FEDERAL COURT OF AUSTRALIA

Dalby Bio-Refinery Ltd v Allianz Australia Insurance Limited [2018] FCA 1806

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| File number: | VID 1170 of 2017 |
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| Judge: | **LEE J** |
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| Date of judgment: | 31 October 2018 |
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| Catchwords: | **INSURANCE –** industrial special risks insurance policy – referee reports adopted by consent – construction of exclusion clause – *Wayne Tank* principle – meaning of spontaneous combustion – proximate cause of loss – irrelevance of possible antecedent causes – application dismissed |
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| Legislation: | *Federal Court of Australia Act 1976* (Cth) s 43  *Federal Court Rules 2011* 28.67(1)(b) |
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| Cases cited: | *Baulderstone Hornibrook Engineering Pty Ltd v Gordian Runoff Ltd* [2008] NSWCA 243; (2008) 15 ANZ Insurance Cases 61-780  *Calderbank v Calderbank* [1976] Fam 93  *Darlington Futures Limited v Delco Australia Proprietary Limited* (1986) 161 CLR 500  *Fitzpatrick v Job t/as Jobs Engineering* [2007] WASCA 63; (2007) 14 ANZ Insurance Cases 61-731  *Gunns Forest Products Ltd v North Insurances Pty Ltd* [2006] VSCA 105; (2006) 14 ANZ Insurance Cases 61-691  *McCann v Switzerland Insurance Australia Limited* [2000] HCA 65; (2000) 203 CLR 579  *McCarthy v St Paul International Insurance Co Ltd* [2007] FCAFC 28; (2007) 157 FCR 402  *Selected Seeds Pty Ltd v QBEMM Pty Ltd* [2010] HCA 37; (2010) 242 CLR 336  *Wayne Tank & Pump Co Ltd v Employers Liability Assurance Corporation Ltd* [1974] QB 57 |
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| Date of hearing: | 31 October 2018 |
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| Registry: | New South Wales |
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| Division: | General Division |
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| National Practice Area: | Commercial and Corporations |
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| Sub-area: | Commercial Contracts, Banking, Finance and Insurance |
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| Category: | Catchwords |
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| Number of paragraphs: | 58 |
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| Counsel for the Applicant: | Mr S R Horgan QC with Mr B J Murphy |
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| Solicitor for the Applicant: | McCullough Robertson Lawyers |
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| Counsel for the Respondents: | Mr G McArthur QC |
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| Solicitor for the Respondents: | Lander and Rogers Lawyers |

ORDERS

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|  | | VID 1170 of 2017 |
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| BETWEEN: | DALBY BIO-REFINERY LTD  Applicant | |
| AND: | ALLIANZ AUSTRALIA INSURANCE LIMITED  First Respondent  CHUBB INSURANCE AUSTRALIA LIMITED  Second Respondent  ZURICH AUSTRALIAN INSURANCE LIMITED  Third Respondent | |

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| JUDGE: | LEE J |
| DATE OF ORDER: | 31 OCTOBER 2018 |

THE COURT ORDERS THAT:

1. The originating application dated 25 October 2017 be dismissed with costs.
2. The date by which a notice of appeal must be filed pursuant to FCR 36.03(b) is fixed as 14 days after the date on which reasons revised from the transcript are published.

Note: Entry of orders is dealt with in Rule 39.32 of the *Federal Court Rules 2011*.

REASONS FOR JUDGMENT

Revised from the transcript

LEE J:

# a introduction

1. Since July 2015, the respondents (**Insurers**) have insured the applicant (**Dalby**) pursuant to an industrial special risks insurance policy (**Policy**). The Policy provided indemnity to Dalby in respect of any loss or damage at the Dalby commercial premises, including consequential loss. Central to this case, however, is the fact that the indemnity was subject to a number of exceptions.
2. During the currency of the Policy, damage was occasioned to Dalby’s stockpile of dry distillers’ grain and solubles (**Product**), which was stored at the Dalby Bio-Refinery in four bays: known as Bay 1, Bay 2, Bay 3 and Bay 4.
3. At approximately 6.30 am on 2 March 2016, smoke was detected in Bay 2. Queensland Fire and Emergency Services attended the site and conducted tests on small samples which indicated that the Product was unlikely to develop into large scale flaming combustion. When the stockpile of Product in Bay 2 was opened, there was significant discolouration below the surface, while Product near the surface remained pale. The Product had a “burnt smell” and, as a result, the entire stockpile of the Product in Bay 2 was discarded. Subsequent inspection of the Product in Bays 1 and 3 uncovered significant damage and the stockpiles were also discarded. Bay 4 was in a separate part of the storage shed, was only partially filled at the time, and the Product showed no sign of damage.
4. It is common ground that the Policy responds to damage occasioned by the disposal of the Product. Both parties agreed during the course of the final hearing this morning that it was appropriate that all issues of liability be determined separately and before issues relating to quantum on a final basis, as it will be unnecessary to deal with any quantum issues in the event that the exclusion applies. Accordingly, the sole issue for determination presently is whether the exclusion relied upon by the Insurers is engaged. That exclusion is in the following terms:

**Perils Exclusions:**

The Insurer(s) shall not be liable … in respect of:-

…

6. physical loss, destruction or damage occasioned by or happening through:-

…

(c) (i) spontaneous combustion

(ii) spontaneous fermentation or heating or any process involving the direct application of heat

Provided that Perils Exclusions 6(c)(i) and 6(c)(ii) shall be limited to the item or items immediately affected and shall not extend to other property damaged as a result of such spontaneous combustion, fermentation or heating or process involving the direct application of heat.

# B Procedural History

1. This matter first came before the Court on 29 November 2017 when, after hearing from the parties as to the limited nature of the dispute, the Chief Justice asked the parties to consider whether or not the Court would be better assisted by the appointment of a referee to report upon the circumstances that gave rise to the damage (rather than following an interlocutory regime which contemplated a stately progression of expert evidence).
2. Notwithstanding this, the parties proceeded to obtain a volume of expert material. The cost of this exercise would largely have been avoided in the event that earlier attention had been given by the parties to the possibility of retaining a joint expert or asking the Court to appoint a referee. In any event, belatedly, on 31 May 2018, the Insurers applied for the appointment of a referee. After two case management hearings (the second of which dealt with a contested question as to the identity of the proposed referee), orders were made on 27 July 2018 referring two questions to a referee who had been proposed by Dalby, being Dr Rodney Weber.
3. On 31 August 2018, Dr Weber issued a report which was adopted by the Court by consent on 24 September 2018 (**Referee Report**). At that same hearing, an order was made for the provision of a supplementary report (**Supplementary Report**). The purpose of this Supplementary Report was to clarify an issue raised by the Referee Report that remained in contention between the parties. The Supplementary Report was provided to the Court on 17 October 2018 and the parties thereafter provided written and oral submissions as to whether: (a) the Supplementary Report should be adopted; and (b) the determinative issue of liability, being whether the exception was engaged.
4. At the hearing today, again by consent between the parties, the Supplementary Report was adopted. At the hearing, the Referee Report and the Supplementary Report (together, the **Reports**) were both before the Court (as having been adopted) and the Policy was tendered. This constituted the entirety of the evidence on the hearing.

# C Findings arising from the reports

1. On 27 July 2018 the referee was asked to address two questions. They are worth setting out in full:

1 Whether, in the opinion of the referee, it is more likely than not, that the damage to the Applicant’s product (stockpiles of dry distillers grain and solubles) was occasioned by or happened through: (i) spontaneous combustion of the product; (ii) or spontaneous fermentation; (iii) or heating; (iv) or any process involving the direct application of heat.

2 Whether, in the opinion of the referee, it it is more likely than not, that the damage to the Applicant’s product was occasioned by or happened through some other process and, if so, what caused the damage.

1. Following the filing (but prior to the adoption) of the Referee Report, Dalby submitted that the report was not pellucid in that it referred to the term “self-heating”. Reference was made to earlier expert reports (not in evidence on the final hearing) to suggest that there was an important scientific distinction between “self-heating” and “spontaneous combustion”, and that the Referee Report did not explain what led to the combustion and damage to the Product. It was in these circumstances that an application was made for the referee to answer further questions aimed at clarifying this issue. This occurred by direction being made pursuant to FCR 28.67(1)(b) that the referee explain by further report:

(a) whether his conclusions that the damage to the Applicant’s product was occasioned by or happened through self-heating means that damage was occasioned by or happened through spontaneous heating;

(b) if the answer to question (a) is either yes or no, please explain; and

(c) if the answer to question (a) is not necessarily, please explain.

1. During the course of oral submissions today, it was accepted by Mr Horgan QC (who appeared with Mr Murphy on behalf of Dalby) that the referee’s opinion, as demonstrated by the Reports, was that it was more likely than not that the damage to the Product was occasioned by or happened through the process of self-heating. This was plainly correct. If one looks at the Referee Report, this conclusion is expressed on five separate occasions with the referee noting:

(i) In my opinion the damage to the [Product] was most likely occasioned by or happened through self-heating.

(ii) The most probable cause of the damage to the [Product] is self-heating.

(iii) The observations that:

* product in the first Bay to be filled; namely Bay 2, which was where the smoke and localised flaming was first noticed, had reached a temperature in excess of 65 degrees Celsius, had a burnt smell and was found to be damaged within the stockpile;
* product in the next Bay to be filled; namely Bay 1, had also reached a temperature of 65 degrees Celsius and was found to have similar damage within the stockpile; and
* the last Bay to [be] filled; namely Bay 3, was also found to have product damage (no temperature measurements given) but deeper within the stockpile;

lead me to conclude that the most probable cause of the damage to the [Product] was self-heating.

(iv) The most probable cause of the bulk of the damage to the [Product] is self-heating.

(v) One cannot be absolutely certain of the most probable cause of damage to the [Product]. Unfortunately, based upon the information and materials available, it is not possible to identify a single cause for the self-heating which probably led to combustion and damage of the [Product]. It may well be that all of the factors identified above acted together to cause the damage, but without conducting large scale tests, it is likely that detailed causal relationships will remain unknown.

1. Further, in the Supplementary Report, the referee noted:

Unfortunately, it is not possible to be certain of all the factors that contributed to the product damage in the current case. In particular, the cause of the observed flaming combustion on 2 March 2016 cannot be determined with certainty; it may have been self-heating reaching criticality, but it may have been the result of a more complex mix of factors.

In my opinion the most probable cause of damage to the [Product] was self-heating and the observations on the 2nd March 2016 were an alert that product damage had occurred.

1. The question posed to the referee was framed deliberately in terms of probabilities. That is, whether it was “more likely than not” that damage to the Product “was occasioned by or happened through” one or other of the matters specified in the perils exclusion clause. The question for the Court after construing the terms of the exclusion is whether a cause, being a relevant proximate cause, was one which was encompassed by the contractual exclusion agreed between the parties: see *Baulderstone Hornibrook Engineering Pty Ltd v Gordian Runoff Ltd* [2008] NSWCA 243; (2008) 15 ANZ Insurance Cases 61-780 at 77,008-77,009 [263]-[264]. Subject to an additional argument of Dalby with which I will deal separately below, ultimately what the resolution of this proceeding turns on, is the correct construction of the Policy.

# D Submissions

1. Following receipt of the Supplementary Report, both parties filed further written submissions. The position of Dalby at the hearing was: *first*, the Insurers had failed to discharge their burden of proving that perils exclusions 6(c)(i) or (ii) of the Policy applies; and *secondly*, the Court should enter judgment against the respondents in an amount to be later determined.
2. Dalby’s principal arguments can be summarised into a number of propositions:
   1. the referee has been unable to determine the proximate cause of damage;
   2. “self-heating is not within the relevant Perils exclusion” since the exclusion clause should be interpreted to mean “spontaneous heating”;
   3. the conclusion that “self-heating” had occurred is not to identify a cause, proximate or otherwise, and the referee was unable to determine the cause of the self-heating; and
   4. the respondent’s case was limited by its concise statement in response dated 13 December 2017, which stated that the relevant proximate cause was “spontaneous combustion and/or spontaneous heating”.
3. These contentions are in some respects overlapping and interconnected, and I will deal with them below in three categories: construction; spontaneity; and proximate cause. This leaves the last point which can be dealt with very briefly: the concise statement was not a pleading, the statement relied upon does not constitute an admission that the Insurers need leave to withdraw, and there was no want of procedural fairness in the way the Insurers ran their case.
4. The case of the Insurers is relatively straightforward. It is submitted by Mr McArthur QC that in short, the terms of the exclusion are tolerably plain. It is said that the damage claimed falls squarely within the exclusion for damage occasioned by or happening through “heating” in the perils exclusion 6(c)(ii). It is submitted that contrary to Dalby’s interpretation, the clause is not limited to “spontaneous heating”. Even if this is not the case, it is said that “self-heating”, which has clearly been identified as a proximate cause by the referee, falls within the definition of “spontaneous heating”, and further, to the extent that this process then led to spontaneous combustion, then the damage which was caused by fire when the heating progressed to combustion, was caused by “spontaneous combustion” within the meaning of the perils exclusion 6(c)(i).

# E Consideration

## E.1 Construction of the Exclusion Clause

### Applicable Principles

1. It seems to me appropriate that I deal first with the competing arguments of construction.
2. The relevant principles are not the subject of any dispute between the parties. The overarching principle relevant to the interpretation of commercial contracts, including insurance contracts, is that such contracts should be given a business-like interpretation and attention should be given not only to the language used by the parties but also the commercial circumstances addressed by the document and the objects which it intends to secure: see *McCann v Switzerland Insurance Australia Limited* [2000] HCA 65;(2000) 203 CLR 579 at 589 [22] per Gleeson CJ. More specifically, in construing an exclusion clause, the principles explained by the High Court in *Darlington Futures Limited v Delco Australia Proprietary Limited* (1986) 161 CLR 500 at 510-511 are applicable:

… the interpretation of an exclusion clause is to be determined by construing the clause according to its natural and ordinary meaning, read in the light of the contract as a whole, thereby giving due weight to the context in which the clause appears including the nature and object of the contract, and, where appropriate, construing the clause contra proferentem in case of ambiguity. Notwithstanding the comments of Lord Fraser in *Ailsa Craig,* the same principle applies to the construction of limitation clauses. As King C.J. noted in his judgment in the Supreme Court, a limitation clause may be so severe in its operation as to make its effect virtually indistinguishable from that of an exclusion clause. And the principle, in the form in which we have expressed it, does no more than express the general approach to the interpretation of contracts and it is of sufficient generality to accommodate the different considerations that may arise in the interpretation of a wide variety of exclusion and limitation clauses in formal commercial contracts between business people where no question of the reasonableness or fairness of the clause arises.

(citation omitted)

1. Further, and consistently with the above, in *Selected Seeds Pty Ltd v QBEMM Pty Ltd* [2010] HCA 37; (2010) 242 CLR 336 at 344 [29] the High Court stated:

According to general rules of construction, whilst regard must be had to the language used in an exclusion clause, such a clause must be read in light of the contract of insurance as a whole, “thereby giving due weight to the context in which the clause appears”.

(citation omitted)

1. In applying these principles one must, of course, identify the risk covered by the policy and therefore the purpose of the policy.
2. Consistent with the notion that the onus of proof in relation to the applicability of an exclusion clause rests upon an insurer, if an exclusion clause is open to two interpretations, one of which would inappropriately circumscribe the cover provided by the insuring clause and one which would not, the latter is to be preferred: see *Fitzpatrick v Job and Job t/as Jobs Engineering* [2007] WASCA 63; (2007) 14 ANZ Insurance Cases 61-731 at 76,076-76,077 [268].

### Purpose, Context and Text

1. Before coming to the text of the exclusion in question, reference should be made to the commercial context and purpose of the Policy. The Policy is an industrial special risks insurance policy. Dalby is a manufacturer and distributor of ethanol as well as the property owner and occupier of a bio-refinery and takes part in other related activities. Dalby sought and obtained by the Policy insurance for loss, destruction or damage of physical assets, and also obtained cover for consequential loss. The material loss or damage clause in Section 1 of the Policy provided an indemnity in relation to any physical loss, destruction or damage not otherwise excluded. Similarly, the consequential loss indemnity in Section 2 provided for indemnity in relation to such loss in the event of damage causing interruption or interference with the business of Dalby.
2. The exceptions relevant to the cover provided under Sections 1 or 2 are provided by the nine perils exclusion clauses. As noted above, it is perils exclusion 6 with which we are concerned. It is useful to set out the relevant exclusion clause again:

Perils Exclusions:

The Insurer(s) shall not be liable … in respect of:-

…

6. physical loss, destruction or damage occasioned by or happening through:-

…

(c) (i) spontaneous combustion

(ii) spontaneous fermentation or heating or any process involving the direct application of heat

Provided that Perils Exclusions 6(c)(i) and 6(c)(ii) shall be limited to the item or items immediately affected and shall not extend to other property damaged as a result of such spontaneous combustion, fermentation or heating or process involving the direct application of heat.

### Dalby’s Submissions

1. The applicant’s position is that the noun “heating” is modified by the adjective “spontaneous” in cl 6(c)(ii). This is said to be the case for a number of reasons. The requirement to establish *spontaneous heating* is said to be consistent with the requirements to establish *spontaneous combustion* in cl 6(c)(i) and *spontaneous fermentation* in cl 6(c)(ii). In particular, it is said that cl 6(c)(i) includes spontaneous combustion to the exclusion of all other kinds of combustion, meaning that anynon-spontaneous combustion cannot fall within the exclusion. Combustion or burning is not sufficient it is submitted, even though combustion or burning is each a form of heating. If any combustion was enough to engage the exclusion then there would be no need for the word “spontaneous”, which was said to be a limiting word in this context.
2. Dalby recognised that a counter-argument to this construction is that the word “heating” has been included in cl 6(c)(ii) because it is seeking to do some work over and above a spontaneous event. Mr Horgan QC insisted that Dalby’s interpretation was put beyond doubt by the inclusion of the proviso which uses the modifier “spontaneous” to qualify each of combustion, heating and fermentation. The grouping of words in the proviso is said to indicate that for combustion, fermentation or heating, the exclusion only operates where the condition is spontaneous, that is, from rapid oxidation, fermentation or heating of its own constituents, without heat or any fermenting agent from any external source. These are said to be exclusions not involving what were described as “externalities”. To read the clause in such a way, it was submitted, would be consistent with the context of the Policy being an all risks insurance policy, such that all risks are covered save for unexpected internalities. The exclusion in cl 6(c)(ii) of a “process involving the direct application of heat” is an external cause, to be considered separately. It follows, the applicants contend, that the respondents have accepted the risk for damage arising other than by spontaneous reactions (combustion, heating or fermentation) or by any process involving the direct application of heat.
3. Even if these contentions were not self-evidently correct, it was asserted, in the alternative, that there is sufficient ambiguity which requires that the construction argument be resolved in favour of Dalby by the Court adopting, in accordance with principle, the *contra proferendem* rule relating to construction.

### Insurers’ Submissions

1. Unsurprisingly, the Insurers submit there is no basis for construing “heating” as spontaneous heating only. The clause operates so as to exclude damage occasioned by or happening through heating, and spontaneity is not the basis for the exclusions that are not specifically so prefaced. The Insurers frame the relevant question as whether, as contended for by Dalby, the word “spontaneous”, used at the beginning of cl 6(c)(ii), carries over so as to modify not just “fermentation”, but also the meaning of “heating”?
2. The Insurers submit this is not the case and rely on the text of the exclusion clause and the ordinary meaning of the words. *First*, the disjunctive “or” in cl 6(c)(ii), between “spontaneous fermentation” and “heating”, is said to separate the terms such that any qualification would need to be repeated in order to attach to “heating”. *Secondly*, it would be illogical to read spontaneous as qualifying or modifying all concepts referred to in cl 6(c)(ii). There is nothing about the sub-clause which suggests that the third listed cause (“any process involving the direct application of heat”) is to be limited by any spontaneity; indeed, such a limitation, it is submitted, would be contrary to the use of the word “any” and the ordinary meaning of “spontaneous”, which generally refers to internal processes. *Thirdly*, contrary to Dalby’s submission, the Insurers submit that the proviso demonstrates that heating is *not* intended to be qualified in any way. Again, the use of “or” before “heating” (in contradistinction to the comma between “combustion” and “fermentation”) demonstrates that “heating” should be read as referring to a separate and unmodified process.
3. The short point is that there is no textual toehold from which a reading down of the word “heating” is justified, and there is no warrant for reading “heating” as being modified to connote a particular type of process of heating. Further to this, the Insurers argue that heating is to be construed without limitation, such that the exclusion embraces heating from any source which, in the present case, means a process internal to the stockpile of Product or external. This is because the first mentioned cause in the sub-clause (“spontaneous fermentation”) is internal and the last mentioned cause (“any process involving the direct application of heat”) is external.
4. Dealing with the applicant’s submission that read as a whole, the exclusions operate for a “condition that is unable to be anticipated or controlled”, the Insurers point to perils exclusion 4(c)(iv) “error or omission in design” and perils exclusion 5(a)(ii) “faulty workmanship” as being perils unable to be anticipated and controlled. It is further contended that the wording in the Policy is to be interpreted as it would be understood by reference to its natural and ordinary meaning and that by adopting such an interpretation, the word “heating” embraces the type of self-heating referred to by the referee which, as described in the Referee Report, is an “increase in temperatures due to internal exothermic reactions”.

### Conclusions

1. It seems to me it is tolerably plain, from both the text of the exclusion and having regard to the relevant context, that the Insurers were not prepared to accept a risk of damage to the Product occasioned by or happening through heating of any type. I accept the submissions of the Insurers that there are a number of textual matters pointing against the constructions agitated by Dalby.
2. The *first* and most obvious is that the word heating is not qualified or modified by the word “spontaneous” as is the case with “combustion” or “fermentation”. The notion that spontaneity qualifies all of the perils in cl 6(c)(ii) cannot be sustained in circumstances where one of the matters referred to in that clause involves what is clearly an external process (being the application of heat, and is itself qualified by the word “any”).
3. *Secondly*, there is a difference between damage occasioned by spontaneous combustion and damage that would be occasioned by any form of heating (including self-heating); it follows that “heating” has work to do in the exclusion clause properly construed. Indeed the circumstances of this case make it clear that there could be damage to the Product occasioned by heating which fell short of any combustion and it seems to me that this is precisely the sort of eventuality to which perils exclusion 6(c)(ii) is directed.
4. *Thirdly*, contrary to the submissions of Dalby, I do not believe that the proviso assists. The proviso refers to “property damage as a result of such spontaneous combustion, fermentation or heating or process involving the direct application of heat”.
5. Plainly, given the comma between “combustion” and “fermentation” prior to the disjunctive appearing before the word “heating”, “spontaneous” is qualifying “combustion” and “fermentation”. What is also evident is that the insertion of the disjunctive before “heating” points to the fact that “heating” is embracing a broader causal concept as is “any other process involving the direct application of heat”. For these reasons, I do not consider there to be any ambiguity and the Insurers’ submissions as to the proper construction of the perils exclusion are to be preferred.
6. It also follows that the argument of Dalby based on the application of the *contra proferendum* rule, such as it is, must be rejected.

## E.2 Meaning of Spontaneous Combustion

1. In any event, even if I am wrong in relation to the above issue of construction, it seems to me clear that the self-heating referred to by the referee would, in any event, be a form of “spontaneous heating” and hence fall within the exclusion as construed by Dalby.
2. In determining this issue, I was referred by the parties to various dictionary definitions. The Macquarie Concise Dictionary, 5th ed, provides a definition of “spontaneous” and a definition of “spontaneous combustion” in the following terms:

**spontaneous */*** *adj.* 1. Proceeding from a natural personal impulse, without effort or premeditation; natural and unconstrained; *a spontaneous action; a spontaneous remark*. 2. (of impulses, motion, activity, natural processes, etc.) arising from internal forces or causes, or independent of external agencies. 3. growing naturally or without cultivation, as plants, fruits, etc. 4. produced by natural process.

**spontaneous combustion /** *n.* the ignition of a substance or body from the rapid oxidation of its own constituents, without heat from any external source.

1. The Oxford Encyclopaedic English Dictionary sets out definitions of the same terms as follows:

**spontaneous /** *adj.* **1** acting or done or occurring without external cause. **2** voluntary, without external incitement (*made a spontaneous offer of his services).* **3***Biol.* (of structural changes in plants and muscular activity esp. in young animals) instrinctive, automatic, prompted by no motice. **4** (of bodily movement, literary style, etc.) gracefully natural and unconstrained. **5** (of sudden movement etc.) involuntary, not due to conscious volition. **6** growing naturally without cultivation.

**spontaneous combustion** the ignition of a mineral or vegetable substance (e.g. a heap of rags soaked with oil, a mass of wet coal) from heat engendered within itself, usu. By rapid oxidation.

1. The Supplementary Report provides the referee’s reasoning process for drawing some meaningful distinction between the concept of “self-heating” and “spontaneous heating”. The referee expresses his view that they are “not quite synonymous terms”. This is because, according to the referee, spontaneous suggests “an event or a suddenness” and self-heating can be a “very slow process” which can take months to reach “criticality”. It is for this reason that the referee described the process as self-heating rather than spontaneous heating. Both parties agreed that it was for the Court to determine the content to be given to the word “spontaneous” as used in the Policy to the extent that it was relevant. It seems to me that the ordinary, usual and relevant meaning of the word “spontaneous”, is that it describes the occurrence of something *without external cause*. Although spontaneous combustion is usually related to something that occurs with some rapidity, when talking about spontaneous in the sense of qualifying the causal concept of heating, it simply means that it occurs without external incitement or factors, rather it is something which occurs by reason of internal processes.

# F Proximate Cause

1. The above is not sufficient to determine the case because Dalby argues that the Insurers have failed to discharge their evidentiary and persuasive burden of identifying that heating (or more precisely, self-heating) is the proximate cause of the damage. Reliance is placed by Dalby on the cautions, or more specifically, the “caveat” expressed by the referee. In the Referee Report, under the heading “Overall Caveat”, the following appears:

Without detailed records of the manner in which Bays 2, 1 and 3 were stacked with product (DDGS); including the quantities delivered, the dates of delivery, the temperature of each delivery and the ambient temperature and relative humidity at each delivery, and without further information of the physical properties of the product (DDGS), one cannot be absolutely certain of the most probable cause of damage to the Applicant’s product. Unfortunately, based upon the information and materials available, it is not possible to identify a single cause for the self-heating which probably led to combustion and damage of the Applicant’s product. It may well be that all of the factors identified above acted together to cause the damage, but without conducting large scale tests, it is likely that detailed causal relationships will remain unknown.

1. A similar comment is made in the section quoted above from the Supplementary Report.
2. What the referee was relevantly reporting upon was his opinion as to what was the likely cause of damage to the Product. As both parties accepted on the application for adoption of the Referee’s Report, the referee properly attended to his task and his process of reasoning set out in the Referee’s Report is relatively clear. He starts by identifying that the damage to the Product “was most likely occasioned by or happened through self-heating”. He then proceeds to note that “as there is more than one mechanism that can cause self-heating, each of these mechanisms need to be considered in turn”. The reference to “cause” in this context needs to be examined more closely. Although the referee was expressing a view that damage was caused through self-heating, the referee was also directing himself to the anterior issue as to the mechanism which itself caused the self-heating.
3. The referee then considers various “mechanisms” which could cause self-heating, being: ambient temperature and stockpile size, initial temperature and stockpile size, wetting, and spontaneous fermentation. Dealing with each of these in turn, the referee notes that the ambient temperature and stockpile size could only have caused self-heating leading to spontaneous combustion if the stockpile size was significantly larger than the stockpile size that had been referred to in the reports provided to him. As to initial temperature and stockpile size, the referee considered it was difficult to estimate its contribution as there was, apparently, insufficient material available to make an estimate of the critical stockpiling sizes or stacking temperatures at the relevant times.
4. As to wetting, while there was evidence that ingress of water caused localised wetting, the referee considered the amount of water appeared to be quite small in comparison to the overall size of the stockpile. This factor, and other indications, suggest that wetting would have had little effect on heating, although it could not be conclusively ruled out. The conclusion was formed that it seemed unlikely to be a singular cause of the self-heating.
5. Finally, the referee ruled out spontaneous fermentation as all investigators had concluded that there were insufficient quantities or sources of yeast within the stockpile.
6. In this way, what can be observed is that the referee was carefully going through the various factors which either individually or together might have been the *basis* for self-heating to occur. The way in which Dalby puts it, is that it could not sensibly be said that self-heating was the real and proximate cause of the damage, but rather there needs to be recognition of the fact that the referee could not identify what, in fact, caused the loss and damage to the Product.
7. This submission requires consideration of an issue somewhat different to the well-known circumstance commonly arising where there are two or more causes, only one of which falls within an exclusion. As is well known, in these circumstances the policy will generally not respond: see *Wayne Tank & Pump Co Ltd v Employers Liability Assurance Corporation Ltd* [1974] QB 57; see also *McCarthy v St Paul International Insurance Co Ltd* [2007] FCAFC 28; (2007) 157 FCR 402 at 429-438 [88]-[115] for an examination in detail of the content of operation of the so-called “*Wayne Tank* principle”.
8. The point here is the distinction between a cause in the sense that physical loss, destruction or damage was occasioned by or happened through the existence of a phenomenon, and the question of what was the reason for the existence of the phenomenon. This distinction can be seen in an analogous context in the decision of the Victorian Court of Appeal in *Gunns Forest Products Ltd v North Insurances Pty Ltd* [2006] VSCA 105; (2006) 14 ANZ Insurance Cases 61-691.
9. In that case, Gunns Forrest Products Ltd (**Gunns**) owned and operated a woodchip manufacturing mill in Tasmania. Flakes of rubber were found in woodchip stockpiles awaiting export and in stockpiles at its mill. The presence of the rubber rendered the woodchips “unmerchantable”. The source of the rubber pieces was identified as a damaged part of the conveyor belt taking milled woodchips to a screenhouse. Gunns was insured under an industrial special risk policy and made a claim in respect of “loss and damage” to the woodchips. In that case the only issue was the applicability of the perils exclusion in the policy, and the dispute was referred to arbitration. The exclusion provided for loss or damage “occasioned by or happening through … contamination”.
10. The arbitrator found that the damage to the woodchips was occasioned by their contamination. The award was then the subject of an unsuccessful appeal. Gunns then sought leave to appeal in the Court of Appeal where Gunns submitted that the contamination itself should have been considered as the damage, and the arbitrator had manifestly erred by failing to examine the cause of (or reason for) that damage, being the various causes of the antecedent damage to the conveyor belt. Gunns contended the arbitrator failed to distinguish what “constituted” the damage to the woodchips from what had “caused” the damage to the woodchips.
11. The application for leave to appeal was dismissed. In doing so, Chernov JA noted that the proximate cause of the damage was the contamination, and it would be inaccurate to say that the real and proximate cause of the damage was the problem with the machinery. Mandie AJA (with whom Chernov and Redlich JJA agreed) noted that contamination may be a condition or it may be a process. The mere fact that the damage can be described as contamination does not preclude contamination also being the *process* by which the damage was caused. The relevant exclusion was concerned with the events or perils described in the clause, that originated from within the premises of the insured. It was therefore highly probable that any eventuation of the specified events or perils would result from a cause, or a combination of causes, originating from within those premises which do not fall within the exclusion clause. It would always be possible by examining antecedent events to identify such an anterior cause or combination of causes.

**G CONCLUSION**

1. As was noted in *Baulderstone Hornibrook* at 77,008-77,009 [263], ultimately the matter with which I am concerned is a matter of construction of the Policy and the relevant question is whether the parties intended the Policy to respond in circumstances where physical loss, destruction or damage was occasioned by or happened through heating. For reasons I have already explained in the context of the construction argument, there is no reason in the context of the exclusion, or the Policy as a whole, to search for antecedent events in order to identify anterior causes of the heating. There is no reason to think that the exclusion was not intended to cover what could be reasonably characterised as damage occasioned by or happening through heating.
2. In these circumstances, the application must be dismissed.

# H COSTS

1. The Insurers seek a special costs order. On 7 September 2018, after the delivery of the Referee Report, an offer was made which was said to be an offer in accordance with the principles explained in *Calderbank v Calderbank* [1976] Fam 93. The Insurers offered to resolve the proceedings by an order dismissing the proceedings and that there be no order for costs and each party bear their own costs, including any reserved costs.
2. The discretion provided to me under s 43 of the *Federal Court of Australia Act 1976* (Cth) is a broad one. Although the Referee Report was sufficient, in my view, to establish that the damage was caused by heating, as was evident from the order I made seeking further assistance from the referee in the form of a further report, there was a not insignificant argument that was able to be advanced in relation to the proper construction of the Policy and there was sufficient ambiguity in the Referee Report to require me to seek clarification.
3. In all the circumstances, doing the best I can to do justice between the parties, I think the appropriate order is that costs follow the event and those costs be payable on the ordinary basis.

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| I certify that the preceding fifty-eight (58) numbered paragraphs are a true copy of the Reasons for Judgment herein of the Honourable Justice Lee. |

Associate:

Dated: 28 November 2018