

ELIAS CJ:

Thank you Mr Gray.

MR CAMPBELL QC:

May it please Your Honours, I appear for the respondent with Ms Parlane.

ELIAS CJ:

Thank you Mr Campbell, Ms Parlane.

MR GRAY QC:

Your Honours, it's a narrow issue before us today. It's of narrow compass factually and legally really it is a matter of first impressions so without wishing to make predictions which will come back to haunt me we may not detain you for too long.

It is an appeal in respect of a construction of an insurance policy. It involves a residential building which was not occupied by the owner but was rented. It was within the red zone.

GLAZEBROOK J:

Is there a significance, because you do make something of it being rented, is there a significance to that?

MR GRAY QC:

Yes there are, the Southern Response forms of policy are different –

GLAZEBROOK J:

So it's just a policy issue, thank you.

MR GRAY QC:

Yes. The owner elected option 2 in the red zone scheme so they sold the lands to the Crown –

ELIAS CJ:

Sorry, just on that point, the long rental policies have similar clauses though presumably do they in other –

MR GRAY QC:

Yes but one additional option.

ELIAS CJ:

But?

MR GRAY QC:

One additional option.

ELIAS CJ:

Right.

MR GRAY QC:

To rebuild at another site.

ELIAS CJ:

Yes, yes.

MR GRAY QC:

Otherwise they're pretty much the same.

ELIAS CJ:

Yes.

MR GRAY QC:

Look, just to give Your Honours a sense of the scale for policies of this type about 1728 claims have been settled on a similar basis. There's another r-

ELIAS CJ:

Similar to what?

MR GRAY QC:

The policy which is before the Court today.

ELIAS CJ:

I see.

MR GRAY QC:

Another 200 are beyond economic repair but have not yet made an election. There are 530 claims which are beyond economic repair. There's an election to rebuild but building hasn't started and so about 2500 policies –

GLAZEBROOK J:

Rebuild on another site you mean?

MR GRAY QC:

Yes.

GLAZEBROOK J:

Thank you.

MR GRAY QC:

Not rental properties. The issue between the parties which are still live and are before the Court concern two allowances within the cost of rebuilding a house. The first is an allowance for contingencies or unexpected things which might arise and the second is the scope of an allowance for professional fees which might be incurred in rebuilding. The main reason we're here, however, is that the Court of Appeal in expressing its judgment made some reference to condition of the land perhaps still being live and that's the matter which has really caused some uncertainty for claimants and some problems for the appellant.

ELIAS CJ:

Ah, yes I wondered that, thank you.

MR GRAY QC:

And is the heart of why we're here.

ELIAS CJ:

So what paragraph is that again in the Court of Appeal decision?

MR GRAY QC:

It's 55 Your Honour. It's in volume 1 of the bundle.

GLAZEBROOK J:

And why is that causing problems?

MR GRAY QC:

It's leaving some people to wonder whether existing settlements can be reopened on grounds that they're entitled to additional compensation by reason of the condition of their land.

WILLIAM YOUNG J:

They're probably not, are they?

MR GRAY QC:

No. No.

WILLIAM YOUNG J:

That meant on the basis of if they've settled, they've settled.

MR GRAY QC:

Yes, and this policy is responding to the house itself.

ELIAS CJ:

But there might be knock on claims I suppose arising out of the settlements on arguably a mistaken basis.

MR GRAY QC:

That's the issue that is occurring to people.

ELIAS CJ:

Yes.

GLAZEBROOK J:

Didn't the Court of Appeal endorse Justice Dobson's judgment which actually ruled out that out?

MR GRAY QC:

Yes the Court of Appeal said and agreed with Justice Dobson in *Turvey Trustee Ltd v Southern Response Earthquake Services Ltd* [2012] NZHC 3344 –

GLAZEBROOK J:

It's not entirely clear how that fits with the decision itself –

MR GRAY QC:

Correct.

GLAZEBROOK J:

– to me anyway, but in fact they did endorse that position.

MR GRAY QC:

Your Honour's got the point. They said they agreed with *Turvey*. We're not sure they analysed *Turvey* correctly when they said they agreed with it.

WILLIAM YOUNG J:

Turvey was rebuilding the house on another site?

MR GRAY QC:

Yes it was.

WILLIAM YOUNG J:

So the slightly different issue there is that it might be silly putting down 15 metre foundations if one metre foundations are fine?

MR GRAY QC:

Yes and the factual distinction is that in the case of *Turvey* you're actually digging new foundations and you don't know what you'll find until you dig.

WILLIAM YOUNG J:

Yes.

MR GRAY QC:

But so is paragraph 53 and in particular that first sentence, is it?

MR GRAY QC:

Yes, it is. Now, what the Court of Appeal possibly had in its mind when it said that is what the policy entitles the policyholder to is an amount of money equivalent, well, not more than but they treat it as the equivalent to, the cost of rebuilding the house, and the Court of Appeal possibly intended to say, we don't necessarily accept that the cost of rebuilding the house doesn't include an additional amount for foundations because we don't know that we can assume that you're simply replicating what's there. And that's a different proposition of course, and when I articulate it in that way you can see where the tension with the proposition –

ELIAS CJ:

You mean they're making the point that all of this is a proxy and necessarily hypothetical and they're using this to illustrate that?

MR GRAY QC:

Yes. That could well be what the Court of Appeal intended, but the words don't necessarily say that and others have interpreted the words differently. Your Honours –

GLAZEBROOK J:

Because one of the difficulties here is that that actual issue of what you're entitled to in terms of land that you can't rebuild on and how you calculate that isn't actually before us –

MR GRAY QC:

Not on –

GLAZEBROOK J:

– so I'm not sure that any decision that we make on contingencies or professional fees is going to be of any help one way or another in terms of whether you do calculate the 70 foot or whatever it is that you have to put in now on land that doesn't work any more.

MR GRAY QC:

That's the point, Your Honour.

GLAZEBROOK J:

But our, this decision's not going to help you on that, is it?

MR GRAY QC:

No, but saying that is going, we think, to fix the problem, if we can respectfully say that.

GLAZEBROOK J:

So we would just say, well, we're not deciding that point because it's not before us, or, how would that help? Sorry, I'm just trying to –

MR GRAY QC:

Yes.

GLAZEBROOK J:

It's, I mean, obviously it, we've given leave because the position of contingencies can apply to other contracts –

MR GRAY QC:

Yes.

GLAZEBROOK J:

– so it has its public and general importance, but I'm just not entirely sure what help we can be or will be on the other point.

MR GRAY QC:

In my submission what the policy will respond to, and the parties seem to be pretty close on their submissions, written submissions on this point. If the cost of the physical house component of the land and property, the proposition that a claim under the policy for the cost of rebuilding the house will in some way take account of problems with the land is a very troubling proposition and, in my submission, is one that the Court can address itself to. The construction of this policy will, in our submission, show that it responds to the condition of the house itself, the dwelling, and that the entitlement of the policyholder is to be indemnified in the terms of the policy for the destruction of the house itself.

GLAZEBROOK J:

The trouble is a house doesn't arise without its foundations and its attachment to the land, so you would have to have something in there –

MR GRAY QC:

Yes.

GLAZEBROOK J:

– that deals with foundations, wouldn't you?

MR GRAY QC:

You're right –

GLAZEBROOK J:

So do you go back to what's the land was like in 2007 then?

MR GRAY QC:

Our proposition –

GLAZEBROOK J:

Which was when the land was, which was how the land was valued for the EQC.

MR GRAY QC:

Yes.

GLAZEBROOK J:

Have I got the date right, it was 2007, wasn't it?

MR GRAY QC:

It's a matter of construing the policy, Your Honour, and I'll answer Your Honour's question in more detail by looking at the policy itself. But our proposition is that what the policyholder is entitled to is a replication, on a new for old basis, of what was there before.

WILLIAM YOUNG J:

Yes. But also while it complies with the Building Code?

MR GRAY QC:

Ah...

WILLIAM YOUNG J:

Or do you say that that's right because that –

ELIAS CJ:

Well, it's an existing house that's being purchased, isn't it?

WILLIAM YOUNG J:

Yes, but, sorry, but the rebuild has to be, is assumed to comply with the, isn't it?

O'REGAN J:

Well, that's part of the new for old, isn't it?

WILLIAM YOUNG J:

Yes.

O'REGAN J:

Because it's near the rest of –

WILLIAM YOUNG J:

Yes.

MR GRAY QC:

That's on the basis – yes, Your Honour, but I need, the reason I hesitate and don't just rush to say yes, is yes on the basis of new for old but not on the basis of the cover for additional costs on page 4 of the policy, which deal in a different context with increased costs by reason of compliance with the Building Code when building a new house, and I'll come to –

WILLIAM YOUNG J:

But you couldn't rebuild the house unless you complied with the Building Code.

MR GRAY QC:

No, no, I'm not quibbling with that Your Honour but yes, His Honour Justice O'Regan's response is the right one. Compliance with the Building Code arises from the new for old definition within the policy.

WILLIAM YOUNG J:

But doesn't it just arise as a matter of common sense? You can't rebuild without complying with the Building Code?

MR GRAY QC:

Of course. Of course.

WILLIAM YOUNG J:

So even if it didn't have the other stuff in the policy that you say is a separate condition, a separate payout provision, AMI would have to, when rebuilding, comply with the Building Code.

MR GRAY QC:

Yes, it has to be a house. I mean it has to be a house which complies with the Building Code. You couldn't –

WILLIAM YOUNG J:

And if that means heavy foundations, then that means heavy foundations. Or if that there's a risk there will have to be heavy foundations, that's something that's factored into the rebuild cost. I don't think you would accept that actually.

MR GRAY QC:

Well if you get to that, the answer is a qualified yes Your Honour, to yes in terms of a policy, and perhaps the helpful thing is to go to the policy itself. It's in volume 3, it begins at page 187. 187 is an illustration, 188 is some information, 189 includes a description of the documents that comprise the policy and a definition of rental house and then the operative part of the policy is at 190. "What is covered by the policy," and the operative clause, "Your rental house is covered for any unforeseen and sudden physical loss or damage that is not excluded... There are some circumstances when you are not covered." Please refer to the exclusion in the policy.

"What we will pay. We will pay to repair or rebuild your rental house to an 'as-new' condition, up to the floor area stated in the Policy Schedule. B. We will use building materials and construction methods in common use at the time of repair or rebuilding. C. if your rental house is damaged beyond economic repair you can choose any one of the following options. To rebuild on the same site. We will pay the full replacement cost of rebuilding your rental house. Two, to buy another house. We will pay the cost of buying

another house, including necessary legal and associated fees. This cost must not be greater than rebuilding your rental house on its present site.” So the amount of money is defined by reference to the cost of rebuilding. And 3, a cash payment market value, which is an indemnity value. And then d. applies to repair.

Over the page at 191 a cover for additional costs and we say these additional costs are only payable where the house is actually rebuilt. “1.a. We will pay the reasonable cost of any architects and surveyors’ fees to repair or rebuild your rental house. These expenses must be approved by us before they are incurred.” The interesting thing about this provision, and this entitlement, is they are about costs which are actually incurred and the control over the costs rests with the underwriter not with the insured. Often professional fees are regarded as being within the control of the homeowner and the definition which was offered by Mr Harrison who was the expert quantity surveyor called by the insured and which was accepted by Mr Farrell the quantity surveying expert called by Southern Response was about control over these expenses being with the homeowner and the interesting thing about this provision is that it gives control to the insurer. Second, demolition and removal –

GLAZEBROOK J:

Although presumably it would have to be exercised reasonably, you’d accept that?

MR GRAY QC:

Well it says reasonable cost.

GLAZEBROOK J:

Yes.

MR GRAY QC:

The answer is yes, Your Honour, but what we say that provision entitles a homeowner to do is when they are rebuilding either on the same site or a different site, and they get to a part of the house which they’d like to change a

little bit, so that they don't simply replicate, then often what a homeowner will do is say look I want to vary my building contract and change slightly what it is that's being rebuilt and I'd like to get a drawing with some windows that open or some doors that swing inwards rather than outwards, and so there's a cost associated with designing it and specifying it, and that's the kind of cost which is additional to the costs simply of replicating.

GLAZEBROOK J:

I must say I wouldn't have thought so, because if you're going to change it it's at your cost, isn't it? Because the only responsibility of the insurer is to build what's there as-new –

MR GRAY QC:

Well –

GLAZEBROOK J:

– so I can't possibly see that there's an obligation to pay the reasonable costs of doing something different.

MR GRAY QC:

Well, for a start it's in the context of an actual build, and often it comes up in a circumstance where there's an older building and the builder says, "Well, yes, that's the way it was but we don't do it that way these days."

GLAZEBROOK J:

Yes, but you use, "Building materials and construction methods in common use at the time of repair or rebuilding," so that's covered by clause 1.b. So if you don't do it any more then you, you use whatever's common now.

MR GRAY QC:

Yes. Our submission, Your Honour, is that the page 2 is the replication and the page 3 is a reasonable variation.

GLAZEBROOK J:

Well, it doesn't say so. I mean, demolition is sort of fairly obvious because you can't rebuild until you've got rid of it –

MR GRAY QC:

Yes.

GLAZEBROOK J:

– so it's not a variation, it's just allowing you to get rid of what you've got there so you can rebuild, isn't it?

MR GRAY QC:

If you do rebuild.

GLAZEBROOK J:

And rental house contents, and compliance with building regulations as Justice Young – is not optional.

MR GRAY QC:

In my submission the question has to be asked why is 4 there, if it's not optional.

ELIAS CJ:

4?

MR GRAY QC:

Yes. Why – on page 191, Your Honour, "Cover for additional costs" –

ELIAS CJ:

Yes.

MR GRAY QC:

– why is there a provision for cover for additional costs including compliance with buildings regulations? The starting point in our submission is it is in respect of an actual rebuild.

WILLIAM YOUNG J:

Well, it could be belt and braces.

MR GRAY QC:

Well, these are –

WILLIAM YOUNG J:

I mean, I would have thought it was implicit in an obligation to rebuild that you'll rebuild it in accordance with the law.

ARNOLD J:

Isn't perhaps the key the reference to "additional work" in 4, because if you go back to 1.b. as Justice Glazebrook's pointed out, it's using building materials and construction methods in common use. But what 4 on 191 refers to is additional work, so it seems to contemplate something extra that has to be done involving some presumably significant extra cost.

MR GRAY QC:

Yes, Your Honour, but the tension in the questions that other Judges, including Justice Young, have asked, is if the Building Code requires the work to be done anyway, wouldn't that necessarily fall within the cover that's on page 190 of the policy –

ARNOLD J:

Yes, I understand that but –

MR GRAY QC:

– so that it is unnecessary for, there isn't in fact an additional cost.

ELIAS CJ:

But if you have to have it supervised, as you obviously will have to have it supervised, that is treated in the policy as an additional cost, that's your point, isn't it?

MR GRAY QC:

The point that I'm making –

ELIAS CJ:

I think you may have confused things a little bit, Mr Gray, maybe I'm wrong, in referring to variations. Because isn't your principal point that the policy makes a distinction between what replacement is and what additional costs are?

MR GRAY QC:

Forgive me if I've confused things by referring to variations, I'll explain the context for that later. My submission is that the proper construction of this policy is to treat the page 2 cover as being the replication of what was there before and the page 3 cover as being provision for more than was there before on certain circumstances, and those –

ELIAS CJ:

Well, it may not be more than was there before. It's the additional costs I getting to replace what was there before upgraded by what's required by the Building Code or whatever.

MR GRAY QC:

It's the additional cost of the upgrade, Your Honour, so it's more in a monetary sense –

ELIAS CJ:

Yes.

MR GRAY QC:

– although it's not a bigger house.

ELIAS CJ:

Yes.

WILLIAM YOUNG J:

But do we really have to say that anything that's covered in page 3 is necessarily excluded from page 2? Because you see to say that because something's addressed in page, on page 3, it's therefore not within the contemplation of, the cost of what's contemplated by the cost of rebuilding.

ELIAS CJ:

Isn't it rather that its identified as additional cost?

MR GRAY QC:

My proposition is that page 3 has to be given a meaning.

WILLIAM YOUNG J:

Of course it does.

GLAZEBROOK J:

For avoidance of doubt if you have to have a whole pile of extra money to comply with the Building Code, we'll pay for it.

MR GRAY QC:

My submission is that's not the preferable interpretation.

GLAZEBROOK J:

So we don't want it implicit in a rebuild that you comply with the Building Code, we'll make it explicit. We don't want it implicit that you've got to get rid of the existing building before you can, demolish the existing building before you can replace it. We don't want it implicit but you might need to get architects and surveyors to look at something. In fact if it was built in 1902 you may well have to because you probably won't get a building consent if you don't have somebody draw up some plans for you.

MR GRAY QC:

Your Honour, it can be analysed in that way, but we say that in fact it isn't that. It's that page 2 is a replication of what's there and page 3 – and I say that –

WILLIAM YOUNG J:

That's not quite true because page 2 has the new for old concept that's built into it by reason of replacement cost, doesn't it?

MR GRAY QC:

Yes. Can I respectfully remind Your Honours about insurance. What you get indemnity for is what you have lost.

GLAZEBROOK J:

Not on replacement cost actually but...

MR GRAY QC:

The starting point. The starting point is what insurance does is protect you against what you have lost. These policies enable you to recover not only what you've lost but more as well, and it's a very common way for policies now to be sold and to be drafted. But within those normal insurance parameters it's not unusual for there to be, the part of the policy that says we pay you the indemnity value, and then another part of the policy that says, and we're giving you something else besides. In my submission that's the way these insurance policies tend to provide the cover that in the end is promised. And we say that you can see that in pages 2 and 3 of the policy. So of course if a house is built it must comply with the Building Code and if a house is built it will comply with the Building Code and it will do it under 191, page 3.

WILLIAM YOUNG J:

So are you saying that the cost, the rebuilt that you assume for the purposes of 190, 1.c.ii. wouldn't include compliance with the Building Code?

MR GRAY QC:

Correct Your Honour, it's the cost of replicating what was there because that's what you'd lost.

ARNOLD J:

Well just to understand this, so I mean if you're using building materials and construction methods in common use at the time you're carrying out the repair, they may well be less costly than replacing what's there in an as-new condition, particularly if you're dealing with a very old house.

MR GRAY QC:

That's the new for old debate Your Honour that's the subject of other litigation.

ELIAS CJ:

You better tell us what, we don't want to say incautiously something that's going to impinge on other litigation so what's the new for old debate that's the subject of other litigation?

MR GRAY QC:

Well one illustration, Your Honour, is that people who owned older buildings with heritage characteristics, tongue and groove flooring, exposed timber floors –

ELIAS CJ:

Yes.

MR GRAY QC:

– had been coming along and saying, I want to have replicated, replaced my Kauri tongue and groove flooring, and in some cases Judges have said, Where the flooring was exposed and was a feature of the house, then we agree, that something that looks like that, the modern equivalent of that is what you're entitled to." In other cases the Judges have said, "But the floor was covered with carpet. You were indifferent to what it was that was underneath, it had the potential to be exposed and finished but wasn't, and therefore the modern equivalent is something which is suitable for sitting underneath carpet." But the issue in that case is about characteristics of buildings, which are regarded as adding particular benefit to it, from the perspective of the home owner, and there are cases involving that which are coming through the Courts.

But just for the sake of completeness, the way in which this is achieved in this policy is at 199 and there's a definition of "full replacement", and that's the provision referred to by Justice O'Regan earlier, "Full replacement means replacement with a new item or repairing to an as-new condition."

WILLIAM YOUNG J:

But if I could query, what's the total, what's been paid out to date on all of this? I mean, the figures I could see in the case on appeal were remarkably different, there was about 685 by Arrow and about 1.6 by –

MR GRAY QC:

Part of that arises, Your Honour, because this house was actually about 500 square metres but the policy schedule described it as being 336 square metres only.

WILLIAM YOUNG J:

Right.

MR GRAY QC:

And so the amount of cover abates to reflect the floor area –

WILLIAM YOUNG J:

Oh, I see.

MR GRAY QC:

– included in the schedule to the policy and on which the premium was fixed –

WILLIAM YOUNG J:

Okay.

MR GRAY QC:

– and that's in the proposal, Your Honour, which forms part of the documents.

WILLIAM YOUNG J:

Yes, so effectively – but there were two – that actually would explain, doesn't explain what seemed to me to be quite a big difference.

MR GRAY QC:

I'll ask Mr Johnstone to dig out the precise figure.

WILLIAM YOUNG J:

Right.

MR GRAY QC:

We're talking about six or \$700,000 –

WILLIAM YOUNG J:

Yes.

MR GRAY QC:

– 600 to \$800,000, Your Honour.

WILLIAM YOUNG J:

Right, okay.

MR GRAY QC:

We're talking about a 10% allowance for contingencies, and we're talking about the difference between a further 10% for professional fees and an allowance made by Mr Farrell, who was the expert for the appellant, of about \$29,000. So the dollars we're talking about are 120, \$150,000 in this case. We're talking about a difference of plus 10% and plus 10% for all claims of this type. So the proposition that I'm advancing is that the cover on page 2 of the policy is –

ELIAS CJ:

Sorry, "in issue" in this case are both 10%? I –

MR GRAY QC:

Yes.

ELIAS CJ:

Both 10%, oh.

MR GRAY QC:

Well, the whole of one of the 10 percents –

ELIAS CJ:

Yes.

MR GRAY QC:

– the contingency –

ELIAS CJ:

Yes.

MR GRAY QC:

– and part only of the 10% for professional fees –

ELIAS CJ:

Yes, because of the...

MR GRAY QC:

– because there's an acceptance that the drawings for the house, which were made in 1978, will need to be updated by being redrawn. But that would be a cost that would be incurred in rebuilding this house.

WILLIAM YOUNG J:

Wouldn't that also be a cost that would fall under 191, 1.a. and on your theory of the case not covered?

MR GRAY QC:

No, Your Honour. Because 191 applies where a house is actually being rebuilt.

WILLIAM YOUNG J:

Yes.

MR GRAY QC:

And in this case a house is not actually being rebuilt and that –

WILLIAM YOUNG J:

So what's the allowance you accept for –

MR GRAY QC:

It's about \$29,000, Your Honour, Mr Farrell.

WILLIAM YOUNG J:

Yes, but that would be an architect fee associated with the repair or rebuild of the house, wouldn't it?

MR GRAY QC:

Yes, it would.

WILLIAM YOUNG J:

So therefore on your interpretation it shouldn't be in there at all, should it?

MR GRAY QC:

No, we accept, Your Honour, that it is a page 190 or page 2 cost that would be incurred in the building of a house.

WILLIAM YOUNG J:

Even though it's also covered by 191,1.a.?

MR GRAY QC:

Even though, in a different circumstance where a house was actually being rebuilt, it could also be covered under 191, although we say 191 has the potential to cover other things as well.

WILLIAM YOUNG J:

Well – all right. So then it's just a matter of working out what's an appropriate figure to allow for expenses?

MR GRAY QC:

Yes.

WILLIAM YOUNG J:

And you say, "Well, but this just comes back to we're going to plot what's there back on the land notionally and we don't care whether it would comply with the building consent – whether it would comply with the Building Code"?

MR GRAY QC:

We say we're indemnifying on a new for old basis, a replication of what was there. What we're not doing is paying for something that now is required which wasn't there before at all, and we say that our expert, Mr Farrell, said in evidence that in his experience the redrawing of existing plans would cost \$29,000. Mr Harrison, the expert quantity surveyor called by the policyholder said, "I always allow 10% in a build." Justice MacKenzie, you've heard the witnesses, preferred the evidence of Mr Farrell –

WILLIAM YOUNG J:

Well it's not really preferring the evidence, isn't it, it's simply do you assume, as the Court of Appeal said, safe ground. If you assume –

GLAZEBROOK J:

Well professionals fees I think are slightly different because isn't what's said against you that Mr Farrell actually accepted that you would have engineering

fees in matters of that kind, but then made no allowance for them. So isn't, that's purely factual, isn't it?

MR GRAY QC:

Yes, I don't know whether Your Honours want to drag through this today but yes –

GLAZEBROOK J:

Well I think in some ways maybe because if that's what's said against you, that Mr Farrell says I agree that there would have been fees in these categories, but then makes no allowance for them, then it's difficult to say well the only thing you get is redrawing the plans and you don't get what Mr Farrell accepted were going to be professional expenses that were going to be associated with a rebuild.

MR GRAY QC:

That is said against us Your Honour. We say it's a slight misunderstanding of what Mr Farrell said. We say Mr Farrell said, when you're building a house normally you allow 10% for professional fees. But this is not rebuilding. This is not actually building a house, this is replicating what's there, and the part of the 10% which would actually be incurred in this case is having an architectural draftsman redraw the existing plans and I estimate that cost to be \$29,000.

GLAZEBROOK J:

So he's saying you wouldn't get engineering or any of those things that he admits you would get normally?

MR GRAY QC:

Yes.

GLAZEBROOK J:

Okay well –

MR GRAY QC:

In the usual run of cases but not where you're not actually building.

GLAZEBROOK J:

Well but it's a notional rebuild and you get the cost of a notional rebuild, don't you, that's what it says? The cost must be not greater than rebuilding your rental house on its present site. Where do you get anything – it's a notional rebuild, where do you get a notional rebuild but taking out some of the costs for not rebuild, that you would incur for rebuilding but not others?

MR GRAY QC:

The proposition that Mr Farrell advanced, in answer to that, is this Your Honour. When you are building for the first time, you have not built before, you do not know what will happen when you dig into the ground, you don't know what's there. In this case you're not building for the first time. You're not building something new. You're building something that is precisely the same as what was there before. You know exactly what you will find under the ground because it's already there. The holes for the foundation –

ELIAS CJ:

Under which ground are you talking about, your replacement house or your –

MR GRAY QC:

The notional –

ELIAS CJ:

– the replaced house?

MR GRAY QC:

The notional rebuild.

ELIAS CJ:

The notional rebuild.

MR GRAY QC:

Of the existing house on the existing ground.

ELIAS CJ:

But I'm not sure that that's right, is it? Because no one's gone back and reassessed it.

GLAZEBROOK J:

Even assuming no earthquake in many cases you would still, especially to comply with the Building Code and council regulations, they would still say we want to see whether anything shifted or anything different. Something built in 1902 we can't assume that they actually even had safe foundations necessarily.

MR GRAY QC:

Except that, Your Honour, this not a house built in 1902.

GLAZEBROOK J:

No, no I understand that, but even 1978 I would have thought you would still have to check what was under the ground, wouldn't you?

MR GRAY QC:

On a case by case basis the existing plans might or might not be adequate.

GLAZEBROOK J:

Okay well – thank you.

MR GRAY QC:

It would depend on the age of the building, the quality of the plans.

WILLIAM YOUNG J:

Adequate for what? Do you mean adequate for –

ELIAS CJ:

The Building Code.

WILLIAM YOUNG J:

To comply with, you don't mean adequate to comply with the Building Code because you dumped that all onto page 3 of the policy.

MR GRAY QC:

So far as the foundations are concerned.

WILLIAM YOUNG J:

So what do you mean by the foundations are adequate? Adequate, what, to keep the house from falling down or –

MR GRAY QC:

What I am saying Your Honour is that in this case, I don't think there had been a change in the Building Code between 1978 and pre-earthquake.

WILLIAM YOUNG J:

No but I'm not interested in it pre-earthquake, I'm interested in now. What would it cost now to rebuild the house on the site and you say, well we've got plans for a house and we're just going to put that there, but we accept sometimes there has to be an inquiry into the adequacy of the existing plans or the adequacy of the –

MR GRAY QC:

Yes.

WILLIAM YOUNG J:

– existing as-built structure of the house. Now what I'm trying to explore with you is what do you mean by "adequacy", adequacy measured against what? Functionality, compliance with building codes or something else?

MR GRAY QC:

Yes, can you in fact build it in a manner which will enable that structure, not an enhanced structure, not a changed structure to comply with changes, but that structure to comply with what is required.

WILLIAM YOUNG J:

But that may require quite a lot of work on the foundations, mightn't it?

MR GRAY QC:

Well, Mr – we say that what Mr Farrell in fact said is in the usual run of cases you just allow 10%. But in this case 10% wouldn't be spent because we have plans, we can update the plan by spending some money with an architectural draftsman –

WILLIAM YOUNG J:

But we don't know whether the plans in relation to the foundations will work though, do we?

MR GRAY QC:

Well, he says, his proposition was, yes, you do. You know what the foundations are, you know where they are, they're already dug out. So that the allowance, the reason you have an allowance, is to design for things that you don't expect and encounter unexpectedly. But we won't have things we don't expect and we won't have things that we encounter unexpectedly because we're replicating what's already there.

WILLIAM YOUNG J:

Well, one way of doing it would be, I suppose, to do geotechnical investigations on the site. It would be rather sort of a hollow and wasteful exercise because you would be doing investigations for a building that's never going to be built, but presumably they could have been built, it could have been done.

MR GRAY QC:

Yes, look, in fairness to Mr Harrison, his response to that is you might always encounter soft spots. Even if what you're doing is replicating what is there, when you pick it up you might encounter something that you didn't think would be there when you started, and you didn't know about before you started, and there might be a requirement for there to be geotechnical investigations and expenses incurred as a result of that. But that's Mr Harrison's proposition, and he says in the normal run of cases you make an allowance because those sorts of things might happen and need to be accounted for. Mr Farrell's proposition is, "I accept that in the normal run of cases you allow 10% for professional fees for those kinds of things, but I say in this case there aren't unexpected things because we're building, we're compensating, we're paying an amount of money which is the equivalent to rebuilding what is there." And that's the contest between the experts and it's the contest between the propositions before Your Honours in respect of the professional fees.

GLAZEBROOK J:

So, just let me get this straight. I didn't actually understand that the professional fees were so much a contingency as fees that, certainly with the architectural fees and possibly some of the engineering fees, that were going to have to be incurred in any event to get a building permit, leaving aside whether there's been earthquake damage. I remember having to get an engineering report, for example, to put a fence up at our house –

MR GRAY QC:

We all have our stories, yes.

GLAZEBROOK J:

– in order to get a consent to put a fence up. Now I mean it wouldn't have been something that I would have thought of straight off the bat, and it wasn't that we were getting any soft spots or anything, we'd done nothing, we just had to do it before we could even get through the door.

MR GRAY QC:

Living on the slopes of Maungakiekie, Your Honour, we had to get an investigation before digging a garden. So I just –

GLAZEBROOK J:

But, no, but you understand what I mean –

MR GRAY QC:

Yes, I do, yes.

GLAZEBROOK J:

– that's what I, so I wasn't sure – I mean, the difficulty here is I'm not sure to the extent to which these were contingency fees that arise just in respect of soft spots, but I must say I haven't read the evidence in detail to really understand that but...

MR GRAY QC:

And it will take more than one reading, Your Honour, because the evidence was given initially separately –

GLAZEBROOK J:

I understand it was quite difficult, yes.

MR GRAY QC:

– and then in a hot tub.

GLAZEBROOK J:

Yes.

MR GRAY QC:

Your Honour, my reading of the difference between the witnesses is the one that I've already submitted, and that is the Mr Harrison says, "We estimate the amount of fees that are ordinarily incurred at 10%," Mr Farrell says, "Yes, I agree, that's what we estimate fees ordinarily incurred to be, but I say in the

particular circumstances of this claim under the policy that estimate is not appropriate because some of fees would not be incurred,” and that's –

GLAZEBROOK J:

And is that because you could do it without a building permit?

MR GRAY QC:

That's because you're replicating what's there, yes.

GLAZEBROOK J:

No, no, I understand that, but if you couldn't even put your spade in the ground in order to build something unless you had a geotechnical report, then it will be incurred in the rebuild, won't it?

MR GRAY QC:

Yes.

GLAZEBROOK J:

And is he saying that none of those would have been incurred in this rebuild because you'd get a building – of course it's ridiculous in the sense that it's not going to be rebuilt and the land is not able to be rebuilt on, I mean it might physically be able to be but not because it's red zone.

MR GRAY QC:

We need to do two things Your Honour. We need to look at what Mr Farrell did to calculate his \$29,000. That's found in volume –

ELIAS CJ:

Sorry, why do we need to look at this? I would have thought, just going from the arguments that, the written arguments, that this is only a matter of interpretation of a policy?

MR GRAY QC:

Yes it is.

ELIAS CJ:

And there's not dispute but that the implications are a 10% estimate built in, or some best stab at what fees were inevitable on the basis that you put forward.

MR GRAY QC:

Yes. Look, I accept that in this Court Your Honour that's exactly what is happening but –

GLAZEBROOK J:

Well my problem with that is that you have a contingency because you could well incur them. Some of them will be, would be incurred in a rebuild and if you, for instance, asked a builder to give you a fixed price, the builder would build in contingencies in that because inevitably at least some of those contingencies will come home to roost, and for myself I can't see, at all, that cover for rebuilding the rental house on its present site can't include at least some of those expenses that are likely to be incurred. Whether it includes the whole of the 10% or not but I can't on a construction of the policy say you either end up with no contingency or all of the contingency. That's not a choice that I think arises on construction, it has to arise on the actual facts.

MR GRAY QC:

We're yet to separate, Your Honour, contingencies and professional fees.

GLAZEBROOK J:

Well, no, you've just said that the professional fees are contingency fees.

MR GRAY QC:

Which is what - Your Honour, what I say is that Mr Harrison's assessment of professional fees is approached on a contingent basis. This is what we do experience in the normal run of events and this is what I think might occur. We say that what Mr Farrell has done in relation to professional fees is say that because of the particular nature of the claim under this policy they wouldn't all be incurred and therefore a lower number is appropriate.

These are the ones that I say would be incurred and therefore form part of the cost of rebuilding this house on this site.

O'REGAN J:

And Mr Harrison didn't engage with that, he didn't say well I think, even if you took that approach you would get twice as much or...

MR GRAY QC:

No Your Honour.

O'REGAN J:

His is 10% or nothing basically?

MR GRAY QC:

Yes, yes, 10% because it's what we always do, in the ordinary run of things when we're building a house.

ARNOLD J:

The point that Justice Glazebrook has raised has troubled me as well, that on the contingency fee we seem to be facing two extremes. Either you apply the standard 10% or nothing, and yet it does seem to me that even accepting the approach that this was a known situation, so that some of the uncertainties that would underlie a normal contingency fee arrangement had been removed, there still will be some uncertainties and some scope for contingency, and yet that's not, we don't seem to have any sort of proposition to that effect, it's either one extreme or the other.

MR GRAY QC:

Yes. moving to contingencies, Your Honour, away from professional fees and to contingencies. Again the proposition is that normally a 10% allowance is made for contingencies and that is standard, and that was accepted between the parties. Mr Farrell's position is we're simply replicating so there are none. Mr Harrison said, no, we always allow contingencies therefore we should have some, and Your Honour is right, there's nothing really in the evidence to help

you decide whether some intermediate amount, more than nothing but less than 10%, could be appropriate in a different case.

ARNOLD J:

Well, as I understand it, your expert's position is really that all the contingencies, or the bulk of it anyway, was in the ground –

MR GRAY QC:

Yes.

ARNOLD J:

– and for that reason he doesn't give weight to it.

MR GRAY QC:

Well, Mr Harrison said that –

ARNOLD J:

But in fact contingencies cover more than simply what's in the ground, don't they?

MR GRAY QC:

Yes, they do. Mr Harrison was cross-examined in volume 3 at page 173 about this, he, at line 19, was asked what a contingency was –

GLAZEBROOK J:

Sorry, what – volume 2?

MR GRAY QC:

Volume 2, Your Honour, at 173. From line 22 he quotes New Zealand Standard 4212 with the definition of "contingency". I can tell you that later Mr Farrell accepted that definition. But at the bottom line of the page he says, "The unknowns are mostly in the ground."

GLAZEBROOK J:

Sorry, what page are we?

MR GRAY QC:

173, Your Honour.

GLAZEBROOK J:

I see, sorry.

WILLIAM YOUNG J:

Is it essentially the position that your client's case is that, "We look at replicating what was there, we're not interested in building consent requirements and therefore we're not interested in what's under the ground and what would actually be required to get a building consent?" Mr Harrison's position is, "Well, we don't know actually what's there but it's likely to be expensive and that's why I built in a contingency."

MR GRAY QC:

I don't know about "expensive", Your Honour. It's like that we'll encounter something that we haven't foreseen and there will be additional cost, and –

WILLIAM YOUNG J:

Well, I mean, it's in the red zone, it's almost certainly going to, I mean, they're going to encounter something unpleasant.

MR GRAY QC:

I don't know that Mr Harrison, Your Honour, is saying, "Because it's in the red zone we've got to design for the red zone –

WILLIAM YOUNG J:

And it's presumably near the river, isn't it?

MR GRAY QC:

Yes, the river is the issue...

GLAZEBROOK J:

But even leaving aside a red zone, let's assume – because if we're just looking at a normal policy and we've got a house that is not able to be

replaced and somebody decides they're going to build a new one, accept that option, and decides they're not going to rebuild, you'd still have to get a building site consent, you would conceivably still have to get engineering reports, even assuming nothing wrong with the land at all that you know of.

MR GRAY QC:

If there were no earthquake, Your Honour, if the house had been destroyed and the policyholder was electing not to be rebuilt but to buy a new house on another site and we were quantifying it, the entitlement under the policy to doing that, Mr Harrison says when you're building, rebuilding this house on this site with no known problems, nevertheless there would be things that you don't expect, mostly in the ground, and I –

GLAZEBROOK J:

Well, does he accept that? Yes.

WILLIAM YOUNG J:

Why does it matter – isn't the real issue what it would cost to rebuild now, isn't that, I mean, that you have to look at it in terms of ground conditions as they now are and, at least on my hypothesis, regulatory constraints as they now are?

MR GRAY QC:

In my submission, no. In my submission the fact that this is in the red zone is irrelevant –

ELIAS CJ:

Well, there is no legal status of the red zone.

WILLIAM YOUNG J:

Yes, well, yes, I accept it's not, it's not legally relevant. It's just in – when you say there might be something unforeseen, it's just that it doesn't, I think it's very plausible to assume that there will be something unpleasant.

MR GRAY QC:

Your Honour's touched on the point which is the real area of concern, and it's that policyholders are saying, "Am I entitled to be paid the sum of money it would cost to rebuild my house on red-zoned property, with all of the –

WILLIAM YOUNG J:

No, on that site, on that site.

MR GRAY QC:

The site's in the red zone.

WILLIAM YOUNG J:

Yes.

ELIAS CJ:

I am surprised that although we're being taken in a sort of atomistic fashion to bits of this, there's been no attempt to look at the policy overall, and isn't it significant to your argument that the occasion for this option is that the house is damaged beyond economic repair? So that if you add back in the costs of reinstating on that site aren't you undoing that purpose in the policy?

MR GRAY QC:

I'm sorry, I haven't understood Your Honour's question.

ELIAS CJ:

No, it's just, I suppose it's just an invitation to you to range a bit more through the policy.

GLAZEBROOK J:

Assuming there's nothing wrong with the land, no you're not, because all you're doing – that's why I think it's useful to assume there's nothing wrong with the land. If the standard way of costing when you're rebuilding something is always to add 10%, because he doesn't say I'm adding 10% because this is in the red-zone, because this is difficult. He's saying industry standard, which

Mr Farrell agrees with, is to add 10% for contingencies. Well if anyone's ever built anything you usually say, let's double it, because that's what it always seems to come out at, but the industry standard is to add 10%, it's agreed it's an industry standard, that's whether or not there's a rebuild on the red-zone or in, or anywhere, and so why in this circumstance – so your argument would have to be that the industry standard doesn't apply under this policy, whether there's anything wrong with the land or not.

MR GRAY QC:

Again Your Honour I do need to distinguish between contingencies and professional fees, and I'll give different answers in respect of each of them. In relation to professional fees, what we say Mr Harrison is saying is when you actually build, our experience is you encounter things that you have not foreseen. When you build a house. Mr Farrell is saying, yes, that's right, but we're dealing with something different. We're dealing with assessing the money you get paid under this policy by reference to, and that's assessed by reference to what it will cost to build what is there. So many of the unexpected things, or many of the professional costs that you would incur if you were actually building a new house, won't be incurred, and therefore do not arise under this part of the policy. And that's –

GLAZEBROOK J:

And just correct me if I'm wrong that is whatever the state of the land is, this would apply just generally if my house, I don't know, somebody, or a fire. If my house goes by fire, I would only be entitled under this policy to, what?

MR GRAY QC:

Well, whatever would be the costs on the facts of the particular case – well, Your Honour, he set it out, it's in volume 3 at page 324D, and it is –

ARNOLD J:

Sorry, could you give me the reference?

MR GRAY QC:

Volume 3, at 324D.

GLAZEBROOK J:

So even if the council comes along and says, I'm sorry, I'm not letting you put a stump in the ground until you get me a geotechnical report because we have a bank up behind our place as to that status of the bank?

MR GRAY QC:

Well in fact it wouldn't because you don't, you're not applying for a consent.

GLAZEBROOK J:

Well no I'm not but if I were rebuilding and that would be part of the cost of rebuilding to get the consent and to do anything necessary to get the building consent, wouldn't it, or permit or whatever we call them now.

MR GRAY QC:

Conceptually the tension is, yes, there's an acceptance that you would make an application for a building consent and the cost of doing that are included but because you're not, in fact, doing it, there won't be unexpected things that arise following it, and there won't be further cost.

GLAZEBROOK J:

I can understand that argument but the argument seemed to me to go further than that on professional fees, that was all. But if, to get a building consent I have to, I can understand the contingent ones that I know I'm not going to meet a soft spot or whatever it is...

MR GRAY QC:

Well –

GLAZEBROOK J:

Do you accept that if, as part of getting a building consent I have to have a geotechnical report, or an engineering report, or an Uncle Tom Cobley report, that that would be included?

O'REGAN J:

Yes, because Farrell has allowed for a geotechnical report, he's allowed for geotechnical investigations in his 29,000?

MR GRAY QC:

Yes, he would say that –

WILLIAM YOUNG J:

He's assumed good ground, hasn't he, I mean isn't this the sort of critical expression? Why does he assume good ground, why doesn't he, I mean, one option, as I said, would be to do a geotechnical investigation on the site to see what it would cost. Why should we make an assumption that that may not be true?

ELIAS CJ:

Didn't they do that exercise?

WILLIAM YOUNG J:

No.

ELIAS CJ:

What was the estimate that was undertaken?

MR GRAY QC:

The estimate is for a confirmation that what is there is fine. And the reason for the assumption, Your Honour, is it's there, you know it works, you know it has been working, it's dug out. So –

WILLIAM YOUNG J:

Say the reason the house was so badly damaged is that the foundations weren't very good.

MR GRAY QC:

Oh, well, that's speculating, Your Honour, maybe –

WILLIAM YOUNG J:

I know, but why is that speculating and it's not speculating for you to say, we know it really worked that well, it's just, it's a complete rebuild? I mean, it's, we don't know, do we? I mean, there are lots of photographs of the house that I can't get my head around really but...

MR GRAY QC:

Yes.

WILLIAM YOUNG J:

I mean, presumably foundation design is intended to prevent houses being destroyed in earthquakes, or to mitigate the risk of it, I should say.

MR GRAY QC:

Gosh, we'll range far and wide if we do that. The foundation design at the time accepted that a raft was appropriate –

WILLIAM YOUNG J:

Yes.

MR GRAY QC:

– because of an understanding of the risk in the city at the time.

O'REGAN J:

We're left in a pretty difficult situation where we've got Mr Farrell saying, "This is my estimate of the cost of this particular house on this particular site," and Mr Kennedy just not engaging with that. I mean, was there any – I mean, he's

just saying, “Ten percent is what we always do,” but that seems to mean that the evidence is really two ships passing in the night, isn’t it, there isn’t...

MR GRAY QC:

It is a little bit, Your Honour.

WILLIAM YOUNG J:

But isn’t it, doesn’t it really come back to this assumption of good ground?

MR GRAY QC:

It does, because Mr Harrison says, “The reason I always allow 10% is because there are issues in the ground, almost all of the issues that are within my 10% are in the ground.”

WILLIAM YOUNG J:

Yes. And Mr Farrell says, “Well, we’re just going to assume that there are not issues, and therefore I won’t allow a contingency.”

GLAZEBROOK J:

And yet Mr Harrison would allow a 10% contingency if this was in – I’m trying to think of – Auckland, well away from any volcanoes and with a low earthquake risk, he would still have 10% there, and Mr Farrell would agree that that was a, that was what is done in the industry and is reasonable.

MR GRAY QC:

Yes, I –

GLAZEBROOK J:

So somehow in the earthquake zone it’s not reasonable, which one would have thought you might have had a contingency of 50% in those circumstances, if you were asking somebody to take a fixed price contract.

MR GRAY QC:

If you were compensating for it. There is something of a trend in recent cases, Your Honours, including a decision given by the Court of Appeal last

week in a case my learned friend, Mr Campbell, was counsel and called *East, Medical Assurance Society of New Zealand Limited v East* 2015 NZCA 250, judgment given on 17 June, in which Justice Harrison for the Court said, “Look, we should not be in advance of costs being incurred making declarations the contingencies or allowances will fall within policies, because the risks inherent in that are too great.” In that case he was setting his comments particularly in the context of a litigation-funded action seeking declarations which might apply to other policyholders who similarly were funded by the same funder, and it’s possible to see some caution in His Honour’s approach to the claims being made in that case by reason of the funding.

GLAZEBROOK J:

I mean, I can understand that. But isn’t the reason you do the 10% because otherwise you’d have to build in extra costing into each of the thing? It’s just a convenient way of saying, “Well, we’re bean counters, we bean-count what it’s going to costs but there may be price increases, there may be differences that we have to do.” If you had to do it on an individual basis for every rebuild you do, you could actually land up on an industry basis with very, very expensive valuations, et cetera that you land up with and very expensive arguments. So isn’t that the justification for just doing that 10% because that is just a sort of a figure they take in when they’re doing a quantity survey –

MR GRAY QC:

In different cases.

GLAZEBROOK J:

– which is what Mr Farrell would agree?

MR GRAY QC:

Mr Farrell would agree they normally do it, but he would also and did say, “In this case I’ve actually estimated it and my estimate is for \$29,000 and I say –

WILLIAM YOUNG J:

Yes, but it hasn't really, because he's said, "But I'm making an assumption, I haven't estimated what it will cost, I'm estimating what it might cost if everything's just great."

MR GRAY QC:

His evidence in that, Your Honour, is at volume 2, 174, lines 25 and –

ELIAS CJ:

But it's if the, it's on the assumption of good ground –

MR GRAY QC:

Yes.

ELIAS CJ:

– it might not be that everything's great, but at least that is assumed.

MR GRAY QC:

What he said is we, that the bill has been priced as per good ground, we are familiar, we have designs –

GLAZEBROOK J:

And I just – sorry, so can you just give me that reference again, sorry, while if remember?

MR GRAY QC:

174 Your Honour.

GLAZEBROOK J:

Thank you.

MR GRAY QC:

Line 25 and following. "We have designs for the current foundation, therefore as far as we can see being a notional build there is no risk in the ground."

That's his proposition and that's the proposition that the appellant is advancing, that in this case you don't need to take a formulistic pre-estimate –

WILLIAM YOUNG J:

But he would say even if there'd been a geotechnical survey that said that this requires huge foundations, you'd say that's irrelevant wouldn't you?

MR GRAY QC:

I would say that an entitlement to receive those would be under page 3, not page 2.

WILLIAM YOUNG J:

No, no –

MR GRAY QC:

So, yes.

WILLIAM YOUNG J:

So say that the plaintiff here had got a geotechnical engineer to do a survey of the site and the surveyor had said, "Well, the ground conditions are terrible and this will be a very expensive house to rebuild here and hundreds of thousands of dollars on foundations," Mr Farrell would say and you would say that's irrelevant –

MR GRAY QC:

Well, I would say it's the wrong measure.

WILLIAM YOUNG J:

Yes, because you'd say, yes, you'd say, it's irrelevant because we are assuming good ground?

MR GRAY QC:

Yes.

WILLIAM YOUNG J:

Even though –

O'REGAN J:

No, but this is about the fees involved we're talking about here.

MR GRAY QC:

Yes.

O'REGAN J:

I mean, he's just saying you don't need to incur fees to get advice about the ground when you already know what's it's like, and whereas Mr Kennedy is saying –

WILLIAM YOUNG J:

Harrison, Harrison.

GLAZEBROOK J:

Harrison.

O'REGAN J:

– essentially, "I'm assuming," Harrison, rather, is saying, "Well, I'm assuming we don't know what it's like."

MR GRAY QC:

Your Honour –

O'REGAN J:

I mean, so they're both making assumptions and we don't know which one's the correct assumption

WILLIAM YOUNG J:

Well, but in fact we don't know what the ground's like, do we?

ELIAS CJ:

Isn't your point that it's irrelevant –

MR GRAY QC:

Yes, it is, Your Honour.

ELIAS CJ:

– what the ground is like, because it's a proxy that you're looking for and there's going to be a replacement on other ground?

MR GRAY QC:

Well, no, they're either buying an existing house –

ELIAS CJ:

Yes, yes, sorry –

MR GRAY QC:

– they're not actually building...

ELIAS CJ:

– they're not building, yes.

MR GRAY QC:

Your Honour's right. We say that the policy provides at clause 1.c.i, ii and iii, three options, and those options define the entitlement under the policy, so that you can rebuild on the same site and if you do there are financial consequences. You can buy another house, and if you do you get a sum of money which is the equivalent of the cost of building on a new for old basis, the house you lost. Not a new one newly complying with new conditions, the house you lost. Or you can get the indemnity value, you can get the cash payment. And those are the financial options available to the policyholder.

ELIAS CJ:

The market value, you mean –

MR GRAY QC:

Yes.

ELIAS CJ:

– is the third option there.

MR GRAY QC:

And they're triggered by an election made under the policy. And that's the point Justice Dobson made in *Turvey*, the starting point is the choice made by the policyholder, and then it's an analysis of what the entitlement is –

WILLIAM YOUNG J:

Can I look at, can you look at section, at page 190 for a moment?

MR GRAY QC:

Yes, Your Honour.

WILLIAM YOUNG J:

The first option in c. is to rebuild on the same site, “We will pay the full replacement cost of rebuilding your rental house.”

MR GRAY QC:

Yep.

WILLIAM YOUNG J:

Might it not be thought that the rebuild cost in c.ii. will correspond to that cost?

MR GRAY QC:

Yes.

WILLIAM YOUNG J:

And when it says, “Rebuild on the same site,” isn't it really fundamental that that assessment that what you pay must be referable to the conditions as they are on that site?

MR GRAY QC:

If it were possible to rebuild, yes.

WILLIAM YOUNG J:

Well, it's not impossible to rebuild here, it's just, it wouldn't be very sensible.

MR GRAY QC:

Sold the land. Your Honour, we'd then have a different kind of argument. If that election had been made the first point I make is the cost of the enhanced foundations as on page 191, not on page 190.

WILLIAM YOUNG J:

Well, maybe, maybe.

MR GRAY QC:

This –

WILLIAM YOUNG J:

I mean, that's on the basis you don't accept 191 as a belt and braces, just making it clear –

MR GRAY QC:

No, it's –

WILLIAM YOUNG J:

– what's covered by "rebuild".

MR GRAY QC:

It's additional cover, Your Honour, it's not a different description of the same cover, it's a different cover.

ARNOLD J:

I must say, I was a bit puzzled at the answer you earlier gave Justice Young about professional fees, as I had thought the logic of your position was that professional fees, the additional cost of complying with addition work,

upgraded foundations, et cetera, would all fall within the 191, but you accept that professional fees do fall within the notional rebuild.

MR GRAY QC:

Some, yes.

ARNOLD J:

Well, so, but again I –

ELIAS CJ:

The ones that are intrinsic.

ARNOLD J:

– don't understand why you, when then in relation to extra compliant costs some of those don't fall within. In other words, I just don't understand the logic, so maybe you can explain it to me again, of the way you treat professional fees as compared to the way you treat item 4, compliance with additional costs.

MR GRAY QC:

Your Honour, it starts with the proposition that I've advanced about the nature of insurance, that what 190 does is basically give, first, indemnity value, old for old –

ARNOLD J:

Yes, yes.

MR GRAY QC:

– and enhance that to new for old.

ARNOLD J:

Yes.

MR GRAY QC:

What 191 does is offer more as well, which is not only a new expression of your old house but a changed expression of your old house which complies with new building requirements.

ARNOLD J:

Right.

MR GRAY QC:

And as a consequence of it being a changed expression of your old house, there might be costs incurred in complying with the Building Code and there might be additional professional fees which would not arise under 190.

WILLIAM YOUNG J:

Can you just take – what page is Mr Farrell’s analysis of the engineering fees he’d allow?

MR GRAY QC:

324D, Your Honour.

WILLIAM YOUNG J:

324D.

MR GRAY QC:

In volume 3.

WILLIAM YOUNG J:

You see, all of those – sorry.

ARNOLD J:

Right, so 1 and 4 then are just dealing with additional costs associated with, let’s say upgrading, and that applies to –

MR GRAY QC:

Yes. More than was there before.

ARNOLD J:

– professional fees as well?

MR GRAY QC:

Yes.

ELIAS CJ:

Yes, you've said that they're separate but they really are linked, aren't they, because it's the geotechnical professional fees that really bump the thing up, so I don't see that the contingency argument is really very different from the professional fee contingency allowance.

MR GRAY QC:

It may not be, but I do want to address it separately because in relation to professional fees the evidence is that Mr Farrell says, "This is what they would actually be." In respect of contingencies, Mr Farrell hasn't done that, and really haven't touched separately on contingencies yet, but the debate will be more generic and will be repetitive, but just with the generic part.

WILLIAM YOUNG J:

Can I just ask you, if you look at 342D, and keep your thumb in the bundle at 191 as well, how do all the fees that he allows at 324D literally within –

ELIAS CJ:

324.

WILLIAM YOUNG J:

324D.

ELIAS CJ:

Yes.

WILLIAM YOUNG J:

Aren't they also literally within 1.a. on 191?

ELIAS CJ:

Sorry, 324...

MR GRAY QC:

D.

WILLIAM YOUNG J:

324D.

ELIAS CJ:

Oh, I see, sorry, that's all right, yes.

WILLIAM YOUNG J:

Because they are the costs, effectively professional fees, to repair or rebuild the rental house. I mean, this is the proposition I was putting to you before, that on your argument it seems to me that Mr Farrell was quite wrong to and too generous to allow any fees at all, because they're all 1.a. expenses and not – or 191 cover not 190 cover.

MR GRAY QC:

Your Honour, it is possible to read the words on page 191 paragraph 1.a and find within those words a description of the costs which Mr Farrell says in his expert testimony would be incurred in the replication of this house, the rebuilding of this house on the site. That does not mean, in my submission, that the policyholder is entitled to recover Mr Farrell's costs pursuant to clause 1.a. on page 191. We say construing 190 and 191 together the costs that would actually be incurred, inevitably be incurred, in a rebuilding of the house on the site, are recoverable and are the ones that Mr Farrell said would be incurred.

WILLIAM YOUNG J:

But why is it only the costs that will inevitably be incurred, why isn't it the best estimate of the costs likely to be incurred that's the test? Because the costs

that will inevitably be incurred are likely to be far lower than the costs that would be incurred.

MR GRAY QC:

Well, the proposition, Your Honour, is it's on the balance of probabilities, the costs that will be incurred.

WILLIAM YOUNG J:

Yes.

MR GRAY QC:

I mean, we're talking about onus and standard of proof, aren't we?

WILLIAM YOUNG J:

Yes, but you're looking at a range and you would normally pick a point of equipoise where it is as likely to be higher as it is lower, wouldn't you?

MR GRAY QC:

Well, I wouldn't necessary accept, Your Honour, that identification of a range or an envelope's the technique you would use. In my submission, you would say, "On the balance of probabilities what will happen and what will the cost of it be?"

WILLIAM YOUNG J:

Okay. But that's not, but that will still be a higher figure than the barest minimum that would inevitably have to be incurred if everything goes really well, which is what you seem to be talking about.

MR GRAY QC:

In my submission, the language in Your Honour's question pejorative –

WILLIAM YOUNG J:

Yes.

MR GRAY QC:

– at its barest minimum. What Mr Farrell has done, as I say –

WILLIAM YOUNG J:

Sorry, it's a response to, would inevitably be incurred, that's the –

MR GRAY QC:

Then I'm...

WILLIAM YOUNG J:

– that's the, it's my response to that.

MR GRAY QC:

Well, I'm advocate, Your Honour, I don't...

ELIAS CJ:

But is it incurred on any site? It's an attempt to make it neutral, is that the...

MR GRAY QC:

In my submission, Your Honour, Mr Farrell is saying, "I'm being particular. I'm saying these costs would be incurred on this site in relation to this building with these house plans being in the state that they are and the building being at the age, condition and nature that it was.

WILLIAM YOUNG J:

All right. Well, say Mr Maine had gone to the trouble of getting a geotechnical report and the technical report has said, well, we really need to do whole more work, we're absolutely emphatic that further costs of \$100,000 will be incurred, you would say that's irrelevant?

MR GRAY QC:

Yes, I would, Your Honour.

WILLIAM YOUNG J:

Even though on that evidence you could say with complete confidence that there would be costs of at least 100,000 to be incurred?

MR GRAY QC:

Well, they'd be higher costs, whatever they would be, Your Honour.

WILLIAM YOUNG J:

Yes, okay, on that hypothesis.

MR GRAY QC:

Yes. And the reason for that – well, there are a number. One is there isn't rebuilding, two, the policyholder's already been compensated for the change in condition of the land by selling it to the Crown at its market price at 2007, its rateable value at 2007 –

WILLIAM YOUNG J:

But that can't –

GLAZEBROOK J:

Yes, but that's a very odd situation. Normally the policyholder would be selling – if there'd been a slip somewhere the policyholder would be selling the land for whatever it was after the slip, wouldn't it? I mean, you can't just –

MR GRAY QC:

And also –

GLAZEBROOK J:

– you can't just interpret it against the EQC and what actually happened here and the Government bailout effectively with the buyout at 2007 values. This has to be interpreted as if somebody's house is not able to be built on the site because the site's disappeared.

MR GRAY QC:

Your Honour, the Court should not be allowing double compensation, double recovery.

WILLIAM YOUNG J:

But the policy means what it – the policy was in place before the red zone announcement, it's interpretation can't be affected by what happened to the land, can it?

MR GRAY QC:

But, Your Honour, it's a policy about the house.

WILLIAM YOUNG J:

I just, I don't see the, I don't see –

MR GRAY QC:

It's not a policy about the land.

WILLIAM YOUNG J:

– I don't see in construing the policy whether it's, what the respondent got for the land is material.

MR GRAY QC:

Well, in my submission it would be quite wrong for policyholders who have been compensated for the change in condition of their land to then come along and say, but I'm entitled to a higher recovery under my policy of insurance because of the changed condition of my land.

GLAZEBROOK J:

But that's not in front of us –

MR GRAY QC:

But they –

GLAZEBROOK J:

– at the moment –

MR GRAY QC:

No.

GLAZEBROOK J:

– because in fact all that's being applied is an industry standard that doesn't purport to take account of the changed condition of the land.

MR GRAY QC:

Yes, so –

GLAZEBROOK J:

It's an industry standard that would apply whether it was in Auckland, Christchurch or Invercargill, as one understands from Mr Farrell's evidence and Mr Harrison's evidence.

MR GRAY QC:

Yes, and it's a point that was made in the Court of Appeal, that the policyholder hasn't asked for it.

GLAZEBROOK J:

But it's the problem you have with paragraph 53, which is a different –

MR GRAY QC:

Yes.

GLAZEBROOK J:

– but that's a different point.

ELIAS CJ:

Yes.

MR GRAY QC:

Yes.

ELIAS CJ:

Well, it's not the case the parties put up.

MR GRAY QC:

No, and it hasn't been litigated.

GLAZEBROOK J:

No.

MR GRAY QC:

This policyholder has not come along and said –

GLAZEBROOK J:

Yes.

MR GRAY QC:

– “Please construe the policy to compensate me for the cost of building enhanced foundations because of the changed condition of the land.”

WILLIAM YOUNG J:

Well, I mean, the big case that could have been mounted was, to rebuild this house requires big foundations.

MR GRAY QC:

“And I want the cost of that.”

WILLIAM YOUNG J:

Yes. But that could only really be mounted with, there was geotechnical investigation, which there hasn't been.

MR GRAY QC:

It's not in issue before the Court today.

WILLIAM YOUNG J:

But this is really a bit shadow of that argument, saying, well, the land might not be great and we want an allowance for that built in.

ELIAS CJ:

Or that it is great.

MR GRAY QC:

Yes...

WILLIAM YOUNG J:

No, where there's an allowance for the risk.

ELIAS CJ:

Yes, yes.

MR GRAY QC:

Only a faint shadow, Your Honour, and only really as a consequence of Mr Harrison saying, "Look, my industry standard approaches the right one," and Mr Farrell responding by saying, "No, I don't think it is, in the circumstances of this particular case, and I've tried to make an, well, I've made an assessment of what I say it will be."

ELIAS CJ:

When you say, "In the circumstances of this particular case," though, you're referring to all cases where a substitute house is opted for –

MR GRAY QC:

Is purchased.

ELIAS CJ:

– aren't you?

MR GRAY QC:

Yes.

ELIAS CJ:

Yes.

MR GRAY QC:

Yes. It's this election under this policy.

ELIAS CJ:

This election, yes.

MR GRAY QC:

And it's an election for a sum of money and we're simply talking about the quantification of the amount of money.

ELIAS CJ:

But then on that basis, if that's all it is, and I tend to think it is, why, what is response again, can you re-state it to Justice Young's question as to why there isn't equivalence in terms of the payments that you can expect?

MR GRAY QC:

Because we say –

ELIAS CJ:

If you rebuild and if you –

MR GRAY QC:

Yes.

ELIAS CJ:

Or if you are building on another site where you'd get your 10% allowance –

MR GRAY QC:

Yes.

ELIAS CJ:

– that's probably the better comparison.

MR GRAY QC:

Because we say the structure of the policy is that 190 provides the replication of what was there before, and in circumstances where 191 is available because there's an actual rebuilding additional sums become available under 191 to compensate for unexpected things which arise because the replacement of the house is more than a replication and because 191 is not available for an election made, like the one that's made in this case. That's the case for Southern Response.

ELIAS CJ:

If one is – and I haven't done this – but if you do read the whole policy there are additional benefits that are obtained if you take the option of purchasing a replacement, you get your lawyer's fees and things like that.

MR GRAY QC:

Yes.

ELIAS CJ:

What do you get if you rebuild on another site – oh, no, you don't get that, you'd get a cash payment, and that's simply market value.

GLAZEBROOK J:

Well, you do if it's not rental, you get, you're allowed to –

ELIAS CJ:

Yes.

GLAZEBROOK J:

– rebuild on another site.

ELIAS CJ:

Yes, that's right.

WILLIAM YOUNG J:

Actually, there isn't a rebuild on another site, is there?

ELIAS CJ:

Not in this one.

GLAZEBROOK J:

No, because that's only if –

WILLIAM YOUNG J:

Yes.

GLAZEBROOK J:

– it's non-rental.

MR GRAY QC:

No, no, that's the difference, Your Honour, between an owner/occupier policy and a rental house policy.

ELIAS CJ:

But in cases where – it's not before us but I'm just curious – where the policy is for an owner/occupier and the option is rebuild on another site –

MR GRAY QC:

Yep.

ELIAS CJ:

– what's the position there? You'd get your 10% allowance there?

MR GRAY QC:

Well, we would say that you get under 190 the replication of your house where it was, and under 191 the additional costs you'll incur by reason of it being on another site where there are uncertainties about the ground, because the ground hasn't been dug before, the foundations haven't been there before, together with –

GLAZEBROOK J:

Wouldn't you just get whatever it cost to rebuild it –

MR GRAY QC:

Yes, because –

GLAZEBROOK J:

– as long as that wasn't more than what it would have cost under the previous one, which – but of course when you're rebuilding, under the previous one, if you're rebuilding you'd get the 191 costs. I know we don't have this in this case, but it surely couldn't be the point that you wouldn't get additional costs on the new site when you would have got them under the old site?

MR GRAY QC:

No, Your Honour's right, the response to the Chief Justice's question is you will get amounts actually incurred, not an estimate of them, and you will get the value of what was there before, and you might, and you will get some extra as well under 111.

GLAZEBROOK J:

Well, you'll have to, wouldn't you?

MR GRAY QC:

Yes.

GLAZEBROOK J:

Because otherwise it would be ridiculous, because what you're supposed to be is – well, what I think these are supposed to be is that you're in a neutral position whether you rebuild, whether you buy a new house, or whether you rebuild on another site. It's supposed to be absolutely neutral between those three. And then if you take a cash payment then it's not neutral because you only get indemnity value. So what you're supposed to be able to do is to replace, rebuild, buy another house, costs the insurance company the same, and whatever that case we had that was exactly the issue, the insurance company should be indifferent between the options, it's just money. So the insurance company is –

MR GRAY QC:

It's like – yes.

GLAZEBROOK J:

– responsible for the same amount of money no matter what happens, subject to extras like paying for solicitors' fees if you buy something else.

MR GRAY QC:

A slight variation to that, Your Honour. There's one rebuild option and two cash options. The two cash options are to buy another house and to get cash which, the amount of which is determined by reference to the cost of rebuilding, and the other is to get cash which is the indemnity value effectively, market value at the time of loss. So in fact –

GLAZEBROOK J:

Sorry, I'm really saying three –

MR GRAY QC:

– it's not two –

GLAZEBROOK J:

– replacement-type options –

MR GRAY QC:

Yes.

GLAZEBROOK J:

– and one indemnity option.

MR GRAY QC:

Yes, I'm not disagreeing with the substance –

GLAZEBROOK J:

Yes.

MR GRAY QC:

– Your Honour, the form of it, in my submission, is –

GLAZEBROOK J:

No, I understand you. So you say the cash option in the non-indemnity is different from the rebuild options?

MR GRAY QC:

Yes.

GLAZEBROOK J:

And that is because of the additional costs. Is that the only reason that's so?

MR GRAY QC:

Yes, yes.

Now I said I hadn't addressed myself explicitly to contingencies as distinct from professional costs, and really the, I accept that the challenge in this part of the argument is the one that, with respect, Justice Arnold made, which is that there are always some contingencies, yes, it's simply not possible to say from the outset that, when you build a house, something doesn't crop up. Life experience is contrary to that and I doubt there's a person here who hasn't experienced it. But again we say the reasoned way in which this should be approached is to say, "What's the policy doing?" The policy is paying to replicate what is there. The method adopted by quantity surveyors is to really treat it as a sum of the parts and to value all of the parts, so you value the wiring and the skirting boards and the walls and the roof and so forth, and to treat that as a proxy for the building of the whole, and within that it is simply not possible to say, "And there's something else."

WILLIAM YOUNG J:

Why? I mean, why not just envisage what the plans would look like –

MR GRAY QC:

The focus – well...

WILLIAM YOUNG J:

– and see what someone would offer, would be prepared to build a house to those plans for?

MR GRAY QC:

There are two parts to the answer, Your Honour. The first is that the operative part of the sentence I said was “is”.

WILLIAM YOUNG J:

Sorry?

MR GRAY QC:

That the operative word within my proposition is “is”. You can’t say there “is” something. You might suspect there will be, you might speculate about what there will be, but it’s an unknown. And the second part of the answer is the definition offered by Mr Harrison, which was accepted, is about changes made within the control of the owner –

GLAZEBROOK J:

Well, no, no, sorry, that isn’t the definition of “contingency”, that’s one of the elements.

WILLIAM YOUNG J:

Also, isn’t he really talking about what the word means when it’s in a building contract, as opposed to how someone might price a contract?

GLAZEBROOK J:

I think all he’s saying is the architect has it and can say whether it should be paid or not to the builder. So if the builder says, “I’ve had to put in an aluminium window which costs,” or, “I’ve had to put in a wood window, which costs more than an aluminium window,” then the architect says, “Well, sorry,

buddy, that was covered in the, you had to put in the wood window and that was covered under the contract.” I’m just looking at the definition you say at 173.

MR GRAY QC:

Yes.

GLAZEBROOK J:

I think it’s just saying, “Well, the architect decides whether it’s actually a contingency that had to be incurred that’s outside of the contract or whether it’s in the contract.” So you have 10% and then you have to go to the architect, the builder has to go to the architect and say, “I had to do this and it was outside of the contract.”

O’REGAN J:

Yes, but on 174 he says that it includes clients changed their minds –

GLAZEBROOK J:

No, I understand that.

O’REGAN J:

– and being awkward. I mean, how can you get insurance for that?

MR GRAY QC:

You can’t. And you can’t, for the reason articulated by Justice Glazebrook, because it’s outside the contract.

GLAZEBROOK J:

No, no, well, I can understand that –

MR GRAY QC:

If they’re actually additional.

GLAZEBROOK J:

– part of the contingency, but I don't think that's the only part of the contingency.

O'REGAN J:

But if that's part of it, it can't – if that's part of his 10% it can't, the 10% figure can't be right.

MR GRAY QC:

And that's the point made by Mr Farrell. Yes, when you build a –

GLAZEBROOK J:

Yes, but then he says nothing.

MR GRAY QC:

And he says nothing because he says you're simply replicating it. Yes, when we build it costs more, but it costs more usually because we change our minds or because it's not known in advance because it's not drawn up, the detailed drawings are not done, and so when you come to do it you find you're doing things that you didn't understand before that you would be doing. But Mr Farrell says, "That's not what's happening here, we know precisely what we're doing, we're replicating what's there. We know what it is and we're building that, and we can price that and I have."

WILLIAM YOUNG J:

Yes. But is still comes really back primarily, doesn't it, to the safe ground assumption?

MR GRAY QC:

Ah, well, not – well...

WILLIAM YOUNG J:

But most of the contingencies are underground.

MR GRAY QC:

That's what Mr Harrison says.

WILLIAM YOUNG J:

Yes. So –

MR GRAY QC:

It's kind of a double accounting.

WILLIAM YOUNG J:

– but that, I mean, I know he's thrown in the reference to client change of heart but most of it – which can't be right – but most of it is dealing with a state of uncertainty as to what the ground conditions are. Your man would probably accept this, I'm certain, but he says, "We're going to make an assumption," and that, it is, it's, the case is as simple as that, isn't it?

MR GRAY QC:

And as complex as that.

WILLIAM YOUNG J:

Would he deal with it on a real basis or an assumed basis?

MR GRAY QC:

And as nuanced as that, yes.

ELIAS CJ:

Well, it's not on a real basis, on either basis it's not real.

WILLIAM YOUNG J:

Sorry, on a real state of the ground or on a same state of the ground basis.

ELIAS CJ:

No, it's not on the real state of the ground.

O'REGAN J:

Well, they're both assuming, they're both making assumptions.

ARNOLD J:

It's not a real state of the ground, you don't know.

O'REGAN J:

One's assuming good and one's assuming bad.

GLAZEBROOK J:

No, no, if one's assuming the –

ELIAS CJ:

One's assuming the norm.

GLAZEBROOK J:

The norm generally.

WILLIAM YOUNG J:

Yes, one's assuming it may be bad.

ELIAS CJ:

Yes.

MR GRAY QC:

That's morning tea time, Your Honour.

ELIAS CJ:

Yes, perfect, thank you.

COURT ADJOURNS: 11.32 AM

COURT RESUMES: 11.54 AM

MR GRAY QC:

To move towards concluding submissions, Your Honour, the, perhaps the most succinct place to find the distinctions between the position in respect of professional fees and contingencies is in the evidence-in-chief of Mr Farrell in volume 2 at page 118 at paragraphs 9 and 10, and there Mr Farrell explained that for a proposed notional rebuild he applied a reasonable cost to prepare documentation needed for building consent, "Cost to withdraw existing, redraw existing drawings, apply any compliance-driven changes, including engineering required to secure consent for the same design, and consent costs were included, no contingency has been applied to the replacement estimate as we've assume good ground and precluded any unknowns within the foundations and excavation. No contingency is applied to the superstructure as once again we're applying the theory of a notional build to compliant drawings under a fixed lump-sum contract. This in my view constitutes standard practice within the market place and appropriate to this particular project."

GLAZEBROOK J:

Well, would a fixed sum lump-sum contract, you're saying they wouldn't have a contingency in?

MR GRAY QC:

No, because the price would be negotiated with the builder and the builder has the risk.

WILLIAM YOUNG J:

But wouldn't the builder factor that risk into the lump sum contract? Maybe, go out of business pretty quickly if they didn't factor risk in.

MR GRAY QC:

Well, Mr Farrell's the expert, Your Honour, I don't want to give alternative evidence.

WILLIAM YOUNG J:

No, no, but I think really the drift of what Mr Harrison is saying is, "Well, okay, we allow a contingency because that's the way we do things as quantity surveyors," but in reality any builder who was being asked to give a lump-sum contract will factor contingencies into the price, which is actually why I thought the reference to the contractual reference contingency wasn't very helpful.

MR GRAY QC:

My submission is that Mr Farrell has given evidence focused more precisely on the questions.

GLAZEBROOK J:

Well, is he a builder, is he saying that a builder would actually just accept the quantity surveyor, wouldn't put a 10% contingency in, which is standard practice, and would accept the risk that, it's not going to be lower than the fixed sum, is it, that Mr Farrell says, it's always going to be higher. So a builder would actually say, "Well, I don't mind, I'll just accept the fact that I might make it but I might actually have a, up to a 10% - and I think doesn't he put a builder's margin of 8% on, so actually all, more than my profit would go on a contingency if that contingency arises?"

MR GRAY QC:

He's a quantity surveyor, Your Honour, with Arrow, experienced in supervising the reinstatement, the rebuild or repair of homes in Christchurch.

GLAZEBROOK J:

Well, just answer the question. Would a builder accept a fixed-price contract with no contingency with an 8% builder's margin, ie, profit as I understand it –

MR GRAY QC:

Yep.

GLAZEBROOK J:

– and a possible 10% if the contingency all come to roost?

MR GRAY QC:

Your Honour, pricing's quite, more complex than permits a simple yes or no answer. A builder would price risk, a builder will not take risk that is not priced. The question in this case is what is the risk where there is a known building.

GLAZEBROOK J:

Well, assuming good ground and precluding any unknowns, a builder would actually accept a fixed-price contract excluding all of those things.

MR GRAY QC:

If the price is what does it cost to build these plans on this ground, which is known –

GLAZEBROOK J:

No, no, it's assumed good –

MR GRAY QC:

– where is the risk?

GLAZEBROOK J:

– and it's assumed that there are no unknowns.

MR GRAY QC:

Yes. What the evidence says is there is no risk to be priced.

GLAZEBROOK J:

Well, there isn't if you assume good ground.

MR GRAY QC:

Precisely.

GLAZEBROOK J:

Well, why did they assume good ground?

WILLIAM YOUNG J:

If you assume there isn't a risk then there won't be a risk to be priced, but that's just a circular argument, isn't it?

MR GRAY QC:

Well, it's Mr Farrell's evidence.

WILLIAM YOUNG J:

Yes, but it rests on a circular proposition that, "We're not going to price in risk because we're going to assume no risk."

MR GRAY QC:

We're going to assume there is no risk.

WILLIAM YOUNG J:

Yes, and therefore we don't price risk.

MR GRAY QC:

Yes.

WILLIAM YOUNG J:

But the real question is, are we right to assume no risk, are we right to assume there is no problem with the ground?

MR GRAY QC:

He wasn't really cross-examined on that, Your Honour.

WILLIAM YOUNG J:

Yes, I know, but it's self-evident, I mean, that's – if its premise is wrong then –

MR GRAY QC:

Yes, I can't take it any further. Again, I don't want to make up his evidence or to say what I think he would have asked if being cross-examined or what the further explanation would be.

WILLIAM YOUNG J:

Can I just put it to you? His evidence is premised on an assumption?

MR GRAY QC:

Yes, it is.

WILLIAM YOUNG J:

And if that assumption's wrong then his evidence doesn't help much.

MR GRAY QC:

Well, then he hasn't answered the subsequent question.

WILLIAM YOUNG J:

Yes.

MR GRAY QC:

If there in fact was risk what would the price for it be?

ELIAS CJ:

Is it even that, does it go that far? It's not whether there was actual risk in respect of the existing site, it's whether he's right to assume that you just don't take a precautionary approach, sorry, that it doesn't – the 10% thing is not, the 10% allowance is not done on the basis that, of the actual site, it's just an industry precautionary approach?

MR GRAY QC:

Mr Harrison was cross-examined on that, and the question is, "Why do you allow 10%, what's it for?" and his answer was, "Mostly it's in the ground."

ELIAS CJ:

Yes, but that would be true wherever you're building.

MR GRAY QC:

Well, yes, wherever you're building a new house on a new site. What Mr Farrell says is, "Because we're not building a new house on a new

site but the same house on the same site, where the existing foundations have been and are known, then there isn't risk." But, Your Honours, I've trespassed long enough saying again and again.

ELIAS CJ:

As you say, it really is a matter of impression largely, although difficult nonetheless.

MR GRAY QC:

Well nuanced, yes, it is, Your Honour. But it is a matter of first impression. Unless Your Honours have any further questions, those are my submissions.

ELIAS CJ:

Thank you, Mr Gray. Yes, Mr Campbell.

MR CAMPBELL QC:

Your Honours, before addressing directly the two issues of contingencies and professional fees, I'll make a very brief submission on what, in my view, is the only point of construction for the Court, and this is reflected in the judgment of the Court of Appeal where the Court accepted the submission that was made to them that in estimating the cost of rebuilding the house on its existing site it's not relevant that the rebuilding will not actually take place or that Avonside will not actually incur any rebuilding costs, and this I think is a point that Justice Glazebrook picked up earlier on. One has to make the best estimate of what those costs would be if rebuilding did actually take place. And the reason that I make that submission is that, as I hope to show, the approach of the witnesses for Southern Response, particularly Mr Farrell, was to attempt to justify his treatment of contingencies and professional fees by reference to the fact that rebuilding would not actually take place. So that broad submission's at paragraphs 33 to 36 of my written submissions.

Now if I deal with contingencies first or next. Southern Response's written submissions on contingencies emphasise or make the point that –

ARNOLD J:

If I could just interrupt, I was just thinking about that point you just made. As I understood thrust of the argument that's been made this morning it was that, for example in relation to contingencies, there are no unknown factors of the sort that would normally exist when you were doing a building; in relation to professional fees there are existing plans. So the point, as I understood it, of the argument, wasn't really that it's the rebuilding won't actually take place, the argument was we have a certain amount of knowledge and pre-work that we can build on in terms of calculating the rebuild cost, and that's a different point, isn't it?

MR CAMPBELL QC:

Yes, I think that's correct, Your Honour. However the explanations that the Southern Response witnesses gave at trial don't really reflect that argument, particularly in relation to contingencies. So I'll come to the evidence that they gave. In my submission the resolution of both the contingency issue and the professional fees issue is actually just a question of fact on the particular circumstances that faced the parties in this case, and so resolution of those issues has to be determined by reference to the evidence that was given at trial, and so for instance when it comes to contingencies – and I'll take you to the evidence shortly – all three witnesses, two for Southern Response and Mr Harrison for Avonside, recognised that there were uncertainties. Notwithstanding that this was a notional rebuild of a known building on a known site, all three of them recognised that there were uncertainties. But Mr Farrell for Southern Response nonetheless did not make any allowance for contingencies and it appears from his evidence that the reason that he made no allowance was that it was just a notional rebuild which was not actually going to happen. So I'm, in my view I have to confront the evidence that was given, because it is ultimately for both of those issues, contingencies and professional fees, a question of fact, so we have to look at the evidence. Now my learned –

ARNOLD J:

Well, except that as I understood it your expert's evidence wasn't an estimate of contingencies based on this particular circumstance but was just a standard 10%, similarly in relation to professional fees. So isn't that a problem that in a sense, this was said earlier, the experts have not really grappled with the positions that each have been espousing?

MR CAMPBELL QC:

It is the case, of course, that any expert quantity surveyor, when making allowance for contingencies, is going to make that allowance, at least probably in large part, on the basis of past experience of what's happened with other building projects on other sites. But nonetheless there is a recognition in the evidence, and really from all of the witnesses, that they've taken into account the particular characteristics of this site, such as its proximity to the river and the effects of, the relevance of that to, for instance, the likelihood of liquefaction on the site and the effect of that on ground conditions.

ARNOLD J:

I see. And so Mr Harrison's taken into account in professional fees the fact that there are existing drawings and so on?

MR CAMPBELL QC:

Yes, he has, and he –

ARNOLD J:

Yes. Okay, thanks.

MR CAMPBELL QC:

That's put to him, and he explains that he hasn't allowed for a fully fledged architect, he's allowed for an architectural draftsman.

ARNOLD J:

Right, okay.

GLAZEBROOK J:

So are you saying that the 10% is not a standard amount?

MR CAMPBELL QC:

For contingencies, Your Honour?

GLAZEBROOK J:

Yes.

MR CAMPBELL QC:

I imagine it is rather standard, and there was no –

GLAZEBROOK J:

But did he not arrive at it on that sort of approach?

MR CAMPBELL QC:

Well, I expect that he did largely apply the standard but in, when the, particularly when Mr Harrison and Mr Farrell were empanelled –

GLAZEBROOK J:

Yes.

MR CAMPBELL QC:

– or in the hot tub, they were both examined about contingencies and they both made reference to the particular circumstances of the site. So Mr Harrison had visited the site I think on three, maybe four, occasions, these things are not done completely in the dark, I think Mr Farrell had visited the site once. So, as I said to Justice Young, without – I'm sure that any quantity surveyor is going to make their estimate based on past experience, so in that sense they're not going to just start from the ground up with any particular, and not take that past experience into account when making an allowance for contingencies.

So at paragraph 9 of my written submissions I have pinpointed the various evidence given by Mr Harrison, Mr Farrell and Mr Phillips as to the risks or uncertainties, and the reason for that is that contingencies are all about making an allowance for uncertainties or unknowns. Southern Response's written submissions at least were that there were no uncertainties because we were just rebuilding a known structure in a known location so Mr Harrison identified, as has been discussed already, that a lot of the uncertainties were in the ground but he also referred to the quality of the documentation, variations by consultants and clients, and staffing, and I've noted with pinpoint references that Mr Farrell accepted there were uncertainties in relation to ground conditions, quality of documentation, product availability and weather, and he also agreed that it wasn't unusual to use 10% as a contingency allowance.

Mr Phillips, who shouldn't be overlooked, accepted there were risks, council changes to plans, client changes, product specification, delays in arrival of products, weather and staffing capacity. So that doesn't even include reference to ground conditions.

GLAZEBROOK J:

Of course client changes couldn't be part of what Southern Response was required to pay, could they?

MR CAMPBELL QC:

I expect it didn't form a large part of either Mr Phillips or Mr Harrison's approach. Mr Phillips accepted that Mr Harrison's approach was standard, orthodox quantity surveying practice and that an allowance of 10% for contingencies was not unreasonable, particularly since the earthquakes.

GLAZEBROOK J:

Did anyone, because what was being said against you is that that might be the case for new builds on new sites, but not for rebuilds on known sites. Was that dealt with particularly by any of the witnesses? I think you'd probably say no?

MR CAMPBELL QC:

Well Mr Farrell, as I move on to say, his reason for not allowing contingencies was that it was a rebuild on a known site. I'm not sure if this is going to answer your question Your Honour but –

GLAZEBROOK J:

What did Mr Harrison, or Mr Phillips say about that?

MR CAMPBELL QC:

I don't think that Mr Phillips was asked particularly as to whether the fact that it was a rebuild of a known house on a known site made any difference. But I'm sure it was put to Mr Harrison by Southern Response's counsel and Mr Harrison, as I recall, did not think that it made any difference.

GLAZEBROOK J:

All right.

MR CAMPBELL QC:

So the point I wish to emphasise is that Mr Farrell's reason for not allowing any contingency was not as one may have assumed, from my learned friend's submissions, that there, that Mr Farrell didn't think there were any uncertainties. It was simply that a notional rebuild wasn't actually going to happen and this is reflected in a – I might add to that, that Mr Farrell also made the assumption of good ground, and I've emphasised that in the written submissions. But at paragraph 40 I've set out an exchange between Southern Response's counsel and Mr Farrell. Mr Farrell is asked, "Does the notional rebuild change things for you?"

GLAZEBROOK J:

Sorry what are you, where are you referring to?

MR CAMPBELL QC:

Paragraph 40 of my written submissions. I might actually take you to the evidence actually, Your Honours, because it might be useful to start at page 178 of volume 2 and just start from line 25 on page 178. That's Mr Johnstone for Southern Response putting a question to Mr Harrison. So at this point in the hot-tubbing there had been discussion, examination of both Mr Farrell and Mr Harrison on contingencies and what the uncertainties were and from line 25 it's put to Mr Harrison, "Your answer would apply to building contracts generally?" "Yes," and then there is a question about, "Well this is a notional exercise," and I think summing that up it's suggested that because it's a notional exercise that makes a difference. Mr Harrison says, "Whether it's for this site or any site I think the contingency factor would still be there. There is that element that something not going to be in the drawing that needs to be, whether it's a notional rebuilt or an actual rebuild. I don't think there's any differences between the two." And then the same question is put to Mr Farrell. "Does the notional rebuild change things for you?" "In my view, yes." "Why?" "A notional build is not going to happen. There is no risk." So that's where the risks, or why, according to Mr Farrell, the risks get removed, because it's just a notional exercise and that goes back to the submission I made at the opening that what one has to do is estimate the cost as if the rebuild did actually happen.

If I go back to my written submissions from paragraph 41, Mr Farrell made the same sort of point in relation to one of the particular risks, and perhaps one of the more significant ones, the risk posed by ground conditions. I think my learned friend took you to Mr Farrell's brief where he said where, and I've quoted this at paragraph 41 of my submissions, "No contingency has been applied to the replacement estimate as we have assumed good ground and precluded any 'unknowns' within the foundation and excavation." And in the hot-tubbing Mr Farrell expanded upon that by saying, "Where we've come from with the estimate is that this is a notional build." So again emphasis on it being a notional rather than an actual build.

GLAZEBROOK J:

I've just noticed something. At page 92 he hasn't assumed a fixed term contract that doesn't take account of contingencies. He said that would be an unknown and a variation. So the fixed price contract he's assuming would be on the basis that there is no risk and any risk that's found later would be an addition to the contract, as I understand what he's saying at the bottom of page 92.

MR CAMPBELL QC:

That's page 177 of the case Your Honour?

GLAZEBROOK J:

Page 177 of the case. So, in fact, what I put to Mr Gray, that the builder wouldn't accept a contract and take the risk, he seems to accept that, and that would be a variation to the contract if it did occur rather than having a contingency in the contract itself as how I understand his evidence to be.

MR CAMPBELL QC:

I think that must be right Your Honour. Well that appears to be Mr Farrell's approach there, that the –

GLAZEBROOK J:

That the fixed sum contract doesn't include contingencies but that they would be costed separately as variations?

MR CAMPBELL QC:

Yes, that appears to be what he's saying there.

GLAZEBROOK J:

Sorry to interrupt. I just, having seen that I thought I better just check.

MR CAMPBELL QC:

Thank you. And I've referred also at paragraph 42 to other statements in Mr Farrell's evidence about assuming good ground. The other passage that I

would take you to, if I might, is on page 175 of volume 2, and from half way down the page Mr Shand, counsel for Avonside, puts a number of questions to Mr Farrell which are essentially to the effect that this is red zone land, it's next to the river, these are risk factors are they not, and you see from his response at line 28, "Yes, when close to a river and then when an earthquake that has taken place it is more likely of being something spread." I infer a lateral spread and it's put, "Well a 10% contingency would not be unreasonable, would it?" "That really depends. If we were to follow the process that we're doing now in Southern Response we would have which is not dissimilar to what, in fact, it's absolutely similar to how we deal with the technical category 3 properties. We would have a full geotech report," et cetera. "We would have the foundation designed and completed in which case we would not hold a contingency for the foundation and ground conditions." So that's assuming that a whole lot of work has gone on to find out what the ground conditions actually are. But what we have here, of course, is a situation where we don't know what they are, which is then put, "You don't truly know the ground condition until they excavate and start putting in the foundation, correct?" and Mr Farrell feels unable to comment on that, says, "We'd have a geotech report." So the proposition that one shouldn't be assuming good ground or can't assume good ground was, in my submission, fairly put to Mr Farrell. So that's why – perhaps to go back to Justice Arnold's question of me after I made my first submission – why I didn't want to emphasise that the fact that this is a notional rebuild is not relevant to a determination of an estimate or calculation of what the costs would actually be, yet that is really what Mr Farrell has done in taking the view that there should be no contingency allowance.

And if I can move to professional fees. Now in any rebuilding it is going to be necessary to incur various professional and other fees in order for the rebuilding to occur, and those are just part of the costs of rebuilding like any other cost, such as cost of the physical work itself or cost of the materials, and that is why, no doubt, Southern Response has even allowed for some professional fees in its rebuild cost estimate. Once again, what the appropriate allowance is in this case is a question of fact, which has to be

resolved on the evidence that was presented. And so from paragraph 47 I've made reference again to the evidence from Mr Harrison, Mr Phillips and Mr Farrell. So, firstly, I've given reference to Mr Harrison's evidence of the professionals and other fees that he allowed for in his 10% allowance. It's not just professional fees but it is mostly; there were also consent fees, which both parties allowed for. But otherwise Mr Harrison was allowing for a draftsman for design or redrawing the plans, a structural engineer, a geotech engineer, a land surveyor, consent fees, and a project manager or quantity surveyor. Now apart from Mr Farrell and Mr Phillips both accept that Mr Harrison's approach was reasonable, Mr Phillips himself agreed that in order to rebuild this house on its present site there would be fees involved in consents, geotech and structural engineers, a land surveyor, a draftsman and a project manager, and I've given you the references to Mr Phillips's evidence where he accepts all of that. Now those are exactly the same professionals that Mr Harrison allowed for, and so it was unsurprising that Mr Phillips accepted that Mr Harrison's approach to costing was orthodox quantity surveying practice, and nonetheless there was a vast difference between the position of Mr Harrison on the one hand, who allowed 10%, which came to about 157,000, whereas Mr Farrell allowed only 29,000, and in my submission the Court of Appeal was right to prefer Mr Harrison's estimate.

The first reason is that Mr Phillips, for Southern Response, had accepted that the professionals who were going to be required would be exactly the same ones that Mr Harrison allowed for, and he accepted that Mr Harrison's approach was reasonable, yet Mr Farrell's 29,000 estimate made no allowance for two of the professionals that Mr Phillips acknowledged would be needed, the land surveyors and the project managers, and it also estimated geotech fees on the assumption of good ground, so there is an overlap between the two issues, contingencies and professional fees, in that that assumption, which was never explained, except by Mr Farrell saying that, "Well, this is a notional rebuild," that was not a proper assumption to have made.

The other reason that the Court was right to prefer Mr Harrison's estimate was that Arrow had itself in an earlier costing allowed a sum of just over a hundred thousand for design and consent fees, and that figure was actually calculated as a, as 9% of the, if you like, the core building costs. So I have referred you to the two documents in which that earlier estimate was allowed for. So the 9%, obviously, is rather close to the 10%. I think Mr Farrell's 29,000 comes to probably something like 2% by contrast. The reason that there's still a big gap between the hundred thousand and the 157,000 allowed by Mr Harrison is that earlier rebuild estimate by Arrow had a lower basic building cost. The parties ended up coming closer together in that respect. But what's important is that Arrow had earlier taken the view that 9% was a, or had earlier allowed 9% for these items.

WILLIAM YOUNG J:

So it's a total building cost of around, just over a million dollars?

O'REGAN J:

Must be 1.5 million.

MR CAMPBELL QC:

Yes, I think 1.5.

WILLIAM YOUNG J:

Or 1.5 million, 1.5, okay.

MR CAMPBELL QC:

The figure of, say, 157,000 and 29,000, I'm fairly sure are the gross amounts before there is the apportionment to reflect the under-insurance.

WILLIAM YOUNG J:

The one – the under-insurance, okay.

MR CAMPBELL QC:

Yes. So that's the other reason that the Court was right to prefer Mr Harrison's evidence, because Arrow itself had taken the view earlier that 9% was a proper allowance. That document was put to Mr Harrison –

O'REGAN J:

Can I just ask you, why do the professional fees become cheaper if the building's smaller? If you still need the same people doing the same work, why do you abate them?

MR CAMPBELL QC:

Well, that's not before Court, but I assume it's because – and that happened, I mean, the parties really agreed on that proposition. I assume that's because the, if you've insured only for a 300 square metre house and you end up with a 500 square metre, and it was actually a 500 square metre –

O'REGAN J:

Yes, but if you need geotechnical advice for a house you need it whether a house is big or small, don't you? I mean, engineers don't say, I'm charging you \$200 an hour on this house but if it was a bigger house I'd charge you \$300 an hour.

MR CAMPBELL QC:

That may be right, but what's done is done, that's how the parties apportioned those.

WILLIAM YOUNG J:

They just did it rateably, they just pro-rated it, I take it.

GLAZEBROOK J:

Well, it did say the, "The price for a 500 is this and we'll just rate it down, because you're under-insured."

MR CAMPBELL QC:

I'm fairly sure that's what happened. So that earlier estimate was put to Mr Farrell in cross-examination and his, and then when he was re-examined, during the hot tub, Mr Farrell said that the hundred thousand dollar or 9% figure was calculated to give Southern Response – and I've quoted this at paragraph 52 of the written submissions – to give Southern Response an indication of full exposure, "If they were to rebuild that house on site with full architectural input," but that was not the figure that applied for a notional rebuild exercise. But what's in issue here is what it would cost to rebuild the house on site. Admittedly not necessarily with full architectural input, but the difference between full architectural input and an architectural draftsman is not significant, you still needed all those other professionals as well. And what we see there is that Mr Farrell again is relying on the fact that it's a notional build and that this somehow affects the allowances that should be made, in this case for professional fees.

ELIAS CJ:

Mr Campbell, because it is one of the two matters you rely on, that earlier costing for the rebuild, can you explain the circumstances in which that was arrived at? I'm just not sure what its status was. It was something that, an internal document, was it, which was put to Mr Farrell?

MR CAMPBELL QC:

Well, there are two earlier documents. One's at page 311 of volume 3 and that is the document that Mr Farrell produced as appendix A to his brief so I will just find how Mr Farrell described it.

ELIAS CJ:

What is this document? Oh, he's described it, yes.

MR CAMPBELL QC:

Yes, in his brief, which is at page 117 of volume 2, at paragraph 5. So the acronym DRRA detailed, or sometimes I think the document itself says details rebuild/repair analysis. It was a tool devised to assist AMI, now

Southern Response, to capture and report on damage of earthquake related claims. It summarises the dwelling with specific measures and elements of the building, room, walls, et cetera, and so that's what appendix A is. And one doesn't want to spend too much time examining it, given the size of the font that one sees there, but I have pinpointed the relevant item on page 317 of volume 3. If you like you can think of it as an elemental costing exercise and on –

ELIAS CJ:

But this was for rebuild on site, was it?

MR CAMPBELL QC:

Yes.

WILLIAM YOUNG J:

Do you know the date of it?

MR CAMPBELL QC:

Yes, in some ways, I'll tell you what it was –

WILLIAM YOUNG J:

August 2011.

MR CAMPBELL QC:

Ah, it's actually the 5th of March 2013 because you'll see on page 311 on the top left, if you come down to about line 12 it says –

WILLIAM YOUNG J:

I see.

MR CAMPBELL QC:

– “Revision,” there's something in red, revision being 5 March 2013.

WILLIAM YOUNG J:

Well it can't really have been an estimate for a rebuild that was intended to happen given that by then the property had been red-zoned.

ELIAS CJ:

Which has no legal status.

WILLIAM YOUNG J:

But it was most unlikely that by this stage it was envisaged that the property would be rebuilt in Avonside Drive.

MR CAMPBELL QC:

That's correct.

WILLIAM YOUNG J:

So the suggestion that this is actually an estimate of what it's really going to cost us when we rebuild the house doesn't seem to be right. Doesn't seem very plausible, anyway, for the moment.

ARNOLD J:

Well it was originally done in August 2011.

WILLIAM YOUNG J:

Yes, but the red zone was June 2011.

ARNOLD J:

Yes, that's right.

GLAZEBROOK J:

Well isn't it really just going and saying well this is what this – this is the costing for the house, not an actual rebuild, but just costing what it would cost to rebuild.

ELIAS CJ:

On the actual site.

GLAZEBROOK J:

Well, sort of, but...

ELIAS CJ:

I'm just really struggling for the status of it and what reliance, because you place a lot of reliance on it, and so did the Court of Appeal I think.

MR CAMPBELL QC:

Well the only element on which I rely is that, and I don't rely on the elemental build up because I don't want to go there, we don't have to, but on page 317 the allowance that Arrow made for design fees and consent is expressed as 9%.

ELIAS CJ:

Where's that, sorry?

MR CAMPBELL QC:

Page 317.

GLAZEBROOK J:

Yes, I'm just trying to find it as well.

O'REGAN J:

It's about eight lines down from the top of the page.

GLAZEBROOK J:

I see, yes, I see.

WILLIAM YOUNG J:

I can't see it.

GLAZEBROOK J:

It's, there's about five or six lines at the top –

ELIAS CJ:

The line that says design fee and consents.

MR CAMPBELL QC:

And the notation is indented to about half way across the page there.

GLAZEBROOK J:

So right at the top of the page, there are about four lines, it's about the third line down, in the middle column.

WILLIAM YOUNG J:

Okay, yes.

GLAZEBROOK J:

Well you'd say the reliance is that he's relying on this, in fact, in his evidence.

MR CAMPBELL QC:

Indeed, yes, yes.

GLAZEBROOK J:

So he's saying we use this tool, their tool includes 9% and you say he doesn't explain why he went from 9%, apart from saying it was a notional not an actual rebuild –

MR CAMPBELL QC:

Correct.

GLAZEBROOK J:

Is that the reliance?

MR CAMPBELL QC:

Yes, yes.

GLAZEBROOK J:

So this isn't a document that was internal? Well it was a document that was internal but it was relied on by Mr Farrell in his evidence. It was attached to it.

MR CAMPBELL QC:

Yes, he produced it so –

ELIAS CJ:

But his evidence is you don't use the rebuild analysis because it is just notional and it's simply a proxy to enable you to get to the cap in the policy once they have opted to go to purchase of a replacement house.

MR CAMPBELL QC:

Yes but –

ELIAS CJ:

I mean I'm just not sure that it entirely answers the point. What it shows is that, which I don't really understand to be in contention, that a conventional figure of around 10% if you're looking at rebuilding or building on a new site, might be perfectly in order, but the case that is being put by the appellants is that it isn't appropriate where you are exercising the option of purchasing another dwelling.

MR CAMPBELL QC:

That is –

WILLIAM YOUNG J:

Well there are two or three issues I think. that's one argument, that you just assume good ground and we don't worry about risks because they're never going to crystallise. But the other one is, what's the –

ELIAS CJ:

Well sorry, can I just have a, just is that right, and then you can put your other point.

MR CAMPBELL QC:

I don't know that Southern Response is quite making the argument that just because you've chosen the option of buying another house that this, in itself, affects the way in which one estimates the cost of rebuilding on the original site. Mr Farrell certainly had that approach, however, this is why I made that submission at the outset and then taken you to Mr Farrell's evidence where he doesn't allow contingencies because it's a notional rebuild –

ELIAS CJ:

Yes.

MR CAMPBELL QC:

– and the risks are never going to happen.

ELIAS CJ:

Yes.

MR CAMPBELL QC:

In relation to professional fees, I've taken you to this document which Mr Farrell produced because Mr Farrell himself said this was our estimate of how much it was going to cost to rebuild on the original site.

ELIAS CJ:

Yes.

MR CAMPBELL QC:

And my submission is, that's exactly what Avonside is entitled to under the policy.

ELIAS CJ:

Yes, well I understand that argument, that's really where you're in contention. What I don't understand is why the evidence actually assists in the critical question that the Court has to decide, which I would have thought was simply a question of interpretation of a policy.

WILLIAM YOUNG J:

It might be material to the suggestion that there was no need for professional fees because there were in existence plans because that presumably would have been factored into this document's assessment.

MR CAMPBELL QC:

Indeed.

WILLIAM YOUNG J:

So accepting that there are a set of plans, we still think it's 9% professional fees.

MR CAMPBELL QC:

Yes.

O'REGAN J:

Well no, because he said this assumes full architectural input, which seems to assume there aren't existing plans.

GLAZEBROOK J:

Where does he say that?

WILLIAM YOUNG J:

Where does he say that sorry?

O'REGAN J:

In Mr Campbell's submission at paragraph 52 he quotes Mr Farrell as saying, "It was a figure that was used to give an indication of full exposure if they were

to rebuild that house [on site] with full architectural input.” So that, I think, assumes there isn’t existing plans.

MR CAMPBELL QC:

But he also said that it wasn’t a figure that applied for a notional rebuild exercise so his, Mr Farrell’s contrast was between rebuilding the house on site with full architectural input and a notional rebuild exercise.

WILLIAM YOUNG J:

But in any event even by August 2011 they were never going to rebuild the house on the site.

ELIAS CJ:

Well that’s not clear.

ARNOLD J:

The recommendation is we recommend demolishing it and rebuild it.

WILLIAM YOUNG J:

But how could they.

ARNOLD J:

Yes, well how could they, but I mean that’s –

ELIAS CJ:

But that is to look to externalities surely.

WILLIAM YOUNG J:

But it’s document though.

ELIAS CJ:

No but interpreting the document at the time, before the options have been exercised, is that right, before the options have been exercised under the policy?

MR CAMPBELL QC:

I suspect –

ELIAS CJ:

When you have a declaration of the status of red zone, which doesn't translate into any illegal status, it's all quite unclear, isn't it, that it was never going to be built on again?

MR CAMPBELL QC:

That's correct, I expect that the, that one of the reasons that Arrow would have gone through this exercise with hundreds, if not thousands, of houses, is to see what needs to be done to repair it, how much that's going to cost, is it going to be economic to actually repair as opposed to rebuild.

ELIAS CJ:

Yes.

MR CAMPBELL QC:

But I have to say that's partly just my assumption from other experiences.

ELIAS CJ:

Yes.

MR CAMPBELL QC:

But probably a reasonable one.

ARNOLD J:

Does this schedule allow for contingencies?

MR CAMPBELL QC:

No, I don't believe so. I think there's a line for contingencies that says 10% but then has no figure.

ARNOLD J:

So whereabouts is that?

MR CAMPBELL QC:

Well, I'm, that might be on a different document actually.

GLAZEBROOK J:

What's, "P and Gs"?

MR CAMPBELL QC:

"Preliminary and general."

GLAZEBROOK J:

That's helpful.

MR CAMPBELL QC:

Does that help?

ELIAS CJ:

I see that this document is headed, "Details repair/rebuild analysis" – oh, that's what DRRA stands for.

MR CAMPBELL QC:

Indeed.

ELIAS CJ:

So it does look as if it's part, as you suggest, that sorting analysis, yes.

MR CAMPBELL QC:

Justice Arnold, the DRRA doesn't have a contingency line, I believe.

ARNOLD J:

It doesn't, okay.

MR CAMPBELL QC:

But the –

ARNOLD J:

No, no...

MR CAMPBELL QC:

There is another Arrow costing at page 319 which does, but it just says 10% but then has no figure, which –

ARNOLD J:

Right.

MR CAMPBELL QC:

– to be fair is consistent with the approach. And that one is much easier to read and was simply put to Mr Farrell during the hot-tubbing process, I think. That's the one that also has design and consent fees of a hundred thousand, but I don't think there's sufficient in the evidence to tell you very much about this particular, the history of that document. What I should also point to you that what Mr, one of the documents that Mr Farrell produced that had the \$29,000 for professional fees as opposed a hundred thousand, that's at page 324, "Offer of settlement by construction breakdown."

GLAZEBROOK J:

Sorry, I can't see that – oh, okay.

MR CAMPBELL QC:

Page 320, about seven or eight lines up from the bottom.

GLAZEBROOK J:

Oh, 320, no wonder I can't see it.

MR CAMPBELL QC:

I'm sorry, are you referring to the last document that I referred to?

GLAZEBROOK J:

Yes.

MR CAMPBELL QC:

Sorry, that's at page 324, Your Honour.

GLAZEBROOK J:

Oh, sorry, they've got A, B, Cs and Ds. So it's actually at 324, is it?

MR CAMPBELL QC:

Yes. That's the original 324.

GLAZEBROOK J:

Okay, right, I see.

ELIAS CJ:

That's the 29,000, is it?

MR CAMPBELL QC:

Yes. I think I've, there are references in my submissions to all of those documents, references to the case, that is.

Your Honours, unless you've got further questions on the professional fees issue, that's all I intended to say. I don't want to say anything about issues that aren't before the Court. In that case, those are my submissions.

ELIAS CJ:

What do you say about paragraph 53 of the Court of Appeal's decision?

MR CAMPBELL QC:

I think that's one of the issues that I'm not sure is...

ELIAS CJ:

Well, if it's not, then we'd like that confirmation from you, because it probably suggests that we should distance ourselves from it. Is that what you're saying?

MR CAMPBELL QC:

Yes, I think I've made that reasonably explicit at paragraph 30 of my written submissions, although that doesn't refer to...

ELIAS CJ:

Yes, I wondered what that was – yes, I hadn't...

MR CAMPBELL QC:

Oh, not only paragraph 30, but also paragraph 44. Paragraph 44, I confirm and make clear that –

ELIAS CJ:

The last sentence?

MR CAMPBELL QC:

Yes, "Avonside was not –

ELIAS CJ:

Yes.

MR CAMPBELL QC:

– seeking as part of its estimate of the cost of rebuilding –

WILLIAM YOUNG J:

But you would say that in assuming the costs of the rebuild, the safe ground assumption of Mr Farrell isn't right?

MR CAMPBELL QC:

Correct, yes. That's a different issue, Sir, from whether one's entitled to –

WILLIAM YOUNG J:

Big foundations.

MR CAMPBELL QC:

– enhance foundations –

WILLIAM YOUNG J:

Yes, yes.

MR CAMPBELL QC:

– because the Code's changed, yes.

GLAZEBROOK J:

Well, you'd presumably would say that if this was in Auckland you couldn't assume safe ground either, even on a known rebuild, is that –

MR CAMPBELL QC:

Correct.

GLAZEBROOK J:

– because this is an industry standard contingency taking account of the fact that even, even with existing plans and a known structure, with Mr Harrison's evidence there can still be these issues like soft spots?

MR CAMPBELL QC:

Yes.

GLAZEBROOK J:

And Mr Farrell would say, "Well, that would be dealt with by a variation of a fixed-price contract, not by a contingency"?

MR CAMPBELL QC:

He might say that, he might say, "Well, it's a notional rebuild so we assume no risks."

GLAZEBROOK J:

Or, "It's a notional rebuild so we don't have to."

MR CAMPBELL QC:

Yes.

ELIAS CJ:

Is it a bit misleading to even refer to assumptions about good ground, because there's no assumption of bad ground either? It's just an allowance that is made across the board, isn't it?

MR CAMPBELL QC:

Well, I think it's probably best to put it that you don't assume either –

ELIAS CJ:

Yes, that's what I mean.

MR CAMPBELL QC:

– you assume that you don't know.

ELIAS CJ:

Yes, yes.

WILLIAM YOUNG J:

You might assume a risk though because, as they refer to in the evidence, that it's by the river, it's been regarded as unsuitable for building in the medium term and there's apparently liquefaction.

MR CAMPBELL QC:

Well, you're probably right, Your Honour, if you're suggesting that there might be some situations where the contingency would be, or should be higher –

ELIAS CJ:

Yes.

MR CAMPBELL QC:

– than in others.

ELIAS CJ:

But this is a standard amount, isn't it? I mean, that's what I've taken from the argument addressed to us, that around 10% is a, is industry standard.

MR CAMPBELL QC:

Yes, and that would suggest that it's –

ELIAS CJ:

And that would suggest that it's neutral, that there is no specific assessment of the actual land, or there's no attempt to. So that the discussion about close to the river and so on doesn't lead anywhere on the cases put by the parties.

MR CAMPBELL QC:

If anything, it suggests that maybe the allowance was conservative.

ELIAS CJ:

Well, it's not done by reference to the actual position.

WILLIAM YOUNG J:

To some extent it is – I mean, there are references to it.

ELIAS CJ:

Well, I know, but they don't lead to anything.

GLAZEBROOK J:

Well, apart from to say, "This is the industry standard and there are risk factors here that suggest we definitely should have it in," rather than –

ELIAS CJ:

Yes, at least the industry standard.

GLAZEBROOK J:

– “We don’t have to have it in.”

ELIAS CJ:

Yes.

GLAZEBROOK J:

So it’s relevant to the extent that you say, “Well, we can’t do without it,” is that fair.

MR CAMPBELL QC:

We shouldn’t depart from the standard.

GLAZEBROOK J:

Yes.

MR CAMPBELL QC:

Yes.

ELIAS CJ:

Yes.

MR CAMPBELL QC:

Those are my submissions, unless there are further questions.

ELIAS CJ:

No, thank you, Mr Campbell. Yes, Mr Gray.

MR GRAY QC:

Two quick points only, Your Honours. We say the document at 311 is a red herring. It was prepared in, initially in 2011, it’s a provisioning document, not an analysis of a settlement entitlement under the policy.

GLAZEBROOK J:

So do you say – no, I understand that it's not a settlement document under the policy, but do you say that the provisioning therefore is therefore the absolutely maximum that could possibly come, or what do you say that is, what was the evidence on that?

MR GRAY QC:

I say, Your Honour, that is the meaning of the answer that Mr Farrell gave to the question which is at page 185 in volume 3 – 2, of the case. My learned friend, Mr Campbell, has extracted this particular answer and put it into his submissions. The exercise was conducted to give Southern Response an indication of full exposure, if they were to rebuild the house with full architectural input. It's their full exposure.

WILLIAM YOUNG J:

But it's not just a sort of a general provision document because it's got a recommendation in it. It's not saying on the worst case we'd have to do this. It's saying we recommend that the house be demolished and rebuilt on the site.

MR GRAY QC:

Well that's the basis of the provision.

WILLIAM YOUNG J:

Yes.

MR GRAY QC:

So it's not a repair.

WILLIAM YOUNG J:

And by, mmm, and by the date of the last iteration of this document it was never going to be rebuilt on the site.

MR GRAY QC:

By then it wasn't, no. And by then AMI had been sold, Southern Response had been formed and capitalised by the State. That's my first point. My second is the \$29,000 for legal fees is not intended to abate by reference to the under-insurance –

ELIAS CJ:

The legal fees did you say?

MR GRAY QC:

The professional fees I'm sorry. Was not intended to abate by reference to the reduced size or the under-insurance but was –

GLAZEBROOK J:

We don't really have, that's not really before us.

MR GRAY QC:

No.

GLAZEBROOK J:

I'm just thinking of the complications that –

MR GRAY QC:

No but my learned friend Mr Campbell suggested that it might be a number which was expected to abate by reference to the difference in floor area, and we say no it isn't.

ELIAS CJ:

And it wasn't.

MR GRAY QC:

No.

ELIAS CJ:

Because it was the evidence he gave.

MR GRAY QC:

Yes.

ELIAS CJ:

Yes.

MR GRAY QC:

Unless Your Honours have any other questions those are my submissions in reply.

ELIAS CJ:

No, thank you. Thank you counsel for your submissions. We'll take time to consider our decision.

COURT ADJOURNS: 12.52 PM