IN THE HIGH COURT OF AUSTRALIA
SYDNEY REGISTRY
ON APPEAL FROM NEW SOUTH WALES COURT OF APPEAL

No S110/2010 &
S219/2010

BETWEEN

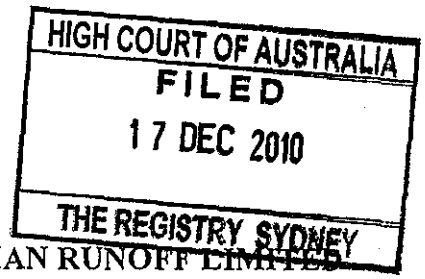
WESTPORT INSURANCE CORPORATION
(ABN 48 072 715 738)
First Applicant/Appellant

ASSETINSURE PTY LIMITED
(ABN 65 066 463 803)
Second Applicant/Appellant

MUNICH REINSURANCE COMPANY OF AUSTRALASIA LIMITED
(ABN 51 004 804 013)
Third Applicant/Appellant

XL RE LIMITED
(ABN 54 094 352 048)
Fourth Applicant/Appellant

SCOR SWITZERLAND LTD
(ABN 92 098 315 176)
Fifth Applicant/Appellant



and

GORDIAN RUNOFF LIMITED
(ABN 11 052 179 647)
Respondent

APPELLANTS'/APPLICANTS' REPLY SUBMISSIONS

Part I: Certification

1 These reply submissions are in a form suitable for publication on the internet.

Part II: Concise Statement of Issues

2 The appellants/applicants (**Reinsurers**) respond to the respondent by reference to the headings and paragraph numbers in the respondent's submissions filed on 10 December 2010.

3 The respondent's suggested issue (at [3] of the submissions) as to whether the grant of special leave should be revoked appears to be based on a misapprehension as to the Reinsurers' case on the Reasons Ground. For the reasons explained at [8]-[9] below, there is no issue as to the revocation of the grant of special leave.

4 Grounds 5 and 6 of the Reinsurers' amended special leave application (AB5:2022) have been referred to the Full Court. Grounds 1 and 2 of the respondent's notice of contention (AB5:2254) raise the question of leave under s 38 of the CAA. In the event special leave is granted on Grounds 5 and 6, and Grounds 1 and 2 are

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determined in favour of the Reinsurers, this Court will be able to grant the orders sought by the Reinsurers. For these reasons, it is contended that the issue raised in [5] of the respondent's statement of the issues is a false issue.

Part IV: Contested Material Facts

5 At [9] of the submissions, the respondent mischaracterises the findings of the arbitrators as containing a finding that "the treaties covered all policies written by Gordian and classified by it as D&O insurance." The finding of the arbitrators was in fact that the treaties only covered D&O policies which had up to three year reporting periods and did not cover the FAI D&O Run-Off Policy {award [81], AB1:14, summarised at [21(a)] of the Reinsurers' submissions}.

6 The footnote reference to [62] of the CA judgment (AB4:1943) is a reference to the terms of the expiring 1998 treaty and not the terms of the treaties the subject of the dispute as found by the arbitrators. The 1999 placing slips provided that wording was to be "as expiring as far as applicable, *amendments to be agreed by reinsurers*" {CA [63], AB4:1943} (emphasis added).

7 At [10] of the submissions, the respondent suggests a further finding of the arbitrators is to be found at [90] of the award (AB1:17). [90] of the award sets out part of the arbitrators reasoning in relation to the application of s 18B. It does not record additional findings of fact. The relevant findings are recorded at [80]-[81] of the award (AB1:14). The arbitrators did not find it necessary to determine a rectification argument pursued by the Reinsurers partly because it found that the FAI D&O Run-Off Policy was not covered by the treaties {award [80], AB1:14}.

Part VI: Statement of Argument

Revocation of Special Leave – [13] Respondent's Submissions

8 As is apparent from [84]-[86] of the Reinsurers' submissions, the Reinsurers do not resile from the contention that this Court should decide that in a complex arbitration, attended by the formalities of legal proceedings and chaired by an eminent retired appeal court judge, reasons of a judicial standard should be given. The Reinsurers' still contend that *Oil Basins* should be preferred to the decision of the court below.

9 The submission advanced at [78] is that a determination by this Court that inadequate reasons were provided by the arbitrators does not necessarily involve this Court preferring *Oil Basins* to the decision of the court below. The Reinsurers' contend that inadequate reasons were given by the arbitrators applying the *Bremer v*

Westzucker test preferred by the court below (see [80]-[83] and [87] Reinsurers' submissions).

Scope of Cover – [34] and [37] Respondent's Submissions

10 The arguments advanced at [30]-[54] of the Reinsurers' submissions address the basic proposition that a provision of a reinsurance treaty that identifies which insurance contracts are covered by the treaty (a provision stipulating the scope of cover) is not regulated by s 18B. This has always been the Reinsurers' contention at all levels in this dispute. No argument has been abandoned as suggested in [34] of the respondent's submissions. The specific focus on the legal nature of treaty reinsurance was introduced in argument in the CA (AB5:2223) but that should not obscure the fact that this case has always been about treaty reinsurance (see award [73], AB1:13) and whether the FAI D&O Run-Off Policy is covered by the treaties.

11 The respondent persists in characterising the treaties as covering all D&O policies (at [37]) when that it inconsistent with the arbitrators' findings. Once it is recognised that the FAI D&O Run-Off Policy, on the arbitrators' findings, is not covered by the treaties there is no prima facie entitlement to indemnity and no room for s 18B to operate to provide cover.

Part VII: Respondent's Notice of Contention

Manifest Error and Strong Evidence of Error – [46]-[54] Respondent's Submissions

12 [46]-[54] of the respondent's submissions seems to advance a new argument on the construction of s 38(5)(b). The suggestion seems to be that if an applicant under s 38(5)(b) identifies the error of law without reference to "evidence" other than the award itself, the applicant is effectively restricted to relying on the manifest error limb (s 38(5)(b)(i)). The proposition needs only to be stated to be rejected.

13 Section 38(5)(b) has two gateways: manifest error (obvious error in the terminology of the new NSW Act) and strong evidence of error (open to serious doubt in the terminology of the new NSW Act) of a kind that may add to the certainty of commercial law. Manifest error must be found on the face of the award, but the second limb establishes a lower threshold and does not depend on utilising other "evidence."

Grounds 5 to 12 Notice of Contention

14 The respondent's submissions in relation to Grounds 5 to 12 of the notice of contention ignore the fact that, under s 22(2) of the CAA, the arbitrators were not bound to observe the strict rules of evidence and procedure or common law rules of

construction of contracts (*Woodbud v Warea* (1995) 125 FLR 356 at 355-6, *Eagle Star v Yuval* [1978] 1 LLR 357, Mustill & Boyd, *The Law and Practice of Commercial Arbitration in England,* 2nd Ed, 1989 at 82, O'Neill & Woloniecki, *The Law of Reinsurance,* 2nd Ed at 14-15). Further, the parties had expressly permitted the arbitrators to rely on their own knowledge and expertise (see transcript at AB3:1406P-S, AB3:1439K-1440D). All of the criticisms of the arbitrators' methodology fall away once these points are recognised.

Expiring Reinsurance Applied to Policies Written for 12 Months Plus Odd Time – [71]-[76] Respondent's Submissions

15 The arbitrators found that, in accordance with general industry practice, the expiring 1998 treaty applied to policies written for 12 month periods plus odd time. There was substantial evidence to support the finding of fact as to the general industry practice[1] and no evidence to the contrary. The arbitrators noted that no credible alternative was offered by the respondent as to the existence of the practice {award [78], AB1:14).

Agreement to a 3 Year Limit – [78]-[84] Respondent's Submissions

16 The arbitrators found that under the 1999 treaties the Reinsurers agreed to cover D&O policies with up to 3 year periods. The respondent focuses on the letter dated 15 December 1998 (AB2:512-4) which has to be read in conjunction with the acceptance from the lead reinsurer on 22 December 1998 (AB2:555) which stated "Original Contracts: Up to three years acceptable." The parsing of the 15 December 1998 letter in the respondent's submissions does not survive consideration of all the relevant correspondence.

3 Year Limit Applies to Run-Off Cover – [85]-[91] Respondent's Submissions

17 The arbitrators rejected the suggestion that a relevant distinction could be drawn between run-off policies and operational policies at [73] of the award (AB1:13). This was soundly based on the evidence. The suggestion by the respondent's witness, Mr Fletcher, in his witness statement that he considered the FAI Run-Off Policy was covered because it was a run-off policy (at [58], AB1:130) was undone in his cross-examination when he accepted that the 3 year limit applied to both run-off and operational policies (AB3:1333C-I). It should be noted that the arbitrators expressly recorded that they were unimpressed with Mr Fletcher's

[1] Margot Rathbone at [11], [12], [17], [18] (AB1:154-156); Peter Backe-Hansen at [20] (AB1:168); Bill Hassos at [5], [6], [10]-[17] (AB1:185-187).

"demeanour, obvious lack of recall and other unsatisfactory aspects." {award [74], AB1:13).

Construction of 5xs5 and 3xs2 Contracts – [92]-[100] Respondent's Submissions

18 There was substantial evidence to support the arbitrators' finding {award [76], AB1:13} that the different layers of the reinsurance programme were to be on uniform terms. This was the usual practice[2] and consistent with the letter of 15 December 1998 which requested "the same cover provided by the $10m xs $10m treaty" for the $5m xs $5m layer (AB2:514).

The Respondent's Established Acceptance and Underwriting Criteria – [113]-[122] of the Respondent's Submissions

19 The respondent led evidence before the arbitrators from its principal witness, Mr Fletcher, that it was its normal practice to convert existing D&O policies into run-off policies with up to 7 year periods[3] and Mr Fletcher was cross-examined, without objection, on the unusual features of 7 year policies and the need to obtain special acceptance if such policies were to be covered (AB3:1328). Mr Fletcher's evidence was not accepted (see [17] above).

20 Written submissions of both sides addressed these questions (AB1:231 at [29], AB1:255-6 at [41] to [43]). The respondent's established acceptance and underwriting criteria was part of the factual controversy before the arbitrators and the arbitrators were entitled to make the findings they did at [79] (AB1:14).

21 The observations of the CA at [291] (AB5:2012) appear to have overlooked considerations set out in [19] and [20] above (all of which were submitted to the court below). Nevertheless, the CA was right to observe that no application under s 42 of the CAA alleging misconduct by the arbitrators was made by the respondent and, in the absence of such an application, it was inappropriate to deal with the respondent's contentions on this topic.

17 December 2010

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[2] Margot Rathbone at [42] (AB1:160-161); Peter Backe-Hansen at [18]-[19] (AB1:167-8); Bill Hassos at [37]-[38] (AB1:192).

[3] Fletcher statement at [6]-[10] (AB1:120-1).