NSWLR 257 at 261.

16 See the discussion by Sheller JA in *Promenade Investments Pty Ltd v New South Wales* (1992) 26 NSWLR 203 at 216.

17 *Pioneer Shipping Ltd v BTP Tioxide Ltd* ("*The Nema*") [1982] AC 724 at 741.

18 [1979] 2 NSWLR 257 at 262.

> "Unless an arbitrator is required under s 19 of the [1902 Act] to state in the form of a special case for the opinion of the court a question of law arising in the course of the reference, he is not under any obligation in law to give his reasons for what he has decided. Indeed, to do so in the award itself may undermine its finality by exposing the party in whose favour it is given to the risk of the expense and delay involved in what in effect is an appeal on a point of law from his decision that may be taken as far as the highest court in the land, and the possibility that at the end of it all, the award may be set aside and a new reference held. On the other hand, if he wants to inform the parties of his reasons without making the award vulnerable, all he has to do is to put them down on a separate piece of paper which, he makes it unequivocally clear, is not intended to form part of his award."

35 The scheme adopted by the Arbitration Act was described by Giles J in *R P Robson Constructions Pty Ltd v D & M Williams*[19]. After indicating that the encouragement otherwise offered for unreasoned awards was radically altered by the new legislation, his Honour went on:

> "The jurisdiction to set aside or remit an award on the ground of error of law on its face was abolished (s 38(1)). In lieu thereof, an appeal was to lie to this Court on any question of law arising out of the award, which appeal might be brought by any of the parties to the arbitration agreement with the consent of all other parties thereto or, subject to an exclusion agreement, with the leave of the Court (s 38(2) and (4)). Leave was not to be granted unless the Court considered that the determination of the question of law could substantially affect the rights of one or more of the parties (s 38(5)(a)). Necessarily, in order that a dissatisfied party could effectively appeal, s 29 of the Act provided for the award to be in writing and, as has been seen, for the arbitrator to include a statement of the reasons for making the award. The statement of reasons is necessary in order that it can be seen whether or not the arbitrator was in error on any question of law arising out of the award."

36 From that last sentence it follows that failure to provide a statement of the reasons for the making of the award, as required by s 29(1)(c), may itself amount to a manifest error of law on the face of the award within the meaning of

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19 (1989) 6 BCL 219 at 221.

s 38(5)(b)(i) of the Arbitration Act[20]. The reasons, for this purpose, are part of the award. The submission to the contrary by Mr Jackson QC for one set of *amici curiae* should not be accepted.

The 1979 UK Act

37 The enactment of the Arbitration Act had been preceded by the 1979 UK Act. Like s 38(1) of the Arbitration Act, s 1(1) of the 1979 UK Act removed the jurisdiction with respect to errors on the face of an award. However, the jurisdiction then created by the balance of s 1 for an "appeal ... on any question of law arising out of an award" was expressed in terms which did not correspond with the balance of s 38. In particular, the provision in s 1 of the 1979 UK Act with respect to the grant of leave (s 1(4)) did not contain the detailed statement in s 38(5)(b) of the Arbitration Act set out earlier in these reasons. In its original form, s 38 was closer to the terms of the 1979 UK Act, as Sheller JA pointed out in *Promenade Investments*[21], but this litigation concerns s 38 in the form taken after the *Commercial Arbitration (Amendment) Act* 1990 (NSW). Some caution thus is required in applying to the leave requirements in s 38(5) remarks made in United Kingdom decisions dealing with s 1 of the 1979 UK Act.

38 However, some assistance in considering the operation of the leave requirement in s 38 is provided by Lord Diplock in *The Nema*[22]. Having described the power to refuse leave in the 1979 UK Act as conferring an "unfettered" judicial discretion, he added:

> "[T]his, in the case of a dispute that parties have agreed to submit to arbitration, involves deciding between the rival merits of assured finality on the one hand and upon the other the resolution of doubts as to the accuracy of the legal reasoning followed by the arbitrator in the course of arriving at his award, having regard in that assessment to the nature and circumstances of the particular dispute."

The litigation in the Supreme Court and the Court of Appeal

39 The primary judge in the one proceeding dealt both with the application by the reinsurers for leave to "appeal" and with the "appeal" itself. By orders

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20 *Ridler v Walter* [2001] TASSC 98 at [9].

21 (1992) 26 NSWLR 203 at 217.

22 [1982] AC 724 at 739.

entered 23 April 2009 his Honour granted the reinsurers leave to appeal and allowed the appeal, set aside the award and in place thereof dismissed the claim of Gordian in the arbitration. What his Honour described as the "primary error of law" was the failure of the arbitrators to recognise that an agreement made at the request of Gordian to extend cover to include D and O policies issued for up to three years was not a "limitation" or "exclusion" in the sense contemplated by s 18B(1) of the Insurance Act. Such an error, in his Honour's view, made inappropriate a remitter to the arbitrators.

40 The Court of Appeal[23] discountenanced the procedure adopted by the primary judge in which, over the opposition of Gordian, his Honour had heard concurrently the application for leave and the "appeal" itself.

41 The Court of Appeal granted Gordian leave to appeal from the decision of the primary judge, allowed the appeal, and made an order refusing leave to the reinsurers under s 38(4)(b) to "appeal" in respect of the award dated 10 October 2008[24]. If they are to have any measure of success in this Court the reinsurers must show that the Court of Appeal erred in that refusal of leave. This requires particular attention to the construction and operation of pars (a) and (b) of s 38(5). In submissions to this Court rather too much attention was diverted away from the threshold issues and to the very fully argued question of whether the arbitrators erred in the engagement and construction of s 18B of the Insurance Act.

Paragraph (b) of s 38(5) of the Arbitration Act

42 Paragraph (b)(i) of s 38(5) may be awkwardly expressed, but the words "a manifest error of law on the face of the award" comprise a phrase which is to be read and understood as expressing the one idea. An error of law either exists or does not exist; there is no twilight zone between the two possibilities. But what is required here is that the existence of error be manifest on the face of the award, including the reasons given by the arbitrator, in the sense of apparent to that understanding by the reader of the award. If that error is manifest and its determination could substantially affect the rights of at least one of the parties, as specified in par (a) of s 38(5), then the Supreme Court may go on to decide to grant or refuse leave in the exercise of the power conferred by s 38(4)(b).

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23 (2010) 267 ALR 74 at 92-95 [102]-[113].

24 (2010) 267 ALR 74 at 126 [304].

43 If there be no such manifest error on the face of the award but there is presented to the Supreme Court on the leave application "strong evidence" that an error of law was made, and its determination may add, or be likely to add, substantially to the certainty of commercial law (par (b)(ii) of s 38(5)) and also may substantially affect the rights of at least one of the parties (par (a) of s 38(5)), then leave may be granted.

44 If either s 38(5)(b)(i) or s 38(5)(b)(ii) has been engaged to enliven the power to grant leave, then, upon the grant of leave, a "question of law arising out of an award" is presented to provide the subject matter of the appeal which lies to the Supreme Court under s 38(2).

45 Much difficulty in the operation of these provisions has been occasioned by the majority decision of the New South Wales Court of Appeal in *Natoli v Walker* (Kirby P and Mahoney JA; Meagher JA dissenting)[25]. The majority appear to have treated the use of "manifest" in par (b)(i) of s 38(5) not as directed to what is presented upon the face of the award but as requiring the error of law itself to have a particular quality or character so as to include within par (b)(i) facile errors and to exclude those of complexity. This would exclude from par (b)(i), for example, an error in the construction of a complex law such as s 18B of the Insurance Act. Yet, as par (b)(ii) indicates, the policy of the statute is not to leave entirely to the operation of the arbitration agreement questions of law the determination of which may be likely to add to the certainty of commercial law. In an age when much commercial activity is regulated by statute, such questions are likely to be matters of statutory interpretation. It would be incongruous to favour judicial determination merely of egregious error apparent on the face of the award.

46 In the present case, counsel then appearing for the reinsurers in the Court of Appeal, no doubt aware of what had been said in *Natoli* by the Court of Appeal, conceded that he did not press a case of manifest error of law on the face of the award. However, in his reasons, Allsop P said that he did not take the concession as going beyond the particular point of construction of s 18B upon which the primary judge had based his decision[26]. Nevertheless, his Honour applied *Natoli* to the construction of par (b)(i) of s 38(5)[27], so that answers given

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25 (1994) 217 ALR 201 at 215-217, 223.

26 (2010) 267 ALR 74 at 106 [178].

27 (2010) 267 ALR 74 at 95 [116].

by arbitrators upon difficult questions of law, which had been open to competing arguments, did not qualify as errors of law.

47 In this Court the reinsurers relied upon par (b)(i) as well as par (b)(ii) of s 38(5) and were at liberty to do so. *Natoli* should not be accepted in this Court as correctly construing s 38(5)(b)(i) of the Arbitration Act. The character or quality of the error of law falls for consideration, if relied upon, at the next stage, namely when the Supreme Court is considering under s 38(4)(b) whether to grant leave.

48 In the Court of Appeal counsel for the reinsurers based the case upon par (b)(ii) of s 38(5). This is expressed disjunctively from par (b)(i), but the same circumstances may attract both paragraphs. The correct construction of s 18B of the Insurance Act, as Allsop P indicated[28], would be likely in the sense of par (b)(ii) to add substantially to the certainty of commercial law, and the "strong evidence" of error would appear from the Reasons themselves. So also the question of the content of the requirement in s 29(1)(c) that there be included a statement of the reasons for making the award.

Inadequate reasons?

49 The Court of Appeal rejected the submission by the reinsurers that there had been an error of law in the failure of the arbitrators to give adequate reasons for their conclusion respecting the application of the proviso in the concluding words of s 18B(1) of the Insurance Act[29]. The reinsurers had submitted that the findings by the arbitrators had compelled the contrary conclusion, namely, that it was not reasonable for them to be bound to indemnify Gordian. The reinsurers had supported their submission as to the inadequacy of reasons by reference to what they saw as having been decided by the Court of Appeal of Victoria in *Oil Basins*[30].

50 The relevant proposition from *Oil Basins* upon which the reinsurers relied before the Court of Appeal was that the requirement for reasons specified in par (c) of s 29(1) of the Arbitration Act was a statutory importation of the same standard as applies in Australia to the giving of reasons by judges.

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28 (2010) 267 ALR 74 at 106 [173].

29 (2010) 267 ALR 74 at 107-108 [186].

30 (2007) 18 VR 346.

51 Allsop P considered[31] that the applicable standard was that stated by Donaldson LJ when giving the judgment of the English Court of Appeal in *Bremer Handelsgesellschaft mbH v Westzucker GmbH (No 2)*[32]. As his Lordship had said:

> "All that is necessary is that the arbitrators should set out what, on their view of the evidence, did or did not happen and should explain succinctly why, in the light of what happened, they have reached their decision and what that decision is. This is all that is meant by a 'reasoned award' [in s 1(6) of the 1979 UK Act]."

It may be noted that immediately following this passage Donaldson LJ had gone on to distinguish a reasoned award from reasons for judgment.

52 This Court granted special leave to appeal on the ground that the Court of Appeal had erred in not concluding that the arbitrators had failed to give reasons as required by par (c) of s 29(1) of the Arbitration Act for their conclusion that it was reasonable for the reinsurers to be required to indemnify Gordian within the meaning of the proviso to s 18B(1) of the Insurance Act, and for their conclusion that considerations of general justice and fairness did not compel the conclusion that the reinsurers should not be required to indemnify Gordian within the meaning and on the proper construction of s 22(2) of the Arbitration Act. In the circumstances of this matter the considerations of general justice and fairness spoken of in s 22(2) are encompassed within the alleged failure to give reasons for the applicability of s 18B(1) of the Insurance Act, as required by s 29(1)(c) of the Arbitration Act. This ground of appeal is subsumed within the first ground.

53 The reference in *Oil Basins* to the giving by the arbitrators in that dispute of reasons to a "judicial standard"[33] and cognate expressions[34] placed an unfortunate gloss upon the terms of s 29(1)(c). More to the point were observations in *Oil Basins* to the effect that what is required to satisfy that

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31 (2010) 267 ALR 74 at 114 [220].

32 [1981] 2 Lloyd's Rep 130 at 132-133.

33 (2007) 18 VR 346 at 366 [54].

34 (2007) 18 VR 346 at 364 [50], 367 [56].

provision will depend upon the nature of the dispute and the particular circumstances of the case[35]. Their Honours illustrated the point by saying[36]:

> "If a dispute turns on a single short issue of fact, and it is apparent that the arbitrator has been chosen for his or her expertise in the trade or calling with which the dispute is concerned, a court might well not expect anything more than rudimentary identification of the issues, evidence and reasoning from the evidence to the facts and from the facts to the conclusion[37]."

But in *Oil Basins* itself, the central issue in dispute in the hard-fought and lengthy arbitration[38]:

> "was whether the expression 'overriding royalty' in the royalty agreement was used as a term of art, as the respondents contended (with the result that any right to royalty ceased upon surrender of the tenement to which it related (a 'title based' royalty)), or whether the expression meant simply an additional royalty, as the appellant argued (with the result that royalty was payable in respect of production derived by the respondents from within the area regardless of surrenders (an 'area based' royalty))."

The primary judge in *Oil Basins* had, as the Court of Appeal put it, properly[39]:

> "held that, in order to provide reasons of the standard required by s 29(1)(c), it was necessary for the arbitrators to decide and give reasons for deciding whether 'overriding royalty' was a technical term with a meaning usually understood by persons in the oil and gas industry and, if so, whether the context of the royalty agreement or the surrounding circumstances implied that the parties intended a different meaning from the technical meaning."

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35 (2007) 18 VR 346 at 367-368 [57]-[58].

36 (2007) 18 VR 346 at 367 [57].

37 Mustill and Boyd, *The Law and Practice of Commercial Arbitration in England*, (1982) at 552.

38 (2007) 18 VR 346 at 353 [28].

39 (2007) 18 VR 346 at 353-354 [29].

This the arbitrators in *Oil Basins* had failed to do.

54 In the present case, the reinsurers correctly submit that no wholly satisfactory formula can be found to flesh out the requirement in s 29(1)(c). Both Gordian and the reinsurers are content in this Court to rest, like Allsop P, upon what was set out above from the reasons of Donaldson LJ in *Bremer*. But the parties differ respecting the outcome of applying *Bremer* to the Reasons. The submissions of the reinsurers on this point should be accepted.

55 Treating s 18B of the Insurance Act as a critical element in reaching their award, the arbitrators were obliged to explain succinctly why the various integers in that complex statutory provision were satisfied. Those integers included the proviso.

56 There is no indication of factual findings in the Reasons which supported the inapplicability of the proviso, nor, indeed, of those considerations tending to support its application. In particular, there was no apparent attention to the contention that Gordian could have sought a special acceptance with respect to the FAI policy but had not done so, and if Gordian had done so it was at best conjectural that the reinsurers would have accepted. Nor was there consideration of the reinsurers' rejoinder pleading concerning the adjustment in premium. Nor was there any apparent consideration that the proviso in s 18B(1) was designed to guard against a strained application of the sub-section.

Conclusions respecting inadequacy of reasons

57 The result is that in this respect there was both a manifest error of law on the face of the award (s 38(5)(b)(i)), and strong evidence that the arbitrators made an error of law, the determination of which may add substantially to the certainty of commercial law (s 38(5)(b)(ii)).

58 Sub-sections (3) and (7) of s 38 of the Arbitration Act state:

> "(3) On the determination of an appeal under subsection (2) the Supreme Court may by order:
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> (a) confirm, vary or set aside the award, or
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> (b) remit the award, together with the Supreme Court's opinion on the question of law which was the subject of the appeal, to the arbitrator or umpire for reconsideration or, where a new arbitrator or umpire has been appointed, to that arbitrator or umpire for consideration,

and where the award is remitted under paragraph (b) the arbitrator or umpire shall, unless the order otherwise directs, make the award within 3 months after the date of the order.

...

(7) Where the award of an arbitrator or umpire is varied on an appeal under subsection (2), the award as varied shall have effect (except for the purposes of this section) as if it were the award of the arbitrator or umpire."

59 The remedy in respect of the inadequacy of reasons which then would be appropriate would be an order for remitter to the arbitrators for reconsideration pursuant to s 38(3)(b). However, the reinsurers contend that if they succeed in obtaining special leave on either of the remaining grounds respecting the operation of s 18B of the Insurance Act which were referred to the Full Court and extensively argued, and they succeed on those grounds, they should obtain a more drastic remedy. This would be the setting aside of the award by order under s 38(3)(a) by the restoration of the order to that effect made by the primary judge.

Section 18B special leave grounds

60 Critical to the outcome favoured by the arbitrators was the application by them of s 18B of the Insurance Act, and the reinsurers complain that in doing so the arbitrators misconstrued and misapplied s 18B in two respects. These are grounds 5 and 6 in the draft Notice of Appeal.

61 The starting point for consideration of ground 5 is the finding by the arbitrators that the FAI policy was outside the terms of the reinsurance treaties. The reinsurers then submit that there could be no three year claims within the terms of the reinsurance treaties if they were made under a policy to which the treaties had no application. The stipulation in the reinsurance treaties that they speak only to D and O policies limited to reporting periods of less than three years is then said by the reinsurers to render those treaties inapt to attract s 18B at all. A policy which is limited to three year reporting periods is not a policy with a seven year period, as was the situation with the FAI policy. It is no answer that three year claims might fall within both policies. The exclusion upon which the treaties operated was in respect of "policies issued for periods longer than 36 months".

62 There was in the provisions of the treaties no stipulation by or under which (in the terms of s 18B) the reinsurers excluded or limited their liability to

indemnify Gordian by reason of the circumstance that the FAI policy had the seven year period, so that Gordian thereby was disentitled to what otherwise would have been its right to indemnity under the treaties. The words in s 18B(1)(a), "on the happening of particular events or on the existence of particular circumstances", mark off exclusions and limitations from the content of the "contract of insurance" identified in the opening words of the sub-section. Accordingly, s 18B was never engaged.

63 These submissions should be accepted and special leave granted accordingly with respect to ground 5 in the draft Notice of Appeal and this ground should be upheld.

64 The second ground referred for consideration by the Full Court, ground 6, concerns the construction of the phrase in s 18B(1) "if ... the loss in respect of which [Gordian] seeks to be indemnified was not caused or contributed to by ... the existence of those circumstances [identified in par (a)]".

65 Contrary to the submissions by Gordian, this presented a question of law for decision by the arbitrators[40]. The error of which the reinsurers complain is readily conveyed by repeating what was said by the Court of Appeal[41]:

> "There was an underlying policy; it provided for more than a 3 year reporting period; it can be said that the existence of such a policy was the relevant circumstance; the claims to be met by the reinsurance came from that policy, irrespective of whether they were reported within 3 years. In that sense, the loss in respect of which Gordian sought to be indemnified might be seen to be caused or contributed to by the existence of the circumstance – the policy with a reporting period of more than 3 years. But for the existence of the policy (with a 7 year reporting period) there would have been no claims on the reinsurers.
>
> That is not how the arbitrators approached the question. They viewed the relevant aspect of the FAI policy as creating the risk, as the existence of the extended reporting period in the fourth to seventh years. That circumstance, which increased the risk of loss occurring, did not cause the loss, because all the claims were within 3 years. This approach

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40 See *Roncevich v Repatriation Commission* (2005) 222 CLR 115 at 126 [27]-[28], 139-142 [76]-[82]; [2005] HCA 40.

41 (2010) 267 ALR 74 at 106-107 [180]-[181].

tended to emphasise the relevance of the underlying claims against FAI within the 3 years, rather than the connection between the existence of the (7 year) policy and (any) claims under it."

The Court of Appeal saw merit in the approach contrary to that of the arbitrators in the Reasons. Allsop P said[42] that he would not have reached the same conclusion as the arbitrators and went on[43]:

> "Looking at the facts, the definition of cover was excluded or limited by reference to the circumstances of underlying policies of insurance with reporting periods of more than 3 years. That limitation was inserted because the circumstance, in the view of reinsurers, was likely to increase the risk. There was a policy of such a description. That policy gave rise to the claims. In that sense the loss can be seen to be caused by the circumstance: the existence of an underlying policy with an extended reporting period.
>
> This way of looking at the matter can be seen to reflect the sensible operation of s 18B in a [manner] which relevantly takes into account the safeguards built into s 18B by the legislature. This would also be the case if a policy excluded fire caused by arson. No operation of s 18B could require an underwriter to pay if the fire was caused by arson; this would be so not because of some notion of essential scope of cover, but because the event or circumstance caused the loss."

66 However, the Court of Appeal desisted from concluding that there was a manifest error of law upon the face of the award partly on the ground that a contrary argument to that put by the reinsurers had been tenable. But, as indicated earlier in these reasons, this was not to deny, as the Court of Appeal should have determined, that, complex though s 18B might be, there had been manifest an error of law to attract s 38(5)(b)(i) and the grant of leave.

67 Should special leave now be granted with respect to ground 6 as well as ground 5? Each ground would lead to an order restoring that of the primary judge to set aside the award. But ground 5 is logically anterior to ground 6. If s 18B was never engaged (ground 5), the causation issue does not arise and there would be no utility in a grant on ground 6. Accordingly, because in our view ground 5 succeeds, special leave should be refused with respect to ground 6. It

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42 (2010) 267 ALR 74 at 119 [257].

43 (2010) 267 ALR 74 at 119 [258]-[259].

should, however, be observed that, in a sense, the cogency of the reasoning by Allsop P upon the ground 6 issue supports the threshold denial of any application of s 18B to the reinsurance treaties with Gordian.

Remaining matters

68 Gordian relies upon a Notice of Contention, in effect to support on additional grounds the decision of the Court of Appeal. This decision was to allow the appeal by Gordian and, in place of the decision of the primary judge, refuse leave to the reinsurers to "appeal" on a question of law arising out of the award, within the meaning of s 38(2) and (4) of the Arbitration Act. In oral submissions the range of grounds in the Notice of Contention was reduced.

69 Counsel for Gordian relied upon remarks of Lord Steyn when construing s 1 of the 1979 UK Act in *The Santa Clara*[44] that under that statute a respondent to an award itself did not require leave to appeal in order to sustain before the court an award on a ground not relied upon by the arbitrator.

70 However, as explained earlier in these reasons[45], under the Arbitration Act the subject matter of the "appeal" to the Supreme Court in the present case comprised the errors of law of which the reinsurers complained. At the earlier stage of the consideration by the Supreme Court of an application for a grant of leave under the Arbitration Act it may be open to a respondent to resist the grant of leave on the footing that the award is to be sustained on other grounds. If so, it also may be that the respondent may rely upon those other grounds even if they concern no more than matters of fact. Were that approach upon an application to grant leave permissible, which it is unnecessary to decide here given our agreement in the next paragraph with the reasons of Kiefel J, caution would be required of the Supreme Court lest there be defeated the policy of the Arbitration Act that the parties be held to their bargain to accept the findings of fact by the arbitrator.

71 In the present case, Gordian sought to draw this Court into consideration of the treatment by the arbitrators of questions of fact respecting the relations between Gordian and the reinsurers, independently of any reliance upon s 18B of the Insurance Act. In particular, Gordian sought to agitate questions respecting the existence and extent of the three year limit in the reinsurance treaties as

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44 *Vitol SA v Norelf Ltd* [1996] AC 800 at 813-814.

45 At [25]-[27].

disclosed by the documents passing between the relevant actors, in particular the letter of 15 December 1998. We agree with what Kiefel J has written on this subject, leading her Honour to the conclusion that it cannot be said that the arbitrators erred in their conclusion.

Orders

72 The grant of special leave should be expanded to include ground 5 but not ground 6. The appeal should be allowed with costs. The decisions of the primary judge to grant leave and allow the "appeal" under the Arbitration Act should not have been set aside by the Court of Appeal. The orders of the primary judge will be restored if orders 2, 3 and 4 of the orders of the Court of Appeal entered 29 April 2010 are set aside, and in place thereof the appeal to that Court is dismissed with costs.

73 HEYDON J. The proceedings in this Court raise many issues[46].

The anterior issue

74 But there is one issue which is anterior to the rest. That issue is thrown up by ground 8 of Gordian's Notice of Contention. Gordian there indicated that it wished to contend that the decision of the Court of Appeal should be affirmed, but on the grounds that the Court of Appeal erroneously failed to decide that the arbitrators "erred in law by construing the contracts of reinsurance so that they only applied to D&O policies which provided cover for a period of three years." Below this will be called "the construction point". If the arbitrators did commit that error in relation to the construction point, and if the Court of Appeal erred in failing to deal with it, then the trial judge's order setting aside the award would be incorrect, and the Court of Appeal's order allowing Gordian's appeal from the trial judge's order would be correct. The issues which the reinsurers raise about s 18B of the Insurance Act would not arise. Nor would the issues about inadequate reasons which Gordian raises, for the alleged inadequacy related only to s 18B. Nor would issues of causation. Nor would various issues which Gordian raises in the Notice of Contention. Nor would various issues agitated by the amici curiae.

Two preliminary points

75 Except in two particular respects, the reinsurers did not advance any substantive argument against what Gordian urged in relation to the merits of the construction point. But the reinsurers relied on two preliminary points as absolute bars to consideration of Gordian's construction point arguments on their merits.

Is leave to raise the construction point necessary?

76 Gordian raised the construction point before the Court of Appeal, in which it was the appellant. The Court of Appeal's reasons for not dealing with the point proceeded in three steps. First, had an application been made for leave to appeal under s 38(4)-(5) of the Arbitration Act on this ground, it would not have been granted. Secondly, to deal with the point would call for a factual examination of the dealings between the parties in great detail. Thirdly, to deal with the point would reveal that the Arbitration Act had failed in its role of limiting review of

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46 The facts, circumstances and relevant legislation are set out in the plurality judgment. The abbreviations it employs are employed below.

arbitration awards. Hence "parties who wish to complain about questions of law arising out of an award must obtain leave to appeal."[47]

77 The reasons for judgment of the Court of Appeal spoke twice of "complaints" about an award, twice of "complaints" about questions of law arising out of an award, and once of "complaints" about the reasons for an award[48]. They did so as if each of these propositions were identical. There is a distinction between an "appeal" against an order and a "complaint" about the reasoning which led to that order. Appeals lie only against orders, not against the reasoning which led to them[49]. An order is the outcome of legal proceedings; it is distinct from the process which led to that outcome. Similarly, an award is the outcome of an arbitration; it is distinct from the process which led to that outcome. In s 38, the word "award" is used several times to mean "outcome". Section 38(1) denies the Supreme Court jurisdiction "to set aside or remit an award" on certain grounds. When a s 38(2) appeal has been determined, one power of the Supreme Court is to confirm, vary or set aside the award (s 38(3)(a)). Another is to remit the award for further consideration (s 38(3)(b)), in which case the arbitrator or umpire to whom the award has been remitted is to make another award within three months. Where the award of an arbitrator or umpire is varied in an appeal under s 38(2), the award as varied is to have effect as if it were the award of the arbitrator or umpire (s 38(7)). An award shall, unless otherwise agreed in writing by the parties, have included in it a statement of the reasons for making the award (s 29(1)(c)), but the reasons do not constitute the award. The Court of Appeal erred in equating appeals against awards with complaints about the reasons for, or questions of law arising out of, awards. Section 38 is in terms directed only to challenges to the award – the orders made by arbitrators – even though the challenges may raise questions of law about the reasoning that led to those orders. Section 38 does not apply to attempts, not to challenge awards, but to sustain them by raising another question of law urging a particular answer.

78 It was not procedurally open to Gordian to seek leave from Einstein J under s 38(4)-(5). Section 38(2) provides that an appeal shall lie to the Supreme Court on any question of law arising out of an award. Gordian was not the party which desired to appeal, for the award gave it a substantial measure of success; it

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47 *Gordian Runoff Ltd v Westport Insurance Corporation* (2010) 267 ALR 74 at 123 [280] per Allsop P, Spigelman CJ and Macfarlan JA concurring.

48 *Gordian Runoff Ltd v Westport Insurance Corporation* (2010) 267 ALR 74 at 122 [274]-[275] and 123 [280] and [282].

49 *Driclad Pty Ltd v Federal Commissioner of Taxation* (1968) 121 CLR 45 at 64; [1968] HCA 91.

was the reinsurers which sought leave to appeal. Hence the question whether leave would be granted, or would have been granted, if it had been sought, is beside the point. Where a party contends that an award is correct because of a question of law which the arbitrators either decided correctly, or failed to decide correctly, the Arbitration Act imposes no express requirement on that party to seek and obtain leave to raise that question. It only imposes on an appellant a requirement to obtain leave to appeal against the award. The Arbitration Act is not to be presumed to alter the conventional processes of appeal in a manner about which its terms are silent. To treat the Arbitration Act as requiring leave on points of contention as well as points of appeal is to assume a particular construction. And assuming that particular construction as an answer to the question how far the Arbitration Act limits review is to assume the answer to the question posed.

79 It may be accepted that, as the Court of Appeal said, a function of the Arbitration Act is to limit appeals against awards. But that function is served by the requirement that there be a grant of leave for the appeal. To permit the party which is not appealing to raise other questions as a means of sustaining the award does not undermine the finality of awards. To permit questions of law to be raised by way of contention is a means of ensuring the defeat of applications for the review of arbitration awards which are unsatisfactory applications in the sense that the award is entirely sound, though not necessarily for the reasons given by the arbitrators. It does not expand the scope for reviewing arbitration awards.

80 In *Vitol SA v Norelf Ltd*[50] Lord Steyn gave reasons supportive of that conclusion, with which Lord Mackay of Clashfern LC, Lord Griffiths, Lord Nolan and Lord Hoffmann agreed. The context was not identical to the present, but it was similar. The House of Lords was considering whether s 1(7) of the *Arbitration Act* 1979 (UK) applied to respondents. Section 1(7) provided:

> "No appeal shall lie to the Court of Appeal from a decision of the High Court on an appeal under this section unless –
>
> (a) the High Court or the Court of Appeal gives leave; and
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> (b) it is certified by the High Court that the question of law to which its decision relates either is one of general public importance or is one which for some other special reason should be considered by the Court of Appeal."

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50 [1996] AC 800.

Lord Steyn said[51]:

> "Under the stated case procedure, which existed before the Act of 1979, a respondent who wished to argue that the award should be sustained for reasons not expressed or fully expressed in the award or not considered or upheld at first instance did not have to obtain a certificate of the type envisaged by section 1(7). The idea that in 1979 the legislature intended to make the position of a respondent, who had won an arbitration, more difficult by requiring him to obtain a certificate under section 1(7) before he would be permitted on appeal to the Court of Appeal to defend the award on other grounds is convincingly refuted by the history and policy of the Act of 1979. The primary purpose of the Act of 1979 was to reduce the extent of the court's supervisory jurisdiction over arbitration awards. It did so by substituting for the special case procedure a limited system of filtered appeals on questions of law. The change was intended to tilt the balance toward greater emphasis on the finality of arbitration awards. Now postulate a respondent in the Court of Appeal who at first instance won on the main point but lost on a sound alternative argument. He loses on the main point on appeal. If he requires a certificate to argue the alternative case there is a risk that he may not obtain a certificate. A perfectly good award may then be set aside. In a very relevant sense such a risk would imperil the finality of arbitration awards. It would also be a manifestly unfair consequence in cases when the respondent has a good alternative argument which does not pass the test of being a question of general public importance, eg the construction of a 'one off' exception clause. And it is no answer to say that in some cases a judge may grant a certificate for some other special reasons."

Lord Steyn described the view he rejected as "indefensible"[52]. He went on: "It militates against the finality of arbitration awards, it would cause injustice and, if adopted, would be perceived to be a serious flaw in our arbitration system." The same is true of the view that a respondent requires leave under s 38.

81 The reinsurers submitted that if Gordian was correct in arguing that a respondent to an appeal could rely on points of law without obtaining leave, there was no textual reason why it could not also rely on points of fact without obtaining leave, and that was so "rebarbatively unattractive [a] possibility" as to suggest some error in Gordian's construction. This Court, however, for example, often puts up with just such possibilities in many appeals. It is commonplace for special leave to be granted on a short, interesting and important point of law

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51 [1996] AC 800 at 813-814.

52 [1996] AC 800 at 814.

which, if it is a good one, leaves the Court obliged to listen to arguments raised by notice of contention and addressed to it as of right which are long, boring and unimportant. This can be necessary if the curial function is to attain just outcomes, rather than simply to enjoy interesting journeys. The attainment of just outcomes is often accompanied by boredom. The function of arbitration, as much as that of conventional litigation, is the attainment of just outcomes.

82 If the issue whether leave to appeal would have been granted to debate the construction point is material, it should be noted that the construction point involves questions of law. It involves a question of law in the mundane sense that the interpretation of a written agreement between private parties is a question of law[53]. But beyond that mundane question of law there may be two specific but important errors of law. The arbitrators may have erred in their use of the phrase "common understanding and intention of the parties". That suggests that they erred in searching for the subjective intentions of the parties. That is an extremely important matter, not always well understood[54]. It is very well established in this Court, and indeed in other ultimate appellate courts[55], that the question is not what contracting parties subjectively intended, believed or understood. The question is, subject to special common law or equitable rules usually based on error or disadvantage[56], what each party by words or conduct would have led a reasonable person in the position of the other party to believe[57]. A departure from these principles by arbitrators is a serious matter. They are not principles merely reflective of some quaint minor guide to construction. They go to central substantive conceptions of the law of contract in the Anglo-Australian common law. A second respect in which the arbitrators may have erred is their seeming reliance on post-contractual events as a guide to contractual interpretation. Some see that as more controversial, but it is a very important question of law.

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53 *Pioneer Shipping Ltd v BTP Tioxide Ltd* [1982] AC 724 at 736. See also *Pilgrim Shipping Co Ltd v The State Trading Corporation of India Ltd (The "Hadjitsakos")* [1975] 1 Lloyd's Rep 356 at 361 per Roskill LJ and 366 per Sir John Pennycuick.

54 On a closely related question – the role of intention in determining whether trusts have been created – compare *Saunders v Deputy Commissioner of Taxation* [2010] WASC 261 at [22] with *Byrnes v Kendle* (2011) 85 ALJR 798; 279 ALR 212; [2011] HCA 26.

55 For example, the House of Lords: *Pioneer Shipping Ltd v BTP Tioxide Ltd* [1982] AC 724 at 736.

56 *Byrnes v Kendle* (2011) 85 ALJR 798 at 820 [101]; 279 ALR 212 at 238.

57 *Pacific Carriers Ltd v BNP Paribas* (2004) 218 CLR 451 at 461-462 [22]; [2004] HCA 35; *Toll (FGCT) Pty Ltd v Alphapharm Pty Ltd* (2004) 219 CLR 165 at 179 [40]; [2004] HCA 52.

83 That deals with the first and third of the Court of Appeal's points. The merit of the second point in this particular case depends on considering what is actually involved in Gordian's argument. As will be seen, it is not necessary to examine a mass of detailed evidence. The relevant materials comprise only a few pages.

Does s 22(2) of the Arbitration Act defeat Gordian?

84 The reinsurers put the second preliminary point thus. They submitted, in answer not only to ground 8, but also to grounds 5-7 and 9-12, in the Notice of Contention that those grounds "ignore the fact that, under s 22(2) of the [Arbitration Act], the arbitrators were not bound to observe the strict rules of evidence and procedure or common law rules of construction of contracts". For this proposition they gave four citations, to be analysed below. The reinsurers also submitted: "the parties had expressly permitted the arbitrators to rely on their own knowledge and expertise". For this they gave two references to the transcript of argument before the arbitrators. The reinsurers then submitted: "All of the criticisms of the arbitrators' methodology fall away once these points are recognised."

85 These points may answer some aspects of grounds 5-7 and 9-12. They do not answer ground 8.

86 Section 22 of the Arbitration Act provides:

> "(1) Unless otherwise agreed in writing by the parties to the arbitration agreement, any question that arises for determination in the course of proceedings under the agreement shall be determined according to law.
>
> (2) If the parties to an arbitration agreement so agree in writing, the arbitrator or umpire may determine any question that arises for determination in the course of proceedings under the agreement by reference to considerations of general justice and fairness."

According to the arbitrators, the reinsurance treaties contained an agreement attracting s 22(2). But what does the expression "considerations of general justice and fairness" mean?

87 One of the citations to which the reinsurers referred was *Eagle Star Insurance Co Ltd v Yuval Insurance Co Ltd*[58]. The English Court of Appeal had

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58 [1978] 1 Lloyd's Rep 357.

under consideration a clause providing that the arbitrators were not bound by the strict rules of law, and enjoining them to decide "according to an equitable rather than a strictly legal interpretation of the provisions of" the agreement. It was submitted that the clause was void as ousting the jurisdiction of the courts. The Court of Appeal, in ex tempore judgments, rejected that submission, but did not specifically propound any construction supporting the reinsurers in this appeal. Lord Denning MR said that the clause "only ousts technicalities and strict constructions."[59] Goff LJ said that the clause rendered the arbitrators "able to view the matter more leniently and having regard more generally to commercial considerations than would be done if the matter were heard in Court"[60]. On that point Shaw LJ agreed with both judgments. Their Lordships did not say whether the clause rendered the interpretation inquiry "objective" or "subjective". In any event the relevant clause was different from s 22(2).

88 The second citation to which the reinsurers referred was a passage in Mustill and Boyd[61]. The passage referred to treated *Eagle Star Insurance Co Ltd v Yuval Insurance Co Ltd* as offering a narrow interpretation – the second narrowest out of seven – of a particular type of provision. The learned authors gave two instances of that type of provision[62]. One was: "The arbitrator shall be entitled to decide according to equity and good conscience and shall not be obliged to follow the strict rules of law". The other was: "The arbitrator shall be entitled to act as *amiable compositeur*." Again, the clauses are different from s 22(2); and, again, the learned authors, in their discussion of the seven interpretations, did not offer any opinion about whether the objective rule of contractual interpretation or the rule against taking into account post-contractual events were to be abandoned.

89 The third citation referred to by the reinsurers was a passage from O'Neill and Woloniecki[63]. That passage discussed s 33(1) of the *Arbitration Act* 1996 (UK), which provided that an arbitral tribunal is obliged to:

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59 [1978] 1 Lloyd's Rep 357 at 362.

60 [1978] 1 Lloyd's Rep 357 at 363-364.

61 *The Law and Practice of Commercial Arbitration in England*, 2nd ed (1989) at 82.

62 Mustill and Boyd, *The Law and Practice of Commercial Arbitration in England*, 2nd ed (1989) at 74.

63 *The Law of Reinsurance in England and Bermuda*, 2nd ed (2004) at 762-763 [14-15].

> "(a) act fairly and impartially as between the parties, giving each party a reasonable opportunity of putting his case and dealing with that of his opponent, and
>
> (b) adopt procedures suitable to the circumstances of the particular case, avoiding unnecessary delay or expense, so as to provide a fair means for the resolution of the matters falling to be determined."

The learned authors say nothing to suggest that the legislation empowers an arbitrator to depart from the common law rules of contractual interpretation.

90 The fourth citation referred to by the reinsurers was a discussion by Young J on the meaning of s 22(2) in *Woodbud Pty Ltd v Warea Pty Ltd*[64]. Young J treated s 22 as deriving from "the conception of an amiable compositeur." He uttered the following tentative remarks:

> "Probably the clause goes further than evidentiary and procedural problems and permits an amiable compositeur to disregard such rules as the parol evidence rule, the rule that contracts by specialty cannot be varied by oral contract … and the rule that one cannot look to subsequent conduct to construe a contract …
>
> The amiable compositeur may also disregard the rule that collateral contracts cannot be inconsistent with the main contract, he or she may apply principles of rectification and perhaps may also supplement the contract by filling out the contractual regime in areas where the parties have not thought it through. It is uncertain how far, if at all, the amiable compositeur can go beyond this."

Of course, to apply principles of rectification is not to depart from legal principle. These remarks were not only tentative, but also were obiter dicta, because Young J held that for various procedural reasons s 22 did not apply. Even if this passage is correct about the subsequent conduct rule, which is, with respect, to be doubted, it is silent about subjective/objective interpretation. Like the other three citations, the passage is not strongly persuasive against permitting Gordian's construction argument to be considered. It is to be noted that the reinsurers did not contend that s 22(2) was supportive of any particular step in the detailed reasoning of the arbitrators on construction.

91 The reinsurers' submission that "the parties had expressly permitted the arbitrators to rely on their own knowledge and expertise" does not seem to apply to ground 8 of the Notice of Contention, whatever its application to other grounds. In construing the contract the arbitrators did not purport to rely on any

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64 (1995) 125 FLR 346 at 355-356.

knowledge and expertise distinct from their skills in contractual construction. The transcript passages relied on are irrelevant to the construction point.

The construction point

92 The arbitrators saw the question as being whether any of the reinsurance treaties covered the FAI policy. The FAI policy covered claims made and notified to Gordian within a period of seven years from 31 May 1999. The arbitrators saw that question as turning on the ambit of the 1999 reinsurance treaty.

93 The documentary arrangements between the reinsurers and Gordian were, characteristically for this industry, disorganised and casual to a degree. But the parties do agree that there was a contract. Gordian contended, and the reinsurers did not deny, but on occasion seemed positively to accept, that the contractual documents are to be found in "reinsurance placing slip No. 99AX4050", which each of the reinsurers stamped and signed on various dates between 23 and 31 December 1998, and documents attached to that document, particularly a letter of 15 December 1998 also stamped and signed by each reinsurer on those dates. The serious, precise, decorous, methodical and regular solemnity of this conduct, giving the relevant documents special significance in a sea of chaos, strongly supports Gordian's contention. It also strongly suggests that while anything that happened later may have been an attempt to negotiate a variation of the contract, it was not part of the contract as initially formed.

94 The arbitrators noted that the:

> "1998 reinsurance treaty did not expressly include, limit or exclude cover in respect of run-off policies or policies for extended periods or with extended reporting periods other than by a Professional Indemnity North America ('PINA') clause which excluded claims which arose in the United States of America or Canada out of policies with reporting periods exceeding 36 months beyond the expiry of the policy unless specially accepted (exclusion (iii)) or which were issued for periods longer than 12 months plus 'odd time' not exceeding 18 months in all unless specially accepted (exclusion (v))."

This "PINA clause", dealing with North American risk, was not applicable to the claims in issue in the arbitration.

95 Later the arbitrators said:

> "Apart from the PINA clause, neither the 1998 reinsurance treaty nor the slips signed and stamped by the reinsurers in late 1998 expressly included, excluded or limited cover for policies for extended periods or with extended reporting periods."

96 The arbitrators then proceeded to make a series of findings. They said:

> "According to the reinsurers, the context for Gordian's request in its letter of 15 December 1998 for 'multi year' reinsurance cover was that, in accordance with general industry practice, the then current 1998 reinsurance treaty applied to D&O policies which provided cover for a period of 12 months plus odd time not exceeding 18 months in all."

Why did the reinsurers make that submission? The "period of 12 months plus odd time not exceeding 18 months in all" corresponded with exclusion (v) of the PINA clause, but that only applied to North America.

97 The arbitrators said:

> "Gordian disputed that premise. However, it did not offer any plausible alternative. It was effectively left with the unattractive proposition that the 1998 reinsurance treaty covered every Gordian D&O policy irrespective of the period of cover for which it provided, even policies which were for an unlimited period, at least if such policies were within Gordian's 'established acceptance and underwriting policy in respect of' D&O policies."

The quoted words come from Art 16 of the 1998 treaty, which provided:

> "The Reinsured undertakes not to introduce any change in its established acceptance and underwriting policy in respect of the class or classes of business to which this Agreement applies without prior approval of the Reinsurers, and any reinsurance arrangements relating thereto shall be maintained or be deemed to be maintained unaltered for the purpose of this Agreement."

In the reinsurance placing slip issued in December 1998 and signed by the four reinsurers, opposite the word "CLASS" appeared the following:

> "Business underwritten by the Reinsured and classified by them as Professional Indemnity, Directors and Officers Liability Insurance (which term includes Company Reimbursement Insurance) and Superannuation Trustee Liability."

Opposite the word "WORDING" appeared the words: "As expiring as far as applicable, amendments to be agreed by Reinsurers." Hence, contrary to what the arbitrators said, Gordian did have a "plausible alternative" to the reinsurers' argument that their reinsurance obligations only applied to D and O policies providing cover for "12 months plus odd time not exceeding 18 months in all". The "plausible alternative" – which is not an "unattractive proposition" – was that the reinsurers were protected by the obligation on Gordian not to change its "established acceptance and underwriting policy", about which the reinsurers had

full knowledge from disclosures made to them. If that policy was to issue cover for long periods, nothing stopped the 1998 reinsurance treaty applying. But if that policy was to issue cover for short periods, they could not be lengthened unless Art 16 was complied with. The protection for the reinsurers – the "plausible alternative" – did not lie in specific short time periods, but in adherence to Gordian's established acceptance and underwriting policy. Gordian's submission that this was true for both the 1998 and the 1999 years is sound.

98 After the arbitrators stated a step in their reasoning to which it will be necessary to return below, they said:

> "[W]e are satisfied that the 1998 reinsurance treaty applied to D&O policies which provided cover for a period of 12 months plus odd time not exceeding 18 months in all."

They gave no explanation for this conclusion other than the following:

> "That was plainly the common understanding and intention of the parties when the 1999 reinsurance treaty was arranged at the end of 1998 and Gordian's letter of 15 December 1998 was initialled and stamped by all reinsurers which signed and stamped the slip for the 1999 reinsurance treaty."

The arbitrators did not explain why the period fixed by exclusion (v) of the PINA clause should apply rather than any other period. They did not explain how the "common understanding and intention of the parties" not referred to in any contractual document or conversation was material in law. Nor did the reinsurers[65].

99 The arbitrators then said:

> "The reinsurers accept that they agreed by the reinsurance treaties to cover D&O policies which covered claims which were made and notified to Gordian within an extended period of three years and that the reinsurance treaties should be regarded as having that extended operation although it might not have been satisfactorily recorded."

But was the acceptance soundly based? And what is the relationship between the "extended period of three years" and "12 months plus odd time not exceeding 18 months in all"? Why did the arbitrators select that three year period?

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65 Cf the authorities cited at [82] fn 55-57.

100 The arbitrators continued:

> "Gordian's subsequent communications with Aon Re and internal memoranda confirmed that the reinsurance which it had sought and obtained covered claims which were made and notified to Gordian within an extended period of 3 years. Nothing in the subsequent events, including the reinsurers' attempts to have that position formally recorded in the documentation, causes us to doubt that the reinsurance treaties did not cover the FAI D&O run-off policy which covered claims which were made and notified to Gordian within the much longer period permitted by that policy of 7 years."

The arbitrators did not explain how "subsequent communications", "internal memoranda" and "subsequent events", to which they had also referred earlier, could be material in law to the issue of construing a contract complete before they happened. Nor did the reinsurers[66].

101 Underlying the arbitrators' reasoning may be the circumstance that exclusion (v) in the PINA clause, which spoke of "policies issued for periods longer than 12 months plus 'odd time' not exceeding 18 months in all", was omitted after 1998. The new PINA clause, however, retained exclusion (iii), dealing with "claims made coverages with an extended reporting period obligation exceeding 36 months beyond the expiry of the policy unless specially accepted." This may explain the shift from references to the shorter period to references to a three year period – but not convincingly, since it does not explain why the PINA clause, relating only to North American risk, was relevant at all.

102 The reinsurers described what was said by the arbitrators in these passages as "factual findings". So far as they are factual findings, they are factual findings relevant only to a question of law, the interpretation of the reinsurance contract, and factual findings themselves affected by errors of law.

103 Success for Gordian on the construction point will not flow merely from destructive criticisms of the arbitrators' reasoning. What was Gordian's positive case on construction? Gordian argued that the key terms of the contract for present purposes were to be found in the letter of 15 December 1998 from Gordian to Gordian's broker dealing with the "$10M XS $10M" treaty. That letter was attached to the reinsurance placing slip and, like that slip, stamped by all reinsurers by 31 December 1998. In par 4.0, the letter said: "For 1999 we seek the following". Among the matters then listed were: "multi year cover (see paragraph 6.0)" and "equivalent cover to 1998 (or better)". Gordian argued that

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66 Cf *Administration of Papua and New Guinea v Daera Guba* (1973) 130 CLR 353 at 405, 446 and 459; [1973] HCA 59.

the specification that cover was to be equivalent to 1998 or better was a stipulation that there was to be no exclusion of or limit on multi year cover, because there had been none in the expiring reinsurance contract for 1998. Gordian also argued that the reference to "multi year cover" indicates that there was to be no limitation to any particular time frame for the contracts in relation to which reinsurance was to be provided such as three years. Are those arguments invalidated by par 6.0 of the letter? It said:

> "As I mentioned earlier, we do not have the treaty contracts for 1998, nor on checking, do we appear to have the wordings for 1997 or 1996 and will follow up with Flemings, however, I recall that there was a limit on the treaty that it would cover original contracts issued for 12 months plus odd term but not to exceed 18 months in all. This is certainly the case pertaining to USA/Canada risks as set out in the 'PINA Special Clause.'"

Gordian argued that the writer's recollection was correct for USA/Canada risks, to which the PINA clause in its 1998 form applied, but not for other risks, for in relation to them there was no limitation for 1998. Paragraph 6.0 continued:

> "Multi year contracts have gained popularity in recent years and we are frequently asked to write for periods of two to three years, usually as a stretched aggregate over the terms or on annual limits basis. In some cases, we are asked after the first year of a multi year contract to 'roll forward' the contract for another year so that a new (2 or 3 year) period commences. Our competitors are able to offer this and we have been offering it within our retention but need to obtain reinsurers agreement to use the treaty capacity to write multi year contracts and would appreciate the Everest's comments on this issue, including under the 'PINA Special Risks Clause.'"

Gordian accepted that this language proceeded from the erroneous assumption that the 1998 treaties did not apply to multi year contracts – ie those extending for any period beyond the year of the reinsurance treaty, whether for "12 months plus odd term but not to exceed 18 months in all", or longer. But Gordian submitted nonetheless that the language was stipulating multi year cover, as distinct from multi year cover but only up to a three year limit, which the reinsurers contended for. Gordian submitted that when all four reinsurers stamped the reinsurance placing slip and also stamped the 15 December 1998 letter attached to it, they accepted that stipulation.

104 The reinsurers did not respond to Gordian's submission. That submission is correct. It is appropriate to read cl 6.0 in that way so as to make it harmonious with cl 4.0, and that clearly refers to unconditional and unlimited multi year cover.

105 What about a letter from one of the reinsurers to Gordian's broker on 22 December 1998? It confirms a quote and says, inter alia: "Original contracts: Up to three years is acceptable. PINA Clause to be amended." Gordian submitted that on its true construction, this statement related only to the PINA clause. That is correct. Even if that is not so, as the arbitrators found, the 22 December 1998 letter did not go to two of the reinsurers; it was, unlike the 15 December 1998 letter, not affixed to the reinsurance placing slip; and hence it is at most an item of pre-contractual negotiation not reflected in the contract itself. The reinsurers did not respond to Gordian's submission. Gordian's submission is correct.

106 The assent by all four reinsurers to the 15 December 1998 letter was manifested in solemn formalities – their stamping of it and its attachment to the reinsurance placing slip, also stamped by them on various dates from 23 to 31 December 1998. This solemnly formalised assent demonstrates that Gordian's submissions on the construction point are correct.

107 However, the arbitrators made a finding which, although it was stated as part of the arbitrators' reasoning quoted at some length above[67], is conveniently to be dealt with now.

> "We are not persuaded that the FAI D&O run-off policy, which covered claims which were made and notified to Gordian within the extended period permitted by that policy of 7 years from 31 May 1999, was within its then 'established acceptance and underwriting policy in respect of' D&O policies."

It is necessary to deal with this finding because, if it had been open to the arbitrators, it would have created an obstacle to Gordian's success. Indeed Gordian conceded that that finding was "utterly fatal" to it, if it were properly made. But by ground 7 of the Notice of Contention, Gordian contended that the finding had not been properly made. That was because the issue had been expressly withdrawn by the reinsurers on the first day of the arbitration. The withdrawal arose as a consequence of amending the reinsurers' cross-claim to delete an allegation that the underwriting "represented a change to the established underwriting policy of the claimant". The contention which Gordian put to this Court was also put to the Court of Appeal. It said[68]:

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67 See above at [96]-[101].

68 *Gordian Runoff Ltd v Westport Insurance Corporation* (2010) 267 ALR 74 at 125 [291].

> "There are powerful considerations in support of this contention: the pleading of the point appears to have been abandoned, no evidence was led by the reinsurers on the question and the hearing otherwise appears to have been so conducted."

With respect, these points are sound, and Gordian's argument must be accepted.

108 The reinsurers argued in this Court that some written submissions on both sides addressed the question, that Gordian's established acceptance and underwriting policy was part of the factual controversy, and thus that the arbitrators were entitled to make the finding of which Gordian complains. One difficulty is that the written submissions in question were lodged with the arbitrators and exchanged between the parties before the amendment to the cross-claim dropped the issue: when it was silently dropped, so were the corresponding parts of the written submissions. A further difficulty is that the arbitrators were reminded, in Gordian's closing written submissions, that the issue had been abandoned. This Court was taken to no denial by the reinsurers of that assertion.

109 The reinsurers also argued that they had cross-examined one of Gordian's witnesses on the issue. In fact the cross-examination was on another point.

110 Gordian's construction of the reinsurance contract is correct. No claim for rectification was made in this Court. No other issue arises.

The merits of arbitration

111 The arbitration proceedings began on 15 October 2004 when Gordian served points of claim. This appeal comes to a close seven years later. The attractions of arbitration are said to lie in speed, cheapness, expertise and secrecy. It is not intended to make any criticisms in these respects of the arbitrators, of Einstein J, or of the Court of Appeal, for on the material in the appeal books none are fairly open. But it must be said that speed and cheapness are not manifest in the process to which the parties agreed. A commercial trial judge would have ensured more speed and less expense. On the construction point it is unlikely that the arbitrators had any greater *relevant* expertise than a commercial trial judge. Secrecy was lost once the reinsurers exercised their right to seek leave to appeal. The proceedings reveal no other point of superiority over conventional litigation. One point of inferiority they reveal is that there have been four tiers of adjudication, not three. Comment on these melancholy facts would be superfluous.

Orders

112 It follows that the appeal and the balance of the application for special leave to appeal must be dismissed with costs.

113 KIEFEL J. These proceedings concern an Award of arbitration which determined the rights of the parties to treaties for reinsurance and the effect of s 18B(1) of the *Insurance Act* 1902 (NSW) upon the obligation of the appellant reinsurers under the treaties to indemnify the respondent, Gordian Runoff Limited ("Gordian"). The New South Wales Court of Appeal held that leave should not have been granted by the primary judge, under s 38(4)(b) of the *Commercial Arbitration Act* 1984 (NSW), to the reinsurers to bring an appeal with respect to that Award.

114 Gordian was an underwriter of professional indemnity ("PI") insurance and directors and officers liability ("D&O") insurance. Prior to December 1998 its PI and D&O portfolio was partially reinsured under a treaty for reinsurance whereby it was agreed that risks underwritten by Gordian with respect to those classes of insurance would be the subject of excess of loss reinsurance. The reinsurers included the first and second appellants, Westport Insurance Corporation ("Westport") and Assetinsure Pty Limited ("Assetinsure"). That treaty ("the 1998 reinsurance treaty") was due to expire on 31 December 1998.

115 Gordian, together with a Lloyd's syndicate, had previously written a D&O policy for FAI Insurance Limited ("FAI"). In the latter part of 1998 a takeover of FAI by HIH Winterthur International Holdings Limited was imminent and FAI's broker negotiated with Gordian for a run-off policy. Those negotiations culminated in an agreement, on 23 December 1998, that Gordian would indemnify FAI for claims in respect of wrongful acts occurring before the effective date, later agreed to be 31 May 1999, which were made and notified to Gordian within seven years of that date ("the FAI policy").

116 On 17 December 1998 Gordian's broker approached Westport for reinsurance of a part, or layer, of Gordian's PI and D&O portfolio for the 1999 calendar year ("the $10 million in excess of $10 million layer"). One of the matters discussed by the broker with Westport was the prospect of "multi year covers". In that regard a copy of Gordian's letter to the broker of 15 December 1998 was forwarded to Westport. The letter did not mention Gordian's proposal with respect to the FAI policy or its term, but it stated that Gordian had often been asked by clients to write insurance for periods of two to three years and that it wished to seek "reinsurers [sic] agreement to use the treaty capacity to write multi year contracts". Gordian asked the broker to seek comments from the lead reinsurer (who did not, however, participate in the 1999 reinsurance treaty). Westport's quotation on its proportion of the layer, of 22 December 1998, included the statement: "Original contracts: Up to three years is acceptable. PINA Clause[69] to be amended."

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69 Professional Indemnity North American clause.

117 On 23 December 1998, the day on which the agreement between Gordian and FAI was struck, a placing slip was signed and stamped by Westport, Assetinsure and the third appellant, Munich Reinsurance Company of Australasia Limited, with respect to the $10 million in excess of $10 million layer. The latter signed again on 29 December 1998. NAC Reinsurance International Limited ("NAC") signed on 31 December 1998 (NAC's reinsurance liabilities were subsequently acquired by the fourth appellant, XL Re Limited). Each of the reinsurers initialled and stamped a copy of Gordian's letter of 15 December 1998. Only one reinsurer sighted Westport's quotation of 22 December 1998, but it was conceded by all reinsurers in the later arbitration proceedings that the relevant reinsurance treaties covered "D&O policies which covered claims which were made and notified to Gordian within an extended period of three years".

118 Other reinsurance treaties were effected in 1999 with respect to the lower layers of Gordian's portfolio – the $5 million in excess of $5 million layer and the $3 million in excess of $2 million layer. The reinsurers signing placing slips for these treaties were Westport, Assetinsure, Zurich Insurance Company Reinsurance (the reinsurance liabilities of which were acquired by the fifth appellant, Scor Switzerland Ltd) and Copenhagen Reinsurance Company Ltd. The arbitrators found that the terms applying to the treaty for the $10 million in excess of $10 million layer were not materially different from the terms of the treaties for the lower layers. In these reasons "the 1999 reinsurance treaty" refers to the treaty for the higher layer and also to the terms of the other treaties.

119 The placing slip for the 1999 reinsurance treaty was expressed to apply to "[c]laims made on policies attaching during the period 1 January 1999 to 31 March 2000"[70]. The type of reinsurance was confirmed to be "[e]xcess of loss" and the "class" to be "[b]usiness underwritten by the Reinsured and classified by them as Professional Indemnity, Directors and Officers Liability Insurance". It did not contain further terms but rather the statement that "wording" was "[a]s expiring as far as applicable", a reference to the 1998 reinsurance treaty, and "amendments to be agreed by Reinsurers." The placing slip was also stamped "all terms, wordings, special acceptances [or agreements] and amendments to be agreed by [the relevant reinsurer]." All but XL Re Limited provided for a warranty by Gordian of "no more favourable terms".

120 The 1998 reinsurance treaty was expressed to apply to claims made on policies attaching during the period 1 January 1998 to 31 December 1998. The class of business covered was business underwritten by Gordian and classified by it as PI and D&O insurance. The treaty contained one clause, the PINA clause, which excluded claims arising in the United States of America or Canada out of policies having reporting periods in excess of 36 months after the expiry of the

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70 The period was later extended to 30 June 2000.

policy, or which were issued for periods longer than 12 months plus "odd" time not exceeding 18 months, unless specially accepted. It did not otherwise include or exclude policies having an extended reporting period, which is to say the period within which claims were to be made or notified.

121 No other wording of the 1999 reinsurance treaty was the subject of further agreement between the parties. On 20 January 1999 Gordian's broker sent draft wording to Gordian and Westport. Gordian advised that it was in order, but asked for confirmation that cover would extend "for policies that are issued for terms in excess of 12 months (provided of course that the original policy incepts between 01/01/99 and 31/03/00)." Westport agreed with the proposed wording, but not until shortly prior to the expiry of the 1999 reinsurance treaty.

122 In 2001 and 2002, after Gordian was notified of circumstances which could give rise to a claim under the FAI policy and the reinsurers were so advised, further attention was directed to revised wording for the 1999 reinsurance treaty. In particular, it appears that two of the reinsurers raised the issue of an exclusion of policies issued for periods longer than three years, but the addition of such an exclusion was never agreed upon.

Dispute and arbitration

123 The reinsurers did not accept that claims made under the FAI policy were properly the subject of the 1999 reinsurance treaty. They contended that the treaty did not respond to that policy because the policy covered claims made or notified within seven years from its inception, not three. The parties submitted their dispute to arbitration in accordance with the terms of the 1999 reinsurance treaty and appointed three arbitrators.

124 The Award of the arbitrators, expressed with respect to the $10 million in excess of $10 million layer, was that the 1999 reinsurance treaty applied to claims which were made under the FAI policy "within 3 years from the inception of that policy but no other claims". The process of reasoning by which that conclusion was reached was not one simply of the construction of the terms of the 1999 reinsurance treaty. Indeed, the arbitrators' view of the treaty terms favoured the reinsurers. It was reached by the arbitrators applying s 18B(1) of the *Insurance Act* to the treaty.

125 The arbitrators' findings with respect to the indemnity provided by the 1999 reinsurance treaty may be summarised as follows. The nature of the FAI policy, as a run-off policy, did not assume importance. The issue was whether the treaty "covered claims which were made and notified to Gordian within the extended period permitted by that policy of 7 years from 31 May 1999." When the 1999 reinsurance treaty was arranged the common understanding of the parties was that the indemnity provided by the 1998 reinsurance treaty would apply, namely that it would apply to D&O policies which provided cover for a

period of 12 months, plus odd time not exceeding 18 months in all. The arbitrators accepted the reinsurers' contention that this cover accorded with the general industry practice at the time for this type of insurance and that it explained Gordian's request for "multi year" reinsurance. Although disputing this, Gordian's alternative proposition, that the 1998 reinsurance treaty covered every D&O policy written by Gordian irrespective of the period of cover the policy provided, did not commend itself to the arbitrators.

126 To these findings the arbitrators were able to add that the reinsurers accepted that they had agreed, by the 1999 reinsurance treaty, to cover D&O policies which covered claims which were made and notified to Gordian within an extended reporting period of three years, although this may not have been satisfactorily recorded. The reinsurers sought rectification of the treaties, if necessary.

127 The conclusion expressed by the arbitrators was that the 1999 reinsurance treaty "do[es] not cover the 3-year claims under the FAI D&O run-off policy although they were made within 3 years from the inception of that policy because the policy covered claims which were made and notified to Gordian within 7 years from its inception". The arbitrators, however, went on to apply s 18B(1) to reach their ultimate conclusion, that the 1999 reinsurance treaty applied to claims made within three years of the inception of the FAI policy.

128 Section 18B(1) provides:

> "Where by or under the provisions of a contract of insurance entered into, reinstated or renewed after the commencement of this section:
>
> (a) the circumstances in which the insurer is bound to indemnify the insured are so defined as to exclude or limit the liability of the insurer to indemnify the insured on the happening of particular events or on the existence of particular circumstances, and
>
> (b) the liability of the insurer has been so defined because the happening of those events or the existence of those circumstances was in the view of the insurer likely to increase the risk of loss occurring,
>
> the insured shall not be disentitled to be indemnified by the insurer by reason only of those provisions of the contract of insurance if, on the balance of probability, the loss in respect of which the insured seeks to be indemnified was not caused or contributed to by the happening of those events or the existence of those circumstances, unless in all the circumstances it is not reasonable for the insurer to be bound to indemnify the insured."

129 The sub-section is not without difficulty in its application, as will be discussed later in these reasons. However, its purpose is clear enough. It was drawn from s 138 of the *Consumer Credit Act* 1981 (NSW). The concern of s 138, as the New South Wales Law Reform Commission observed[71], was with the unfair practice of some insurers who relied upon exclusion or limitation clauses otherwise than "where the loss is caused or contributed to by the happening of the events or circumstances to which the clauses are directed." Where the event or circumstance has a "true nexus with the loss", the clauses could properly be invoked. Where it does not, it would not ordinarily be unreasonable to require the insurer to provide the indemnity. However, the Commission also recommended that a proviso be added, which allowed consideration as to whether it was not reasonable for the insurer to be bound to do so[72].

130 An example given by the New South Wales Law Reform Commission of an exclusion to which the provision was directed, was one which denied an indemnity under a motor vehicle policy where the driver was unlicensed or disqualified. A vehicle driven by such a driver may be involved in an accident in circumstances entirely due to the fault of another driver. In such a case it is unlikely that the absence of a licence could be shown to have "caused or contributed to" the loss[73].

131 It may also be observed that the sub-section is not expressed to apply to reinsurance. Its evident purpose is the protection of consumers of insurance services, whose bargaining position might not be thought to be analogous to that of insurer and reinsurer. Contracts of reinsurance are now exempt from the operation of the sub-section[74]. But at the time of the arbitration there was authority for the view that "insurance" in the *Insurance Act* included reinsurance[75] and the parties conducted the arbitration on the basis that s 18B(1)

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71 New South Wales Law Reform Commission, *Community Law Reform Program: First Report – Insurance Contracts: Non-Disclosure and Misrepresentation*, Report No 34, (1983) at 31 [4.17].

72 New South Wales Law Reform Commission, *Community Law Reform Program: First Report – Insurance Contracts: Non-Disclosure and Misrepresentation*, Report No 34, (1983) at 53 [7.34].

73 New South Wales Law Reform Commission, *Community Law Reform Program: First Report – Insurance Contracts: Non-Disclosure and Misrepresentation*, Report No 34, (1983) at 52 [7.33].

74 Insurance Regulation 2009 (NSW), cl 4(b).

75 *HIH Casualty & General Insurance Ltd (In Liq) v R J Wallace* (2006) 68 NSWLR 603 at 615 [26].

applied to the 1999 reinsurance treaty. For that reason the Court of Appeal did not allow the reinsurers to adopt a different course on the appeal, to deny the application of the sub-section to reinsurance contracts altogether[76]. That approach was clearly correct. The position adopted by the parties should continue to be maintained. But that does not deny the relevance of the operation and effect of the 1999 reinsurance treaty as a contract of reinsurance when s 18B(1) comes to be applied to it.

132 Before the arbitrators the reinsurers contended that the concern of s 18B(1) is with exclusions or limitations upon what is otherwise provided as the scope of cover. They contended that the language of the provision implies that there be a prima facie liability to indemnify against which a disentitlement, by way of exclusion or limitation by reason of some event or circumstance, operates. In the case of the 1999 reinsurance treaty, there was no liability to indemnify in the first place and questions of exclusions or limitations upon it did not arise. The scope of the cover, the reinsurers submitted, did not include the FAI policy. "It was the wrong sort of policy."

133 The arbitrators did not agree. They said that the reinsurers had "agreed to indemnify Gordian in respect of losses under D&O policies underwritten by Gordian" and that the "reason why the reinsurance treaties did not cover D&O policies which did not require that claims be made and notified to Gordian within 3 years from inception was that such D&O policies were excluded or because the D&O policies which were covered by the reinsurance treaties were limited." The arbitrators pointed to the wording some of the reinsurers had sought to add to the 1999 reinsurance treaty, to effect an exclusion of policies issued for periods longer than three years. Additionally, the reinsurers had sought rectification of the 1999 reinsurance treaty terms, to limit the class of business covered to underlying policies having a term not exceeding three years. The arbitrators had not considered rectification to be necessary, given the conclusion they reached as to the cover given by the 1999 reinsurance treaty. But in connection with the application of s 18B(1) the arbitrators said the "formulation [the reinsurers] initially proposed was an exclusion, the latter a limitation."

134 The arbitrators proceeded to address the text of s 18B(1) and its requirements. In relation to the first part of par (a) of the sub-section, they said that the 1999 reinsurance treaty "do[es] not cover the 3-year claims" under the FAI policy, because the treaty was limited to policies where claims must be made or notified within three, not seven, years. They turned to consider whether that exclusion or limitation was based "on the existence of particular circumstances" and determined that the "particular circumstance" must be that the FAI policy

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76 *Gordian Runoff Ltd v Westport Insurance Corporation* (2010) 267 ALR 74 at 116 [239].

allowed for claims to be made more than three years after the inception of that policy. The arbitrators then identified the "loss in respect of which [Gordian] seeks to be indemnified" as "its liability on the 3-year claims" and concluded that it was not caused or contributed to by that circumstance "because the 3-year claims were made and notified to Gordian within 3 years of the inception of the FAI D&O run-off policy." On this approach s 18B(1) operated upon the treaty for reinsurance.

135 The only matter remaining for the arbitrators' consideration was the proviso expressed in s 18B(1), to the obligation cast by the sub-section upon an insurer to provide indemnity despite it being excluded or limited, namely "unless in all the circumstances it is not reasonable for the insurer to be bound to indemnify the insured." The arbitrators had expressed the view, earlier in their reasons, that "we are comfortably satisfied that it would be reasonable within the meaning of s18B(1), and entirely consistent with 'considerations of general justice and fairness' within the meaning of the reinsurance treaties, for the reinsurance treaties to apply in relation to the 3-year claims." At the conclusion of their reasons they explained that they had construed s 18B(1) consistently with its remedial character in reaching their conclusion and that "[i]f at large, 'considerations of general justice and fairness' would produce the same result."

136 The considerations mentioned by the arbitrators are contained in s 22(2) of the *Commercial Arbitration Act* 1984 (NSW)[77], which provides that where the parties to an arbitration agreement agree, in writing, the arbitrator "may determine any question that arises for determination in the course of proceedings under the agreement by reference to considerations of general justice and fairness."

The Supreme Court appeals

137 Section 38(2) of the *Commercial Arbitration Act* provides that, subject to sub-s (4), an appeal shall lie to the Supreme Court of New South Wales "on any question of law arising out of an award." Sub-section (3) provides that on the determination of such an appeal the Supreme Court may confirm, vary or set aside the award or remit the award together with the Supreme Court's opinion on the question of law. Sub-section (4) requires that unless all other parties to the arbitration agreement consent to an appeal being brought, an appeal under sub-s (2) may only be brought with the leave of the Supreme Court. The grant of leave is conditioned by sub-s (5), which provides:

> "The Supreme Court shall not grant leave under subsection (4)(b) unless it considers that:

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77 This Act has been repealed by the *Commercial Arbitration Act* 2010 (NSW), s 42.

(a) having regard to all the circumstances, the determination of the question of law concerned could substantially affect the rights of one or more parties to the arbitration agreement, and

(b) there is:

(i) a manifest error of law on the face of the award, or

(ii) strong evidence that the arbitrator or umpire made an error of law and that the determination of the question may add, or may be likely to add, substantially to the certainty of commercial law."

138 In the Supreme Court, the primary judge (Einstein J) determined both the question of leave and the substantive appeal at the same time, an approach which was considered by the Court of Appeal to be incorrect[78]. The error of law identified by Einstein J was the failure by the arbitrators to recognise that the agreement by the reinsurers, to extend cover under the 1999 reinsurance treaty to include Gordian's D&O policies issued for up to three years, was not a limitation or exclusion in the sense contemplated by s 18B(1)[79]. His Honour granted leave, allowed the appeal, set aside the Award and ordered in lieu that Gordian's claim be dismissed, and made orders for costs.

139 The Court of Appeal allowed Gordian's appeal from those orders and did so by reference to the requirements of s 18B(1) of the *Insurance Act* and s 38(5)(b) of the *Commercial Arbitration Act*. Allsop P, with whom the other members of the Court (Spigelman CJ and Macfarlan JA) agreed, did not revisit the arbitrators' findings on the construction of the 1999 reinsurance treaty. His Honour held that leave should not have been given by the primary judge on the ground that there was an error of law on the face of the Award, concerning the application of s 18B(1), which was manifest within the meaning of s 38(5)(b)(i). His Honour was assisted to this conclusion by a concession made by the reinsurers on the appeal[80]. His Honour further held that there was not strong evidence of error as required by s 38(5)(b)(ii)[81].

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78 *Gordian Runoff Ltd v Westport Insurance Corporation* (2010) 267 ALR 74 at 95 [113].

79 *Westport Insurance Corporation v Gordian Runoff Ltd* (2009) 15 ANZ Insurance Cases ¶61-798 at 77,418.

80 *Gordian Runoff Ltd v Westport Insurance Corporation* (2010) 267 ALR 74 at 95 [116].

81 *Gordian Runoff Ltd v Westport Insurance Corporation* (2010) 267 ALR 74 at 106 [172].

140 Two matters not dealt with by the primary judge, but which were raised by the reinsurers on the appeal before him, were considered by Allsop P. The first related to the requirement in s 18B(1) that the loss in respect of which indemnity was sought was not caused or contributed to by the circumstance giving rise to the exclusion or limitation; the second related to the sufficiency of the reasons given with respect to the proviso to the sub-section.

141 Allsop P considered that there may have been an error in the reasoning of the arbitrators on the firstmentioned point, in the way in which they dealt with the loss suffered by Gordian[82]. This assumes some importance in these proceedings. However, his Honour did not consider that it qualified as an error for the purpose of s 38(5)(b)(i) or (ii) of the *Commercial Arbitration Act*. The question of causation of loss was not a question of law, in his Honour's view[83]. If there was an error of law, his Honour considered that it was neither manifest nor strongly arguable as such[84]. The arbitrators' reasoning, whilst not following a conventional approach, was nevertheless defensible[85].

142 On the second question, the reinsurers had argued that the reasons given by the arbitrators were inadequate for they had not dealt with the inquiry in the proviso, and nor had they explained why it was reasonable in all the circumstances to hold the reinsurers bound to indemnify Gordian. However, Allsop P considered that the proviso involved an "ultimately evaluative task after all relevant facts had been found", and that no further explanation was required[86]. That conclusion was reached by his Honour after consideration[87] of cases and materials concerned with the provision of reasons by arbitrators and, in

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82 *Gordian Runoff Ltd v Westport Insurance Corporation* (2010) 267 ALR 74 at 106-107 [180]-[182].

83 *Gordian Runoff Ltd v Westport Insurance Corporation* (2010) 267 ALR 74 at 107 [182].

84 *Gordian Runoff Ltd v Westport Insurance Corporation* (2010) 267 ALR 74 at 107 [183].

85 *Gordian Runoff Ltd v Westport Insurance Corporation* (2010) 267 ALR 74 at 107 [184].

86 *Gordian Runoff Ltd v Westport Insurance Corporation* (2010) 267 ALR 74 at 109 [198], 110 [200].

87 *Gordian Runoff Ltd v Westport Insurance Corporation* (2010) 267 ALR 74 at 109-111 [199]-[207], 114 [220].

particular, what had been said in that regard in *Oil Basins Ltd v BHP Billiton Ltd*[88] and *Bremer Handelsgesellschaft mbH v Westzucker GmbH (No 2)*[89].

The issues in these proceedings

143 Section 29(1) of the *Commercial Arbitration Act* requires that, unless otherwise agreed in writing by the parties to the arbitration, an arbitrator make an award in writing, sign it and include in the award "a statement of the reasons for making the award." The reinsurers have been granted special leave to appeal to this Court concerning the sufficiency of the arbitrators' reasons as to the proviso in s 18B(1).

144 The reinsurers also seek special leave to appeal concerning the question whether the arbitrators were wrong to conclude that s 18B(1) applied given (i) the terms of the 1999 reinsurance treaty and (ii) the requirements of causation in s 18B(1), namely whether the loss in respect of which indemnity is sought was caused by the event or circumstance in which the liability to indemnify was limited or excluded (grounds 5 and 6). If this leave were granted, Gordian would contend that the arbitrators should not have found that the 1999 reinsurance treaty, in its own terms, operated only to give cover to policies having a three year limit.

145 Logically the starting point is the construction of the treaty. It is anterior, and essential, to any consideration of s 18B(1). The second question is whether s 18B(1) applies. The answer to these questions may determine whether that as to the sufficiency of reasons concerning the proviso is reached.

The 1999 reinsurance treaty – its operation

146 Gordian no longer seeks to challenge the Award on the basis of an error concerning the arbitrators' understanding of the general industry practice of providing cover for a period of 12 months for this type of insurance. The concession is well made. The error to which Gordian points concerns what was actually agreed between the parties. But this may not involve a question of law.

147 Gordian contends that its letter of 15 December 1998 to its broker requested multi-year cover and this was understood and accepted by the reinsurers. This follows, it is put, because the letter was attached to the placing slip. The letter was also initialled and stamped by each reinsurer. Thus, on Gordian's argument, what was agreed was not just multi-year cover to a

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88 (2007) 18 VR 346.

89 [1981] 2 Lloyd's Rep 130.

three year limit, but extended to policies written by Gordian for any number of years beyond one year.

148 In the letter of 15 December 1998 it was said that the writer did not have a copy of the 1998 treaty to hand, but recalled that:

> "there was a limit on the treaty that it would cover original contracts issued for 12 months plus odd term [sic] but not to exceed 18 months in all. This is certainly the case pertaining to USA/Canada risks as set out in the 'PINA Special Clause.'"

149 The letter clearly enough concerned Gordian's wish to write D&O policies of up to two to three years, for it said:

> "Multi year contracts have gained popularity in recent years and we are frequently asked to write for periods of two to three years, usually as a stretched aggregate over the terms or on annual limits basis. In some cases, we are asked after the first year of a multi year contract to 'roll forward' the contract for another year so that a new (2 or 3 year) period commences."

And it said that Gordian's competitors were able to offer such policies and that Gordian had been offering such policies "within [its] retention". It was in this connection that Gordian said that it needed to "obtain reinsurers [sic] agreement to use the treaty capacity to write multi year contracts and would appreciate [the then lead reinsurer's] comments on this issue, including under the 'PINA Special Risks Clause.'"

150 The letter does not suggest, in terms, that Gordian was seeking reinsurance on policies it wrote which had a reporting period of longer than two to three years. Policies having longer terms may well have been relevant to the reinsurer's premiums and would have been likely therefore to have generated correspondence on that topic. Westport's quotation one week later stated that original policies "[u]p to three years is acceptable. PINA Clause to be amended." Gordian's submission that the maximum of three years was referable only to the PINA clause is not supported by the construction of the statement nor by the terms of the letter of 15 December 1998 to which the quotation was responsive. Clearly enough what was sought was to amend both the terms of the policies Gordian might write and the PINA clause. It cannot be said that the arbitrators were in error in the conclusion they reached.

The application of s 18B(1)

151 Because the construction and application of s 18B(1) are attended with some difficulty, it is necessary to have regard not only to the language of the sub-section but to its context, general purpose and policy[90]. "Context" here is used in its widest sense, to include the mischief to which the provision is directed[91]. As Dixon CJ observed in *Commissioner for Railways (NSW) v Agalianos*[92], matters such as general purpose and policy, and the consistency and fairness of operation of a provision, are surer guides to its meaning than the logic with which it is constructed. These observations are apposite to any formulaic application of the words of s 18B(1), without regard to its intended purpose.

152 Section 18B(1) is directed to the indemnity provided by an insurer and to the circumstances in which any exclusion or limitation affects that indemnity. Its language does not suggest any concern with the means by which the exclusion or limitation is achieved. It extends to any means by which the indemnity is "so defined". This presents something of a difficulty for the reinsurers' argument that the sub-section requires that there be a liability to indemnify in the first place, which is then made the subject of an exclusion or limitation. Within the terms of the sub-section, the exclusion or limitation may be provided within the definition of the cover, or indemnity. As Allsop P observed, these are largely matters of drafting. If a circumstance is perceived to increase a risk, it can be dealt with by a wide insuring clause combined with a limitation or exclusion clause or the insuring clause can itself be framed to exclude the risk[93].

153 The reinsurers' further contention, that the sub-section is intended to regulate provisions that operate by reason of events occurring after the entry into a binding contract of indemnity, also encounters difficulties. It relies upon the exclusion or limitation being expressed as dependent upon events or circumstances happening in the future. But an exclusion or limitation may itself operate differentially. A limitation may operate after an insurer's obligation to

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90 *Project Blue Sky Inc v Australian Broadcasting Authority* (1998) 194 CLR 355 at 381 [69]; [1998] HCA 28.

91 *CIC Insurance Ltd v Bankstown Football Club Ltd* (1997) 187 CLR 384 at 408; [1997] HCA 2.

92 (1955) 92 CLR 390 at 397; [1955] HCA 27 (referred to with approval in *Project Blue Sky Inc v Australian Broadcasting Authority* (1998) 194 CLR 355 at 381 [69]).

93 *Gordian Runoff Ltd v Westport Insurance Corporation* (2010) 267 ALR 74 at 104 [163]; see also Clarke, *The Law of Insurance Contracts*, 6th ed (2009) at 584 [19-1A].

indemnify has arisen; an exclusion operating by way of exception may prevent the obligation to indemnify from arising at all[94].

154 More important, to the operation of s 18B(1), is the event or circumstance which gives rise to the exclusion or limitation, and the relationship between that event or circumstance and the loss which would otherwise be the subject of the indemnity. The purpose of the sub-section is to prevent unfairness to an insured by the denial by an insurer of an indemnity, where there is no real connection between the loss which would otherwise be the subject of the indemnity and the circumstance giving rise to the exclusion or limitation. It achieves that object in those circumstances by negating the exclusion or limitation so that the indemnity operates.

155 The indemnity provided by the 1999 reinsurance treaty was with respect to policies yet to be written by Gordian, as is often the case with modern contracts for reinsurance[95]. The treaty could be described as "an antecedent contract for the reinsurance of a defined portion of risks of a specified kind to be undertaken in the future by the reassured."[96] The treaty provided indemnity to Gordian, but only with respect to D&O policies which conformed to the requirement that claims made under them were to be made and notified to Gordian within three years of their inception. Conformable policies would automatically be ceded to the treaty. In the language of the placing slip, they would attach if made during the period of the reinsurance.

156 The only circumstance that could qualify as a limitation or exclusion on that indemnity was the existence of a D&O policy written by Gordian which did not conform to the requirement of a reporting period of three years. Such was the case with the FAI policy. It could be said of the 1999 reinsurance treaty that it had the effect of excluding such a policy from the indemnity it offered or that its indemnity was limited, with the same result. Thus the 1999 reinsurance treaty defined the obligation to indemnify in the terms of s 18B(1)(a).

157 The purpose of s 18B(1) is to assess the relationship, or causal connection, between the circumstance so identified and the loss in respect of which indemnity is sought. Gordian sought indemnity under the 1999 reinsurance

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94 *Wallaby Grip Ltd v QBE Insurance (Australia) Ltd* (2010) 240 CLR 444 at 459 [35]; [2010] HCA 9.

95 *Colinvaux's Law of Insurance*, 9th ed (2010) at 739 [17-005]; Edelman et al, *The Law of Reinsurance*, (2005) at 6 [1.15].

96 *Tariff Reinsurances Ltd v Commissioner of Taxes (Vict)* (1938) 59 CLR 194 at 215; [1938] HCA 21.

treaty with respect to the losses arising under the FAI policy. But that policy is also the source of the circumstance which gives rise to the exclusion or limitation upon the indemnity. It follows, on this analysis, that the connection of which the sub-section speaks is present and the sub-section does not apply. The reinsurers cannot be required to indemnify Gordian.

158 This was not the approach adopted by the arbitrators. The arbitrators did identify the relevant circumstance as the existence of a D&O policy with a seven year reporting period. But when they came to discuss the "loss" suffered by Gordian, they directed their attention to "its liability on the 3-year claims", thereby reaching the conclusion that there was no causal connection between that loss and the circumstance giving rise to the exclusion or limitation. There are a number of problems with this approach.

159 It is elementary that a reinsurer is not liable unless the loss falls within the cover of the underlying contract of insurance *and* within the cover created by the reinsurance[97]. It is the FAI policy which is the source of Gordian's loss and therefore the basis for its claim to indemnity under the 1999 reinsurance treaty. But, without more, this does not make claims made under the policy the subject of and within the indemnity provided by the treaty. Gordian's loss for the purpose of the treaty is not to be equated with its liability under the FAI policy. As Dixon J explained in *Australian Provincial Assurance Association Ltd v Producers and Citizens Co-operative Assurance Co of Australia Ltd*[98], the liability of a reinsurer does not follow from the mere existence of a primary liability in the reinsured. "It arises from the provisions of the contract of reinsurance, and depends entirely upon the conditions which that contract contains. In this sense the liability is independent."

160 In identifying Gordian's loss as its liability with respect to claims made within three years, the arbitrators have effectively rewritten the 1999 reinsurance treaty and the indemnity it provided, so as to extend the risk which the reinsurers assumed. Section 18B(1) does not warrant such an approach. Its remedy does operate upon the contractual rights of the parties to a contract of reinsurance. It is limited to removing the effect of an exclusion or limitation upon an indemnity. That indemnity and the exclusion or limitation are to be found in the contract of insurance. The remedy is not to be provided upon an initial readjustment of the

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97 *Hill v Mercantile and General Reinsurance Co Plc* [1996] 1 WLR 1239 at 1251; [1996] 3 All ER 865 at 878; *Wasa International Insurance Co Ltd v Lexington Insurance Co* [2010] 1 AC 180 at 199 [35] per Lord Mance, 209-210 [59] per Lord Collins of Mapesbury.

98 (1932) 48 CLR 341 at 363; [1932] HCA 34.

terms of the parties' agreement and in particular of the indemnity provided for loss.

161 Allsop P recognised something of an error in the arbitrators' approach, but did not consider that it was manifest or otherwise came within s 38(5) of the *Commercial Arbitration Act* such that it might warrant consideration of whether leave to appeal should be granted.

Whether leave should have been granted

162 The question respecting the application of s 18B(1) concerned its construction and that of the 1999 reinsurance treaty. It therefore concerned questions of law, regardless of whether the sub-section involved an inquiry as to the circumstance giving rise to a limitation or exclusion upon the indemnity under the treaty and the connection of that circumstance to the indemnity for loss.

163 I agree with French CJ, Gummow, Crennan and Bell JJ[99] that manifest error of law requires that the error appear on the face of the Award, which includes the reasons for it, and that the error be apparent to the understanding of the reader. Such is the case here. It does not require that the error be of a particular quality or that errors involving complex questions be disqualified[100].

164 The reinsurers' concession in the Court of Appeal, that the error could not be said to be manifest, is likely to have been based upon the decision in *Natoli v Walker*[101]. But for that decision the concession was certainly not called for. The error in the reasons of the Award concerning the application of s 18B(1) to the 1999 reinsurance treaty qualified as an error within the meaning of s 38(5)(b)(i).

165 The identification of manifest error on the face of the Award does not conclude the question of whether leave should be given under s 38(5). The statutory scheme is that error of the kind there referred to is a necessary, but not itself sufficient, condition for the grant of leave. It remains in the discretion of the court whether leave should be granted[102]. The other question necessary to be addressed under s 38(5)(a), namely whether the rights of the parties to the arbitration agreement are substantially affected by the determination of the

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99 At [42].

100 At [45] citing *Natoli v Walker* (1994) 217 ALR 201 at 215-217, 223.

101 (1994) 217 ALR 201.

102 *Promenade Investments Pty Ltd v New South Wales* (1992) 26 NSWLR 203 at 225-226 per Sheller JA.

question of law, and the question of leave generally, fall to be determined by reference to all the circumstances pertaining to the case.

166 The primary judge's approach to the question of leave elided the question of leave with the ultimate question under s 38(2) and was therefore incorrect. Nevertheless, there was error manifest on the face of the Award, on a question of law which was determinative of the reinsurers' obligation to indemnify under the 1999 reinsurance treaty and contrary to the terms of the treaty. Thus the decision to grant leave was correct, as was that which followed, that the Award should be set aside for error of law.

The special leave ground

167 Section 18B(1) did not apply to the 1999 reinsurance treaty. No question as to the application of the proviso to the sub-section arises. It is therefore strictly unnecessary to consider whether the arbitrators provided adequate reasons on that question. The rights of the parties fell to be determined by reference to the 1999 reinsurance treaty. However, special leave was granted on this ground and argument advanced. It is therefore necessary to say something about the requirement of reasons.

168 The *Commercial Arbitration Act* does not bind the parties to an arbitration to the outcome of the arbitration they have agreed will take place. It allows for an appeal, albeit one limited to a question of law and one subject to conditions for the grant of leave to appeal. The Act therefore comprehends something of a public, as well as a private, element in the making of an award of arbitration. It is in this context that an arbitrator's "reasons for making the award" are required, by s 29(1)(c).

169 There is nothing in the *Commercial Arbitration Act*, specifically in the language of s 29(1)(c), or in the nature of arbitrations subject to the Act, which suggests as necessary that those reasons be to a judicial standard. But the requirement in s 29(1)(c) cannot be devoid of content, particularly given the context for it. Allsop P considered[103], correctly in my view, that a statement in *Bremer*[104] is apt to apply to s 29(1)(c). There Donaldson LJ said that a "reasoned

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103 *Gordian Runoff Ltd v Westport Insurance Corporation* (2010) 267 ALR 74 at 114 [220].

104 [1981] 2 Lloyd's Rep 130.

award"[105] requires arbitrators to "explain succinctly why, in the light of what happened, they have reached their decision and what that decision is."[106]

170 I agree with French CJ, Gummow, Crennan and Bell JJ that what is required by way of reasons in a given case will depend upon the circumstances of that case[107]. In this case the arbitrators could not apply s 18B(1) without determining whether it was reasonable to hold the reinsurers bound to indemnify Gordian in all the circumstances. More was therefore required than a statement of conclusion. It was necessary that they say why it was reasonable to do so, in order to fulfil the requirement of s 29(1)(c). The failure to do so constituted an error of law.

Conclusion and orders

171 Special leave should be granted with respect to grounds 5 and 6, the appeal allowed with costs and the orders of the primary judge restored. In these two latter respects I agree with the orders proposed by French CJ, Gummow, Crennan and Bell JJ.

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105 See *Arbitration Act* 1979 (UK), s 1(5).

106 *Bremer Handelsgesellschaft mbH v Westzucker GmbH (No 2)* [1981] 2 Lloyd's Rep 130 at 132-133.

107 At [53].