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\ihg CASE NO 685/92

IN THE SUPREME COURT OF SOUTH AFRICA

(APPELLATE DIVISION)

In the matter between:

THE STANDARD GENERAL INSURANCE CO LTD First Appellant

GUARDIAN NATIONAL INSURANCE CO LTD Second Appellant

and

VOEST-ALPINE INDUSTRIEANLANGENBAU GESELLSCHAFT M.B.H. Respondent

CORAM: CORBETT CJ, JOUBERT, HEFER, EKSTEEN JJA et MAHOMED AJA

DATE OF HEARING: 21 MARCH 1994

DATE OF JUDGMENT: 29 MARCH 1994

J U D G M E N T

MAHOMED, AJA

The two Appellants in this appeal and Allianz Insurance Ltd ("Allianz") concluded a written policy of insurance on the 18 November 1986 in terms of which Allianz and the Appellants, as the three insurers, indemnified "the insured" against physical loss or damage to any part of the property insured during the period of insurance. It is common cause that the Respondent was a sub-contractor to whom Iscor Ltd had awarded a contract for work to be undertaken at the K - R Plant at the Iscor Works, Pretoria ("the insured contract") and that it accordingly fell within the definition of an "insured" in terms of the policy.

Although Allianz and the first and the second Appellants were co-insurers in terms of the policy their individual liability to the insured was limited respectively to the proportions 65%, 20% and 15%. Allianz was the "leading insurer".

An incident occurred on the 19th December 1987

which gave rise to a claim under the policy by the Respondent. It resulted in damage to parts of the K - R Plant including the "Melter Gasifier". The loss suffered by the Respondent in consequence of this incident consisted of three components. The first component was the loss caused to those parts of the "Melter Gasifier" undisputably covered by the indemnity. The second component was constituted by damage during this incident, to certain refractory linings to which heat had previously been applied. The third component ("the disputed claim") was made up by the cost of removing and replacing some 85% of the refractory linings which were not damaged in the incident at all, but which had to be so removed and replaced in order to gain access to and to repair that part of the "Melter Gasifier" which was damaged in the incident and which was undisputably covered by the indemnity.

Allianz, to whom the Respondent made its claim

for the loss suffered by it, initially repudiated any liability for any loss suffered by the Respondent arising from the costs of removing and replacing refractory linings to which heat had previously been applied and it assessed the total damages indemnifiable in terms of the policy in an amount of R1 153 620.00. It offered to the Respondent the sum of R1 114 000 in "full and final settlement" of the claim. Later, however, it reconsidered its position and in a letter dated 29th August 1990 it recorded that -

> " ..... The insured is entitled to indemnity in respect of refractory linings inasmuch as its undamaged portion is concerned and which part has only been replaced for the purpose of gaining access to other indemnifiable items requiring repairs".

The total compensation which was determined, in terms of this letter, was increased to R6 444 090.00 of which R3 255 690.00 represented compensation in respect of the "disputed claim". It accordingly tendered and

paid to the Respondent the sum of R4 188 658.00 representing 65% of the total of R6 444 090.00.

Both the Appellant's, however, have repudiated any liability to compensate the Respondent for the loss referred to in the "disputed claim". This repudiation is based on paragraphs 4 and 11 of the "Exceptions" to the liability of the Insurers, contained in the policy of Insurance. These paragraphs read as follows -

> "The Insurers will not be liable for....
>
> 4. The cost incurred in rectifying any defect in The Property Insured arising from design plan specification materials or workmanship. Should The Property Insured suffer physical loss or damage the Insurers will indemnify the Insured for the cost of repairing or replacing lost or damaged property but will exclude any cost incurred in betterment or alteration as well as the costs that would otherwise have been incurred in rectifying any defect had the loss or damage not occurred.
>
> Further the Insurers will indemnify the Insured for the proportional amount of the common costs of dismantling demolition opening up transportation reassembly rebuilding testing and commissioning all necessarily incurred in rectifying replacing reinstating repairing or making good the insured loss and the uninsured costs. The amount of the Insurers contribution to such proportional amount shall be in the

> same proportion as the amount of the insured loss bears to the total cost of reinstatement but excluding the common costs of dismantling opening up transportation reassembly testing and commissioning.....
>
> 11. Loss of or damage to refractory linings from the time that heat is first applied thereto".

The first contention advanced on behalf of the Respondent was that the Appellants were bound by the decisions of Allianz on the claims made by the Respondent and that it was "not open to them to refuse to follow the claim settlement made by Allianz", the leading insurer. This contention is based on the last paragraph of the schedule to the policy which reads as follows -

> "Co-Insurance Clause"
> It is agreed that all Insurers who have subscribed hereto are bound by the decisions of the Leading Insurer and will follow the same rates terms, conditions claim settlements and all other matters relating to the insurance granted by this policy as may be agreed by the Leading Insurer. It is further agreed that all endorsements hereto will be legally binding on all Insurers when signed by the Leading Insurer."

Stegmann J before whom the matter was argued in

the Court a quo upheld the substance of this contention. He accordingly made an order in terms of paragraph 1 of the Notice of Motion declaring that the co-insurers (who are the Appellants in the present appeal) were "bound by the decisions of Allianz Insurance Ltd, as lead insurer, in the admission and settlement of all claims relating to the Insurance" granted by the relevant policy of insurance, but he made this declaration subject to the proviso that the the Appellants as co-insurers were "not bound by any decision of Allianz which either of them may show to have been made without due professional skill and care or in bad faith". The learned Judge also made consequential orders directing the first and the second Appellants in this appeal to pay to the Respondent the sum of R651 133.00 and the sum of R488 349.00 respectively, plus interest thereon at the rate of 18.5% per annum from the 29th August 1990 to date of payment.

The Appellants concede that if they are indeed

bound by the decision which Allianz made on the merits of the claim made by the Respondent, they are liable to pay to the Respondent the amounts directed by the Court a quo, but Mr. Cohen who appeared for the Appellants contended that they were not so bound. That contention was based on two submissions:

a) The first submission was that on a proper interpretation of the terms of the relevant policy of insurance, the Respondent was not indemnified in respect of the losses referred to in the disputed claim.

b) Secondly it was contended that on a proper interpretation of the "co-insurance clause", the Appellants were not bound by the decisions of Allianz relating to losses suffered by the Respondent which did not fall within the risk covered by the policy.

For the purposes of determining the correctness

of the second submission, I shall assume in favour of the Appellants that the first of these submissions is sound in law. For several reasons, however, and even on that assumption, I am not persuaded by the argument in support of the second submission.

In order to determine the proper meaning of the co-insurance clause, it is necessary to have regard to its purpose.

In my view, the object of this clause was to protect the insured so that it could have its claim dealt with conveniently and expeditiously by the leading insurer, without the delays, the costs and the uncertainties which might arise if each of the different co-insurers adopted a different attitude in respect of one or more of the issues of substance or procedure in consequence of the filing of such a claim. That object would clearly be frustrated if one or more of several co-insurers were entitled to resist a claim by the insured

on the ground that the leading insurer had been wrong in making one or other decision relating to the insurance granted by the relevant policy.

Counsel for the Appellant appreciated that the co-insurance clause could not be interpreted in a manner which left the co-insurers free to dispute every decision made by the leading Insurer and thus remove the application of the clause in all areas where the co-insurers disputed the decisions of the leading Insurer. For this reason the Appellants sought to draw a distinction between a decision on the merits of the claim from all other decisions. Counsel sought to contend that a decision by the leading Insurer on the merits of the claim would not be binding on the other co-insurers but that other decisions of the leading Insurer would be so binding. Included in the latter would be procedural decisions such as whether or not the claim of the insured should be resisted on the ground that no timeous notice

of the event giving rise to the claim had been given or on the basis that the insured had not preserved any damaged or defective property which might prove necessary or useful in connection with the claim or because the insured had unreasonably prevented the insurers or their authorized representatives from entering the premises at which the damage had occurred or on the grounds that the insured had offered or promised payment or indemnity to other persons without the consent of the insurers.

There is nothing in the wording of the co-insurance clause or in any other relevant provision of the policy which justifies this distinction sought to be drawn on behalf of the Appellants. Nor, on the wording of the policy, is it possible to draw a rational and relevant distinction between a decision by the leading Insurer on the "merits" of the claim and a decision made by it on the "quantum". The policy provides that "in the event of loss of or damage to the property insured

....the basis of loss settlement .... shall include ....the reasonable cost of repair, re-instatement or replacement of the Property Insured at the time of the final re-instatement of the loss or damage". If a decision by the leading Insurer on the "merits" of the claim by an insured can be resisted by the other co-insurers, why can they not resist such a decision pertaining to the "quantum" on the grounds that the cost allowed by the leading Insurer for the "repair, re-instatement or replacement of the property insured" was not reasonable? It was strenuously contended that the obligation of the other co-insurers to be bound by the decisions of the leading Insurer were limited by the co-insurance clause itself to matters "relating to the insurance granted by this policy" and that for this reason the decision of the leading Insurer on the "disputed claim" could not be binding on the other co-insurers. This argument is based on the assumption that

the phrase "relating to the insurance granted by this policy" in the co-insurance clause qualifies all the "decisions" referred to in the clause and not merely the phrase "and all other matters" which immediately precedes the phrase. I have considerable doubt as to whether that proposition is correct but even assuming that it is, I am not persuaded that this effectively allows the other co-insurers to repudiate a decision which is made by the leading Insurer on the merits of the "disputed claim" by the insured. The words "relating to the insurance" postulate a very wide ambit; "it must logically be regarded as vague and without a purely logical limitation" [Johannesburg City Council v Victteren Towers (Pty) Ltd 1975 (4) SA 334 (W) at 336 A; Springs Town Council v Soonah 1963 (1) SA 659 (A) at 671 B - C)]. Any limitation suggested by the use of such a phrase must be sought sensibly in the context of the relevant instrument and its objects. Thus approached the words "relating to

the insurance" must be construed as meaning that the decision of the leading Insurer which binds the other co-insurers must be "connected" to the insurance granted by the policy and not that such a decision must be legally unassailable in terms of the policy.

It was further contended on behalf of the Appellants that when the lead Insurer pays its contractual portion of the loss of the property insured, it complies fully with its contractual obligation and can therefore have no interest in compelling the co-insurers to settle the claim on similar terms, as far as their portions are concerned. The real motivation for the stipulation contained in the co-insurance clause, however, is not to protect the interests of the leading Insurer. It was inserted in the interests of the insured so that he could conveniently and expeditiously deal with the captain of the team of co-insurers, without the disadvantage of having to deal separately with each of

the co-insurers who might manifest different attitudes on different issues arising from the claim of the insured.

The wording of the co-insurance clause in the policy seems to have had its origins in similar "follow the settlements" clauses in policies of re-insurance. In that context such clauses have been interpreted to mean that the re-insurer was bound by any compromise, "whether of liability or amount", made by the original underwriters unless the re-insurer "could prove that such a compromise was dishonestly arrived at or that the re-assured had failed to take all the proper and business-like steps to have the amount of the loss fairly and carefully ascertained" (The Insurance Company of Africa v Scor (UK) Re-Insurance Company Limited [1985] 1. LL. R 312 (C.A); Insurance Company of the State of Pensylvania v Grand Union Insurance Company Limited v Lowndes Lambert Construction Limited [1990] 1. LL. R 208 [HK]). It was correctly contended, however, on behalf of the Appellants

that there is a distinction between a re-insurance contract and a contract in terms of which co-insurers undertake liability to the insured because in the former case "the loss of a re-assured is not the property damaged but the payment by him in good faith of his assured's claim" (Charman v G R E Assurance P L C [1992] 2 LL. R 607 at 613 - 614). The cases dealing with "follow settlements" clauses in re-insurance policies must therefore be applied with caution in a case such as the present where this clause appears in a contract between co-insurers and the insured, but this cannot detract from the finding of the Court a quo that the co-insurance clause in the present matter was "intended to secure for the insured a benefit of convenience essentially similar in nature to the benefit which such a clause has been held to confer on the re-insured in a contract of re-insurance".

It was also contended that an interpretation of

the co-insurance clause which compelled a co-insurer to be bound by a decision of the leading Insurer, to pay a claim which falls outside the risk covered by the contract of insurance, could never have been contemplated by the parties because it could saddle a co-insurer with a liability which it never intended to incur towards the insured. Two observations are relevant to this objection. If, in the first place, the decision of the leading Insurer is so obviously and demonstrably unjustified as to attract the conclusion that it had failed to exercise professional skill and care in making its judgment or that it had acted in bad faith, its decision would, in any event, not be binding on the co-insurers. This was the reason why Stegman J granted the first prayer in the notice of motion only subject to the proviso that the co-insurers were not bound by any decision of Allianz which "either of them may show to have been made without due professional skill and care or

in bad faith". On the other hand if the decision of the leading Insurer is not so obviously unjustified as to attract such a conclusion, but is a decision, which could honestly have been arrived on a reasonable but mistaken interpretation of the law or the facts, or is a decision which could reasonably and fairly have been arrived at by the bona fide perceptions of the leading Insurer as to what is in the best interests of all the co-insurers, it could not properly be claimed that the co-insurers of the leading Insurer never intended to be bound by such decisions. The decision by Allianz with respect to the disputed claim of the Respondent, is clearly not a decision which falls within the first category of obviously unjustified decisions attracting the inference of mala fides or lack or professional competence. It was never suggested that Allianz had acted in bad faith or that it had not exercised "due professional skill and care" in making its decision on the disputed claim.

In the result I am of the view that the Appellants were bound by the decision which Allianz made with regard to the disputed part of the Respondent's claim and that both Appellants were, in terms of the co-insurance clause, bound to "follow" that decision by making the appropriate payments respectively quantified in paragraphs 2 and 3 in the notice of motion.

Counsel for the Respondent also contended that the co-insurers were, in any event, liable to compensate the Respondent for the losses which it sustained and which are quantified in the disputed claim and that on a proper interpretation, paragraphs 4 and 11 of the "Exceptions" to the liability of the insurers contained in the policy, the insurers are not relieved of this liability.

In view of the conclusion I have arrived at, on the interpretation and application of the co-insurance clause, it is not necessary to determine this issue,

because even if paragraphs 4 and 11 were capable of being interpreted in favour of the Appellants' submissions, the decision of Allianz to make a payment based on the disputed claim, was binding on the Appellants in the circumstances.

In my view, however, there is considerable substance in the submission made on behalf of the Respondent on this issue. Paragraph 11 exempts the insurers from liability for "loss of or damage to the refractory linings from the time that heat is first applied thereto", (and at some time before the incident which gave rise to the Respondent's claim heat had been applied to the refractory linings) but the "loss or damage" claimed by the Respondent was not a loss or damage caused by the incident which gave rise to the Respondent's claim. It represented simply part of the costs which the Respondent would have to incur in order to gain access to and to repair those parts of the Plant

which were indisputably covered by the indemnity provided by the policy of Insurance. Such costs constitute part of the liability of the Insurer to the Insured flowing from the indemnity given by the Insurers to the Insured in the policy "against physical loss of or damage to any part of the Property insured". [Nafte v Atlas Assurance Company Limited (1924) W L D 239 at 248; Gordon and Getz: The South African Law of Insurance 4th Edition (1993) 250; Jonnes v Anglo-African Shipping Company (1936) Ltd 1972 (2) SA 827 (A) at 835 H - 836 B] The terms of paragraph 4 of the "Exceptions" to the policy would appear to support and not detract from this conclusion.

In the result I order that the appeal be dismissed with costs including the costs consequent upon the employment of two Counsel.

I MAHOMED
ACTING JUDGE OF APPEAL

CORBETT CJ)
JOUBERT JA)
HEFER JA) CONCUR
EKSTEEN JA)