IN THE SUPREME COURT OF NEW ZEALAND

SC 32/2016
[2016] NZSC 158

BETWEEN PRATTLEY ENTERPRISES LIMITED
Appellant

AND VERO INSURANCE NEW ZEALAND LIMITED
Respondent

Hearing: 10 and 11 October 2016

Court: William Young, Glazebrook, Arnold, O'Regan and McGrath JJ

Counsel: F M R Cooke QC, S P Rennie and A G M Whalan for Appellant
D J Goddard QC and C M Brick for Respondent

Judgment: 6 December 2016

JUDGMENT OF THE COURT

A The appeal is dismissed.

B Prattley is to pay Vero costs of $25,000 together with reasonable disbursements to be fixed by the Registrar.

REASONS
(Given by William Young J)

Table of Contents

	Para
The appeal	[1]
The Contractual Mistakes Act argument	[6]
The policy terms	[9]
The settlement agreement	[18]
The approach to Prattley's entitlements taken in the High Court and Court of Appeal	[24]
Prattley's argument	[26]
The argument in general terms	[26]

The policy proceeds on the basis that indemnity is to be calculated by the cost of repair or replacement [28]
The policy does not provide for allowances for betterment or depreciation [30]
Prattley is entitled to recover separately and cumulatively in respect of the damage caused by each earthquake [33]
Our analysis [35]
Disposition [51]

The appeal

[1] Prattley Enterprises Limited (Prattley) owns land on Worcester Street, just to the east of Cathedral Square, Christchurch. Prior the Christchurch earthquakes of 2010 and 2011, a three story building known as Worcester Towers occupied the site. It had been built in the 1920s and used by Prattley for purposes which were primarily commercial, that is, the generation of income in the form of rent. Worcester Towers was insured by Prattley with Vero Insurance New Zealand Limited (Vero) on an indemnity, and not reinstatement, basis. The "total building sum insured" was $1,605,000.

[2] Worcester Towers suffered moderate damage in the Christchurch earthquake of 4 September 2010 (the first earthquake[1]) and remained in use until it suffered further damage in the Boxing Day earthquake of the same year (the second earthquake). From this point, the building was "red-stickered" and thus not occupied. In the major earthquake of 22 February 2011 (the third earthquake), the building was severely damaged. A demolition notice was issued on 1 March 2011 by the Christchurch City Council and there was also an order from the Canterbury Earthquake Recovery Authority (CERA) in June 2011 to the same effect. It was eventually demolished in September 2011.

[3] Prattley claimed on its insurance policy with Vero. Valuations of Worcester Towers were obtained. After very limited negotiations, Prattley and Vero agreed that Vero would pay Prattley $1,050,000 plus GST in "full and final settlement" of its insurance claim. The agreement was finalised on 23 August 2011

[1] Only these three earthquakes are material to the case. There were many more than three earthquakes and aftershocks that affected the Christchurch region in the aftermath of the 4 September 2010 earthquake.

and the money was paid two days later. The agreement provided that the amount paid was:

> … in full and final settlement and discharge of the Claim and any claims against Vero arising directly or indirectly out of, or in connection with the Earthquake Activity and/or the Policy and/or the Insured Property Damage whether such claims arise under statute, common law, or equity; are in existence now or may arise sometime in the future; are known or unknown; in the contemplation of the parties or otherwise. This includes the discharge of any further claim under the Policy for damage, loss or other entitlement under the Policy occurring subsequent to the date the Insured Property Damage occurred, whether or not that further claim has been notified to Vero.

[4] In the present proceedings Prattley challenges the settlement. It now quantifies its recoverable loss at $3,388,000 plus GST. Prattley claims that both it and Vero entered the settlement under a common mistake as to the correct measure of indemnity under the policy and that the agreement should accordingly be set aside under the Contractual Mistakes Act 1977. It also seeks judgment for the difference between what it was paid and its claimed entitlement. For ease of discussion and particularly comparison, all figures subsequently referred to will be on a GST exclusive basis.[2] So Prattley is seeking to recover, net of GST, the difference between $3,388,000 (being its claimed entitlement) and $1,050,000 (which is what it was paid), that is $2,338,000.

[5] Prattley was unsuccessful in the High Court[3] and Court of Appeal.[4]

The Contractual Mistakes Act argument

[6] Prattley's challenge to the settlement agreement is based on s 6 of the Contractual Mistakes Act which relevantly provides:

---

2 The insurance policy provides a general condition regarding GST, which relevantly states: "Provided that goods and services tax (GST) is recoverable by *us*, the sum or sums insured by this policy are exclusive of GST to the extent that, in the event of a claim, *we* will pay a maximum of the sum insured plus additional GST to a maximum of the current rate of GST applied to that sum insured."

3 *Prattley Enterprises Ltd v Vero Insurance New Zealand Ltd* [2015] NZHC 1444 (Dunningham J) [*Prattley* (HC)].

4 *Prattley Enterprises Ltd v Vero Insurance New Zealand Ltd* [2016] NZCA 67, [2016] 2 NZLR 750 (Ellen France P, Stevens and Miller JJ) [*Prattley* (CA)].

6 Relief may be granted where mistake by one party is known to opposing party or is common or mutual

(1) A court may in the course of any proceedings or on application made for the purpose grant relief … to any party to a contract—

(a) if in entering into that contract—

…

(ii) all the parties to the contract were influenced in their respective decisions to enter into the contract by the same mistake; … and

(b) the mistake or mistakes, as the case may be, resulted at the time of the contract—

(i) in a substantially unequal exchange of values; … and

…

(c) where the contract expressly or by implication makes provision for the risk of mistakes, the party seeking relief or the party through or under whom relief is sought, as the case may require, is not obliged by a term of the contract to assume the risk that his belief about the matter in question might be mistaken.

[7] Prattley's argument with regard to the Contractual Mistakes Act is along these lines:

(a) The parties entered into the settlement agreement under a common mistake as to Prattley's entitlement under the policy, satisfying s 6(1)(a)(ii). Both parties had assumed the policy was a standard indemnity policy but Prattley argues that, on the proper interpretation of the policy, the measure of loss should have been based on the costs of repair for the first two earthquakes and of reinstatement for the third (in all cases subject to the $1,605,000 limit).

(b) As a result of the common mistake, Prattley received sufficiently less than its entitlement so as to engage s 6(1)(b)(i).

(c) Section 6(1)(c) is not engaged.

[8] We are satisfied that Prattley's first two arguments fail: there was no common mistake as alleged and the settlement was distinctly favourable to Prattley. This means that we do not need to engage with s 6(1)(c), which would have raised issues of some complexity. By settling its claims against Vero in the terms that it did, Prattley abandoned any entitlement to go back to Vero for more money. The other side of the coin to this abandonment might be thought to be an acceptance by Prattley of the risk that it may have been mistaken as to its entitlements, particularly in light of the fact that the settlement was said to be in full and final settlement of any claims, both existing and future and known or unknown. At first sight, such acceptance might appear to engage s 6(1)(c) and thus to disqualify Prattley from relief. But despite the attractive simplicity of this analysis, we have some reservations whether it is necessarily correct. The reality is that a party to a contract is unlikely to seek relief under the Contractual Mistakes Act unless required by the contract to "assume the risk" of the mistake. If not so required, such a party would have no need to seek relief but would instead simply rely on the contract. It follows that if s 6(1)(c) is construed broadly, there would be little, and perhaps no, scope for relief under the Contractual Mistakes Act, which would thus be at risk of becoming a dead letter. This may suggest that some specificity as to, and not merely a general, assumption of risk may be necessary to engage s 6(1)(c). Working out how to resolve all of this may not be easy[5] and we see it as a task best deferred until a case arises where such resolution is critical to the result.

The policy terms

[9] The policy provides:[6]

> In consideration of *you* having paid or promised to pay the required premium *we* agree to indemnify *you* in the manner and to the extent set out in the applicable parts of this policy.
>
> The insurance contract consists of any statements on which this insurance is based, *your* proposal, the applicable parts of this policy, and the *schedule*.

---

5 See Brian Coote "Allocation of Risk under the Contractual Mistakes Act 1977" [1993] NZ Recent Law Review 434.

6 There are two relevant policies in identical terms. The first policy expired between the first and second earthquakes and was renewed. For ease of discussion, we will refer to the policies in the singular.

In the policy words and phrases which are italicised are defined. “You” means Prattley and “we” means Vero.

[10] The material damage section of the policy is relevantly in these terms:

> *We* will indemnify *you* for *damage* to any of the *insured property* occurring during the *period of insurance*.
>
> *You* will be indemnified by payment or, at *our* option, by repair or by replacement of the lost or *damaged* property.
>
> Subject to the reinstatement of amount of insurance extension *our* liability will not exceed the total sum insured …

As noted, the total sum insured was $1,605,000.

[11] A clause headed “Restatement of amount of insurance” provides:

> In the event of *damage* for which a claim is payable under this material damage section the amount of insurance cancelled by such *damage* will be automatically reinstated from the date of *damage*. …

[12] “Earthquake indemnity” cover was purchased under extension MD020, which provides:

> This extension applies to those items of *insured property* that have a company earthquake sum insured shown in the *schedule*.
>
> In the event of any *insured property* to which this extension applies suffering *earthquake damage* … during the *period of insurance we* will cover *you* for such *damage*.
>
> Insurance under this extension is subject to the special provisions set out below.
>
> *“Destroyed”* means so *damaged* that the property, by reason only of that *damage*, cannot be repaired.

[13] MD020 also contained “Special provisions”:

> (a) Limitation on amount payable
>
> Where the *insured property* is *damaged* but not *destroyed our* liability will not exceed the amount *we* could have been called upon to pay if the property had been *destroyed*.
>
> (b) Claim adjustment

> In respect of each *site* at which *insured property* is located each loss or series of losses arising out of one event will be adjusted separately:
>
> (i) net of any salvage and other recoveries; and
>
> (ii) net of any amount payable by the Earthquake Commission; and
>
> (iii) … net of the earthquake extension excess in the *schedule*;
>
> …
>
> A series of events arising from any one cause during any period of 72 consecutive hours will be treated as one event for the purposes of applying the *excess*.

[14] The schedules are not exactly in the form contemplated as they simply stated that the property was "insured" rather than providing for "a company earthquake sum insured". It is not in dispute that MD020 applied, as did the general policy limit of $1,605,000.

[15] The schedules contained Special Notes:

> Heritage Classification C, some earthquake strengthening following renovations to building in 1970's.
>
> "We will repair or reinstate the building to as reasonably equivalent appearance and capacity using the original design and suitably equivalent materials."

The reference to "Heritage Classification" was an error as Worcester Towers did not enjoy heritage protection.

[16] The standard form policy contained separate extensions for "Earthquake full reinstatement cover" (MD022) and "Reinstatement" (MD033). Reinstatement cover applied where an "excess of indemnity value" was shown in the policy schedule. Where earthquake reinstatement cover was taken out, indemnity would extend to the "cost of reinstatement" of an "equivalent building" providing actual reinstatement occurred. Prattley did not take out reinstatement cover.

[17] We also note that the policy began with a reference to the Fair Insurance Code of the Insurance Council of New Zealand:

> As members of the Insurance Council of New Zealand, *we* are committed to complying with the Council's Fair Insurance Code.
>
> This means *we* will:
>
> 1. provide insurance contracts which are understandable and show the legal rights and obligations of both *us* and the policyholder;
> 2. explain the meaning of legal or technical words or phrases;
> 3. explain the special meanings of particular words or phrases as they apply in the policy;
> 4. settle all valid claims fairly and promptly;
>
> …

The settlement agreement

[18] There was no substantial progress with the insurance claim until after the third earthquake. From that point on, all negotiations proceeded on the basis that the building would be demolished.

[19] In May 2011, Prattley received a valuation from its valuers, Ford Baker. This had been commissioned in January 2011, that is, between the second and third earthquakes. Ford Baker estimated both the market indemnity and depreciated replacement value at $700,000. Prattley had been hoping to recover from Vero substantially more than $700,000 and was, therefore, disappointed with this valuation. Prattley did not give a copy of it to Vero. For reasons which will be apparent shortly, we will refer to this valuation as the first Ford Baker valuation.

[20] During a conference call on 14 June 2011 between Mr Cherry, representing Vero, and representatives of Prattley including its insurance broker, Ms Austin, Mr Cherry, who was unaware of the first Ford Baker valuation, agreed to commission a valuation to assist in estimating indemnity value. He instructed the valuation firm Knight Frank to estimate indemnity value as at the date of the first earthquake. Knight Frank reported back on 6 July 2011. This was the first *shared* valuation, that is one known to both parties. It estimated the "Market Based Indemnity Value of the Improvements" at $370,000 and the "Depreciated Cost Value of Improvements" at $1,400,000.

[21] In the meantime, Prattley had sought and obtained legal advice as to whether it was entitled to the full sum insured, that is, $1,605,000. It was advised that it could recover no more than the value of the building.

[22] Following discussions with Ms Austin in relation to the Knight Frank valuation, Mr Cherry agreed to pay for a further valuation. Prattley commissioned Ford Baker to prepare the valuation and, in doing so, mandated certain assumptions as to rent.[7] These assumptions were distinctly in Prattley's favour. Ford Baker's second valuation, based on these assumptions, estimated market indemnity value at $1,050,000 and depreciated replacement value at $1,021,000. The values so assessed were more than $300,000 higher than those provided in the first Ford Baker valuation. Dunningham J concluded, unsurprisingly, that the second Ford Baker valuation was "not a reliable assessment of market value".[8] In her view the actual market value of the building was in the order of $520,000.

[23] Upon receipt of the second Ford Baker valuation, Mr Cherry agreed to settle the insurance claim for $1,050,000, that is the amount of the unreliable market value assessment in the second Ford Baker valuation. Vero prepared a settlement agreement that was modified in some respects by Prattley's solicitors and, as modified, was signed on 23 August 2011 with payment being made two days later.

The approach to Prattley's entitlements taken in the High Court and Court of Appeal

[24] In the High Court, Dunningham J concluded that the proper measure of indemnity was the market value of the building; this given its state in the aftermath of the third earthquake (which was such that it had to be demolished) and the absence of an intention on the part of Prattley to repair or replace the building.[9] She considered that if Prattley were to recover in respect of the unrepaired damage

---

7 Prattley had been working with Ford Baker before Mr Cherry agreed to pay for the valuation: *Prattley* (HC), above n 3, at [35].

8 At [148].

9 At [136].

caused by the first two earthquakes it would be indemnified in respect of losses which it had not incurred and thus would breach the "indemnity principle".[10] So its total claim was confined to the market value of the building. She was inclined to the view that the market value of the building was in the order of $520,000 based on evidence given at trial by a valuer on behalf of Vero.[11] On the basis of this assessment, Prattley's claim to set-aside the settlement because of a qualifying mistake necessarily failed.[12]

[25] The Court of Appeal adopted a different approach to indemnity. Influenced by the Special Notes, it concluded that the primary measure of indemnity was by way of reinstatement which, in the circumstances of the case, was best assessed by reference to the depreciated replacement value of the building.[13] The amount actually paid, although calculated on a market value basis, was within the range of what would have been appropriate if depreciated replacement cost had been recognised as the appropriate measure of indemnity (that is, between $1,020,000 and $1,400,000). Depreciated replacement cost had been recognised in the negotiations as a possible measure of indemnity. These conclusions left no room for Prattley to resort successfully to the Contractual Mistakes Act.

Prattley's argument

The argument in general terms

[26] Prattley's appeal proceeds on the basis that the proper interpretation and application of the insurance policy is:

(a) The damage caused by the first earthquake would have cost $178,000 to repair and Prattley has a claim for that amount against Vero.

(b) The additional damage caused by the second earthquake would have cost $3,739,000 to repair. Prattley has a claim for that amount which is, by reason of the total sum insured, limited to $1,605,000.

---

10 At [143]–[148]; as to the meaning of the "indemnity principle" see the discussion of this below at [35].
11 At [148].
12 At [151]
13 *Prattley* (CA), above n 4, at [118].

(c) The post-demolition cost of reinstatement would have been in the order of $6,000,000–$7,500,000 in respect of which Prattley has an additional claim, albeit also limited to $1,605,000.

(d) The total entitlement is therefore the sum of these figures: $3,388,000.

The figures for costs of repair and reinstatement come from undisputed findings of fact made by Dunningham J in the High Court.[14]

[27] Mr Cooke QC relied on the particular provisions of the policy at issue rather than on the principles that have developed over time in relation to indemnity value and replacement value policies. While generally invoking the contra proferentem rule and the Fair Insurance Code, he based his argument primarily on three particular premises:

(a) The policy proceeds on the basis that indemnity is to be calculated by the cost of repair or replacement.

(b) The policy does not allow Vero the benefit of allowances for betterment or depreciation.

(c) Prattley is entitled to recover separately and cumulatively in respect of the damage caused by each earthquake.

Each of these premises was developed by Mr Cooke in detailed submissions to which we now turn.

The policy proceeds on the basis that indemnity is to be calculated by the cost of repair or replacement

[28] Mr Cooke argued that the measure of indemnity under the policy is the cost of repair or reinstatement. This is based, in part, upon the wording of the relevant obligation:

---

14 *Prattley* (HC), above n 3, at [147].

> *You* will be indemnified by payment or, at *our* option, by repair or by replacement of the lost or *damaged* property.

He submitted that this meant that Prattley was to be indemnified by way of "repair or reinstatement up to the agreed limit". He further submitted:

> The fact that Vero had the option of meeting that obligation "by payment" does not introduce an entirely different kind of cover … . Rather, it is simply introducing the option frequently given in insurance policies allowing the insurer to meet the promise in monetary terms, rather than by actually undertaking the work.

He also relied heavily on the Special Notes[15] which he treated as a "clear and unambiguous promise" by Vero that it "will repair or reinstate the building" and which did not mention betterment or depreciation.

[29] Anticipating that Vero would argue that on his interpretation of the policy, Prattley was seeking reinstatement cover despite not having bought such cover, Mr Cooke argued that the reinstatement cover which was on offer (but not accepted by Prattley) would have been more extensive than that provided by the indemnity cover as he construed it. In particular, he said, reinstatement cover if acquired would have covered additional code compliance costs which he claimed would not be available on his interpretation of the indemnity cover.

The policy does not provide for allowances for betterment or depreciation

[30] Mr Cooke's argument in this respect was based largely on the logic of his arguments as to the nature of the measure of indemnity. His argument came down to the proposition that as the primary measure of indemnity was "repair or reinstatement", and particularly given the language of the Special Notes, there was no scope on the language of the policy for a deduction for betterment or depreciation. Mr Cooke did not accept the proposition that on his argument the policy required repair or reinstatement on a new for old basis. He preferred to put it in terms of "equivalent for old".

[31] The statement of claim on which Prattley went to trial did not foreshadow this argument, which was only identified by Mr Cooke in his closing submissions to

---

15 The Special Notes are set out above at [15].

Dunningham J. As is apparent, the argument is, in large measure, based on the Special Notes. Prior to the closing submissions in the High Court, the Special Notes were relied on to show that indemnity should be assessed by reference to repair and reinstatement costs (as opposed to market value) but it was not suggested that they precluded allowances for betterment or depreciation.

[32] Mr Goddard QC for Vero strenuously objected to the reliance now placed on the Special Notes, indicating that if it had been signalled earlier, further contextual evidence would have been led and a claim for rectification may well have been brought. As it turns out, we are satisfied that the material presently available is sufficient to enable us to deal fairly with the argument. We observe, however, that the late-surfacing of the argument suggests that it is based on a far from obvious reading of the policy as a whole.

Prattley is entitled to recover separately and cumulatively in respect of the damage caused by each earthquake

[33] Mr Cooke argued that the policy provided for separate cover in relation to each of the three earthquakes with the total sum insured cap resetting after each event. He noted that as more than 72 hours elapsed between each earthquake then each claim was to be "adjusted separately".[16]

[34] In support of this argument Mr Cooke relied heavily on the judgment of this Court in *Ridgecrest NZ Ltd v IAG New Zealand Ltd*, a reliance which was predicated on his contention that the policy operated on a repair or replacement basis.[17]

Our analysis

[35] We start our analysis with a much cited passage from the judgment of Brett LJ in *Castellain v Preston*:[18]

> In order to give my opinion upon this case, I feel obliged to revert to the very foundation of every rule which has been promulgated and acted on by the Courts with regard to insurance law. The very foundation, in my opinion, of every rule which has been applied to insurance law is this, namely, that the

16 See above at [13].
17 *Ridgecrest NZ Ltd v IAG New Zealand Ltd* [2014] NZSC 129, [2015] 1 NZLR 40.
18 *Castellain v Preston* (1883) 11 QBD 380 (CA) at 386.

> contract of insurance contained in a marine or fire policy is a contract of indemnity, and of indemnity only, and that this contract means that the assured, in case of a loss against which the policy has been made, shall be fully indemnified, but shall never be more than fully indemnified. That is the fundamental principle of insurance, and if ever a proposition is brought forward which is at variance with it, that is to say, which either will prevent the assured from obtaining a full indemnity, or which will give to the assured more than a full indemnity, that proposition must certainly be wrong.

This is a succinct definition of the indemnity principle, a principle which is generally applicable to the assessment of losses under an indemnity policy[19] and underlies the unwillingness of courts to construe such policies so as to confer entitlements which exceed the loss of the insured.[20]

[36] The general application of the indemnity principle in circumstances similar to the present is illustrated by *QBE Insurance (International) Ltd v Wild South Holdings Ltd*,[21] a case decided after *Ridgecrest*, in which the Court of Appeal addressed its application to successive losses caused by the Canterbury earthquakes:

> [84] The insured may recover successive losses in the same policy term. No difficulty arises where the loss from event #1 had been remedied when event #2 happened. In that case the loss or damage for which the insurer is liable must be calculated separately for each event, the insured having incurred the costs of reinstatement.
>
> [85] The position differs where the damage from event #1 was unremedied when event #2 happened, causing additional damage. In that case, no question ordinarily arises of the insured repairing in isolation the damage from each event; it is the cumulative damage after event #2 that will be repaired. Although the loss is incremental upon that from event #1, it is reasonable to suppose that the insured will achieve economies by repairing all of the damage at the same time. That being so, the cost of repairing the combined damage is likely to be less than the notional cost of repairing the damage from each event in reverse order. Where that is so, the cost of reinstating the property to the policy standard after event #2 is the insured's actual loss for which it may claim indemnity, in addition of course to any expenses already incurred to remedy the damage from event #1.
>
> (citations omitted)

[37] Leaving aside the language used in the Special Notes, the wording of the key clauses in the policy is standard and many of the leading cases concern insuring

---

19 See for instance: *Leppard v Excess Insurance Co Ltd* [1979] 1 WLR 512 (CA) at 518–519; and *Keystone Properties Ltd v Sun Alliance and London Insurance Plc* 1993 SC 494 at 511–512.

20 See for instance: *British Traders Insurance Co Ltd v Monson* (1964) 111 CLR 86.

21 *QBE Insurance (International) Ltd v Wild South Holdings Ltd* [2014] NZCA 447, [2015] 2 NZLR 24.

clauses which are either exactly the same as,[22] or very similar to,[23] the corresponding clauses in the present policy.[24] The approach which the courts take to such language is reasonably well understood, at least in general terms, by those who work in the insurance industry, including the brokers who act for those seeking insurance and often advise as to claims. As will become apparent, we consider that the argument advanced by Prattley is based on a distinctly unorthodox interpretative approach.

[38] The obligation of Vero is to "indemnify" Prattley for damage suffered. Prattley's primary entitlement was to indemnity by payment, but Vero, at its option, was entitled to provide indemnity "by repair or replacement". Insurers reserve this option to themselves to limit moral hazard.[25] It does not signify that indemnity payment is necessarily to be calculated by reference to the cost of repair or replacement. We do not accept that Mr Cooke's re-ordering of this obligation accurately captures its essence.[26]

[39] The calculation of what is required by way of indemnity will vary depending on the circumstances, but this is always calculated against the background that the purpose of an indemnity payment is to make good the insured's actual economic loss.

[40] If the property has been destroyed and is not to be reinstated, the most obvious basis for calculating indemnity is its market value. This is particularly likely to be so in the case of a property held for investment purposes. The market value of such a property will represent its value to the insured and the insured, once paid that

---

22 See for instance: *TJK (NZ) Ltd v Mitsui Sumitomo Insurance Co Ltd* [2013] NZHC 298, [2013] Lloyds Rep 545 at [22].

23 See for instance *QBE Insurance (International) Ltd v Pegasus Group Ltd* [2011] NZCA 268, (2011) 16 ANZ Insurance Cases ¶61-894 at [13] in these terms: "The Insured will be indemnified by payment or, at the Company's option, by repair or by replacement of the lost or damaged property."; *Wild South Holdings Ltd v QBE Insurance (International) Ltd* [2013] NZHC 2781 at [6] in these terms: "The insured will be indemnified by payment or at QBE's option, by repair or by replacement of the lost or damaged property and by payment of the insured costs."; and *Tevcorp Holdings Ltd v QBE Insurance (International) Ltd* HC Dunedin CP3/00, 8 September 2000 at [4] in these terms: "The Insured will be indemnified by payment or, at the Insurer's option, by repair or by replacement of the lost or damaged property and by payment of any insured cost."

24 See above at [10].

25 As to this see generally the discussion in Robert Merkin (ed) *Colinvaux's Law of Insurance* (11th ed, Thomson Reuters, London, 2016) from [7-107].

26 See above at [28].

value, will be able to replace the insured property with a similarly performing investment.[27] Payment calculated on this basis will leave the insured with money which, when added to the value of the land, will equate to the pre-event value of the land and buildings.

[41] Where the property is to be repaired or reinstated, the estimated costs will usually provide a better basis for calculating loss, particularly if the building is well-suited to the business needs of the insured and thus could not easily be replicated.[28] Similar considerations apply if a particular building is to be replaced with a like building.[29] It is, however, elementary that the resulting calculations must recognise that an indemnity policy does not, without specific language, operate on a "new for old" basis. An insured whose property is repaired, reinstated or replaced might, in the absence of a compensating allowance, be better off than before the damage. This can be avoided by a betterment allowance or, alternatively, by deducting from the assessed repair or reinstatement cost an allowance representing the depreciated condition of the insured property immediately before it was damaged.[30] Where replacement cost has been adopted as the measure of indemnity, similar considerations will apply if the actual or notional replacement building is of better quality than the insured building. The entitlement of an insurer to allowances for betterment or depreciation is part and parcel of the indemnity principle and need not be provided for explicitly in the policy.[31]

[42] This is not to say that proper indemnity may not need to be assessed by reference to repair costs and without betterment. Damage to, or destruction of, a particular element of a building may result in a need for repair which, once

---

27 As to this see *Carrick Furniture House Ltd v General Accident Fire & Life Assurance Corp Ltd* 1977 SC 308 at 320; and the discussion in *Colinvaux's*, above n 25, at [11-033].

28 As was said in *Keystone*, above n 19, at 501–502; and held to be the case in *Reynolds v Phoenix Assurance Co Ltd* [1978] 2 Lloyds LR 440 (QB) at 447–448; see also *St Alban's Investment Co v Sun Alliance* [1983] IR 362 (SC).

29 *St Albans Investment*, above n 28, at 375 per O'Higgins CJ.

30 *Keystone*, above n 19; as to betterment see the discussion in John Birds, Ben Lynch and Simon Milnes (eds) *MacGillivray on Insurance Law* (13th ed, Thomson Reuters, London, 2015) at [21-020]; and *Colinvaux's*, above n 25, at [11-137]–[11-138].

31 See the helpful discussion of this in the judgment of Giles J in *Vintix Pty Ltd v Lumley General Insurance Ltd* (1991) 6 ANZ Insurance Cases ¶61-050 (NSWSC) at 77,079–77,081. A subsequent appeal from this judgment, not addressed to this issue, was dismissed: *Lumley General Insurance Ltd v Vintix Pty Ltd* (1991) 6 ANZ Insurance Cases ¶61-087 (NSWCA) [*Vintix* (CA)].

completed, does not result in any betterment. In such an instance, the obligation of the insurer will be to pay the cost of repairs or see to them itself. As well, it may be that complete or substantial reinstatement does not result in any betterment.[32] In such an instance the liability of the insurer will likewise come down to either paying indemnity calculated by reference to the costs (in this case of reinstatement) or attending to what is required itself. The situations just postulated are, however, well-removed from the facts of this case.

[43] An insurer's entitlement to deduct for betterment may be excluded by the terms of the policy and often is, as is the case where insurance is provided on a full replacement or reinstatement basis. There was, however, no such exclusion here.

[44] The approach proposed on behalf of Prattley is inconsistent with the existence in the policy of the option of a reinstatement extension. Under the reinstatement extension, the insured is entitled to more than indemnity value only if repairs or reinstatement are undertaken. Prattley's argument would leave it, in this respect, better off than it would have been if it had purchased the reinstatement extension, in that it is entitled to use the costs of reinstatement as the measure of loss (subject, of course, to the limit provided by the total sum insured) without actually reinstating the building. Such a result would be paradoxical.

[45] Mr Cooke sought to meet, slightly indirectly, the point just made by contending that, on his interpretation, Prattley's entitlement to reinstatement costs would not encompass those associated with compliance with new building requirements whereas, if reinstatement cover had been taken out, such costs would have been covered. It is true that the provisions as to reinstatement encompass compliance costs of the kind postulated whereas the indemnity provisions in the policy document do not explicitly refer to such costs. We are, however, far from persuaded that such costs would not be taken into account where indemnity is to be measured by repair or reinstatement. Indeed, such authority as there is suggests that compliance costs would be covered.[33] In the normal course of events, however, such inclusion will be of little moment in calculating indemnity as compliance with new

---

[32] This was the factual conclusion reached in *Reynolds*, above n 28.

[33] See *Vintix* (CA), above 31, at 77,334.

building standards would presumably result in betterment which would have to be allowed for.

[46] We accept that it is open to the parties to an insurance contract to provide for recovery on a basis which is not constrained by the indemnity principle. Reinstatement and agreed value policies provide examples where this happens. Mr Cooke's argument was that the current policy is another example. To the extent that this argument relied on the language of the insuring clause,[34] we have already rejected it.[35] As noted, that clause is expressed in terms which are customarily used in indemnity policies. Mr Cooke also relied on the Special Notes in support of the argument that the policy provided for reinstatement cover. We, however, see such reliance as misplaced. The policy was a standard offering to the market. In the context of the policy wording as a whole, including the unaccepted reinstatement option, the purpose of the Special Notes is clear; it is to limit liability of Vero to no more than the cost of repair or reinstatement to "reasonably equivalent appearance and capacity using the original design and suitably equivalent materials". They do not stipulate such cost as the measure of indemnity in situations in which the building is not to be repaired or reinstated. Nor can they sensibly be construed as excluding allowances for betterment and depreciation. To construe the Special Notes in the way suggested would be the interpretative equivalent of allowing the tail to wag the dog.

[47] The rejection of the repair or reinstatement measure of indemnity argument means that Prattley's reliance on *Ridgecrest* is untenable. The insurance arrangements in *Ridgecrest* were unusual; the insurance was on a reinstatement basis but with a resetting liability cap unrelated to, and much less than, the actual replacement value of the building.[36] In that case, the Court held that the "indemnity" to which Ridgecrest was relevantly entitled in respect of each event was the replacement value of the building subject to the resetting cap.[37] Its conclusion was that the totality of Ridgecrest's claims in relation to the sequence of losses in issue in that case was not limited to the amount of the cap. This did not breach the indemnity

---

34 See above at [28] .

35 See above at [37] and [38].

36 See *Ridgecrest*, above n 17, at [6]–[10] and [13].

37 At [54] and [61].

principle because (a) the policy provided for reinstatement cover; and (b) the cap reset after each event. On the other hand, the Court made it clear that the resetting of the cap would not have entitled Ridgecrest to recover more than the replacement value of the building.[38] Such recovery would have breached the indemnity principle.

[48] In the present case what was insured was the indemnity value of the building, that is, what it was worth. It would be a clear breach of the indemnity principle for Prattley to recover more than it had relevantly lost, that is what the building was worth when the sequence of earthquakes started.

[49] On our approach, the policy provided, in a very orthodox way, for the indemnity to which Prattley was entitled and in terms which would be well understood by any sensible person engaged in commercial building insurance. We thus see no occasion to resort to the contra proferentem principle. As it happened, the policy was correctly understood by both Mr Cherry for Vero and by those advising Prattley, including its solicitors. More generally, Prattley was at no disadvantage in dealing with Vero. Indeed, when it came to settlement, Vero was at a distinct informational disadvantage (as to the rental assumptions upon which Worcester Towers had been valued). Nor do we see Vero's policy or conduct as breaching the provisions of the Fair Insurance Code, which were recorded in the policy.

[50] As we have noted, Prattley's use of the building was primarily commercial. In light of this and given the destruction of the building and the absence of anything approaching a settled intention on the part of Prattley to replace it, the most obvious approach to the calculation of indemnity was the pre-event value of the land and building and demolition costs less the residual (that is post-demolition) value of the land, so as to leave Prattley with land and money equating to the pre-event value of what it had before the earthquakes. This was the basis upon which the settlement sum was calculated, but this calculation was inflated in Prattley's favour by the inaccurate rental assumptions to which we have referred.[39] On Dunningham J's assessment, from which we see no reason to differ, Prattley's loss was in the order of

---

[38] At [54].

[39] See above at [22].

$520,000.[40] In the result it was paid out more than double its entitlement and it has no legitimate grounds for complaint.

Disposition

[51] The appeal is dismissed. Prattley is to pay Vero costs of $25,000 together with reasonable disbursements to be fixed by the Registrar.

Solicitors:
Rhodes & Co, Christchurch for Appellant
Fee Langstone, Auckland for Respondent

40 See *Prattley* (HC), above n 3, at [148].